

**SUPPORT TO STRENGTHEN THE FRAMEWORK
FOR INSOLVENCY PRACTITIONERS IN
CROATIA**

AS-IS REPORT

prepared by

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and

KPMG Croatia d.o.o.

in cooperation with

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**the European Commission via the Structural Reform Support
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and

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INTRODUCTION

Insolvency practitioners (IPs) are central figures in most insolvency systems, which typically require the partial or total divestment of the debtor's management powers and the appointment of an IP to administer or liquidate the assets of the debtor.

In reorganisation proceedings where the debtor's management remains in place, the IP often supervises management's administration of the debtor's affairs. This proximity to the debtor means that IPs are frequently responsible for keeping the court, creditors and other stakeholders informed of the progress of the insolvency case.

The Ministry of Justice (the "**Ministry**" or "**MoJ**") and the European Bank for Reconstruction and Development ("**EBRD**") co-organised two workshops in Zagreb, the first in 2016 on out-of-court restructuring and the second in 2017 on the Croatian bankruptcy framework, including the role of IPs.

A key message of both workshops was the need to improve the legal framework for bankruptcy. The second workshop also concluded that the entrance requirements for the IP profession needed to be stricter to ensure that IPs have the necessary qualifications, knowledge and skills. Training and education of IPs needed to be more focused on practical issues to guide IPs in handling their day-to-day tasks.

Based on these findings, the Ministry submitted a request for support to the Structural Reform Support Service ("**SRSS**") of the European Commission to strengthen the framework for insolvency practitioners in Croatia (the "**Project**").

The EBRD was designated as implementing agency for the project. Mamić Perić Reberski Rimac Law Firm ("**MPRR**") and KPMG Croatia d.o.o. ("**KPMG**") have been appointed to work on this Project combining valuable legal and business knowledge and expertise relating to the insolvency framework and practices in Croatia.

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IMPORTANT KPMG AND MPRR NOTICE

This report has been prepared by MPRR and KPMG in order to assist the Ministry with strengthening the regulatory framework for the IP profession and providing training for IPs in Croatia. Hereby we kindly ask you to take into consideration the following limitations to this Report.

We kindly request you to take into consideration the following limitations to this report (the "**Report**").

In preparing this report, our primary sources have been information provided by the Ministry, publicly available information and interviews and meetings with key stakeholders (details of which are available within the Report). There can be no assurance that any of the involved parties has responded fully and accurately to our enquiries. There can be no assurance that additional documentation and/or information do not exist which should have been supplied to us by any of the said stakeholders. We cannot accept any liability for omissions and inaccuracies in this report caused by the fact that those documents were not supplied or that information was not made available to us. We have assumed that all documents supplied to us and information given are true and accurate and that no document provided to us has been subsequently amended or rescinded.

We have indicated within our report the sources of the information presented. We do not accept responsibility for such information which remains the responsibility of the party which has provided the information. We have checked that the information presented in our report is consistent with other information which was made available to us in the course of our work in accordance with the terms of our engagement letter. We have not, however, sought to establish the reliability of these sources by independent review or audit.

Any reference to KPMG as a source of information signifies only that KPMG has undertaken certain analytical activities on the underlying data to arrive at the information presented; we do not accept responsibility that the underlying data was true or complete.

DEFINITIONS

In this document, unless the context explicitly requires otherwise, the following terms shall have the following meanings:

Administrator	means, unless the context requires otherwise, an administrator (Croatian: <i>povjerenik</i>) in pre-bankruptcy proceedings as defined by the Bankruptcy Act.
Amendment	means the Law on Amendments to the Bankruptcy Act (Croatian: <i>Zakon o izmjenama i dopunama Stečajnog zakona</i>), published in the Official Gazette of the Republic of Croatia, no. 104/2017.
Bankruptcy Act 1996	means the Bankruptcy Act (Croatian: <i>Stečajni zakon</i>), published in the Official Gazette of the Republic of Croatia, nos. 44/1996, 161/1998, 29/1999, 129/2000, 123/2003, 197/2003, 187/2004, 82/2006, 116/2010, 25/2012, 133/2012, 45/2013 and 71/2015.
Bankruptcy Act	means the Bankruptcy Act (Croatian: <i>Stečajni zakon</i>), published in the Official Gazette of the Republic of Croatia, nos. 71/2015 and 104/2017.
Chapter	means a chapter of this Report.
Consultants	means jointly MPRR, as legal and regulatory expert, and KPMG, as business and training expert.
Croatian National Bank	means the Croatian National Bank (Croatian: <i>Hrvatska Narodna Banka</i>), with the headquarters in Zagreb, Trg hrvatskih velikana 3.
Decision on Criteria and Method of Calculation and Payment of Fees to Insolvency Practitioners	means the Decision on Criteria and Method of Calculation and Payment of Fees to Insolvency Practitioners (Croatian: <i>Uredba o kriterijima i načinu obračuna i plaćanja nagrade stečajnim upraviteljima</i>) published in the Official Gazette of the Republic of Croatia No. 105/15

EBRD	means the European Bank for Reconstruction and Development, an international financial institution established under the Agreement Establishing the European Bank for Reconstruction and Development, a multilateral treaty signed in Paris on 29 May 1990, with its headquarters at One Exchange Square, London EC2A 2JN, United Kingdom.
Financial Agency	means the Financial Agency (Croatian: <i>Financijska agencija</i>), with registered seat in Zagreb, Ulica grada Vukovara 70.
Insolvency	means, depending on the context, pre-bankruptcy proceedings, bankruptcy proceedings or both together.
IP	means, unless the context requires otherwise, insolvency practitioner and, in context of Croatian law, refers to bankruptcy trustees (Croatian: <i>stečajni upravitelj</i>).
KPMG	means KPMG Croatia d.o.o., with a registered seat in Zagreb, Ivana Lučića 2a.
List A	means the list A of the IPs, as regulated by the Bankruptcy Act and other applicable by-laws and explained in more detail in Section 3.7.
List B	means the list B of the IPs, as regulated by the Bankruptcy Act and other applicable by-laws and explained in more detail in Section 3.7.
Lists	means jointly, the List A and the List B.
Ministry	means the Ministry of Justice of the Republic of Croatia.
MPRR	means Mamić Perić Reberski Rimac Odvjetničko društvo d.o.o., with a registered seat in Zagreb, Ivana Lučića 2a.
Programme of the	means the Programme of the Ministry of Justice for

Ministry of Justice for the Continuing Professional Development of IPs	the Continuing Professional Development of IPs, class: 011-01/15-01/123, reference number: 514-03-02-02-16-14 of 27 February 2017
Project	means the project to assist the Ministry with strengthening the existing framework and providing training for IPs in Croatia.
Report	means this Report.
Rulebook on Conditions and Methods for Appointment of IPs by a Random Selection Method	means the Rulebook on Conditions and Methods for Appointment of IPs by a Random Selection Method (Croatian: <i>Pravilnik o pretpostavkama i načinu izbora stečajnoga upravitelja metodom slučajnoga odabira</i>) published in the Official Gazette of the Republic of Croatia No. 106/15
Rulebook on Determining the IP Lists	means the Rulebook on Determining the IP Lists (Croatian: <i>Pravilnik o utvrđivanju lista stečajnih upravitelja</i>) published in the Official Gazette of the Republic of Croatia No. 104/15
Rulebook on Professional Exam, Training and Education of IPs	means the Rulebook on Professional Exam, Training and Education of Insolvency Practitioners (Croatian: <i>Pravilnik o polaganju stručnog ispita, obuci i usavršavanju stečajnih upravitelja</i>) published in the Official Gazette of the Republic of Croatia No. 104/15, 17/2017
Section	means a section of this Report, unless expressly stated otherwise.
SRSS	means the Structural Reform Support Service of the European Commission.
Uniform Programme for Training of Bankruptcy Trustees	means the Uniform Programme for Training of Bankruptcy Trustees (Croatian: <i>Jedinstveni program stručne obuke stečajnih upravitelja</i>) of 7 December 2015, class: 011-01/15-01/123.

1. EXECUTIVE SUMMARY

Key Consultant findings and recommendations for consideration by the Ministry in any review of the regulatory framework for insolvency practitioners are summarised below. Please note that any recommendations are made for the purpose of assisting the Ministry in its policy-making role and are as such provisional and non-binding.

Finding	Recommendation(s)	Reference (Section)	Legislative changes needed:	
			Laws	By-laws
<i>Licensing and registration</i>				
1. Licensing requirements in Croatia should be raised.	A. The IP profession should be limited to persons holding a degree in law, economics or in a similar field.	3.5.2	Yes	Yes
	B. Minimum work experience in bankruptcy and insolvency related fields (e.g. legal, notary, accounting, tax, business advising, etc.) should be introduced for prospective IPs.	3.5.2	Yes	Yes
	C. General training should be required for IP candidates before taking the exam and being admitted to List B (e.g. attending introductory workshops / training where IP candidates would be presented with key legal requirements, typical tasks, their roles and responsibilities).	3.5.4	Yes	Yes
	D. Professional training (i.e. the practice period) of List B IPs should be extended to last longer and ensure that IP candidates get real hands-on experience.	3.5.3	Yes	Yes
	E. IP candidates should be required to demonstrate that they have sufficient organisational capacity and resources to take appointments in insolvency cases.	3.5.2	Yes	Yes
	F. A maximum age limit for IPs should be introduced e.g. 65 or 70 years.	3.5.2	Yes	Yes

Finding	Recommendation(s)	Reference (Section)	Legislative changes needed:	
			Laws	By-laws
2. The entrance examination system should be improved.	A. Exams should be standardised and the questions could be more frequently changed or refreshed. There should be fewer exam sessions per year (e.g. only once or twice a year maximum).	3.5.3	No	Yes
	B. EU insolvency legislation is not part of the examination curriculum and should be added to the curriculum for the IP exam.	3.8	No	Yes
	C. Examples of exams should be published for candidate to prepare in order to enhance the transparency of the examination process	3.5.3	No	No
	D. Literature should be introduced to help IP candidates to prepare for the IP exam.	3.8	No	No
3. The existing licensing/ registration system does not identify "highly qualified" IPs for more complex and high value cases.	A. The Ministry should consider creating, in addition to the List A and the List B, another list of IPs which will need to meet stricter licensing requirements and will have priority in high value and complex case appointments.	3.2.2(iii) 3.5.2	Yes	Yes
	B. The randomised appointment system should be modified to select IPs based on previous work experience, sector experience and qualifications (see below).			
Qualification and training				
4. The mentorship work experience programme for List B IPs is currently not standardised and is largely dependent on the mentor's approach and judgement.	A. The MoJ should consider standardising the mentorship programme (for example, clearly listing roles and responsibilities of mentor and mentee and tasks that need to be performed by List B IPs during the mentorship programme).	3.5.4	No	Yes
	B. IPs admitted to List B should have more "hands-on" work experience while being supervised by a mentor.	3.7	No	Yes
5. The annual CPD programme	A. Materials for workshops should be made available to participants in	3.6	No	No

Finding	Recommendation(s)	Reference (Section)	Legislative changes needed:	
			Laws	By-laws
is determined by the Ministry, while the trainers prepare the workshops and materials for each workshop.	advance.			
	B. The CPD trainings should be digitalised as much as possible (for example: computer-based trainings or workbooks).	3.6	No	Yes
	C. There should be a better balance between the theoretical part of training and business case analysis and practice. Workshops should focus more on new information and knowledge of various skills which were not covered by IPs' formal education and which are required by law.	3.6	No	No
	D. Associations of IPs should participate more actively in the organisation of CPD. Some CPD workshops should also be organised by IP associations (subject to certification by the Ministry) and thus provide more diversity in the organisation of the workshops.	3.6.7	No	Yes
6. On average, there are 15 participants per CPD workshop.	A. Ideally, CPD workshops should be organised for smaller groups (e.g. 8 to 10 attendees) to ensure that they are more interactive and that IPs participate more actively at the workshops.	3.6.6	No	No
7. There is no systematic training for trainers of IPs.	A. The MoJ should consider introducing systematic training for the trainers of IPs and organise projects aimed at sharing of experience between trainers and IPs in Croatia with their counterparts in other EU countries.	3.6.4 3.6.8	No	Yes
Appointment system				
8. IPs are selected for initial appointments on the basis of a random selection algorithm without reference to detailed experience and qualifications.	A. Additional criteria (KPIs) based on which algorithm selects an IP should be introduced e.g. based on previous sector experience and qualifications.	3.4	No	Yes

Finding	Recommendation(s)	Reference (Section)	Legislative changes needed:	
			Laws	By-laws
9. Information on IPs available to judges when making appointments is limited and usually out-of-date.	A. The lists of IPs should contain additional information on IPs, which should be updated regularly and in a form which would allow the computer-based system to use such indicators (KPIs) in selecting IPs for appointments. IPs should notify the MoJ of any relevant changes to this information.	3.4 3.7	No	Yes
10. IPs can only request to be temporarily excluded from further appointments for a fixed duration of two years after the end of the calendar year in which the request was filed.	A. The duration of the temporary exclusion should be made more flexible and capable of being more limited e.g. 3 or 6 months.	3.4.2	Yes	Yes
Regulation and supervision				
11. There is no specific dedicated regulatory body (department or separate body) performing active monitoring and supervision of IPs.	A. Government authorities should consider establishing a dedicated regulatory body for the IP profession, such as a state agency under the MoJ, which will have sufficient staff and resources to monitor and regulate the profession outside of specific cases and court proceedings or, alternatively as in the case of Slovenia, setting up a department of persons with relevant legal, commercial and administrative backgrounds, which is responsible for licensing, supervision, and monitoring of IPs.	3.9.7	Yes	Yes

Finding	Recommendation(s)	Reference (Section)	Legislative changes needed:	
			Laws	By-laws
12. Monitoring tools/ mechanisms need to be established.	A. A monitoring mechanism should be adopted to ensure that a dedicated regulatory body (if introduced) or the relevant department of the MoJ is able to collect relevant information on the conduct and performance of IPs. Monitoring tools may include checklists, templates and questionnaires.	3.9.1	Yes	Yes
	B. Regular monitoring meetings between the IP and regulatory body should be scheduled e.g. every 3-6 years and otherwise where necessary e.g. to investigate a complaint. Monitoring should be conducted with reference to a code of conduct and statements of insolvency practice.	3.9.1	Yes	Yes
	C. The relevant department of the MoJ or a dedicated regulatory body (if introduced) should have a comprehensive and accessible complaints procedure to assess and address any complaints made against IPs.	3.9.4	Yes	Yes
13. Regulatory sanctions need to be reviewed to ensure that IPs perform their duties properly and that appropriate sanctions are imposed according to the level of IP misconduct.	A. A wider range of sanctions should be available for the MoJ or a dedicated regulatory body (if introduced) including reprimands, warnings and fines, in addition to the existing power to remove the licence of IPs.	3.9.4	Yes	Yes
	B. A disciplinary committee should be established by the MoJ or a dedicated regulatory body (if introduced) to consider any allegations of IP misconduct. This should be supported by a disciplinary procedure.	3.9.4	Yes	Yes
	C. The MoJ should consider preventing a person from applying to be listed as an IP for at least two years, if such IP was delisted due to breach of duty.	3.9.1	Yes	Yes

Finding	Recommendation(s)	Reference (Section)	Legislative changes needed:	
			Laws	By-laws
Work Standard and ethics				
14. There is no code of conduct for IPs in Croatia.	A. A code of conduct should be established to set minimum work standards and ethics. This could assist the MoJ or a dedicated regulatory body (if established) with monitoring IPs.	3.9.5	No	Yes
15. There is no practice of publishing statements of insolvency practice.	A. The MoJ should, in partnership with IP associations, considered publishing statements of insolvency practice to guide IPs on critical issues (e.g. the conduct of sales in insolvency, the management of reorganisation in bankruptcy, the handling of funds in insolvency etc.) This could assist the MoJ or a dedicated regulatory body (if established) with monitoring IPs.	3.8	No	No
16. There is no formal literature aimed at education of IPs which could serve as the official literature for examinations during licensing process or later on for the trainings of IPs.	A. Manuals and guidelines for fundamental topics should be available to IPs online and accessible at all times.	3.8	No	No
Remuneration				
17. IPs are not incentivised to push for bankruptcy plans.	A. It should be considered whether to introduce further remuneration mechanisms (e.g. envisage an option for creditors to agree to pay an additional bonus for successfully concluded bankruptcy plans) to motivate IPs to support bankruptcy reorganisation where that would be appropriate.	3.10 3.13	No	Yes

2. METHODOLOGY

The aim of this phase of the assignment "Analysing the existing regulatory framework for IPs" (**Phase I**) was to focus on the analysis and the assessment of the existing regulatory framework and providing key findings and recommendations for improvement.

Our key activities and analysis included:

- a comparative analysis of the profile of IPs under the current regulatory framework and the profile of IPs that are being appointed in order to identify inefficiencies of the current system;
- an assessment of the competences and responsibilities within the examination, and IP licensing process; and
- an assessment of the areas and processes related to the IP profession that need to be standardised, strengthened and/or improved.

Based on the defined scope of the Project, we have performed a number of activities as divided into the following groups, relevant for completion of Phase I:

- desktop analysis;
- interviews with relevant stakeholders;
- consulting with key stakeholders (Ministry of Justice, IPs, judges, EBRD, SRSS, etc.);
- reporting.

2.1 Desktop analysis

As preparation for the meetings, the interviews and the consultation with key stakeholders, we have analysed a number of relevant documents and reports, including among other matters, the following:

- Materials prepared and delivered by the Ministry (relating to current practices):
 - a. laws, programmes and rulebooks relevant for the project including Bankruptcy Act, Rulebook on Conditions and Methods for Appointment of IPs by a Random Selection Method, Rulebook on Determining the IP Lists, Rulebook on Professional Exam, Training and Education of IPs, Decision on Criteria and Method of Calculation and Payment of Fees to Insolvency Practitioners, Programme of the Ministry of Justice for the Continuing

Professional Development of IPs, Uniform Programme for Training of Bankruptcy Trustees, etc.;

- b. samples of decisions by the MoJ regarding the licensing and supervision procedures (e.g. Decision of listing specific IP on List A);
- c. description of internal procedures of the MoJ regarding the licensing procedure, training preparation, selection and appointment of trainers etc.;
- d. example of an evaluation survey (which is provided after every training to evaluate organisation and usefulness as well as quality of trainers);
- e. education/training curriculum for 2018;
- f. the list of trainers in 2016 and 2017 including their assessment by training participants;
- g. list of training attendance for each IP;
- h. other relevant information and statistics (e.g. total number of candidates for IP exam).

As an initial step for this activity, we have prepared a list of required documents and information.

- We have also participated in a workshop/training for the IPs. For specific confidential documents that could not be disclosed we have received insight from the MoJ (e.g. training materials and exams).
- Publicly available materials (Project scope related), including international best practice guidelines defined by KPMG and the international institutions (i.e. where available and applicable), etc. In this respect, our analysis included the following:
 - a. an overview of key findings in EBRD report: "Assessment of Insolvency Office Holders: Review of the profession in the EBRD region", 2014 and the country analysis for Croatia updated in 2016;
 - b. a list of currently active and closed bankruptcy proceedings for the last few years (including pre-bankruptcy and bankruptcy cases). The list included bankruptcy proceeding, selected IP, role of the IP, related commercial court and judge, description of selection procedure including explanation if automatic procedure was not used, commencing and finalisation date. This was used for workload analysis of commercial courts and judges;
 - c. a list of IPs by commercial courts;
 - d. an overview of the IPs' licensing process (based on regulatory framework), including best practice example in UK (ACCA) as well an example of a similar body in Croatia (Croatian Audit Chamber);
 - e. an overview of the trainers' selection process (based on the regulatory framework);

- f. an examination process overview, including best practice examples in UK (ACCA) as well example of similar body in Croatia (Croatian Audit Chamber);
 - g. an overview of other relevant documents (e.g. "EJTN Handbook on Judicial Training Methodology in Europe" and "Study on a new approach to business failure and insolvency: Comparative legal analysis of the Member States' relevant provisions and practices"); and
 - h. key EU insolvency provisions including the European Union Insolvency Regulation and the European Commission's proposal for a Directive on preventive restructuring, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures, which contains provisions relating to practitioners in the field of restructuring, insolvency and second chance.
- Other information, We have also used:
 - a. internally available previous analysis, findings and report(s) relating to insolvency procedures.
 - b. KPMG's internal knowledge base and relevant guidelines (i.e. International Guide to Restructuring, benchmarking tools, etc.); and
 - c. previous analysis from relevant engagements, benchmark information and real case experience, including the Project Report prepared for the Ministry within the scope of the Project "Strengthening the Framework for Bankruptcy and Pre-Bankruptcy Proceedings in Croatia" dated April 2018.
 - Current legal and external regulatory frameworks and practices.

2.2 Interviews with relevant stakeholders

We have interviewed representatives of the following key stakeholders:

- six IPs;
- five bankruptcy judges (including those acting as trainers for IPs);
- five in-house lawyers (representatives of creditors);
- two representatives of the Ministry.

As preparation for the interviews, we have drafted an agenda focusing on the following topics:

- processes,
- roles and responsibilities,
- key issues,
- stakeholder's view on what could be improved.

Initial interviews were organised in two hours sessions (average duration).

Subsequently, we have arranged follow-up calls and meetings when necessary.

Key findings have been reflected in the report and where possible supported by data and analysis.

2.3 Consultation with key stakeholders (MoJ, IPs, judges, EBRD, SRSS, etc.)

Following initial interviews and findings from our analysis, we have organised consultative meetings with key stakeholders.

The aim of these meetings was to:

- clarify findings and open questions;
- provide or obtain additional information and explanation;
- confirm that we have correctly interpreted the received information.

We have included updated information and data in this report.

3 FINDINGS

3.1 Insolvency trends

In this Section 3.1, we have considered recent insolvency trends in Croatia and, where information was available, we have compared this against trends in other EU countries and neighbouring countries.

3.1.1 Legislative trends

Croatian insolvency legislation has been amended numerous times in recent years. The latest significant reform of the insolvency legislation was in 2015 when a new Bankruptcy Act was enacted. Since then, the new Bankruptcy Act was amended in 2017 to fix certain issues detected in practice.

With the new Bankruptcy Act and the supporting by-laws, significant reforms were also made in 2015 to the IP framework. Some of the more notable reforms to the IP framework included introduction of two separate lists of IPs (i.e. the List A and the List B), mandatory professional training for IPs listed on the List B and mandatory continuing professional development for all licensed IPs.

While all this has been seen by the stakeholders as significant improvement of the IP framework in respect to the regime prior to 2015, many believe that there is still room for improvement.

In parallel, the EU has focused efforts on reducing the most significant barriers to the free flow of capital stemming from differences in Member States' restructuring and insolvency frameworks. To that extent, the EU is working on a proposal for new directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures¹. Following enactment of the new directive, which is expected later this year, further reforms to the IP framework in Croatia may be required. Although parts of the proposed Directive are drafted quite broadly, it requires Member States to have "*appropriate oversight and regulatory structures to ensure that the work of practitioners in the field of restructuring, insolvency and second chance is appropriately supervised*" and an effective regime for sanctioning IP misconduct. With reference to IP remuneration, the proposed Directive states that "Member States shall ensure that the fees charged by

¹ European Commission, "Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU" COM(2016) 723 final.

practitioners in the field of restructuring, insolvency and second chance are governed by rules which incentivise a timely and efficient resolution of procedures with due regard to the complexity of the case". The proposed Directive also stresses the importance of Member States encouraging necessary initial and further training and a voluntary code of conduct for the profession. In this Report, expected harmonisation requirements of the new EU directive in terms of the IP framework have been taken into account.

3.1.2 Review of IPs in context of Croatia and neighbouring countries

In our research we have used publicly available data (e.g. relevant laws, programmes and rulebooks) along with documents received from MoJ. A list of IPs and their insolvency cases (available on the web site of MoJ²) was used as the basis of our analysis. However, we note the following limitations to our analysis:

- there seems to be certain inconsistencies in data (due to manual entry by stakeholders), e.g. explanations provided by judges of why they used manual selection of an IP instead of automated (descriptions vary from general to specific and limits more detailed analysis);
- there are some cases of duplicated entries (however, not many and probably largely due to manual entries, as depicted in Figure 16);
- the database includes all active insolvency cases, i.e. there is no clear distinction between cases initiated before and after new Bankruptcy Law (2015.) when the system of automated selection of IPs was introduced;
- the database contains all cases and related judges (i.e. summary cases), hence limiting clear understanding of the list of bankruptcy judges;
- the list of active IPs provides a very narrow set of information (bankruptcy case, selected IP, role of the IP, related commercial court and judge, description of selection procedure including explanation if automatic procedure was not used, commencing and finalisation date) limiting comparative analysis of IPs (especially age and education background where we had to rely on last official list published in 2015 and additional information provided by the MoJ).

Following our request, the MoJ provided additional information relating to licensing and supervision procedures, samples of specific MoJ decisions, description of internal procedures, list of trainers, education curriculum etc. Due to the lack of systematic and regular monitoring on a national level, specific reports and datasets from the EBRD

² List of IPs, website MoJ, <https://e-oglasna.pravosudje.hr/?q=popisi-obraci/8998>, retrieved on 16 April 2018.

have been used for illustrating the general insolvency trends and providing a benchmark overview with comparable countries.

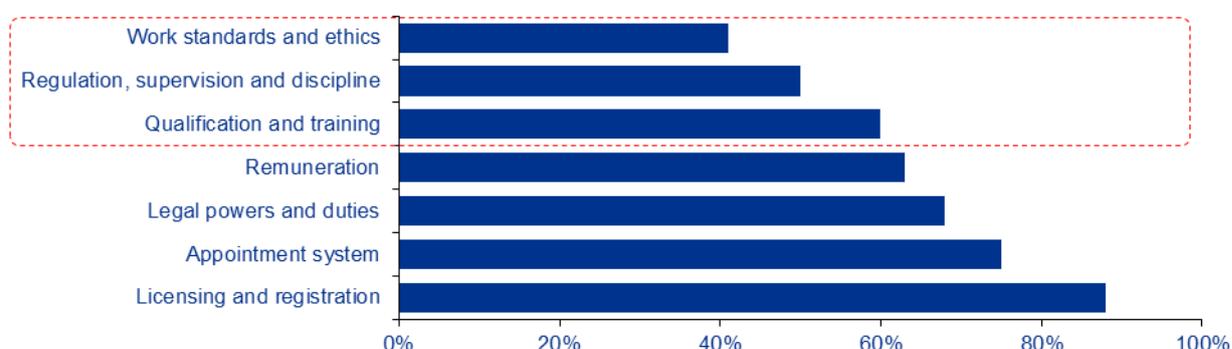
According to EBRD's 2016 country assessment of the IP profession in Croatia (Figure 1), three areas of weakness have been identified:

- work standards and ethics;
- regulation, supervision and discipline; and
- qualification and training.

These deficiencies have been further confirmed during interviews with key stakeholders and have been addressed in this Report.

Figure 1

Croatia - results achieved for each of the assessment benchmarks

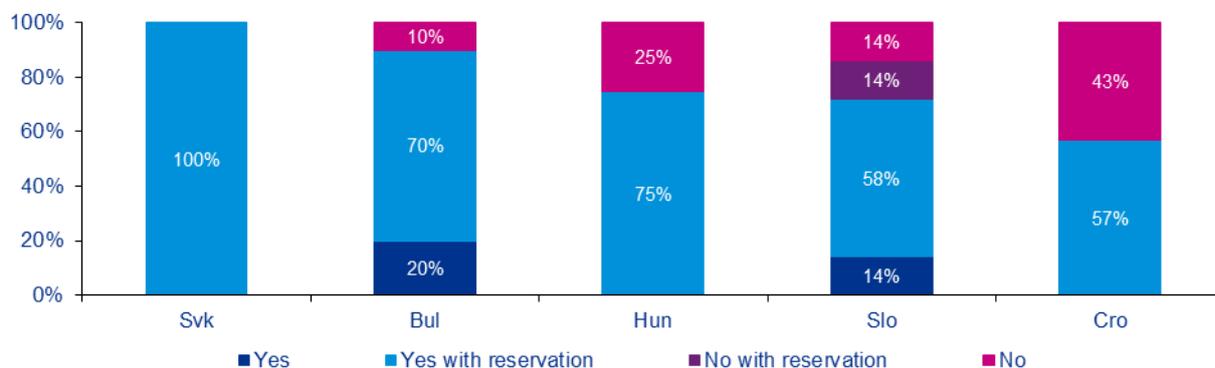


Source: *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>

Based on cross-country analysis of data on the IP profession, the profession is perceived as underperforming in practice, when compared to CEE peers (Figure 2). Furthermore, Croatian regulatory and professional insolvency framework is not perceived as comprehensive (Figure 3) by EBRD analysis.

Figure 2

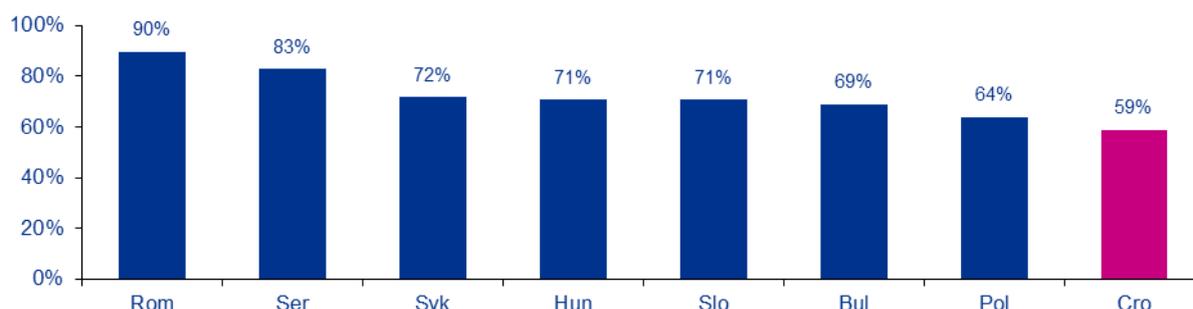
Survey results: Do you think that IPs as a whole perform their professional tasks and duties well?



Source: *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>

Figure 3

Development of the IP profession



Source: *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>

Based on the results of the EBRD analysis, the IP profession is perceived as less efficient compared to similar countries. Issues in current licensing and training process contribute significantly to this situation. Also, regulation and supervision (please see Section 3.9) should be strengthened within current regulatory framework. This may include several options: amplifying the current role of MoJ or introducing an additional monitoring / oversight body, either within the MoJ or as a separable authority / agency / body (as in some comparable countries).

Our assistance during the Project will focus on supporting the process of capacity building of IPs via strengthening the regulatory framework, and suggested improvements especially in respect to the processes of examination, licensing, training and supervision.

3.2 Insolvency practitioners

IPs are usually central figures in insolvency operating models. In Croatian insolvency proceedings, a partial (pre-bankruptcy) or total (bankruptcy) divestment of debtor's management powers is required. In this respect, the appointment of an IP is necessary to administer or liquidate debtor's assets or to oversee the restructuring process.

In order to ensure competencies needed to perform tasks associated with administering a financially distressed or insolvent business, it is crucial to ensure that IPs have the appropriate skills and sufficient legal, financial and commercial expertise.

3.2.1 Legal framework

IPs are persons licensed by the Ministry and listed on the lists of IPs. From such lists, the courts appoint IPs in various insolvency proceedings.

IPs assume slightly different roles and responsibilities depending on different stage and type of insolvency proceedings they are appointed in: (i) as administrator in pre-bankruptcy proceedings; (ii) preliminary bankruptcy trustee in preliminary bankruptcy proceedings; and (iii) bankruptcy trustee in bankruptcy proceedings.

The role and responsibilities of the IPs, as well as the requirements and procedure to qualify to be licensed as an IP are regulated by the relevant regulations, in particular by: (i) the Bankruptcy Act; (ii) the Rulebook on Professional Exam, Training and Education of IPs; (iii) the Uniform Programme for Training of Bankruptcy Trustees; and (iv) the Programme of the Ministry of Justice for Continuing Professional Development of Bankruptcy Trustees.

However, the specific role of IP's is somewhat hindered by particularities of the IP profession as it is significantly different from the profession of other participants in insolvency proceedings (e.g. judges or attorneys at law). Namely, there is no unified background or a specific education system required particularly for the vocation of IP's. Therefore, IPs can come from a wide variety of professions, i.e. any person with a university degree in any field. In most cases, their formal education has not prepared them for the challenges that they will encounter in bankruptcy proceedings. Generally, specific requirements for IP profession mainly relate to language and nationality requirements. Based on EBRD analysis majority of comparable countries in the region do not impose specific professional exclusivity requirements (meaning that IP are allowed to carry out other professional activities). Our understanding is that within the

neighbouring countries, only Serbia imposes (by law) IP profession exclusivity (i.e. IPs are not allowed to work in other professions). In some other countries, e.g. Bulgaria and Romania, IP profession is often closely linked to legal profession.

This means that any decent person with the full legal capacity and a university degree in any field may qualify as IP, if he/she meets the requirements prescribed by law. Consequently, this creates the need for appropriate additional training and experience of IPs during and after the licensing as an IP (see Sections 3.5 and 3.6 below), to ensure that IPs have basic skills and knowledge required to perform their duties in insolvency proceedings.

3.2.2 Licensed IPs - analysis

We have analysed the key characteristics of licensed IPs, based on publicly available data³ (IPs listed in the Ministry's register as published on Ministry's website).

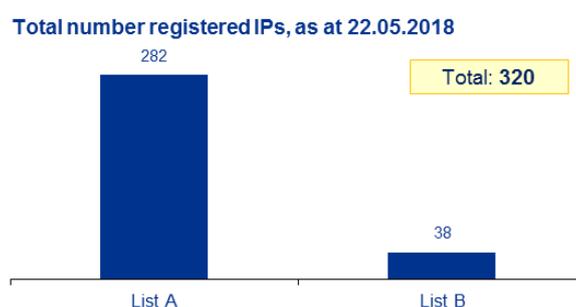
Our analysis focused on the following two areas:

- IPs profile analysis (total number, break-down by lists, age structure, university degree structure), and
- workload analysis – overview of cases per court, cases per IP, cases per judge.

(i) IPs profile analysis

As of 22 May 2018, total of 320 IPs were registered with the Ministry, out of which 282 IPs (88%) are registered on List A and 38 (12%) on List B (Figure 4)⁴.

Figure 4



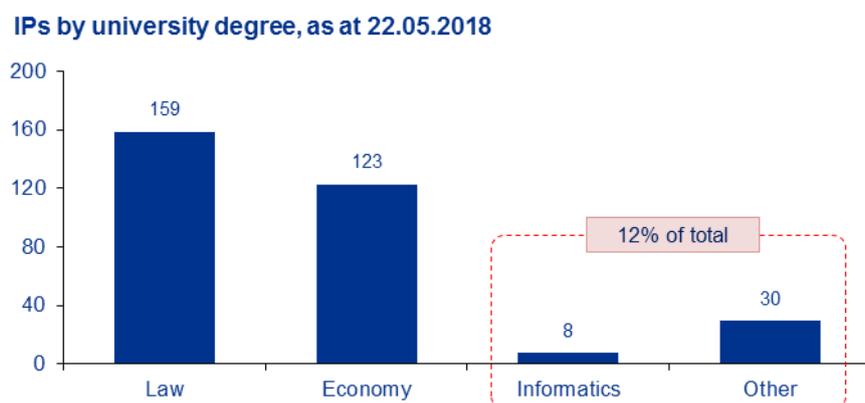
Source: Web site of the Ministry of Justice, List of IPs per commercial courts, May 2018, available at: <https://e-oglasna.pravosudje.hr/?q=node/19>

³ Ministry is publishing and maintaining the lists of IPs and bankruptcy procedures. Tables are available (Croatian version only) on the website: <https://e-oglasna.pravosudje.hr/?q=popisi-obrasci/8998>

⁴ For more information on differences between the List A and the List B see Section 3.7 below.

Comparable data regarding knowledge and competence background of the IPs is limited. We have analysed the information on university degrees of the currently registered IPs on the List A and the List B. According to this data (Figure 5), 50% of IPs graduated from a law school, 38% from economics or business school and the remaining 12% have degrees in various other fields, for example traffic engineers, agronomy, civil engineering, sociology etc.

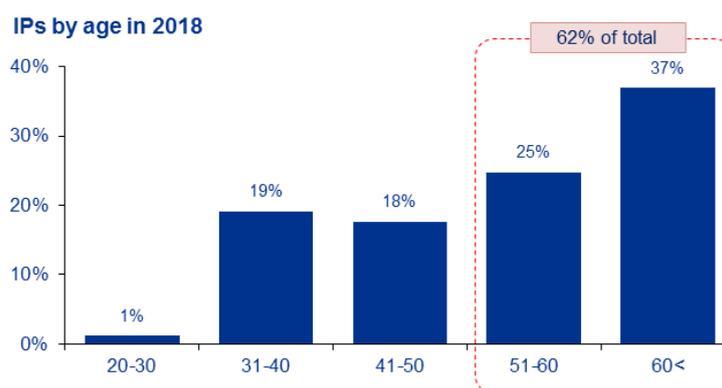
Figure 5



Source: Web site of the Ministry of Justice, List of IPs per commercial courts, May 2018, available at: <https://e-oglasna.pravosudje.hr/?q=node/19>

Based on IPs age structure analysis, around 62% of all IPs are aged 50 and above (Figure 6). More than 20% of IPs are older than 65. Such age structure may be challenging in the future for knowledge transfer and succession process. Also, IT and every-day computer use is perceived low by older IPs.

Figure 6



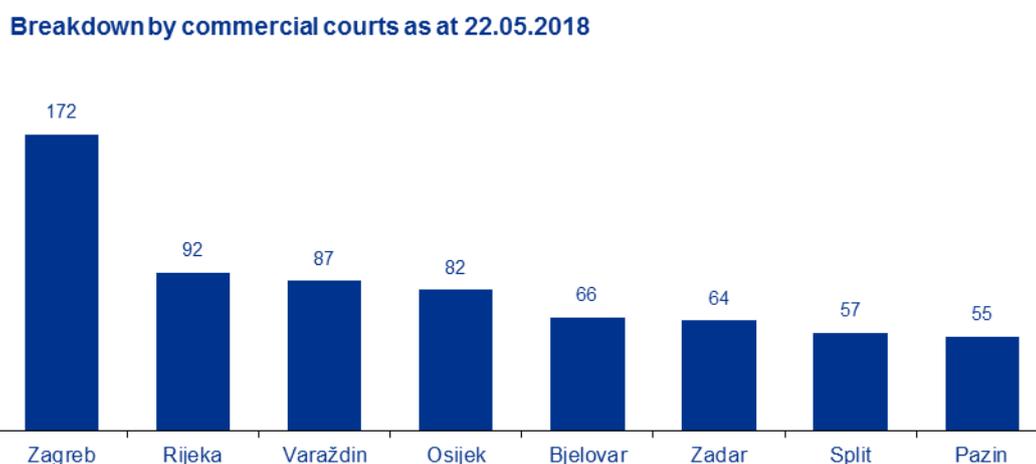
Source: Documentation received from MoJ

Analysis of IPs geographical distributions indicates that 172 IPs (25%) are registered with the Commercial Court in Zagreb (Figure 7), which is almost double compared to

the Commercial Court in Rijeka, which is the second highest ranked. This can be explained by relatively high workload of the Commercial Court in Zagreb⁵.

Excluding the Commercial Court in Zagreb, there are 72 IPs registered per commercial court (on average), with relatively equal dispersion per courts.

Figure 7

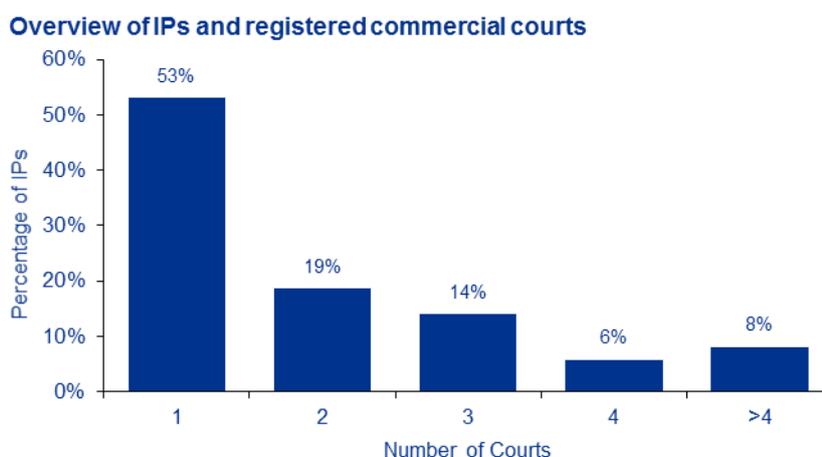


Source: Web site of the Ministry of Justice, List of IPs per commercial courts, May 2018, available at: <https://e-oglasna.pravosudje.hr/?q=node/19>

Although most IPs are registered with only one commercial court (i.e. approximately 53%), approximately 20% of IPs are registered at 3 or 4 courts, while approximately 8% are registered at 4 or more courts (Figure 8). Such practice may result in an increased operative risks, i.e. preventing IPs to efficiently perform their roles (given unfavourable geographical distribution of the courts, i.e. large geographical distance between the courts and companies in bankruptcy). This is particularly relevant as IPs, in principle, may not reject their appointment in insolvency proceedings.

⁵ For more information on the workload (number of cases) per commercial court, please see sub-section (ii) below.

Figure 8



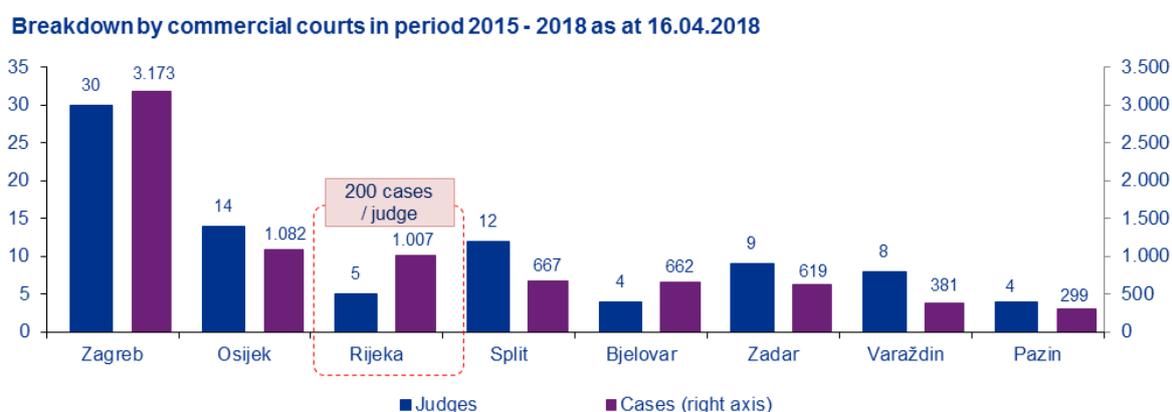
Source: Web site of the Ministry of Justice, List of IPs per commercial courts, May 2018, available at: <https://e-oglasna.pravosudje.hr/?q=node/19>

(ii) Workload analysis – existing data

In this Section is a brief analysis of the workload of IPs and commercial courts based on the data on pre-bankruptcy proceedings and regular bankruptcy proceedings. For the purpose of this Section 3.2.2(ii), summary bankruptcy proceedings⁶ were not taken into account as the expected workload required to conduct summary bankruptcy proceedings is not comparable to regular bankruptcy proceedings.

Based on existing data analysis, Commercial Court in Zagreb has the highest number of cases and judges, followed by Osijek and Rijeka (Figure 9).

Figure 9



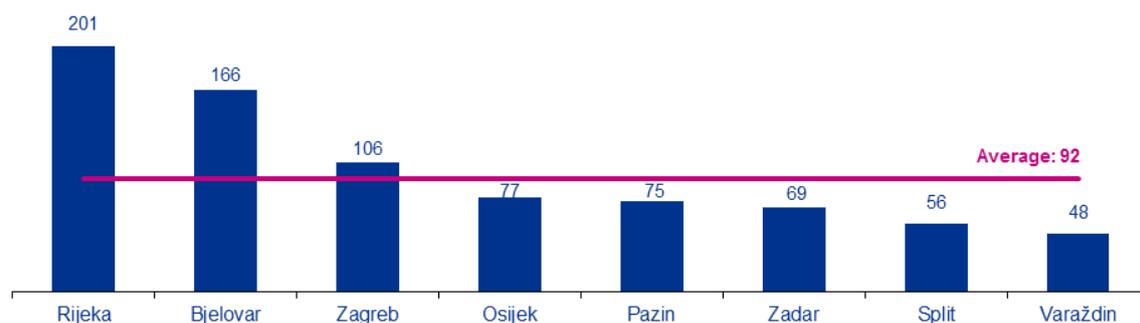
Source: Web site of the Ministry of Justice, List of IPs and bankruptcy procedures, April 2018, available at: <https://e-oglasna.pravosudje.hr/?q=popisi-obraci/8998>

⁶ For more information on summary bankruptcy proceedings, please see Section 3.3.2(xv) below.

In relative terms, Commercial Court in Rijeka has 201 cases per judge, Commercial Court in Bjelovar has 166 cases and Commercial Court in Zagreb has 106 cases per judge (Figure 10). On average, there are 92 cases per judge at the commercial courts in Croatia.

Figure 10

Number of cases per judge in period 2015 - 2018 as at 16.04.2018



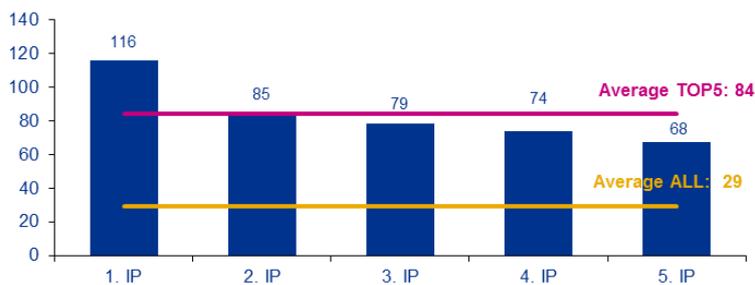
Source: Web site of the Ministry of Justice, List of IPs and bankruptcy procedures, April 2018, available at: <https://e-oglasna.pravosudje.hr/?q=popisi-obraci/8998>

Based on an algorithm which randomly assigns cases to IPs, the key factor defining case assignment to an individual IP is existing workload of the IP. However, there is a possibility to override algorithm selection, where judges manually and directly select an individual IP to be appointed in insolvency proceedings. For example, where specific experience is required, judge may not include IPs without necessary knowledge in the automatic selection procedure or manually select IP with adequate skills. Decision on case complexity and IPs experience is entirely on the judge.

Based on publicly available data, five IPs with the highest number of cases were selected to manage, in average, 84 cases (Figure 11)⁷. This is significantly above the average number of cases per IP in total (i.e. 29 cases per IP).

⁷ Number of cases is influenced by 2015 change of Bankruptcy Law when the random selection procedure was implemented.

Figure 11
Top 5 IPs by number of cases, during 2015 - 2018 as at 16.04.2018

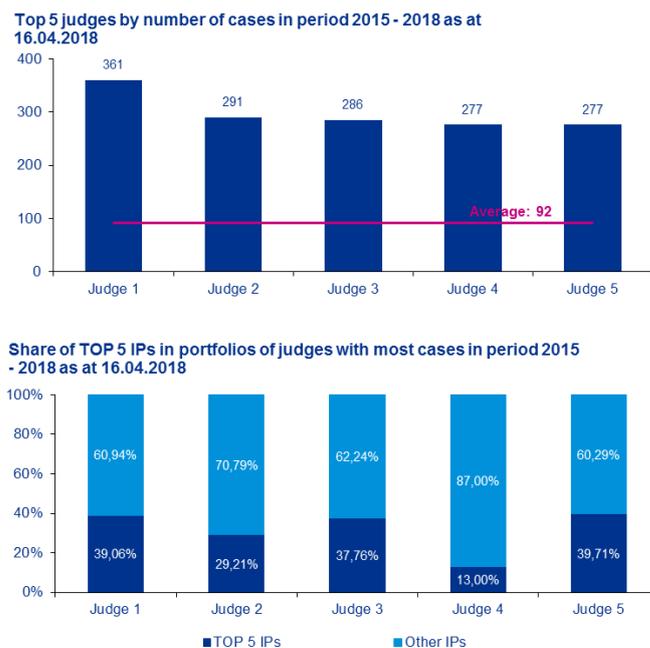


Source: Web site of the Ministry of Justice, List of IPs and bankruptcy procedures, April 2018, available at: <https://e-oglasna.pravosudje.hr/?q=popisi-obraci/8998>

Our analysis also included five judges with the highest number of cases and top five IPs selected on these (the same) cases (Figure 12).

We have analysed links (if any) between top five judges and top five IPs (please see Figure 11 and Figure 12). Generally, there is a limited correlation identified between top five judges and top five IPs on their cases. Overall, judges referred to as 1, 3 and 5 assigned 40% of their cases to the top five IPs on average, with some 65% of these cases being assigned automatically. Judge 2 assigned approximately 30% of cases to top 5 IPs. More detailed analysis indicated that within this statistics one single IP was manually assigned on 72% of cases. Judge 4 assigned only 13% of cases to top 5 IPs, with 95% of these IPs being selected automatically, indicating low direct correlation.

Figure 12



Source: Web site of the Ministry of Justice, List of IPs and bankruptcy procedures, April 2018, available at: <https://e-oglasna.pravosudje.hr/?q=popisi-obraci/8998>

(iii) Workload of part-time IPs

Since it is not required that IPs are engaged as full time IPs to be licensed, the information on employment related issues of IPs is not kept by the Ministry. Any issues concerning potential conflict of interests are managed on a case by case basis. It is primarily up to the IP to detect if there is a potential conflict of interest. However, if a court finds that the appointed IP is conflicted, it may rescind his/her appointment in the proceedings.

However, it is our understanding that the significant number of IPs (if not the majority) are acting as IPs on a part-time basis and are also engaged in other activities or are employed (some even on a full-time basis). For example, there is a significant number of attorneys at law, who in addition to having their own law firm (or being employed with a law firm) are also licensed and active as IPs.

This is generally not an issue where an IP is self-employed (as is the case with most attorneys at law who are IPs), as he/she may organise himself/herself and may allocate enough time to the duties as an IP. However, there are concerns when an IP is employed with an employer, whether he/she may adequately organise his/her time to perform the duty of the IP.

This is particularly relevant considering the randomised system of appointment and the fact that IPs are, in principle, not entitled to refuse appointments in insolvency proceedings.

Given the appointment and remuneration systems for IPs in insolvency proceedings in Croatia, it may not be expected that the IP can rely solely IP appointments to earn a living and it is therefore unlikely that the profession can be performed in Croatia by many on a full time basis.

Steps could, however, be taken to ensure that IPs are able to effectively manage their time and to ensure that IPs can allocate sufficient time to their duties as IPs. For example, IPs could be required to provide the Ministry with a statement of their employer (if any) that it agrees that its employee may act as an IP and that the regular job of the IP will not interfere with him/her acting as the IP.

Also, measures should be taken to increase professionalization of the IP profession. This would also include creating preconditions for IPs to act as IPs on a full-time basis. One of such measures could be the introduction a list of "highly qualified" IPs who can

qualify for such a list if they have certain additional qualifications such as additional years of experience as an IP (e.g. 7 years); (ii) have completed at least two regular bankruptcy proceedings against companies that qualify as large entrepreneurs (Croatian: *veliki poduzetnik*) in terms of the relevant rules on bookkeeping and accountancy; (iii) have completed at least three bankruptcy proceedings with a bankruptcy plan; and (iv) have supporting staff/advisors/consultants to assist them.

Our analysis indicated the following:

- average IP workload is 12 – 15 cases per IP;
- relatively large average age of IPs (with 62% of IPs 50+ age);
- knowledge profiles (competences) vary significantly among IPs, with currently limited standardisation of required know-how / experience or education;
- significant number of IPs are acting as IPs on a part-time basis;
- During last 3 years, manual selection was still significant in practice, overriding the random selection generated by the algorithm⁸, while interviewed stakeholders have noted that the judges are recently not inclined to exercise such authority.

(iv) Required number of trustees

Considering the current workload of the IPs and the number of new cases, it is the general belief of stakeholders that there is sufficient number of licensed IPs on the market. On the other hand, as is to be expected within any profession, not all IPs are on the same level. The challenge is therefore to ensure a minimum level across the profession and encourage competition to raise standards generally.

Therefore, the reforms of the regulatory framework of the IP profession should focus on raising the requirements and improving the quality of the IPs and not on increasing their numbers.

3.3 Skills required by IPs

IPs are not a single uniform profession and various IPs have significantly different professional backgrounds and levels of knowledge and experience. In addition, the current licensing process is open to candidates of all backgrounds and competences (i.e. there are no specific requirements for candidates regarding professional background except for a university degree - please see Section 3.5 for more details).

⁸ For more information on grounds for overriding the random selection algorithm, please see Section 3.2.2(ii) above.

This does not recognise the specialist nature of the IP profession and the importance of relevant financial, business and/or legal skills.

The reasons why candidates apply for an IP position are different. Some of the candidates have had experience working with insolvent companies (e.g., attorneys at law, in-house lawyers or accountants) and have therefore decided to try to pursue a career as an IP or are wishing to expand their existing scope of business and also work as an IP in parallel with their current profession, while others often had no earlier experience with insolvencies. There are also cases of candidates applying for an IP position due to long unemployment, retirement or lack of income from their regular profession, while not having clear picture of the legal implications and risks.

The feedback we have received during interview with key stakeholders was that these differences between IPs cause significant differences in the quality of their work.

Based on our analysis and interviews with key stakeholders, the majority of IPs are still characterised as lacking some of the necessary skills, which is the result of their various backgrounds and previous experience.

Since the introduction of the automatic selection of IPs in insolvency proceedings, the need to have a standardised minimum level of knowledge and skills of IP has increased. For more information on these concerns, please see Section 3.4.

The key skills that IPs need to have to successfully fulfil their duties in insolvency procedures, which are relevant in terms of licensing procedures and education of IPs are briefly described in this Section 3.3.

3.3.1 Pre-bankruptcy proceedings

When opening pre-bankruptcy proceedings, the court may choose to appoint an IP as the administrator if it believes that such appointment is necessary in the pre-bankruptcy proceedings at hand⁹.

If an IP is appointed as an administrator, he/she will be required to do the following¹⁰:

- to examine the business operations of the debtor;
- examine the list of debtors' assets and liabilities;
- examine the credibility of reported claims;

⁹ Article 33 of the Bankruptcy Act.

¹⁰ The list of duties of an administrator is defined in Article 24 of the Bankruptcy Act.

- dispute reported claims if, based on creditors' report or due to any other reason, he/she doubts their existence;
- supervise the debtor's business, particularly the financial business of the debtor, the creation of obligations towards third parties, the creation of security instruments and the sale of goods or services, while ensuring that the debtor's assets are not impaired;
- submit a claim to the court if the debtor acts contrary to the rules of the Bankruptcy Act;
- issue orders and certificates in accordance with the provisions of the Articles 69 and 71 of the Bankruptcy Act;
- monitor the timeliness and completeness of settlement of costs of pre-bankruptcy proceedings;
- carry out other tasks in accordance with the Bankruptcy Act.

To be able to successfully tackle these tasks, an IP will need to have particular set of skills and expertise, as it is explained below.

(i) Assessing the debtor's financial state

When filing for opening of pre-bankruptcy, the applicant (usually the debtor) is required to submit the list of assets and liabilities of the debtor. Such list needs to provide information on assets and liabilities of the debtor, rights of third parties to assets of the debtor, average monthly costs of business operations during last year, court and administrative proceedings in which the debtor is involved as a party. Also, the list must include information on legal and factual grounds in respect to each asset and liabilities as well as evidence thereof¹¹.

To be able to successfully examine the list of assets and liabilities in pre-bankruptcy proceedings, IPs will need to have general knowledge and skills required to perform asset tracing (including reviewing existing databases, e.g. land registry) to be able to check whether the list seems full and complete. They will also need to be able to understand financial reports and cross check them against the list of assets and liabilities so to check if there are any obvious discrepancies.

To analyse whether explanations of the legal title to assets seems reasonable (i.e. that the debtor actually does have legal title to the assets to which it claims that it does), IPs need to have the basic understanding of the legal rules of ownership, various types of encumbrances (pledge, fiduciary transfer of ownership, easements etc.), rules on

¹¹ Article 17 of the Bankruptcy Act.

public registries (e.g. land registry, court registry, cadastral registry, etc.) and some of the typical problems with registration of the title to assets (social ownership, maritime domain, unregistered title to assets, etc.).

(ii) Examination of reported claims

An administrator is required to opine on each reported claim within 30 days as from the day when he/she has been furnished with the table of reported claims and state whether it challenges or not¹².

If the administrator suspects that a reported claim does not exist (on the basis of a notification from a creditor or otherwise), he/she is required to challenge the reported claim of a creditor¹³.

Although an administrator is not expected to examine reported claims in pre-bankruptcy procedure to the extent that a bankruptcy trustee would do in bankruptcy proceedings (the administrator has only limited control over the debtor and the debtor will also be able to challenge the reported claims itself), administrators still need to have appropriate skills to be able to successfully do this. This moreover since usually they cannot rely on external expert assistance (please see Section 3.3.5 below on issues concerning outsourcing).

In particular, administrators will need to have sufficient legal and accounting skills to properly assess each reported claim and will need to have a certain level of personal and professional experience to understand the nature of the reported claim in context of the debtors business.

(iii) Supervising the debtor

According to Article 67 of the Bankruptcy Act, during the course of pre-bankruptcy proceedings, the debtor is allowed only to make payments which are necessary for regular business operations of the debtor (as defined in Article 29(2) of the Bankruptcy Act - mostly referring to obligations towards employees) and servicing of obligations under new financing obtained during pre-bankruptcy procedure in line with Article 62.a of the Bankruptcy Act.

¹² Article 34 of the Bankruptcy Act.

¹³ Article 24 of the Bankruptcy Act.

The administrator (if the court chooses to appoint one) is required to supervise (i) the business operations of the debtor (in particular the financial operations), (ii) creation of new debt by the debtor, (iii) creation of security instruments and (iv) business operations related to sale of goods and services, each with a particular focus that the assets of the debtor are not damaged (diminished). If the debtor is making payments contrary to the Bankruptcy Act, the administrator is required to inform the court about such payments.

Also, during the course of pre-bankruptcy proceedings, the debtor is allowed to dispose of or encumber its assets with prior approval of the administrator (if appointed) or the court.

This means that IPs when appointed as administrators in pre-bankruptcy procedures will be required to assess the ongoing business operations of the debtor and check the payments made by the debtor.

To be able to successfully do this, in addition to having required knowledge of the applicable laws and understanding of the business operations of companies similar to that of the debtor, IPs will also need to have general and professional experience to determine whether payments to be made by the debtor are really necessary and allowed under the Bankruptcy Act.

3.3.2 Bankruptcy proceedings

When IPs are appointed as bankruptcy trustees in bankruptcy proceedings, they have the following duties¹⁴:

- reconstruct the register of bookkeeping records (Croatian: *očevidnik knjigovodstvenih podataka*) for period up until opening of the bankruptcy;
- prepare a cost estimate of the bankruptcy proceedings and submit it to creditors for their approval;
- set-up a committee to prepare the inventory of debtor's assets;
- prepare the initial list of debtor's assets;
- complete commenced, but unfinished business activities of the debtor and business activities that need to be finished to prevent damages to debtor's assets;
- ensure that claims of the debtor are collected;
- continue managing the business activities of the debtor (if they are continued);

¹⁴ The list of duties of a bankruptcy trustee is defined in Article 89 of the Bankruptcy Act.

- submit to the Croatian Pension Insurance Institute documents regarding the employment status of debtor's employees;
- liquidate the bankruptcy estate (if so decided by the creditors);
- prepare and, upon approval, undertake settlement of creditors;
- submit the final report (account) to creditors;
- make subsequent payments to creditors;
- upon the termination of the bankruptcy proceedings, represent the bankruptcy estate in accordance with the Bankruptcy Act

The necessary set of skills varies depending on the type of bankruptcy proceedings. In this Section 3.3.2, we will describe the skills typically needed by bankruptcy trustees in bankruptcy proceedings.

(i) Preliminary stage - opening of bankruptcy

If an IP is appointed as a preliminary bankruptcy trustee (Croatian: *privremeni stečajni upravitelj*) in the preliminary stage of the bankruptcy proceedings (before the bankruptcy against the debtor is opened) he/she may be required to do the following¹⁵:

- protect and maintain debtor's assets;
- conduct business activities of the debtor until opening of bankruptcy, unless the court determines the suspension of business activities to avoid substantial damages to the assets of the debtor;
- assess whether the value of debtor's assets is sufficient to cover the costs of bankruptcy proceedings;
- examines whether the reasons for opening of bankruptcy proceedings exists (i.e. inability to make payments and overindebtedness).

In this stage of bankruptcy proceedings, IPs are faced with two key tasks (i) supervision of the debtor and preserving value of the assets of the debtor; and (ii) assessing financial status of the debtor to determine further actions (whether to open bankruptcy and whether to conduct a regular or summary bankruptcy proceedings)¹⁶.

To be able to properly supervise a potentially insolvent company, IPs need to have an understanding of how companies operate (i.e. what are typical payments made by operating companies, what services are required by a potentially insolvent company,

¹⁵ Article 119 of the Bankruptcy Act.

¹⁶ For more information on difference between regular and summary bankruptcy proceedings, please see Section 3.3.2(xv).

what costs are reasonable in regular business activities, etc.), so to assess whether the action which the management intends to take are reasonable and whether they could be detrimental for the assets of the debtor.

IPs should also be able to understand the nature of the business of the debtor. However, since this may significantly vary across different industries, it may not be reasonable to expect that all IPs are experienced with supervising companies from all types of industries. Therefore, all IPs should have general understanding of how commercial companies operate; while more specialised industry specific training should be made available to more experienced IPs who want to specialise for insolvency in a particular industry¹⁷.

To be able to assess the overall financial state and solvency of the debtor, IPs will need to have skills in accountancy and will need to be able to ascertain the value of assets and the amount of liabilities, including contingent and prospective liabilities. They will also need to be able to consider the achievability of profit and loss, and cash flow forecasts.

These skills are often needed in the process of opening of bankruptcy proceedings as the preliminary bankruptcy trustee will often be asked to assist the judge in determining whether an entity that appears to be insolvent should be made subject to a formal bankruptcy procedure.

(ii) Recreating business records

When appointed as a bankruptcy trustee, an IP immediately assumes the role of all corporate bodies of the debtor. This means that the IP will need, in a short period of time, to take control of all assets, business records and ongoing operations of the debtor.¹⁸

Sometimes this can prove to be burdensome, in particular if the business records of the debtor were not kept properly, if the former management is not willing to cooperate or if the ownership of assets of the debtor was not registered properly with relevant registers.

¹⁷ To enable appointment of IP who have specialised in a specific industry, current randomised computed selection system will need to be reviewed. For more information, please see Section 3.4 below.

¹⁸ Article 88/1 of the Bankruptcy Act.

To be able to sort out the business records of the debtor for a period up until the time of opening of bankruptcy, the bankruptcy trustee will often need to have, in addition to general skills in accountancy, also specific skills in forensic accountancy, asset tracing, basic legal skills in ownership law (Croatian: *stvarno pravo*), registry law (in particular the land registry law) and will need to have certain level of professional experience to be able to predict what actions the former management may have done to diminish the value of the bankruptcy estate.

(iii) Taking-over the bankruptcy estate

Immediately upon declaration of bankruptcy, the bankruptcy trustee is obliged to take over possession of the bankruptcy estate (i.e. all assets of the debtor) and is responsible to manage them.¹⁹

Also, he/she will need to prepare the initial list of the assets that make up the bankruptcy estate. To do this, the bankruptcy trustee will likely need to trace all the assets of the debtor.²⁰

Usually, when the former management is cooperative, they will inform the bankruptcy trustee of all the assets that make up the bankruptcy estate. In such situations, the bankruptcy trustee will, in principle, just need to cross check such information with the available business records and other available evidence to see that the information received from former management is true and complete.

However, when the former management is not cooperative (which, although they are obliged by law to cooperate with the bankruptcy trustee, is often the case), the bankruptcy trustee will need to do the asset tracing.

To be able to do this, in addition to general skills in accountancy to determine what assets the bankruptcy trustee should expect to find, the bankruptcy trustee will need to have certain investigative skills and will need to understand the basics of how various public registries operate and what information is registered where (e.g. what is registered in land registry or ships registry, how to trace if there are any vehicles owned by the debtor, if the debtor has shares in other companies, including those outside of Croatia, etc.). Also, the bankruptcy trustee will need to have understanding of the legislation regulating the ownership to be able to verify the validity of title to

¹⁹ Article 216 of the Bankruptcy Act.

²⁰ Article 89 of the Bankruptcy Act.

assets (e.g. the status of nationalised property, status of unregistered buildings, issues with privatisation).

Furthermore, the bankruptcy trustee will need to have certain level of professional experience to be able to predict what the former management may have done with the assets of the debtor. For example, they may be concealing assets and using them privately or they could have sold them to third parties below market value.

Once the bankruptcy trustee finds the assets of the debtor, he/she will also need to take over possession of them. When such assets are in the possession of third parties who are not willing to hand them over, taking possession may require significant efforts from the IP as well as certain skills. In particular, IPs will need to understand the legal issues involved, what actions are typically required to take over possession (eviction, changing of locks, etc.).

Assets of the bankruptcy estate may also need to be insured. Therefore, IPs should have a basic understanding of how and when insurance policies should be taken, against what risks and if there are any particular considerations to be taken into account when negotiating such insurance policies.

(iv) Assessing business operations of the debtor and reasons for bankruptcy

When taking control over the debtor, the bankruptcy trustee will also need to understand the business of the debtor to be able to understand in what business activities the debtor was involved, are these business activities completed or are they ongoing, are there any unfulfilled contractual obligations of the debtor, etc.

The bankruptcy trustee will also need to understand the reasons why the debtor became bankrupt (e.g., bad business plans, poor implementation of business plans, lack of liquidity, overindebtedness) to make an informed assessment of whether any of these activities should continue in bankruptcy. This decision-making can be critical for creditor recoveries and the value of the bankruptcy estate.

Furthermore, IP should be able to evaluate short-term and the long-term profitability and the potential for the business and/or assets of the debtor to be sold to determine the best strategy for settlement of creditors, i.e. continuation of business and restructuring of the debtor or liquidation of assets (either as whole or piecemeal).

Sometimes, the former management and/or business partners of the debtor will inform the bankruptcy trustee of any ongoing business activities and will help the bankruptcy

trustee understand them and take them over. However, often this will not be the case or the information given to the bankruptcy trustee may be incorrect or misleading.

According to Article 217 of the Bankruptcy Act, until the first hearing for the reporting on the bankruptcy estate (Croatian: *izvještajno ročište*) the bankruptcy trustee is required to complete those business activities (business operations) of the debtor that need to be completed to avoid damage to the assets of the debtor and those business activities which the bankruptcy trustee determines that would be beneficial for the bankruptcy estate.

At the first hearing for the reporting on the bankruptcy estate, the creditors will decide should the debtor continue business operations in bankruptcy or should such business operations be terminated. At least 15 days prior to the first hearing, the bankruptcy trustee is required to submit a report to the court on the commercial status of the debtor and the reasons why the debtor went bankrupt. The creditors will usually decide on continuing of the business of the debtor on the basis of the recommendation made by the bankruptcy trustee in such report.²¹ Therefore the input of the bankruptcy trustee can be critical in terms of continuation of the debtor's business, the maintenance of jobs, recovery strategy (liquidation or restructuring) and, as such, is also critical for the recovery by the creditors.

Furthermore, according to Article 181 of the Bankruptcy Act, if there are unperformed contracts between the debtor and third parties at the time of opening of bankruptcy, the bankruptcy trustee may have option to decide whether to request that these contracts are performed.

All this requires that IPs appointed as bankruptcy trustees have certain skills and experience to be able to independently assess the business operations of the debtor. In particular they will need to have certain skills in (e.g., business administration, debt management, people management, financial report analysis). Also, they will need to have certain level of personal and professional experience, in particular in regard to business operations of commercial companies to be able to understand the nature and significance of any ongoing business activities of the debtor and what it would take to complete them in bankruptcy.

Furthermore, to be able to complete any ongoing business activities that need to be completed (if there are any), the bankruptcy trustee will need to quickly understand the

²¹ Articles 227 and 228 of the Bankruptcy Act.

basics of the core business of the debtor, evaluate business prospects of the debtor and potential for sale of the business and/or assets of the debtor. Also, he/she will need to have certain skills and experience in management of companies to ensure that such ongoing business activities are successfully completed.

Considering that the nature of business activities may significantly vary from one debtor to another, the skills which each IP should have should be focused on the most typical actions and procedures which the bankruptcy trustee needs to do when taking over the company.

(v) Determining who creditors are and examination of reported claims

Upon a declaration of bankruptcy of the debtor, creditors are invited to report their claims and notify the bankruptcy trustee of their exclusion rights and rights of separate settlement.

On the basis of information available from the accounts and business records of the debtor, other documents of the debtor, inputs received from the former management, reported claims or otherwise, bankruptcy trustees are required to prepare the list of all creditors. In such list, creditors need to be sorted into different classes (depending of the ranking of their claim) and if they have a right of separate settlement.

To be able to do this, IPs will need to know (i) how to determine the validity of the claims against the debtor, their amount and ranking (priority); (ii) how to determine rights of separate settlement (Croatian: *razlučna prava*), (iii) how to determine rights of exclusion (Croatian: *izlučna prava*); (iv) determine if any of the aforementioned are disputable, assess them and evaluate how to resolve such dispute and/or evaluate whether or not to challenge them.

Also, when examining reported claims, bankruptcy trustees need to cross check the business records of the debtor with reported claims and other information available. To be able to successfully do this, IPs will need to have sufficient legal and accounting skills to properly assess each reported claim and will need to have a certain level of personal and professional experience to understand the nature of the reported claim in context of the debtors business.

This means that the bankruptcy trustee will need to determine the priority of each claim and propose how to distribute the proceeds.

All these skills will also be needed later-on in the proceedings when the creditors will be settled.²²

(vi) Dealing with misconduct

When taking over bankrupt company, IPs will often find that the former management may have been involved in misconduct and may have committed criminal offences (fraud, tax evasion, illegal disposal of company's assets, etc.).

Therefore, IPs should have good understanding of the type of white-collar crimes and how to identify them. Also, when appropriate, IPs should have skills on how to investigate the misconduct relating to the insolvency and prepare and submit criminal charges and other reports to relevant authorities (as required by law).

(vii) Administering the proceedings

Throughout the bankruptcy proceedings, the bankruptcy administrator is required to file various reports, inform the courts and creditors on different issues, request approvals for intended actions, organise information, propose hearings and meetings of creditors' assembly, etc. All this required a significant amount of administrative work.

Some IPs have supporting staff that helps them with the administrative work (which they usually pay out of their-own pocket), some can use the employees of bankrupt companies to assist them (if there are any), while others are required to do all the administrative work themselves (which is usually the case with many newly licensed IPs).

Such administrative work can be burdensome, in particular if an IP is simultaneously appointed in several high-profile bankruptcies.

With recent reform of the bankruptcy framework in 2015 and introduction of standardised templates for most of the submissions and reporting, this process has been somewhat simplified.

However, IPs still need to have certain organisational and administrative skills to properly manage bankruptcies. These may include, for example: establishing and maintaining files, drafting concise reports, organising staff, coordinating between different stakeholders involved.

²² Articles 273 *et seq.* of the Bankruptcy Act.

(viii) Managing costs of bankruptcy

Since costs of bankruptcy proceedings (Croatian: *troškovi stečajnog postupka*) and other expenses of the bankruptcy estate (Croatian: *ostale obveze stečajne mase*) are, in principle, settled before creditors' claims, it is very important that bankruptcy trustees are cost-sensitive and that the costs are kept to the minimum.

To that extent, bankruptcy trustees are required to seek in advance the approval of costs-estimate from the creditors.²³

To be able to manage costs of bankruptcies properly, IPs should be able to assess when taking over the control over debtor what actions will be required in that particular bankruptcy proceedings, how long the bankruptcy is expected to last and what costs are expected to incur.

Outsourcing (please see Section 3.3.5) can add to the total amount of the costs but is necessary for IPs to be able to draw on relevant skills and experience e.g. legal skills and advice if they are non-lawyers and manpower where the insolvency case requires it.

Therefore, to properly plan costs and the budget, IPs should have skills in business planning, financial forecasting and should have good understanding of bankruptcy framework and the business environment in Croatia in general.

Also, if the debtor will continue business operations in bankruptcy, IPs will need to know how to plan for operational costs as well.

(ix) Employment related issues

Opening of a bankruptcy does not automatically lead to termination of employment contracts, although it is a reason to terminate employment contracts.

Depending on the nature of each bankruptcy proceedings, the bankruptcy trustee may need to keep some of the existing employees or hire new employees.

²³ Article 98 of the Bankruptcy Act.

While bankruptcy trustees can, in principle, seek legal advice from attorneys at law in respect to dealings with employee related legal issues, it would still be beneficial if they have basic understanding of rules of the employment law, including also rules regarding safety at work. This is important, as the bankruptcy trustee is assuming the role of the management and is personally responsible for any breach of employment regulations.

In case of termination of employment contracts (which happens in most bankruptcies where there are employees), IPs need to know what is the procedure to terminate employment contracts and what reports need to be filed with relevant authorities to that extent.

Also, it is possible that employees of bankrupt company are members of unions in which case IPs may also need to deal with union representatives. Therefore, it would be beneficial if IPs also have general understanding of the unions and rights that union representatives have in employment related issues.

(x) Bookkeeping and taxes

The date of opening of bankruptcy is a cut-off date on which new financial year has started and the bankruptcy trustee is liable for the bookkeeping and reporting since then.

Although IPs should have good understanding of the basic principles of the bookkeeping, these services are usually performed by in-house bookkeepers (if they remain employed with the debtor in bankruptcy, which is usually not the case) or they are outsourced to external bookkeepers. Therefore, it is not necessary that IPs have extensive knowledge or experience in bookkeeping to perform these tasks.

Regarding taxation, bankruptcy trustees need to understand the tax rules which may be applicable to the debtor. In particular, they need to understand what key taxes, fees and charges are payable, what triggers their payment and how they should be planned. For example, when considering a sale of real estate in bankruptcy, the bankruptcy trustee may need to plan whether VAT will be payable or not to ensure that the terms of sale of such real estate are set accordingly.

(xi) Liquidation of bankruptcy estate

Unless the creditors have agreed otherwise (i.e., to restructure the debtor - which is rarely the case), one of the principal duties of the bankruptcy trustee will be to liquidate

the bankruptcy estate and settle creditors' claims. This implies many different kinds of activities from recovery of bankruptcy estate to its sale.

Before a bankruptcy trustee can liquidate assets of the debtor, he/she will need to take over the bankruptcy estate and all assets belonging to the bankruptcy estate (for more information, please see Section 3.3.2(iii) above).

Once the bankruptcy trustee has taken-over the possession of the assets, he/she will need to determine their value and the best way to liquidate it (sale of all assets of the debtor as a whole, sale of separate business units or piecemeal sale of assets) to achieve best recovery for the creditors. This requires the understanding of the market and certain experience to be able to predict what is the best way to liquidate what type of asset.

Before liquidation of assets, bankruptcy trustee may need to resolve any pending legal or other issues regarding the bankruptcy estate (e.g., debtor is not registered as the owner of the assets, there are pending disputes regarding the assets which will likely undermine their sale, assets need to be grouped to increase their value, etc.). For most of such issues, the IPs will likely need to hire a specialist or consultant to assist them with resolving issues at hand and will not need to be experts themselves²⁴. However, IPs will still need to have certain basic understanding and skills to properly address the issues at hand.

For example, IPs should have basic understanding of legal issues which are typical with assets in Croatia (ownership is not registered, there are pending disputes, what taxes are payable, how is maritime domain regulated, etc.). While IPs do not need to have an in-depth knowledge on each such issue, they should have the basic understanding to be able to properly evaluate risks involved and to decide how to best address them.

In certain bankruptcy proceedings, there may also be regulatory issues involved with the assets of the debtor (e.g. energy production plants or port infrastructure are heavily regulated). However, the scope of possible regulatory issues that could arise is rather wide. Therefore, IPs should not need to know details of regulatory issues in each industry, but should rather have skills on how to resolve regulatory issues on a general level. Still, more industry-specific training could be organised for experienced IPs to enable them to specialise for a particular industry. This would in particular be useful at

²⁴ For more information on possibility of outsourcing, please see Section 3.3.5 below.

times when economic crisis hits a specific industry (e.g., construction, shipping, credit institutions).

Once the bankruptcy trustee is in possession of the assets and any issues are solved, the assets need to be appraised and sold.

This implies that IPs need to know what is the procedure for different methods for sale of assets (electronic auctions, public auctions, direct sale) to make sure that such procedure is followed and that interests of creditors are not impaired.

Furthermore, IPs should also have certain skills in sales and marketing to be able to attract as many interested buyers as possible and thus achieve highest price possible for the assets being sold. Good bankruptcy trustee will usually have spread the word in the relevant circles of any upcoming auction and would have attracted as many potential buyers as possible.

(xii) Realisations from other sources

In addition to sale of assets, bankruptcy trustees will usually also have to achieve realisations from sources as well. These may include actions such as challenging voidable transactions, settlement of amounts owed to the debtor, receiving profits payments from daughter companies, etc.

To be able to successfully do this, IPs need to identify circumstances that give rise to such potential recovery actions, the creditors who might benefit from pursuing them, how such actions might be funded, and whether they should be pursued.

To challenge voidable transactions, IPs will in particular need to have understanding of what voidable transactions are, how to detect them and what costs are involved in challenging them. For this, IPs would ideally have skills in forensic accounting, understanding of the legal rules behind the invalidity and experience with operating companies.

Settlement of the claims will usually require that IP can identify such claims and that he/she has certain soft skills required to negotiate their payment. If the debtors are not willing to pay voluntarily, bankruptcy trustee will usually hire an attorney at law to try to enforce such claim if it may be expected that any such legal action against debtors of the debtor would be worthwhile.

(xiii) Continuing business operations

Continuing business activities by the debtor in bankruptcy implies that the bankruptcy trustee assumes the role of the management of the debtor.

While in such situations at least some of the staff of the debtor will remain (although not necessarily), this will usually not be the case with the former management.

Although, bankruptcy trustees may hire professionals to assist them in managing bankrupt companies, they will still need to have the basic understanding of the processes and have key skills required to manage operating company, including dealing with finances, using cash flow forecasts and trading budgets, organising employees, managing of operations, compliance with industry licensing, environmental and other regulatory requirements, managing stocks and works in progress, negotiating and executing contracts, dealing with intellectual property, etc.

This is particularly important since bankruptcy trustee, as the responsible person in the company, will often be personally liable for any breach of applicable rules and regulations.

Furthermore, IPs will likely need to quickly get the grasp on the industry specific knowledge to be able to manage the company. Since any such industry specifics may significantly vary from one industry to another, it is important that IPs have good understanding of what is in general required to take-over management of a company so that they can focus on industry specifics when taking over a company.

(xiv) Restructuring and bankruptcy plan - specifics

The restructuring (reorganisation) may be carried out in bankruptcy in many different ways, including by: (i) retention by the debtor of all or a part of the bankruptcy estate in order to continue its business activities; (ii) transferring all or a part of the bankruptcy estate to one or more existing entities or entities that will be established; (iii) merger or consolidation of the debtor with one or more entities; (iv) selling all or a part of the bankruptcy estate (with or without security instruments); (v) division of all or a part of the bankruptcy estate amongst creditors; (vi) determining the method of settling the claims of creditors; (vii) settling or amending rights of separate settlement; (viii) reducing or postponing payments by the debtor; (ix) converting existing obligations into a loan; (x) issuing of a guarantee or providing other collateral as a

security of claims against the debtor; (xi) determining debtor's liability after termination of bankruptcy.²⁵

Restructuring in bankruptcy involves creditors accepting a bankruptcy plan including one or more measures listed above.

The initiative for preparation of a bankruptcy plan will either be on the bankruptcy trustee or on the creditors who may instruct the bankruptcy trustee to prepare the bankruptcy plan. The bankruptcy plan will set out the terms of restructuring. Therefore, in principle, it is the bankruptcy trustee who will be obliged to prepare the terms of restructuring. The creditors' committee (if established) will only have an advisory role in the process. The creditors have to approve the final bankruptcy plan (with majority of 2/3 of all the claims, provided that majority of all creditors in each class of creditors has voted²⁶).

All this implies that the IP, when preparing bankruptcy plan, will need to have a number of specific skills which may not be as relevant in liquidation of bankruptcy estate. These are, for example, diagnostic business and financial analysis, financial planning, operational planning, cash flow forecasting, turnaround skills, negotiating new financing terms and project management. When lacking any of these skills, bankruptcy trustee can (and in case of more complex bankruptcies- should) engage specialist consultants to assist it in preparing bankruptcy plan. However, even in such situations, bankruptcy trustee will need to have at least general understanding of the planning and forecasting process

In addition to specific professional skills, IPs will need to have certain soft skills, such as good negotiation techniques, good coordination skills, mediation and dispute resolution skills, etc. These will be very important in preparation of the bankruptcy plan, as the process will also require significant coordination and mediation efforts to bring together creditors with often opposing interests to support a single bankruptcy plan.

(xv) Summary bankruptcy proceedings

When an entity has no employees, when it has outstanding payments registered in the Payment Transactions Order Register over an uninterrupted period of 120 days and no prerequisites have been met to institute another procedure for deletion from the court

²⁵ Article 303 of the Bankruptcy Act.

²⁶ Article 330 of the Bankruptcy Act.

register, the Financial Agency will file a motion for opening of a summary bankruptcy proceeding against the debtor.

Since the Financial Agency usually does not investigate whether a company has any employees, most motions for opening of bankruptcy filed by Financial Agency are those for opening of summary bankruptcy proceedings.

In summary bankruptcy proceedings, if the court decides to open bankruptcy, it will appoint a bankruptcy trustee and immediately (with the same decision) terminate the bankruptcy proceedings.

As a rule, such bankruptcies should not be difficult as not much is needed from the appointed bankruptcy trustee (since there are usually no material assets or unresolved issues to tackle). Therefore, in summary bankruptcy proceedings, IPs listed on both the List A and the List B can be appointed as the bankruptcy trustee²⁷. If a creditor requests that regular bankruptcy proceedings are conducted or if bankruptcy trustee finds material assets of the debtor, then the bankruptcy trustee will need to be one listed on the List A. This means that if the current bankruptcy trustee is listed on the List B, he/she will need to be replaced with one listed on the List A.

Although summary bankruptcy, in principle, implies that there is not much work for the appointed bankruptcy trustee, the bankruptcy trustee will nonetheless still be the last responsible person in the company. As such, he/she may be called in future to furnish information in different procedures (e.g. in case of a tax investigations, criminal investigations, etc.) therefore, the trustee will need to gather business records and archives of the debtor and store them accordingly.

Also, bankruptcy trustee should investigate if there are any assets of the debtor or unfinished business.

Since inexperienced IPs listed on List B can also be appointed in summary bankruptcy proceedings, they need to be trained in more detail on their responsibilities.

We understand that currently many IPs listed on the List B are not aware of all the responsibilities they have when being appointed and often ignore the decision on their appointment.

²⁷ For more information on the lists of IPs, please see Section 3.7 below.

3.3.3 Industry specific training

When there are insufficient funds to cover the costs of specialised help related to the industry specific issues, the bankruptcy trustee will need to handle these issues on its own.

Since such industry specific issues may significantly vary from one debtor to another, it is not reasonable to expect that all IPs have skills and knowledge and training in all industries. Therefore, industry specific training should not be made part of the standard training of all IPs.

Instead, specific training (as determined by the Ministry from time to time) could be provided to smaller groups of IPs who could then specialise in insolvency of companies in a particular industry.

We understand that there was intention of the Ministry to try and organise, together with DAB (State Agency for Deposit Insurance and Bank Resolution), workshops for advanced IPs on topics related to bankruptcy of credit institutions. This seems to be a good approach for such industry specific training.

Similarly, other industry specific workshops could also be organised (e.g., construction, finance and capital markets, shipping, pharmaceutical industry). Such workshops would not need to be held frequently, as the need for such workshops would likely be limited to the IPs appointed as administrators or bankruptcy trustees of such companies in insolvency proceedings or IPs who are otherwise dealing with bankrupt companies involved in a specific industry.

In principle, organisation of such industry specific trainings could be organised during longer time frame (e.g. every one or two years) or more often if there is interest of IPs for such industry specific training. If it can be expected that there will be an increasing number of bankruptcies in a particular industry (e.g. in case of crisis in shipping or construction) then trainings relevant for such industry should intensify.

Given that such industry specific trainings would significantly differ from the regular trainings relevant for bankruptcies in general, they would ideally be co-organised together with the competent regulator or authority (e.g. DAB, Croatian National Bank,

HANFA, Zagreb Stock Exchange, line ministries). Some of these authorities are already experienced in organisation of trainings²⁸.

Insolvency process may be improved with intense industry specify trainings for limited groups of IPs.

3.3.4 Computer skills

It has been brought to our attention that a number of IPs lack adequate and sufficient computer skills and IT literacy in general. This may represent a challenge for the overall efficiency of the process.

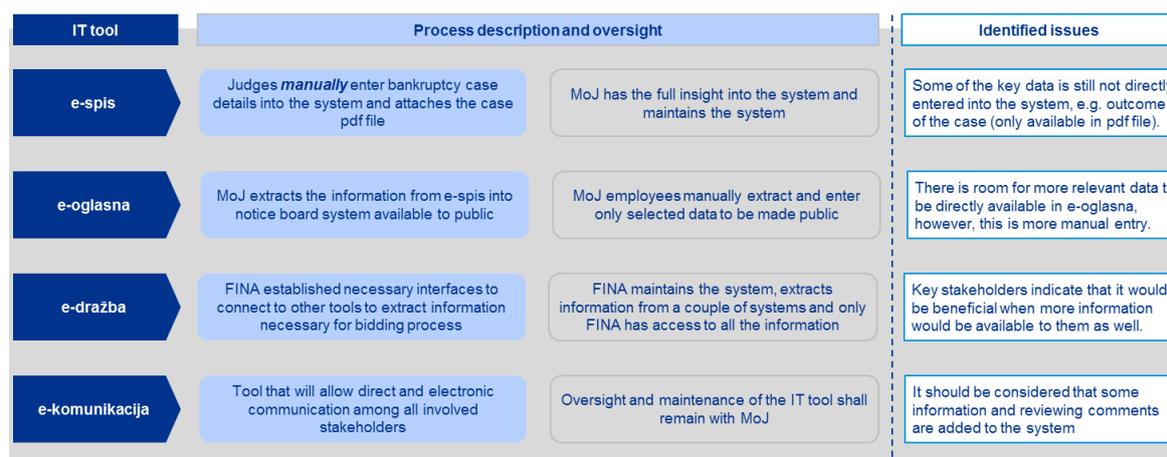
Currently, the process is supported with specific IT tools, which are focused primarily on document management (Figure 13). IT support improvement project focused on establishing active communication and sharing of information between involved stakeholders is currently in progress.

It can be expected the future development of the insolvency framework will result in introduction of further IT tools and that IPs will be more dependent on necessary IT skills. For example, the EU Insolvency Regulation²⁹ envisages establishment of insolvency registers which will need to be interconnectable with other insolvency registers in EU. Similarly, the MoJ is constantly introducing new tools and serviced to digitise the processes within insolvency proceedings (please see Figure 13 below). All this will require that IPs are constantly updating their IT skills and knowledge to adopt new technologies in everyday use.

²⁸ For example, Zagreb Stock Exchange has an academy which organises workshops on topics related to capital markets (e.g. workshops on basics of capital markets, investor relations).

²⁹ Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) [2015] OJ L 141.

Figure 13



Source: Interviews with key stakeholders, Ministry of Justice, FINA website, MPRR – KPMG analysis

In respect to this, setting-up trainings with focus on computer skills, e.g. advanced use of existing IT tools, specific software packages and similar tools – should altogether be taken into consideration.

Insolvency processes may be improved by establishing stronger IT support. The following should be taken into consideration:

- Due to differences in backgrounds of existing IPs and the older profile of the profession, some IPs have inadequate IT skills. It is recommended to set up training for using the basic IT tools and packages relevant for insolvency practice (financial modelling, controlling, management reporting system, etc.).
- Communication and information sharing with insolvency stakeholders including creditors may be improved by introducing central communication system.
- It should be considered to link existing IT tools with relevant databases (e.g. FINA's databases) and to automatically update information. This way, manual data entry (between two IT tools) will be eliminated.
- In the mid-term, online learning platforms could be set up which would include minimum required trainings, general information, manuals and guidelines etc. This approach would allow better facilitation of trainings irrespective of IPs location and assist IPs to participate in more than one training / workshop.

3.3.5 Outsourcing

Considering that the duties of IPs in insolvency proceedings are rather extensive and typical IPs will not have a strong professional background in all relevant areas or will not have sufficient capacities, assistance of external consultants and experts will often be necessary.

In bankruptcy proceedings, bankruptcy trustees will typically outsource those activities which are time consuming or require additional resources which the bankruptcy trustee does not have at its disposal and which non-bankrupt companies usually outsource (e.g. bookkeeping, archiving and services of attorneys at law). This they will do even if they have professional background to be able to do these activities themselves (e.g. if IP is a licensed attorney at law). The costs of outsourced services will be treated as costs of bankruptcy estate and will have priority in settlement over claims of bankruptcy creditors.

While outsourcing certain activities often cannot be avoided, as IPs do not have all the necessary skills or do not have time or resources to perform them, IPs should have basic understanding of the underlying issues to be able to assess whether such costs are necessary and beneficial.

For example, initiating a lawsuit to settle a claim against a third party may seem reasonable expense if it can be reasonably expected that such claim can be enforced and that cash can be recovered. However, if it is evident that the debtor's debtor is insolvent with no assets, then the costs of initiating litigation against it may not be a reasonable course of action even if the lawsuit would be grounded.

Furthermore, in addition to typical services needed in bankruptcies, there is whole range of services which may be needed in particular bankruptcy proceedings. For example, the value of assets will need to be determined by a certified appraiser, location of land plots may need to be determined by certified surveyor, preparation of a bankruptcy plan will likely need to be assisted by a business consultant.

While, IPs should not need to have these skills themselves, they should have basic understanding of the processes behind them to be able to assess if they are required and to be able to supervise and coordinate them.

For example, in case of an appraisal of a real estate, while IP will not be preparing the appraisal himself/herself, he/she should understand the rules on determining the value of real estate as set out in applicable regulations to be able to understand all implications of statements made in such appraisal (e.g. why was certain method of appraisal used).

If debtor is involved in specific industry (e.g., gas, oil or energy trader, construction company, shipping company), bankruptcy administrator will usually also need

assistance with industry-specific issues. These will often be existing employees of the debtor (if they are kept), but may also be new persons hired by the bankruptcy trustee. In each such case, IPs should have good soft skills to supervise and manage such persons.

Unlike the bankruptcy proceedings in which bankruptcy trustees typically do hire advisors and consultants to assist them with performing their duties, in pre-bankruptcy this is not typical as the fees payable to administrators are insufficient for administrators to hire any consultants themselves. While Bankruptcy Act³⁰ envisages that administrator is entitled to reimbursement of reasonable costs incurred in performing its duties, it is not typical that these costs are treated as necessary costs in pre-bankruptcy proceedings.

3.4 Computer-based selection – specific considerations

3.4.1 General remarks

Changes in Bankruptcy Act in 2015, among the others, introduced random selection of IPs to be appointed as administrators and bankruptcy trustees in insolvency cases.

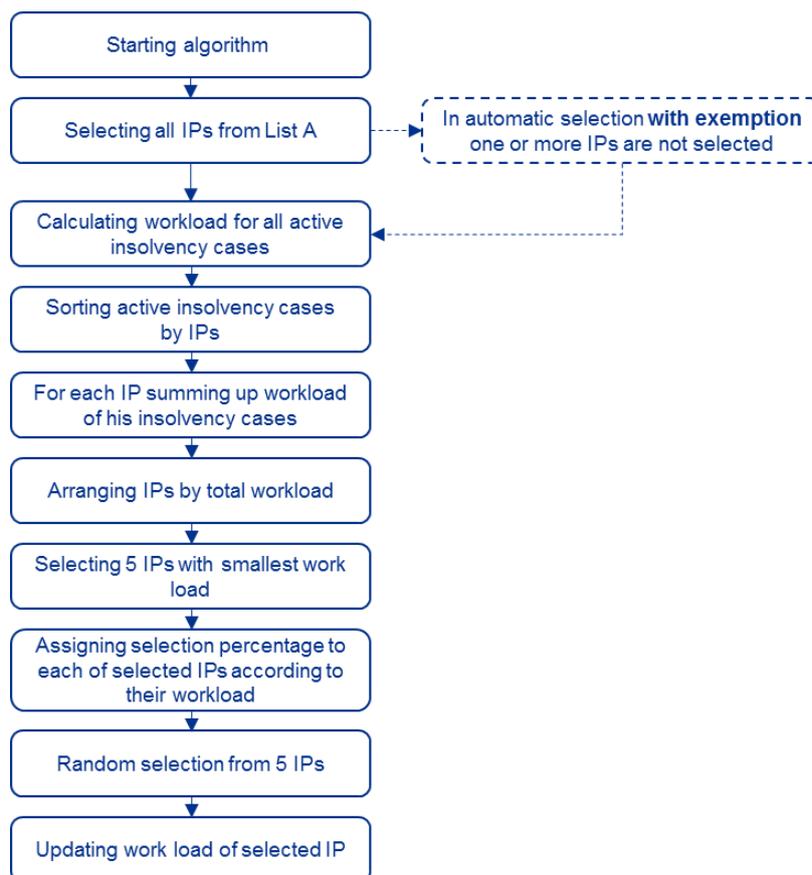
The idea behind this approach was to establish transparent and fair criteria in the process of appointment of the initial administrator or bankruptcy trustee, i.e. to minimise possible issues with subjective preferences in the selection process.

The random process is based on a computer algorithm. For the purposes of this project we have analysed the general functionality of the algorithm, however we have not sought to analyse details or to test the mathematical logic behind the algorithm.

Currently, IPs are selected (by the algorithm) solely based on the workload (Figure 14), i.e. number of cases in which IPs are already appointed.

³⁰ Articles 23(3) and 94 of the Bankruptcy Act.

Figure 14



Source: *The rulebook on the assumptions and manner of election of the bankruptcy trustee by a random selection method, October 2015, Official Gazette of the Republic of Croatia, no. 71/2015, available at: https://narodne-novine.nn.hr/clanci/sluzbeni/2015_10_106_2073.html*

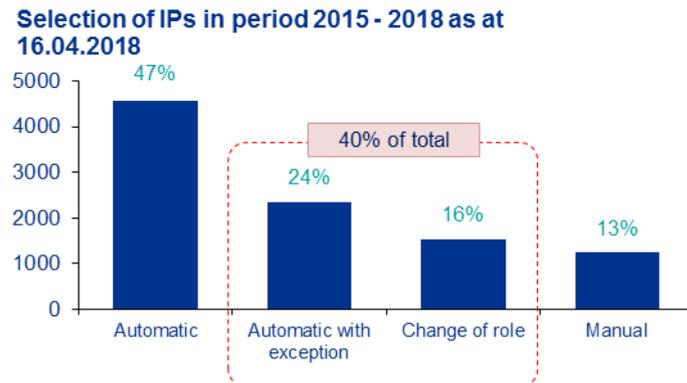
We understand that random selection is not aimed to completely eliminate any human intervention. The interface used by judges, allows exceptions and manual interventions in the randomly chosen IPs. Judges may directly select an IP for bankruptcy cases which, for example, require an engagement by more experienced IPs (which currently cannot be achieved through the algorithm logic)³¹.

Based on the available data (Figure 15), during period 2015 – 2018, most of IPs have been selected using automated process (i.e. algorithm), while in 40% cases, a manual intervention has been made in the automatic selection. In 13% of cases, a complete manual selection of IPs has been performed.

³¹ Article 84(2) of the Bankruptcy Act and Article 3 of the Rulebook on Conditions and Methods for Appointment of IPs by a Random Selection Method.

From the interviews with relevant stakeholders, we understand that judges are recently not inclined to intervene in the random selection process unless absolutely necessary.

Figure 15

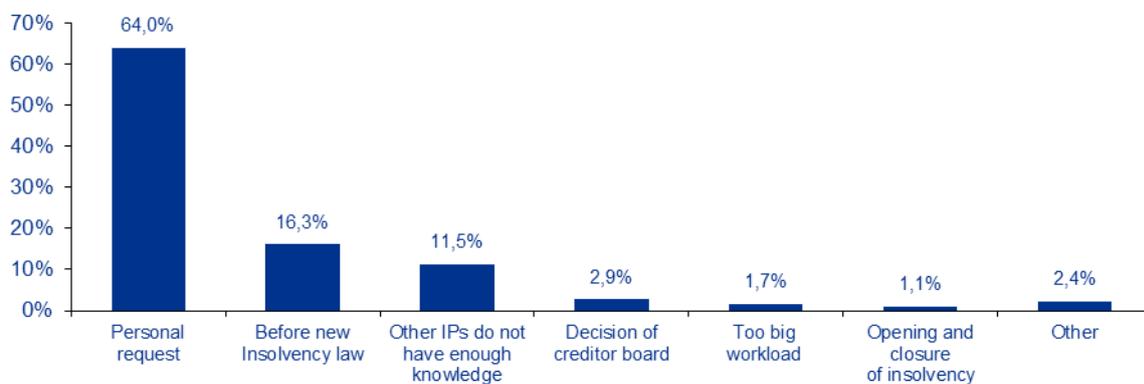


Source: Web site of the Ministry of Justice, List of IPs and bankruptcy procedures, April 2018, available at: <https://e-oglasna.pravosudje.hr/?q=popisi-obraci/8998>

Rationale behind manual interventions in automatic selection (Figure 16), is that in 64% of cases - IPs personally requested exception from a case, but there were also cases where judges determined that a certain IP does not have sufficient/adequate competence or creditor's assembly dismissed an IP, etc.

Figure 16

Reasons for exception in selection of IPs in period 2015 - 2018 as at 16.04.2018



Source: Web site of the Ministry of Justice, List of IPs and bankruptcy procedures, April 2018, available at: <https://e-oglasna.pravosudje.hr/?q=popisi-obraci/8998>

While the computer-based selection has increased transparency, it has also resulted in situations that any IP listed on the List A can be appointed in any insolvency proceedings regardless of its background, knowledge or other skills. Given that judges are, in principle, reluctant to intervene in the selection process and often do not have all the relevant information on IPs to select the best suited IP manually, such system has stressed the need to ensure that each licensed IP needs to have a minimum level of skills and expertise required to handle insolvency cases.

Slovenia, for example, has implemented similar system of random selection and seem to face similar weaknesses as Croatia, i.e. random appointment does not take into consideration track record (in other words, specific industrial experience or outcome of proceedings are not taken into account). Alternative systems of an IP appointment may include the following:

- Debtor selecting an IP which needs to be approved and appointed by creditors (e.g. in Latvia);
- Nomination by creditors and debtors (with creditors' decision prevailing) or nomination by judge of an interim IP (e.g. in Romania);
- Appointment and dismissal by judge upon the creditors' request (e.g. in Serbia).

Key findings are as follows:

- While random algorithm selection of IPs has its benefits and ensures transparency, there is space for improvement. This include, among others, considering additional criteria (KPIs) based on which algorithm selects an IP. Taking into consideration only current workload as a general prevailing criteria results in situations whereby less experienced (or inexperienced) IPs may be selected in very complex cases.
- We understand that any changes in KPIs and "filters" for algorithm will also include introduction of adequate performance management process and KPI data to be kept and monitored.
- More information on IP profiles should be available to judges in the process of selection of the IP to be appointed in insolvency proceedings³².

3.4.2 Temporary exclusion from appointment at the request of an IP

The Amendment introduced the option for IPs to request a temporary exclusion from new appointments. However, the law allows them to exercise such option only if they request to be temporarily excluded from further appointments for two years after the end of the calendar year in which the request was filed. IPs believe this period is too long. There may be a number of justifiable reasons why IPs need to request a temporary exclusion e.g. sickness or maternity or if they have a very large caseload.

IPs have reported that the lack of flexibility is demotivating them from exercising this right. Due to the lack of flexibility of this provision, they will likely opt not to exercise this right even if their workload is excessive or if they have personal issues which

³² For more information on how to improve the information on profiles of IPs available to judges, please see Section 3.7 below.

obstruct them in duly fulfilling their obligations. This may, in turn, result in lower quality and efficiency of their work.

If IPs have an option to request a temporary exclusion from further appointments for a shorter period, they will more likely decide to use such right in situations where they feel that their current workload or personal condition is preventing them from properly taking on new cases. This is particularly relevant as the initial stage of bankruptcy proceedings is usually the most work-intensive for IPs. In the early stages of the proceedings, the IP needs to familiarise him/herself with the company, take control of the company and examine all reported claims. All of this needs to be performed in a short period of time.

IPs believe that instead of a fixed period, the Bankruptcy Act could prescribe a certain minimum and maximum period for temporary exclusion. IPs should be able to determine the duration of the exclusion from new appointments within the prescribed range. It was suggested by IPs that the appropriate range for the duration of such temporary exclusion should be between six months and two years. Therefore, bankruptcy trustees would have the opportunity to adjust their request with demands of their active cases, personal circumstances or other reasons for requesting temporary exclusion.

3.5 Licensing

3.5.1 Overview of the licensing framework and licensing procedure

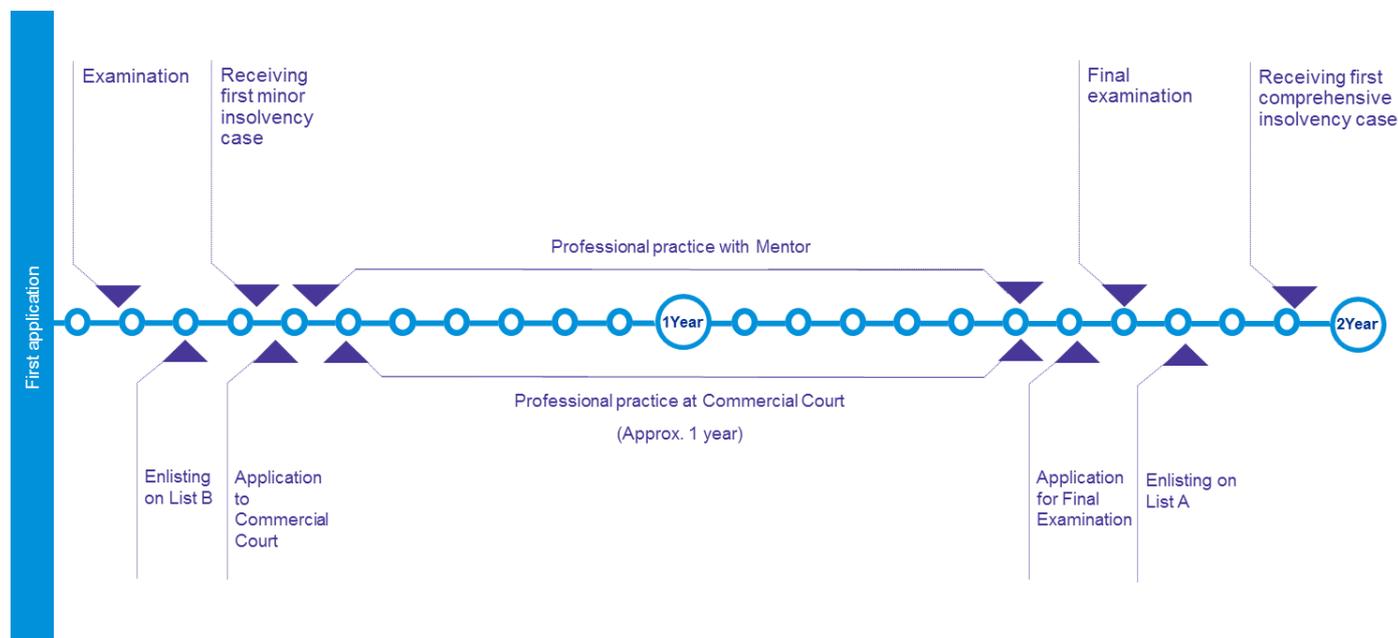
The licensing process for becoming an IP (Figure 17) is currently regulated in the Bankruptcy Act and the Rulebook on Professional Exam, Training and Education of IPs (hereinafter referred to in this Section 3.5.1 as the "Rulebook")³³. The focus is placed primarily on examining whether a candidate meets minimum formal requirements and whether he/she has basic knowledge of the legislation regulating bankruptcy, civil law and bookkeeping.

The existing licensing process for IPs takes approximately two years (Figure 17). Once an IP candidate has completed all the licensing requirements, he/she is admitted to List A. However an IP candidate can be admitted to List B and take summary bankruptcy trustee appointments.

³³ The Rulebook on Professional Exam, Training and Education of IPs, September 2015, Official Gazette of the Republic of Croatia, no. 104/2015, available at: https://narodne-novine.nn.hr/clanci/sluzbeni/2015_09_104_2029.html

During the one year practice period, IPs are supposed to undertake 96 hours of work experience with mentors (12 - 13 working days). Practice before commercial courts includes attending 3 examination hearings, 3 reporting hearings, 3 creditors' assemblies and 3 final hearings. Nevertheless we understand that in practice this is not always respected.

Figure 17



Source: *The Rulebook on Professional Exam, Training and Education of IPs, September 2015, Official Gazette of the Republic of Croatia, no. 104/2015, available at: https://narodne-novine.nn.hr/clanci/sluzbeni/2015_09_104_2029.html*

3.5.2 Licensing requirements

The requirements to be licensed as an IP in Croatia are primarily set out in the Bankruptcy Act and are the following: (i) full legal capacity; (ii) university degree or other high education diploma corresponding to at least 300 ECTS; (iii) professional exam for IPs; (iv) professional training of one year as of the day of passing the professional exam (mandatory only for List A, see Section 3.7 below); (v) a person must be worthy of performing the duties of an IP.³⁴

A person is deemed unworthy if: (i) criminal proceedings are initiated against him/her for a criminal offense which is prosecuted *ex officio*; (ii) convicted for a criminal offense which is prosecuted by the state attorney *ex officio*; (iii) a person has been deleted from the List of IPs on the basis of a decision on dismissal for failure to comply with a court order for recovery of what has been received during the proceedings (applicable

³⁴ Article 79 of the Bankruptcy Act.

for three years as of the date of deletion); (iv) a person has been dismissed as the bankruptcy trustee for negligent performance in more than two bankruptcy proceedings in the course of three years (applicable for three years since the date of dismissal and the person must reinstate the professional exam); or (v) a person who is over-indebted.³⁵

When applying for listing on the List A or List B, the IP must indicate which list he/she is applying for and for which commercial courts. A candidate's CV should be enclosed with the application. The application should also be accompanied by a proof that the person is worthy of performing duties of an IP (attestation that no criminal procedure is pending against the person and a certified declaration that he/she is not over indebted).

It is a general opinion of stakeholders that the criteria to be authorised to act as an IP and to be listed on the List A and the List B (see Section 3.7 below) should be more robust. In particular, candidates for IPs should demonstrate greater knowledge and experience before being licensed as IPs.

Considering the different backgrounds of IPs, it may not be expected that candidates for IPs already have all the needed skills and experience to act as IPs. Nevertheless, candidates for IPs should have certain minimum level of knowledge and experience which is relevant to handle insolvency cases.

The first issue to consider is whether the IP profession should remain open to candidates with a university degree in any field or should it be limited only to candidates with a degree in law or economics. While there are currently IPs with degrees in other fields (approximately 12%)³⁶, some of which are capable of performing duties of IPs, it is general opinion of the stakeholders that it might be better if IPs can only be persons holding a degree in economics or law.

The second issue to consider is the professional experience of candidates for IPs. The tasks of IPs in insolvency cases are such that they can be successfully tackled only if the IP has sufficient experience to handle such cases³⁷. While the lack of experience can, sometimes be compensated by additional efforts by IPs, in most cases such lack of professional experience will cause the IP to oversee an important fact relevant in insolvency proceedings. For example, past experience in managing or supervising

³⁵ Article 79 of the Bankruptcy Act and the Article 5 of the Rulebook on Determining the IP Lists (Croatian: *Pravilnik o utvrđivanju lista stečajnih upravitelja*).

³⁶ For more information on structure of IPs, please see Section 3.2.2 above.

³⁷ For more information on the skills and experience levels needed by IPs in insolvency cases, please see Section 3.3 above.

companies will be useful with many tasks of IPs. While the lack of such experience may cause an IP not to realise what the former management has done with assets of the debtor and may not challenge actions of former management which it should challenge.

It is the general opinion of the stakeholders that there should be an age limit to be able to act as an IP. While interviewed stakeholders have different opinions as to what the age limit should be, most of them have agreed that the age limit should be between 65³⁸ and 70³⁹ years of age. The stakeholders who are in favour of a lower age limit have argued that the nature of IP profession required significant mobility and flexibility by IPs and that this is not expected of older IPs. The stakeholders who argued that age limit of 70 years would be more appropriate have argued that this is the age limit for judges and that the age limit for IPs should be the same.

Considering that the age, on its own, does not imply that an IP is no longer able to perform its duty, the optimal solution would seem to be to set the age limit at 70, with a requirement that the IP needs to file a medical certificate that he/she is fit to perform the duty of an IP, on annual basis starting from the age of 65.

Also, it should be expected that candidates for IPs have certain funds and other resources required to properly perform their duties. Currently, there are no requirements that a candidate for an IP needs to have a certain funds available or that he/she needs to have an office or any other similar requirement.

Key areas for improvement in the licensing requirements are:

- restricting the IP profession only to candidates with degrees in economics, law or similar fields;
- introducing a requirement that a candidate for IP must have relevant professional experience in addition to the one year work experience under the court and mentorship programmes;
- introducing an maximum age limit for IPs; and
- introducing requirements that candidate for IPs must have certain minimum resources.

³⁸ According to Article 112 of the Employment Act (Official Gazette of the Republic of Croatia no. 93/14 and 127/17; Croatian: *Zakon o radu*) general age limit for employment contracts is 65 years (with certain exceptions).

³⁹ According to Article 77 of the Act on State Judiciary Council (Official Gazette of the Republic of Croatia no. 116/10, 57/11, 130/11, 13/13, 28/13, 82/15 and 67/18; Croatian: *Zakon o državnom sudbenom vijeću*) age limit for judges is 70 years.

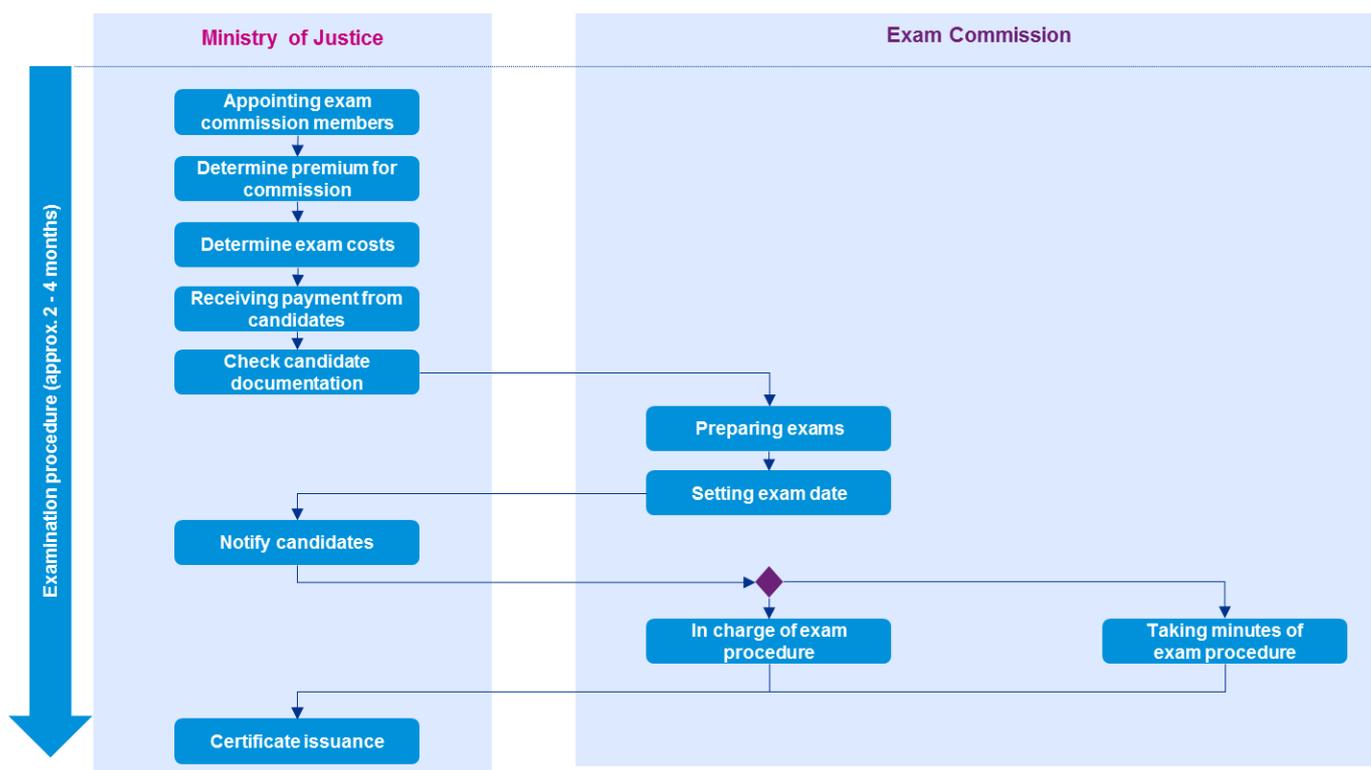
3.5.3 Examination

The role and responsibility of the Ministry during the process of licensing is to appoint the members of exam commission (Figure 18). In addition, the Ministry is responsible for administrative tasks and licensing of the candidates.

The professional examination for IPs is carried out by a three-member exam committee and in accordance with a programme laid down in the Rulebook. The exam committee is appointed by the MoJ which may, but is not required to seek prior recommendations from the Supreme Court of the Republic of Croatia, the High Commercial Court of the Republic of Croatia, law faculties, faculties of economics and other authorities.

Based on information available, the current exam commission has three members and six deputies (i.e. two deputies per each member), who are nominated for the period of two years. Members of the exam commission are fully independent in creating exam curriculum and questions.

Figure 18



Source: *The Rulebook on Professional Exam, Training and Education of IPs*, September 2015, Official Gazette of the Republic of Croatia, no. 104/2015, available at: https://narodne-novine.nn.hr/clanci/sluzbeni/2015_09_104_2029.html

Current process of examination includes:

- Written assignment,
 - Oral exam,
 - Final written exam.
- } IP exam - before being admitted to List B

The IP exam is composed of a written and oral component. In the written part, the candidate prepares a written assignment on the subject within the scope of bankruptcy law, determined by the exam committee. The written assignment takes 120 minutes and is done on a computer, while the Ministry of Justice is responsible for providing all the necessary legislation to such computer. The president of the exam committee evaluates written assignments with a note "passed" or "failed". If a candidate has failed the written part in the subject of bankruptcy law, it is not allowed to proceed with the oral part of the exam.

The oral exam covers the following topics: (i) bankruptcy law; (ii) the basics of civil law, commercial and corporate law; and (iii) the basics of accounting and finance. However, a candidate with the bar exam is not required to pass an exam in civil law, commercial and corporate law, while a candidate with the audit exam is not required to pass exam in accounting and finance.⁴⁰ The exam committee determines legal sources for the professional IP exam.

The oral part of the exam is public. Each subject is marked "passed" or "failed". A candidate must pass all the subjects of the oral exam to pass the IP professional exam. However, if a candidate has failed only one subject, he/she may take a makeup exam in that subject only, within the period not shorter than one month and not longer than three months. If the candidate does not pass the exam within that period, he/ she is deemed failed the professional IP exam. Once a candidate has failed the exam, he/she can retake the whole exam only after four months have passed after his/ her last exam.

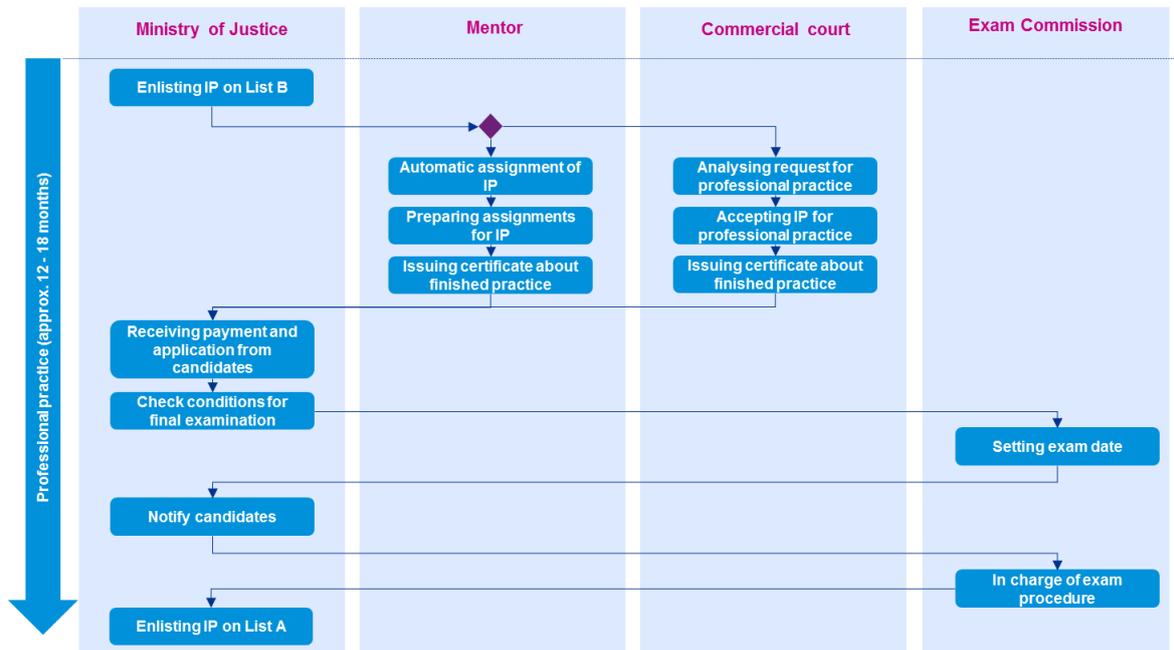
For the purpose of the Project, we were not able to attend an oral exam.

After passing the oral exam, IPs are admitted to the List B and are required to take the one year work experience and mentorship programme before they apply for the final exam. The final exam is held before the examination committee and consists of paper based on actual data from the area included in the professional training.

⁴⁰ The proof of passing a bar or audit exam must be submitted with the application for the IP exam.

After passing the final exam, the IP can be admitted to the List A (Figure 19).

Figure 19



Source: *The Rulebook on Professional Exam, Training and Education of IPs, September 2015, Official Gazette of the Republic of Croatia, no. 104/2015, available at: https://narodne-novine.nn.hr/clanci/sluzbeni/2015_09_104_2029.html*

On average, the pass rate on exams is approximately 60%. Exams are organised five to six times a year. Currently, there are 15 different assignment versions reiterated during exam period. Exams are not published or publicly available.

The costs of examination are born by the candidate, while the exam committee is awarded remuneration for its work in the amount determined by the MoJ.

Before November 2015, the exam and licensing process included only an oral exam. In this respect, since then, significant improvement and standardisation of the process has been achieved.

We highlight the following:

- Exams may be standardised and the questions could be more frequently changed and refreshed.
- Fewer exam sessions per year would also standardise the process (as it is with ACCA – Association of Chartered Certified Accountants Insolvency Exam, for example only once a year, typically in November, which additionally standardises the exam procedure and sets equal conditions for participants in every examination process).

- A practice of publishing examples of exams for candidate to prepare and to enhance the transparency of the examination process should be considered.

3.5.4 Professional training

Pursuant to the Rulebook on Professional Exam, Training and Education of IPs, the examination committee has established the Uniform Programme for Training of Bankruptcy Trustees. The programme sets out the ground rules for professional training of IPs admitted to List B.

The professional training consists of professional practice before commercial courts, professional practice with mentors and final examination before the examination committee (hereinafter: the Examination Committee).

The IP admitted to List B submits the application for professional training to the president of the competent commercial court. The IP has to attend at least three examination hearings, three reporting hearings, three other creditors' assemblies and three final hearings. The president of the court keeps the record on the attendance at hearings by the IP. Based on these records, the competent clerk at the commercial court will issue to the IP a certificate of completed professional training before the court.

The professional training with a mentor is conducted with a mentor assigned from the list of mentors (composed of IPs listed on the List A only) and needs to last at least 96 hours (8 hours per each area). Mentors are assigned automatically by random selection. A mentor may be any IP from List A that opts for the work experience programme.

The training with a mentor needs to include training in following areas⁴¹:

- creating register of bookkeeping data up to the day of opening of the bankruptcy proceedings;
- calculation of expected costs of bankruptcy;
- preparation of reports and attendance at creditors' committee meetings;
- working with the property inventory committee;
- composition of the initial status of debtor's assets;
- examination of reported claims and producing tables of claims;

⁴¹ Article IV of the Uniform Programme for Training of Bankruptcy Trustees.

- composition of documents relating to the employment status of insured persons and documents to be submitted to the Croatian Pension Insurance Institute;
- preparation of cashing of debtor's objects and rights that enter in the bankruptcy mass;
- preparation of payments to creditors;
- participation in execution of payments;
- creation of final account; and
- preparation of subsequent payments to the creditors.

The IP is required to keep a diary on the implementation of professional training, indicating the area, date and duration of the practice, signed by the mentor. After completing the professional training with the mentor, the mentor will issue to the IP a certificate of completed professional training. After completing both professional trainings, the IP can attend the final written examination⁴².

Currently, there are no mandatory courses or workshops which the IPs are required to take during the licensing process. However, IPs admitted to the List B are also required to attend CPD workshops⁴³. We understand that the Ministry has organised, as part of the workshops for CPD, a set of workshops (four modules) aimed at covering the basics of bankruptcy proceedings intended for the IPs listed on the List B. Such workshops could serve as a good model for mandatory training for all candidates for IPs could be created. Such mandatory training should take place during the licensing process (preferably before being admitted to the List B).

Currently, there is no supervision of the mentorship work experience programme and IPs being mentored have very different experiences with the quality and usefulness of the mentorship programme. The mentorship programme should be more standardised and experienced mentors should be incentivised to take-up the role of mentors. Based on interviews and our understanding, IPs do not face issues in obtaining a mentor. However, as there is no standardised procedure of mentorship programmes, nor the tasks and roles of both IPs and mentors during the programme, there is significant differences in the quality of mentorship experience. Concretely, some of IPs highly recommended their mentors and outlined high quality knowledge sharing between mentors and List B IPs. On the other hand, there were rare instances where the mentorship programmed was performed only *pro forma* without real hand-on experience and relevant tasks.

⁴² Please see Section 3.5.3 above.

⁴³ For more information on the CPD, please see Section 3.6 below.

Mentors are not paid for their work as mentors, but are freed from the obligation to attend one workshop required as part of their continuing professional development⁴⁴. While such method of attracting mentors is efficient from a cost-perspective, it would make sense to reconsider this as part of an overall revision of the mentorship programme. Improvements to the existing mentorship programme could include requiring mentors to have more experience (e.g. at least five years of being admitted to List A) and providing greater information and guidance on the areas to be covered by the mentor with the mentee. Consideration should also be given to whether any monetary remuneration or other incentives are needed for mentors. This requires, nonetheless, a delicate balancing exercise with what is required to incentivise the mentee and new joiners to become members of the profession. At present List B IPs do not receive any remuneration from their appointments on summary bankruptcy cases.

The mentorship work experience programme is currently not standardised and largely dependent on the mentor's approach and judgement. This results in various experiences of IPs on List B.

The curriculum is currently not specific, focused, standardised and predetermined. Manuals and guidelines for fundamental topics are not available.

Key areas for improvement in the current process of training and licensing of IPs are:

- mentorship programme – given the fact that there are differences in quality and style, it would be worth considering to standardise the programme (for example, clearly listing roles and responsibilities of the mentor and mentee and the tasks that need to be performed by List B IPs during the mentorship programme);
- providing more guidance on the hands-on experience required to be undertaken by the mentee and verification that this hands on experience is obtained in practice;
- general training would be beneficial for potential IPs before applying for an IP examination– introductory workshops where IPs would be presented with key legal requirements, typical tasks, their roles and responsibilities.

3.6 Continuing professional development

The lack of adequate professional knowledge and practical skills of IPs has been identified as a significant disadvantage of the Croatian IPs regime.

⁴⁴ For more information on continuing professional development and requirement of IPs to attend workshops, please see Section 3.6 below.

While IPs often have a background in accountancy, business or law, it is not necessary that they are qualified in any such profession and can come from many different backgrounds (as explained in Section 3.5.2). This means that their formal education is unlikely to have prepared them for all the challenges they may encounter in insolvency administration.

The mandatory professional training⁴⁵ required to be licensed as an IP on the List A is focused on the basics and does not fully satisfy the needs of the IPs. Also, changing circumstances and new developments require that IPs constantly expand and update their knowledge and skills.

Therefore, continuing and meaningful education of IPs is paramount for efficient insolvency administration.

3.6.1 Recent developments

Up until two years ago, there was no structured educational framework intended for training and continuing professional development ("**CPD**") of IPs. Since 2015, the Ministry has assumed responsibility for training and CPD of IPs, because the law now requires mandatory CPD⁴⁶.

All stakeholders have recognised the introduction of mandatory training (professional practice) in the licensing process⁴⁷ and the mandatory continuing professional development of the IPs as a significant step forward and very beneficial.

Since new methods for IP training and CPD by the Ministry were introduced only few years ago, it is still difficult to assess what impact they have on the quality of the IPs in general. Nevertheless, stakeholders believe that there is still room for improvement of the training and CPD framework.

3.6.2 Overview of the framework for continuing professional development

Continuing professional development of IPs is organised and conducted pursuant to the Programme of the Ministry of Justice for the Continuing Professional Development of IPs.

⁴⁵ For more information on the mandatory professional training, please see Section 3.5.4 above.

⁴⁶ Article 82 of the Bankruptcy Act.

⁴⁷ For more information on the professional training of IPs, please see Section 3.5.4 below.

The annual programme is determined by the Ministry for each calendar year and includes topics from the fields of insolvency, labour, enforcement, commercial and land registry law, accounting and finance, and others fields which contribute to the continuing professional development of IPs, and is published on the Ministry's website.

Generally, there is no standardised curriculum, i.e. no predefined syllabus and trainings that must be covered. Syllabus for trainings and workshops, as well as training materials, are typically defined and prepared by trainers. Materials are available at the workshops in hard copy format. When determining the programme, the Ministry takes into account proposals of IPs.

The working materials are prepared by trainers of each individual workshop. Two trainers prepare and hold a workshop. The trainers are determined by the Ministry primarily amongst judges, bankruptcy trustees from the List A, members of the examination committee and professors of law faculties and economy faculties. However, other experts who have relevant knowledge can also act as trainers.

After publishing of the annual program, the Ministry invites potential trainers to express their interest to act as trainers in workshops. The Ministry reviews the applications and determines the trainers.

According to the programme, the workshops should be held on Saturdays and Sundays, based on previously published schedule, in the premises of the Ministry in Zagreb, Ulica Grada Vukovara 49. However, we understand that the workshops are mostly held on Fridays. Interviewed IPs did not have objections about having workshops on weekdays.

Regarding the location where the workshops are held, IPs with residence in areas further away from Zagreb said that the workshops should be organised also outside the Zagreb area. IPs feel that education should be provided on the level of each commercial court or at least at the four largest commercial courts (Zagreb, Split, Rijeka and Osijek) and not only in Zagreb. Such concerns were not as intensive with the IPs located within a 2 hour drive from Zagreb. Also, IPs stressed that in applying for a workshop, they will give more value to the quality of the workshop than the location where it is held.

Therefore, it would seem reasonable that the more specific and advanced workshops are centralised in Zagreb (as they would target a smaller group of IPs), while general workshops focused on the more basic issues which would be relevant to a wider number of IPs, are organised and held at the four largest commercial courts.

According to the Ministry's programme, the workshops should last 7.5 hours each. We understand that duration of most workshops is around 7.5 hours, although there are exceptions.

Each trainer can hold maximum of two workshops a year. Although we understand that due to limited number of interested trainers or high interest in certain workshops, some trainers hold more than two workshops a year. The limit of two workshops per year does not seem reasonable, as some of the workshops may be interesting to a wider number of IPs and it would make sense to repeat them more than once in a year.

Trainers are evaluated by the attendants and if they are evaluated as unsatisfactory at one workshop, they will not be engaged again to hold workshops.

Participation costs per workshop are HRK 400 (approximately 55 Euro) and are paid by the IPs themselves.

Depending on the interest for a workshop and the number of applications received from IPs per workshop, the Ministry can modify the programme and/or and schedule of the workshops.

The Ministry issues certificate of participation to participants of workshops and keeps record on participation of bankruptcy trustees at workshops.

Based on good practice examples (for example, Auditors association in Croatia and ACCA in UK)⁴⁸, CPD could be improved as follows:

- materials for workshops should be made available to participants in advance;
- the process should be digitalised as much as possible (for example: computer-based trainings). There are more than one training methods, which include virtual instructors and classrooms, on the job trainings, web-based trainings, etc.
- there should be a better balance between theoretical part of education and business case analysis and practice.

3.6.3 Overview of the trainings for IPs

On average, there are 15 participants per training (Figure 20) and two trainings per month. Currently there are 320 active IPs. Since September 2017, on average, five trainings per month are organised (effectively every Friday), with approximately 10

⁴⁸ For more information please see Section 3.12 below.

participants (although there were workshops with up to 41 participants). Key stakeholders indicated that trainings with five to six participants are the most effective, with adequate balance between theoretical part and Q&A sessions. Based on our analysis, interest for trainings is increasing.

Figure 20

Number of trainings per month

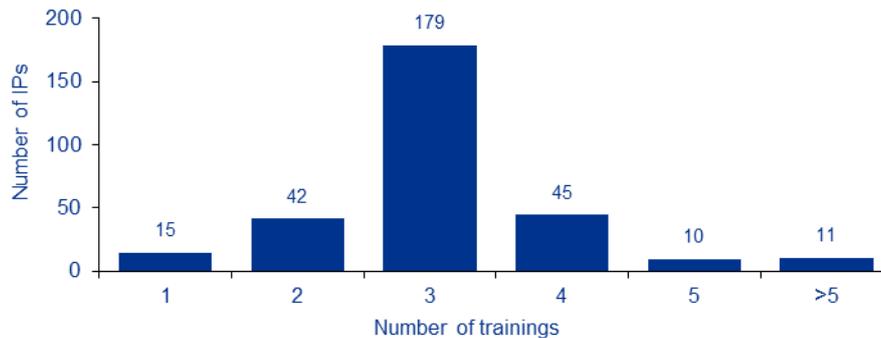


Source: Documentation received from MoJ

Regarding the trainings attendance, IPs largely fulfil their obligation of minimum two training in two years period. Approximately 6% (Figure 21) attend more trainings sessions than legally required.

Figure 21

Number of trainings per IP in 2016 and 2017

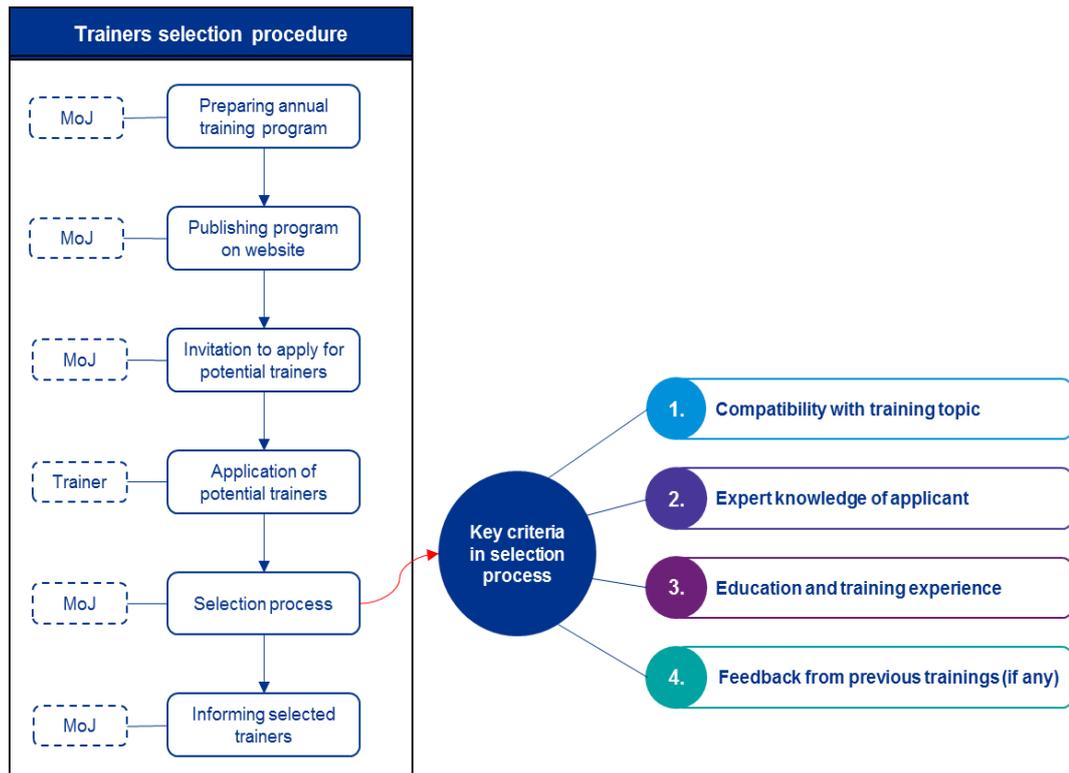


Source: Documentation received from MoJ

3.6.4 Trainers

Judges, IPs from the List A, members of the exam commission, professors, and experts in various fields (e.g. accountants) are typically selected as a trainers. Criteria to be selected as a trainer are: expertise, knowledge, training experience and feedback given from previous trainings (Figure 22).

Figure 22



Source: Web site of the Ministry of Justice

Most of trainers (16) held one training in period 2016 – 2017 (Figure 23). Two trainers held more than five trainings in the same period, i.e. more than two trainings per year (current rule limit is maximum 2 trainings per year).

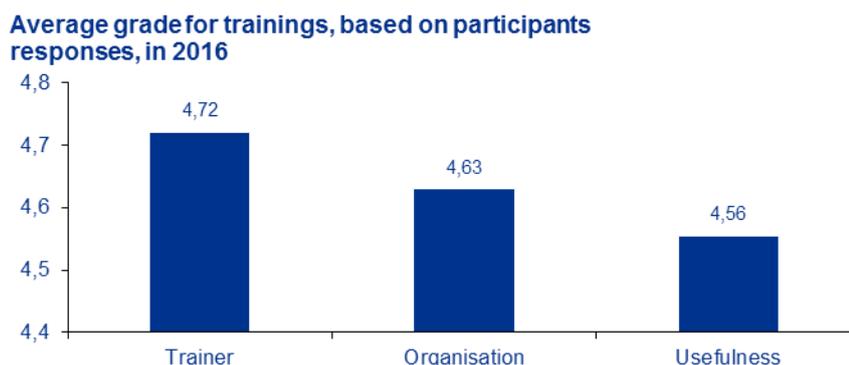
Figure 23



Source: Documentation received from MoJ

Training participants evaluated training sessions as excellent (Figure 24). Average grade of trainers engaged is 4.7 (grade 5 is the best grade).

Figure 24



Source: Documentation received from MoJ

It was suggested that the training for trainers would be beneficial. Particular focus should be made on assisting trainers in preparing the material for the workshops and with technical organisation of the workshops.

Also, training for trainers would help with unifying a curriculum and ensuring that the topics covered by different workshops do not overlap.

Since the IP CPD framework as organised by the Ministry is rather new in Croatia, it might be beneficial to organise trainings for trainers by foreign experts from countries with more experience in organising CPD of the IPs and/or to cooperate with other European IP regulatory bodies which organise training to further develop the Ministry's programme.

3.6.5 Educational needs of IPs

IPs have noted that the educational needs of bankruptcy trustees listed on different lists are not the same since the List B IPs are the most junior members of the profession. Also, the needs of IPs admitted to the List A may significantly vary as the difference in their experience may be significant (ranging from IPs who were only recently admitted to the List A to those who have many years of experience).

The education should be tailor-made to target the needs, the experience and knowledge levels of each group of bankruptcy trustees.

Specifically, the bankruptcy trustees listed on List B will require more general and theoretical training, as well as basic case study training to help them overcome the lack of practical experience in bankruptcies.

On the other hand, more experienced bankruptcy trustees listed on the List A will need more case study training with a greater focus on more specialised and specific skills (e.g. forensic skills required to challenge illegal actions of the debtor prior to opening of the bankruptcy, organisation of restructuring, etc.).

3.6.6 Objections to the current educational framework

While IPs believe that the current educational framework for IPs is a significant step forward and the efforts of the Ministry are generally much appreciated by IPs, they have suggested that certain improvements to the educational framework could be made.

Training should be tailor-made to suit the needs of the bankruptcy trustees. Since their needs may change from time to time, organisation of the training should be responsive and adaptive to the changing needs of the bankruptcy trustees. While the Ministry is constantly re-evaluating the courses and workshops it has previously organised and is asking IPs for their feedback, IPs feel that their associations could participate more in selecting the topics for the training to make the training more useful to them.

The main objections by more experienced IPs were that the workshops are sometimes limited only to going through the legislation to (re)acquaint the IPs with the applicable rules. IPs feel that the training should, instead, focus more on new information and knowledge of various skills which were not covered by their formal education or that are written in the legislation. This can be done through providing workshops which are more case study based and by making available written guidelines on various issues IPs may face (e.g. accounting, examination and challenging of claims, organisation of business operations of the debtor, etc.).

IPs have expressed their view that some of the organised workshops could be more interactive. However, interactive workshops imply that they should be organised for a smaller groups of attendees (e.g. up to 5 or 6 persons).

Also, IPs (in particular the less experienced IPs) often use the workshops as an opportunity to discuss practical issues that they had in their cases with the trainers (who are experts in the field) and their colleagues. IPs attending the workshops often have expectations that they will be able to discuss these issues, regardless whether the Q&A session is envisaged as part of the workshop and regardless whether their questions concern the topic of the workshop. While such questions and discussions can be useful and constructive, the questions asked by IPs often regard very basic issues

and are not useful for other participants who feel that the time at the workshop should be used more constructively.

Therefore, workshops should be more interactive and should involve IPs more in the activities during the workshops, while at the same time ensuring that the activities are focused at the issues relevant for all the attendees.

As an alternative for IPs who are interested in the discussion oriented workshops, it was suggested that workshops in format of roundtable could be organised where the trainers would act as moderators of the discussion rather than lecturers. Such workshops could also be more easily organised outside of Zagreb.

Furthermore, it was noted that most IPs attend only trainings that are mandatory to maintain their licence i.e. three training sessions of 7.5 hours during two years period⁴⁹.

3.6.7 IPs' associations

Currently, associations and organisations of IPs are informal and are organised by IPs themselves.

IPs believe that, if they were better organised into associations (with better funding and more members), such associations could be a useful platform to organise the exchange of experience and knowledge between IPs and aid IPs in everyday challenges that they face.

Also, such associations could then participate more actively in the organisation of workshops for the continuing professional development of IPs and provide more diversity in the organisation of the workshops.

3.6.8 Funding

To be able to improve the continuous professional development of IPs, it was also noted that more funds should be attracted and made available to the Ministry to be able to organise such workshops. Currently IPs are required to pay a fee of HRK 400 per CPD workshop and cover their costs of attendance (travel and accommodation expenses, if required).

⁴⁹ As regulated in the Programme of the Ministry of Justice for the Continuing Professional Development of IPs

The main focus should be on attracting the funding for the projects aimed at training of the trainers and organising projects aimed at sharing of experience between trainers and IPs in Croatia with their counterparts in other EU countries (e.g. by means of an EU Twinning project or a similar project).

Also, fee payable to trainers for designing and holding training in the amount of HRK 2,000 (approximately EUR 270) seems too low to motivate trainers to put more effort into designing new and innovative workshops and drafting adequate training materials. Ministry should either put more efforts itself in designing the workshops (which considering the understaffing at the Ministry and lack of other resources seems a difficult job) or it should pay trainers more to motivate them to put more effort in designing new workshops (which would require further funds).

The fee of HRK 2,000 seems particularly low as one trainer should not hold more than two workshops a years, which means that even if he/she repeats the same workshop twice he/she will still get only HRK 4,000.

3.7 Lists of IPs

The Bankruptcy Act classifies IPs into two groups (i.e. List A and List B) with the only difference being the work experience after the formal licensing.⁵⁰

IPs who have completed the work experience after being licensed and listed on the List B can be listed on the List A. Other IPs are listed on List B.

Apart from the professional training, other criteria are the same for both lists⁵¹

The Minister of Justice establishes the two lists of bankruptcy trustees for the jurisdiction of each court. A person may, however, be listed on a list for the area of jurisdiction of one or more courts. Once established, such lists may be updated and are made publicly available online via web-page of the courts notice board (Croatian: *e-Oglasna ploča*).⁵²

The list also contains indication of all pre-bankruptcy and bankruptcy proceedings a particular IP is appointed in as administrator, preliminary bankruptcy trustee and a bankruptcy trustee; indication of the manner of their selection; indication of the debtor

⁵⁰ Categorization of IPs is regulated by the Bankruptcy Act; the Rulebook on Determining Bankruptcy Trustee Lists and the Decision on Determining Lists of Bankruptcy Trustees.

⁵¹ For more information on licensing requirements, please see Section 3.5.2 above.

⁵² See the link <https://e-oglasna.pravosudje.hr/?q=popisi-obraci/8998>.

and the judge leading the proceedings as well as any decisions, reasoning to the decision and fines imposed to the IP.

Lists contain the following information on each IP: (i) name and family name; (ii) Croatian personal identification number (OIB); (iii) address, contact number and e-mail; (iv) information about education; (v) information on the professional IP exam; (vi) information on professional training of IP; (vii) work experience; and (ix) professional and scientific publications. However, it is questionable whether IPs are updating these information regularly.

Once listed, a person may be removed from the List at its request or *ex officio* (e.g. in case where he/she has been revoked from duty, if a criminal procedure is initiated against it, if he/she does not have proper professional liability insurance; if he/she does not deliver proof that he/she has attended required workshops for continuing professional development organised by the Ministry).⁵³

Stakeholders believe that there are significant discrepancies in knowledge and skills between different IPs who are listed on the same list.

The lists of IPs should contain also additional information on IPs. For example, the type of information could include the following with respect to the cases that the IP has led:

- the number of cases per each industry (e.g., tourism, transportation, metal industry, agriculture, etc.);
- the number of cases involving companies with a turnover exceeding a set amount;
- the number of cases involving companies with a total book value of assets exceeding a set amount;
- the number of cases involving companies with a number of employees exceeding certain number; and
- the average duration of insolvency proceedings where the IP was appointed;
- additional skills of the IP that could be demonstrated with a degree or a different documented proof (e.g., certified auditor, attorney at law, knowledge of foreign languages, court expert, etc.); and
- whether he is a full-time or a part-time bankruptcy trustee (i.e. is he pursuing another career in parallel with bankruptcy administration).

⁵³ Article 81 of the Bankruptcy Act.

Ideally, these would be in a form which would allow the computer-based system⁵⁴ to use such indicators in selecting IPs in each case.

Also, we understand that due to limits in types of insolvency procedures in which IPs listed on the List B can be appointed (i.e. they may not act as bankruptcy trustees in regular bankruptcy proceedings), IPs listed on List B are not motivated to report any assets of the debtor which underwent a summary bankruptcy proceedings (if they find any assets) for so long as they are not listed on the List A, as they would need to do a lot of preparatory work to find such assets, while another IP listed on the List A will be appointed in its place to liquidate the assets and take the fee for it. This may cause damage to the creditors, as appointed IP from the List B will be reluctant to take any actions for so long as it is listed on the List B. To create a fairer system, it was suggested by experienced IPs that the mentorship of IPs listed on the List B could be organised so that the IP listed on the List B can continue to be appointed as bankruptcy trustee in a regular bankruptcy proceedings (which follows summary bankruptcy proceedings in which he/she was appointed as bankruptcy trustee) but that he/she needs to be supervised by a mentor who would then be jointly responsible for his/her work while he/she is being mentored, and would be reimbursed for the work and liability assumed by being entitled to a part of the fee received by the bankruptcy trustee (e.g. 20% or 30% of the fee paid to the bankruptcy trustee). This may also be a good model to structure mentorship programmes for IPs listed on the List B as it would allow IPs to gain actual practical experience while, at the same time, being supervised and supported by their mentors.

Key areas for improvement of the lists of the IPs:

- The lists of IPs should contain additional information on IPs, which should be updated regularly and in a form which would allow the computer-based system to use such indicators in selecting IPs for appointments.

3.8 Literature

There is no formal literature aimed at education of IPs which could serve as the official literature for examinations during licensing process or later on for the trainings of IPs.

Currently, examination curriculum is the list of legislation currently in force in Croatia⁵⁵. EU insolvency legislation is not part of the examination curriculum and should be added

⁵⁴ Please see Section 3.3.6 for more details.

to the curriculum for IP exam. This primarily concerns the following EU legislation: (i) the EU Insolvency Regulation⁵⁶; and (ii) the upcoming directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures⁵⁷.

Drafting of a training handbook for IPs would be helpful for structuring the examination and training process and guiding IPs through the training. Such literature would particularly be helpful for candidates for IPs who have no legal training and who are not accustomed to reading legislative document.

Benefits of having such literature would not only be in helping candidates for IPs in preparing for the exam and guiding them through the mandatory professional training before being admitted to the List A. It would also assist IPs in early stages of their career as it would provide basic guidance as to what is expected of IPs in insolvency procedures.

Considering frequent changes in applicable legislation, any manuals or handbooks prepared for education of IPs will need to be frequently updated and revised. This, in addition to the fact that demand for such literature will not be high (currently there are approximately 320 active IPs in total in Croatia) makes drafting of such literature financially unprofitable to attract any private initiative in that field. Therefore, any initiative for drafting and updating of such literature should be on the MoJ.

In other countries (e.g. United Kingdom) there is good practice of publishing statements of insolvency practice to guide IPs⁵⁸. Such statements of insolvency practice (SIPs) are issued to insolvency practitioners by the regulatory bodies (i.e. are electronically available online) to promote and maintain high standards by setting out required practice and harmonising practitioners' approach to particular aspects of insolvency work. SIPs combine statements of the principles to be adopted with an explanation of key compliance indicators.

⁵⁵ Determined in accordance with Article 20 of the Rulebook on Professional Exam, Training and Education of IPs

⁵⁶ Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) [2015] OJ L 141

⁵⁷ European Commission "Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU" COM(2016) 723 final

⁵⁸ Available at: <https://www.r3.org.uk/index.cfm?page=1296> (07.08.2018).

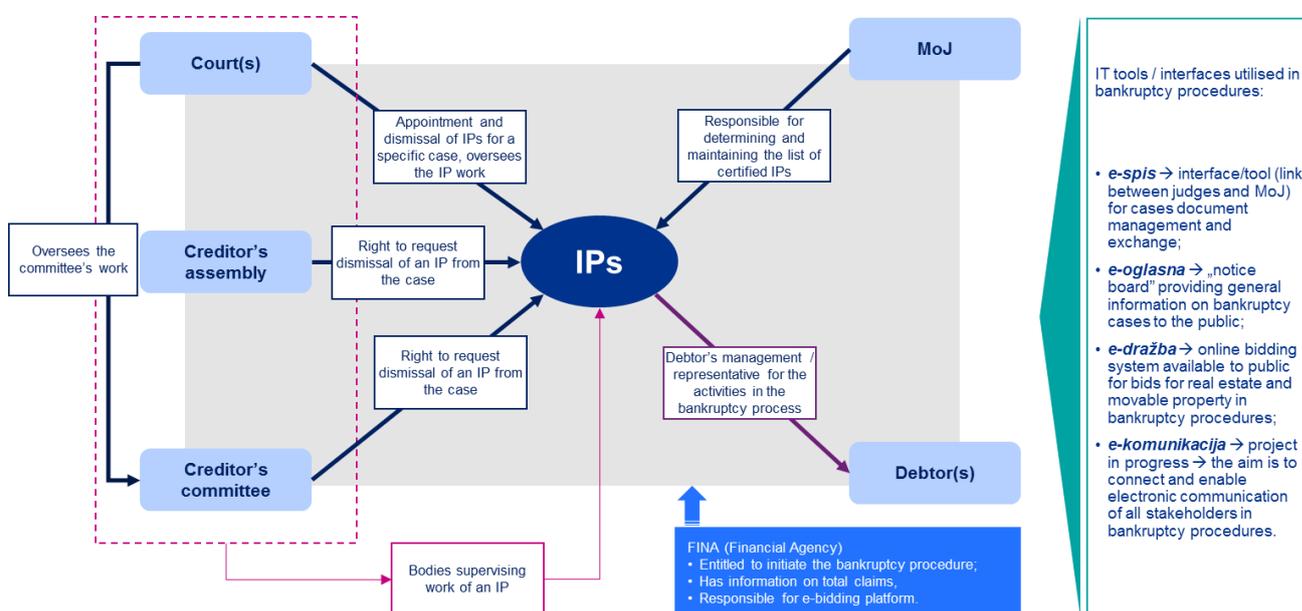
Similar approach would also be beneficial in Croatia, as SIPs could serve as guidance to IPs on how to proceed in situations which are being detected as challenging in practice.

3.9 Supervision of IPs

In Figure 25 below, is a illustrative overview of IPs within the "bankruptcy ecosystem", which includes, in addition to IPs, also the other key participants of bankruptcy proceedings, i.e.: (i) the bankruptcy debtor (bankruptcy estate); (ii) commercial court(s); (iii) creditors (represented by creditor's assembly and creditor's committee; (iv) the Ministry; and (v) FINA.

For illustrative purposes, we provide IPs operating environment:

Figure 25



Source: KPMG Analysis

Within such ecosystem, IPs are effectively supervised by courts, creditors and the Ministry. While courts and creditors supervise the work of IPs in respect to each particular case where the IP is appointed, the Ministry is responsible for supervising the IPs on a more general level.

3.9.1 Supervision by the Ministry

The Ministry is responsible for determining and maintaining the list of licensed IPs. This also includes regular (yearly) monitoring whether IPs listed on List A and on List B meet the criteria described in Section 3.5.2.

If a listed IP no longer meets the required criteria or has breached his/ her duties as an IP, he/she may be delisted by the Ministry. According to the Rulebook on Determining the IP Lists, an IP will be delisted from the List of IPs in following situations:

- death of the IP;
- he/she has committed or is being charged of committing a criminal offence which is prosecuted *ex officio*;
- if it was dismissed from appointment as a bankruptcy trustee in more than two bankruptcy proceedings in past three years due to breach of its duties (the information on such dismissals is sent by the courts to the MoJ);
- he/she fails to abide by courts order to return funds which he/she has received in an insolvency proceedings or is unreasonably withholding transfer of office and documents to another IP or is failing to file reports at the request of a court;
- he/she fails to furnish the MoJ each year with a proof that it has an insurance policy against professional liability;
- he/she fails to furnish the MoJ each two years with a proof that it has attended all required CPD workshops.

The Rulebook on Determining the IP Lists does not, however, contain any restrictions on a delisted IP reapplying to be listed. It should be considered that if an IP was delisted due to breach of duty, it should not be able to reapply to be listed for at least two years.

The Ministry, however, does not supervise how IPs handle insolvency cases in which they are appointed nor should it, as that could be seen as interfering in judicial proceedings. The Ministry is only responsible to ensure that minimum regulatory requirements are met (e.g. that IPs attended required number of workshops, that they have insurance policy, etc.), while the courts and creditors oversee IPs in performance of their duties in particular insolvency proceedings.

If recommendations to introduce a code of conduct for IPs⁵⁹ and professional statement or guidance on insolvency practice are adopted, the Ministry or any dedicated monitoring body or agency set up under the Ministry should be the one supervising that they are met.

To that extent, a monitoring mechanism should be adopted to ensure that the MoJ or any dedicated monitoring body or agency (if introduced) is able to collect relevant

⁵⁹ For more information on introducing a code of conduct, please see Section 3.9.5 above.

information on the conduct and performance of IPs. Monitoring tools may include checklists, templates and questionnaires.

Regular monitoring meetings between the IP and the dedicated monitoring body should be scheduled e.g. every 3-6 years and otherwise where necessary e.g. to investigate a complaint. Monitoring should be conducted with reference to the obligations of IPs pursuant to bankruptcy legislation and rules, a code of conduct for the profession and any professional statements or guidance on insolvency practice. Monitoring can take the form of "desktop monitoring" involving provision of information by the IP to the regulator and monitoring visits or meetings using a risk-based approach (which includes reviews of case files), together with the requirement to produce a written report of such monitoring visits or meetings. In between monitoring visits, IPs may be required to carry out self-certification reviews on a sample of cases selected on a risk-assessment basis. Prior to a monitoring visit, the monitoring authority may issue a pre-visit questionnaire requesting information regarding caseloads, sources of work, and procedures for complying with money laundering requirements and the code of ethics. Following the visit the monitoring authority may issue a report to the IP listing the key findings from the visit and a summary of each case reviewed and inviting the IP to provide feedback.

3.9.2 Supervision by courts and creditors

The work of IPs in each particular insolvency case is supervised by the court and the creditors (represented by the creditors' assembly and creditors' committee). They are entitled to request, at any time, notifications and reports from the bankruptcy trustees.

If the court finds that the bankruptcy trustee is not duly performing his/her duty, it may relieve him/her from the duty of the bankruptcy trustee in those bankruptcy proceedings.

Similarly, if the creditors are not happy with the way IP is handling the case, they may replace the IP with another IP. However, to be able to do that, creditors who want to replace the IP need to have a majority of votes.⁶⁰

Also, if the IP does not abide by an order of the court to fulfil its duty as envisaged in the Bankruptcy Act, the court may fine the IP with a monetary fine of up to HRK 10,000 (approximately EUR 1350)⁶¹.

⁶⁰ Articles 90 and 91 of the Bankruptcy Act.

⁶¹ Article 90(2) of the Bankruptcy Act.

3.9.3 Supervision by peers

Currently, there is no supervision of IPs by their peers. Considering that IPs are not organised into a chamber or in any kind of official organisation, such peer supervision is not possible at the moment.

At present there are informal associations of IPs, but membership in such associations is on a voluntary basis and they have neither the authority nor the capacity to supervise IPs.

In Croatia there are examples of peer supervision (e.g. supervision of attorneys at law by the bar association). However, unless membership in such association is mandatory or consent of such association is required to be licensed in a profession, it may not effectively supervise the work of any individual.

In the current regime, we do not see that meaningful supervision of IPs by their peers is possible. Nevertheless a centralised complaints system (see paragraph 3.9.4 below) should be a useful way of alerting the MoJ or any dedicated monitoring body or agency to instances of IP misconduct, triggering a potential investigation.

3.9.4 Complaints and sanctioning regime

Complaints resolution mechanisms and sanctioning powers are an essential complement to supervision of the IPs.

Other than collective option of the creditors in an insolvency proceeding to exercise their rights to supervise and remove the bankruptcy trustee, there are no other structured and elaborated procedures for stakeholders to complain against an IP to a regulatory authority.

The existence of a complaints system is closely connected to effective supervision and discipline. Complaints by stakeholders may highlight cases of mismanagement by the IP, which are not picked up by regulatory monitoring or by the court overseeing the insolvency case. A formal complaints system denotes a framework in which complaints

are addressed in accordance with a specified procedure and within a given time period.⁶²

The MoJ or a dedicated monitoring body or agency⁶³ (if introduced) should have an elaborated complaint procedure to assess and address any complaints raise against IPs. However, for this to be effectively implemented, further licensing requirements⁶⁴ and a code of conduct for IPs⁶⁵ will need to be introduced.

If the proposed EU Directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures⁶⁶ is enacted, the existing supervision system will likely need to be revised to ensure that the work of IPs is appropriately supervised and the sanctioning regime is both appropriate and effective.

Currently, in Croatia IPs can face following sanctions for misconduct of breach of duty:

- monetary fine up to HRK 10,000 for breach of duty in individual insolvency proceedings⁶⁷;
- dismissal from an individual insolvency case⁶⁸;
- removal from the List of IPs⁶⁹;
- criminal liability in case of committing a criminal offence (e.g. giving or taking bribe in bankruptcy proceedings⁷⁰);
- misdemeanour liability in case of committing a misdemeanour in performing its duties (e.g. any misdemeanour offence committed by the bankruptcy debtor where bankruptcy trustee will also be sanctioned as a responsible person of the debtor).

In addition to these sanctions, a wider range of sanctions should be available for the MoJ or a dedicated regulatory body (if introduced, please see Section 3.9.7) including reprimands, warnings and fines, in addition to the existing power to remove the licence of IPs.

⁶² *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>.

⁶³ Please see Section 3.9.7 below.

⁶⁴ For more information on licensing requirements, please see Section 3.5.2 above.

⁶⁵ For more information on introduction of a code of conduct, please see Section 3.9.5 above.

⁶⁶ DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures.

⁶⁷ Please see Section 3.9.2 above.

⁶⁸ Please see Section 3.9.2 above.

⁶⁹ Please see Section 3.9.1 above.

⁷⁰ Article 251 of the Criminal Act (official Gazette of the Republic of Croatia nos. 125/2011, 144/2012, 56/2015, 61/2015 and 101/2017; Croatian: *Kazneni zakon*).

Also, a disciplinary committee should be established by the MoJ or a dedicated regulatory body (if introduced) to consider any allegations of IP misconduct. This should be supported by a disciplinary procedure.

3.9.5 Code of conduct

We understand that the Ministry has been considering introducing a code of conduct for IPs, which would govern certain minimum ethical standards for the IP profession.

According to EBRD cross-jurisdictional assessment of insolvency frameworks⁷¹, it is widely accepted that IPs should be subject to certain professional standards and ethical rules in the conduct of their activities. The EBRD Insolvency Office Holder Principles states that: "Standards are the most useful way of both establishing and measuring the level of performance expected of office holders."⁷²

A code of conduct may be implemented through primary legislation (by introducing mandatory requirement that all IPs abide by such code of conduct) and more detailed provisions included in secondary legislation.

Regardless of the approach taken, it is important that professional standards and ethics are recorded in written form and are binding on all members of the IP profession. In this way they can serve as a guide for IPs in the conduct of their professional activities and a benchmark for satisfactory performance.⁷³

Compliance with code of conduct rules should be included within the scope of regular monitoring and complaints procedures of the MoJ or dedicated regulatory body (if one is established) and a clear link should be established between breach of a code of conduct provision and sanctions for misconduct.⁷⁴

If the proposed EU Directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge

⁷¹ *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>

⁷² See Principle 6, www.ebrd.com/downloads/legal/insolvency/ioh_principles.pdf (last accessed on 07.08.2018).

⁷³ *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>

⁷⁴ *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>.

procedures⁷⁵ is enacted, the Ministry will be required to encourage the establishment of a code of conduct for IPs.

3.9.6 Managing conflicts of interest

In performing their duties as administrators or bankruptcy trustees, IPs may often find themselves in situations of conflicts of interest. These may be conflicts where the IP will personally be conflicted in insolvency proceedings (e.g. he/she is also a creditor of the debtor) or where two or more debtors where that IP is appointed in insolvency proceedings have opposing interests (often in case of parallel bankruptcy proceedings against affiliated companies).

Currently, any such conflict of interest is managed on a case by case basis in accordance with applicable rules governing insolvency proceedings.

While current conflict of interest framework seems to be adequate, it may be further reinforced with introduction of code of conduct which would further elaborate the standards of how the conflict of interest is managed, including in situations where there is no need for an IP to step down from an appointment in insolvency proceedings.⁷⁶

3.9.7 Dedicated regulatory body

Regulation of the IP profession is very important given the role of IPs and the duties they perform in insolvency proceedings. Supervision of the IP profession is one of the key components of well-regulated IP framework.

However the regulatory system for the IP profession in many countries is weak, with little time, resources and effort devoted to the activity of regulation outside of individual insolvency proceedings.⁷⁷

According to the EBRD cross-jurisdictional assessment of the IP profession⁷⁸, a dedicated regulatory body for the IP profession, such as a state agency or self-

⁷⁵ DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures.

⁷⁶ For more information on adopting of a code of conduct, please see Section 3.9.5 above.

⁷⁷ *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>

regulatory association, is more likely to be an active regulator than a non-specialised ministry, without the necessary human and financial resources and, possibly, experience to oversee the IP profession.

While establishing a dedicated regulatory body requires upfront investment or funding, it may provide the most clear and efficient model for regulation, since it constitutes a central point of authority for IPs and facilitates a coordinated approach to the supervision and discipline of IPs. A dedicated regulatory body provides, in other words, a form of "infrastructure" for the profession.

Non-dedicated regulatory bodies with regulatory powers of oversight, such as the MoJ, are unlikely to have the necessary human resources to focus on day-to-day regulation of IPs. They may, therefore, conduct more "reactive" monitoring and supervision of IP activities and rely to a significant extent on the courts to supervise IPs. Nevertheless as an intermediary step the relevant government Ministry may, as in the case of Slovenia, set up a department which is responsible for licensing, supervision, and monitoring of IPs.⁷⁹

The EBRD Assessment Report has stressed Serbia and its Bankruptcy Supervision Agency (Serbian: *Agencija za licenciranje stečajnih upravnika*)⁸⁰ as a good example of how to organise a dedicated regulatory body. The Serbian model suggests establishing a special dedicated regulatory body (e.g. self-regulatory association, state agency) which acts as the central point of authority and supervision of IPs. In the table below (Table 1) is a comparative analysis of how some of the neighbouring countries have organised their dedicated regulatory bodies.

⁷⁸ *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>

⁷⁹ In Slovenia the Ministry of Justice department is made up of five persons with legal backgrounds and two administrative assistants. The department sub-contracts one accountant to supervise the economic/accounting related activities of insolvency practitioners. All disciplinary proceedings for misconduct are brought by the Association of IPs following a referral by the Ministry.

⁸⁰ For more information on Serbian Bankruptcy Supervision Agency, please see: "http://alsu.gov.rs/en/agencija/".

Table 1

Country	Regulatory body (authority)	Supplementary regulator
Serbia	Bankruptcy Supervision Agency, under the Ministry of Economy in Serbia, is in charge of supervision over the work of IPs and a uniform (standardised) assessment of their performance. It runs regular inspections at least once every 3 years. Also, in case of misbehaviour it can issue different types of sanctions (e.g. warnings, fines, suspension and cancellation of permission to act). Furthermore, Bankruptcy Supervision Agency runs a complaints procedure.	Court can assess work of IPs, and, if needed dismiss it from specific case.
Romania	Self-regulating professional association - National Union of Insolvency Practitioners (UNPIR) with key activities: <ul style="list-style-type: none"> • Establishing and maintaining the legislative framework necessary for the development of IP activity, • Promoting confidence in insolvency proceedings and IP's activities, • Ensuring fair competition between IPs and combating unfair, abusive and fraudulent practices on the insolvency market, • Ensuring transparency and information on the insolvency proceedings market, • Ensuring the application of honest practice standards. Membership of UNPIR is required for all practising IPs.	Courts impose sanctions on IPs for misconduct and/or determine the outcome of sanctions administered by UNPIR. Romanian Ministry of Justice does not retain any regulatory powers in relation to the IP profession.
Slovenia	Supervision and sanctioning power is divided among the courts, Chamber of Insolvency Administrators and the Ministry of Justice. This leads to a situation in which none of them exercises an effective supervisory role. Complaints can be filed with the court, the Ministry of Justice or the Chamber of Insolvency Administrators. However, there is no centralised complaints procedure. Nonetheless the Ministry of Justice in Slovenia has established a department of seven persons responsible for licensing and supervision and monitoring of IPs and enforcement officers.	
Latvia	The Insolvency administration is a state agency that performs supervision of the IPs, operates complaints system and may request information and explanations from IPs. However, there are no legal requirement for the regular monitoring or supervision.	Courts assist Insolvency administration in supervision of IPs and may suspend or dismiss IPs from specific case. Latvian Association of Certified Administrators has the power to revoke the licence from IPs.

Hungary	Ministry of National Economy (the Administrative and Judicial Office).	Hungarian Association of Insolvency Office Holders is a voluntary association which prepares code of ethics, which is binding to its members. Also, it examines any complaints regarding IP conduct.
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Source: Updated country profiles for Serbia, Romania, Slovenia and Latvia (2016) for Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>; Republic of Slovenia: Selected Issues Paper, IMF Country Reports 15/42; web site of Bankruptcy supervision agency, 2018, at: <http://alsu.gov.rs/en/agencija/>, web site of UNPIR, 2018, <https://www.unpir.ro/despre>

Implementation of recommendations made in in this Report (including in particular on trainings, CPD, publishing of statements of insolvency practice and other literature, supervision and sanctioning of IPs) will certainly require that the competent authority has sufficient staff and resources and that it is dedicated on a full time basis to overseeing IP framework. Whether this will continue to be a department within the MoJ or a separate state agency is not that relevant, so long as it will have sufficient staff and resources to do the job.

3.10 Incentives for restructuring in bankruptcy

Practice has shown that liquidation of companies is a preferred model of dealing with bankrupt companies. Although bankruptcy legislation allows restructuring to be conducted also in bankruptcy proceedings, there have been only few examples of successful reorganisations in bankruptcy and/or financial restructurings in Croatia.

Many argue that there would be more cases of attempted restructurings in bankruptcy if there were more initiative (and financial support) from creditors and if the additional workload imposed on the bankruptcy trustee were adequately rewarded.

Without the support of the majority creditors, restructuring in bankruptcy is not possible, as (i) creditors need to approve the bankruptcy plan and (ii) IPs will in most cases lack the necessary resources to prepare and organise the restructuring process (prepare business plan, restructuring plans, coordinate different creditors, etc.) without the support of expert consultants which they usually cannot pay from the bankruptcy estate (i.e. creditors will need to advance these costs).

Secured creditors (who usually have the majority of votes in the assembly of creditors) are often sceptical about restructuring as a way of dealing with bankrupt companies.

They find it easier to proceed directly with the sale of the whole bankruptcy estate in order to liquidate the debtor's assets and settle their claims (as they have priority in settlement) rather than risk with the restructuring process.

Legislative reforms, in and of themselves, will not necessarily change the creditors' attitude towards restructurings. However, many believe that creditors would have more faith in the restructuring processes if the prerequisites for successful restructurings were set in place (primarily if bankruptcy is opened as soon as company becomes financially distressed and if IPs had better skills required to successfully organise the restructuring process - as explained in Section 3.3.2(xiv)).

However, debtors tend to actively delay commencement of bankruptcy proceedings, even when they have been insolvent for years. This negatively affects the chances of successful restructuring, as the debtor that continues to operate while being in financial difficulties usually neglects the regular maintenance and upkeep of its assets (hence their value is reduced), is losing business and is usually unable to service its debts regularly (steadily increasing the total outstanding debt).

IPs believe that IP's work preparing for a restructuring is not appropriately compensated. Namely, the preparation and monitoring of the implementation of the bankruptcy plan means significantly increased workload for the bankruptcy trustee in comparison to the liquidation of the bankruptcy estate. If fees payable to bankruptcy trustees are proportionally higher for restructurings, thus honouring the additional work by bankruptcy trustees, bankruptcy trustees would be more incentivised to proceed with restructuring⁸¹.

It is much easier for bankruptcy trustees to simply proceed with selling the bankruptcy estate. In this way they can at least ensure that the funds (proceeds of the sale of the bankruptcy estate) for their fees will be paid.

3.11 International best practices

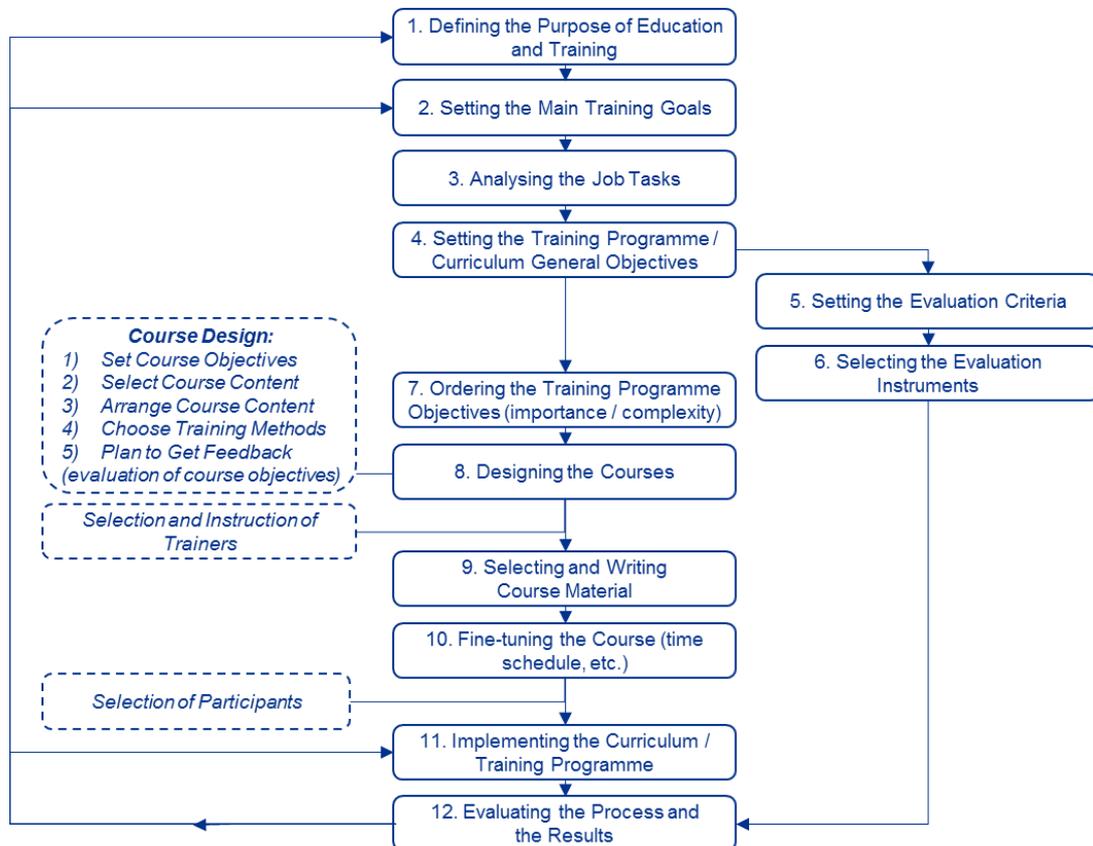
International practices (in EU, UK and Croatia, as described in more detail in this Section 3.11) and KPMG methodology (please see Figure 27 and Figure 28) focus on best practice approach in organising and conducting trainings and workshops. The European Judicial Training Network (EJTN), illustrated on Figure 26, is designed on these three main principles:

- any training programme should be needs oriented.

⁸¹ For more information on remuneration of IPs, please see Section 3.13 below.

- any training programme should make use of a variety of training formats. The approach should be "tailor-made".
- needs-oriented planning should be incorporated in a general conceptual framework.

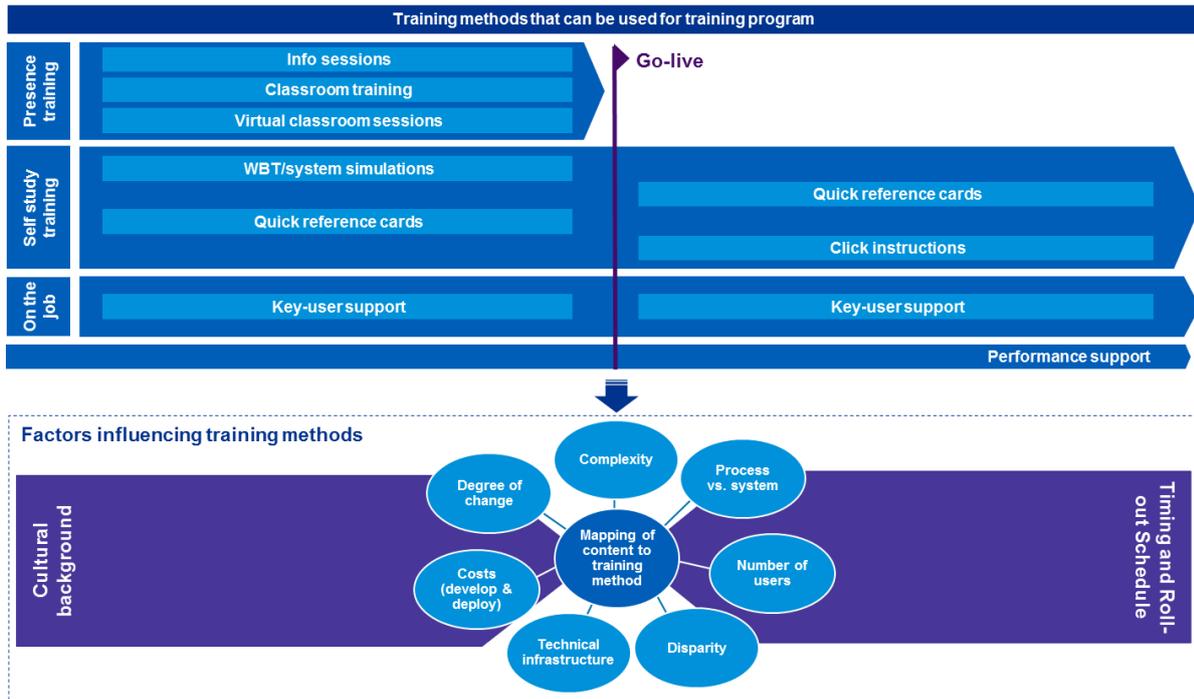
Figure 26



Source: European Judicial Training Network (EJTN): *EJTN Handbook on Judicial Training Methodology in Europe*, January 2016, available at: http://www.ejtn.eu/Documents/EJTN_JTM_Handbook_2016.pdf

KPMG training approach for training programme and types of learning platforms are illustrated on Figure 27 and Figure 28.

Figure 27



Source: KPMG analysis

Figure 28

<p>Instructor Led Training (ILT)</p> <ul style="list-style-type: none"> — Suits moderately complex to very complex material — Allows for hands on practice in the system — Recommended for centrally located user populations — Can be expensive to deliver to a dispersed audience — Recommended maximum class size is 30 	<p>Virtual Instructor Led Training (VILT)</p> <ul style="list-style-type: none"> — LiveMeeting training with real-time desk top sharing, data, application, voice and video sharing capabilities — Sessions can be recorded to be reused — Suits moderately complex to very complex material — Allows interaction with a trainer without requiring travel — If delivering live, consider limiting class size to 30 to increase interactivity 	<p>On the Job (OTJ)</p> <ul style="list-style-type: none"> — Highly interactive, convenient, delivered just-in-time — Allows interaction with a trainer, using the regular or existing workplace tools, documents, knowledge and skills necessary for an end user to learn to effectively perform his/her job. — Limited class size of less than 5 depending on interactivity 	<p>Web Based Training (WBT)</p> <ul style="list-style-type: none"> — eLearning: Self-paced training that includes media in the form of text, image, animation and magnitude, streaming video and audio. — Convenient, just-in-time on demand — Can be boring, risk of learner distraction — Suits simple to moderately complex transactions & processes

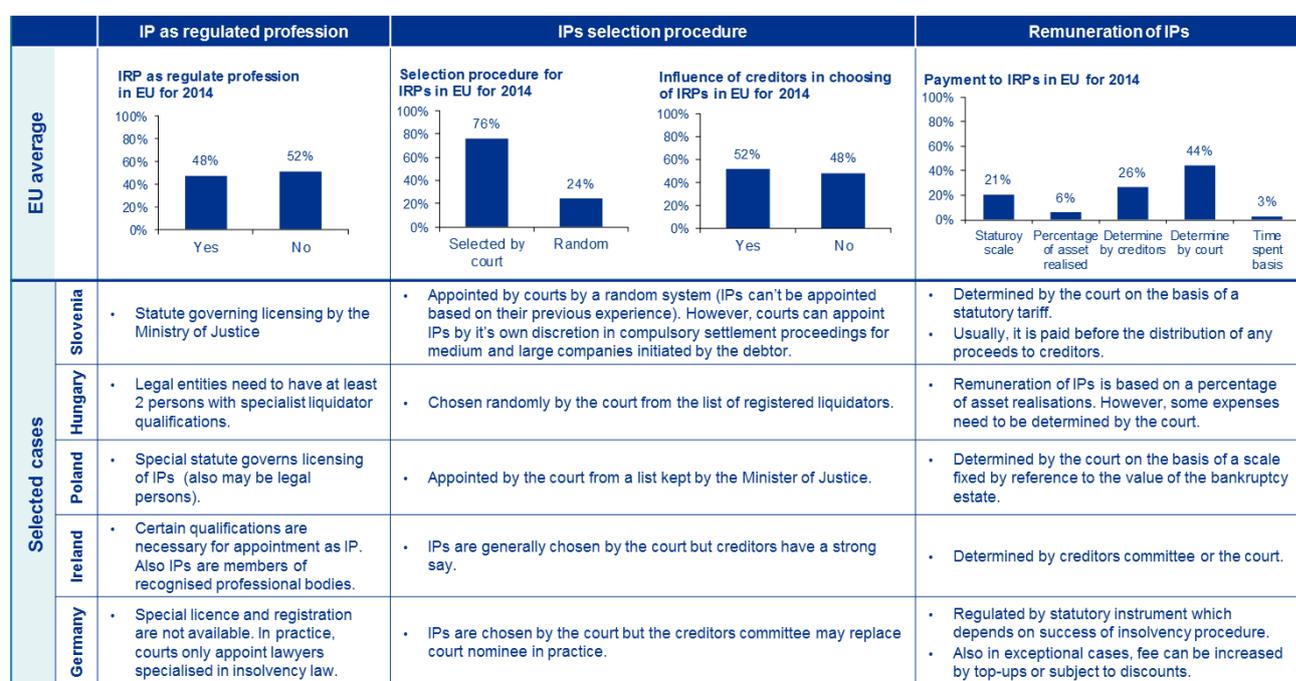
Source: KPMG analysis

3.12 Selected EU cases analysis

Based on feedback received from the key stakeholders, IPs performance may be improved by defining IP as a profession, i.e. registered as such, similarly to public notary model.

The European Commission has analysed IPs in peer/relevant countries (Figure 29), i.e. comparing level of regulation, process and remuneration approach. In this respect, in the majority of the 28 EU countries, IPs are still not regulated as a profession. Most of EU countries (76%) selects IPs directly, i.e. court / judge are responsible to select IP for a case. In most EU countries, creditors are consulted in selecting the IP. Finally, remuneration scheme for IPs in EU is determined by court in 44% of cases, in 26% cases by creditors and in 21% remuneration is regulatory defined.

Figure 29



Source: European Commission, Study on a new approach to business failure and insolvency: Comparative legal analysis of the Member States' relevant provisions and practices, January 2016, available at: https://ec.europa.eu/info/sites/info/files/insolvency_study_2016_final_en.pdf; Updated country profile for Slovenia (2016) for Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>

Also, more stringent rules for licensing should be considered. We have analysed good practice business cases (local and international) and believe that establishing stricter rules for licensing and requiring some knowledge and skills as a prerequisite is necessary. Since IP profession in Croatia does not impose exclusivity (similarly to

majority of neighbouring countries), requiring relevant working (hands-on) experience in bankruptcy and insolvency relating fields (i.e. legal background, notary, accounting, tax, business investment, due diligence, etc.) in the process of licensing should be considered. Such approach would lead to licensing professionals with at least basic understanding of the existing framework and necessary business knowledge. At the same time requirement of specific number of working experience within one of the relating fields would limit individuals applying for IP profession out of questionable reasons (e.g. long unemployment, potential for extra earnings).

In this respect, we focused on two specific case studies (one best practice example in Croatia and in United Kingdom), i.e.:

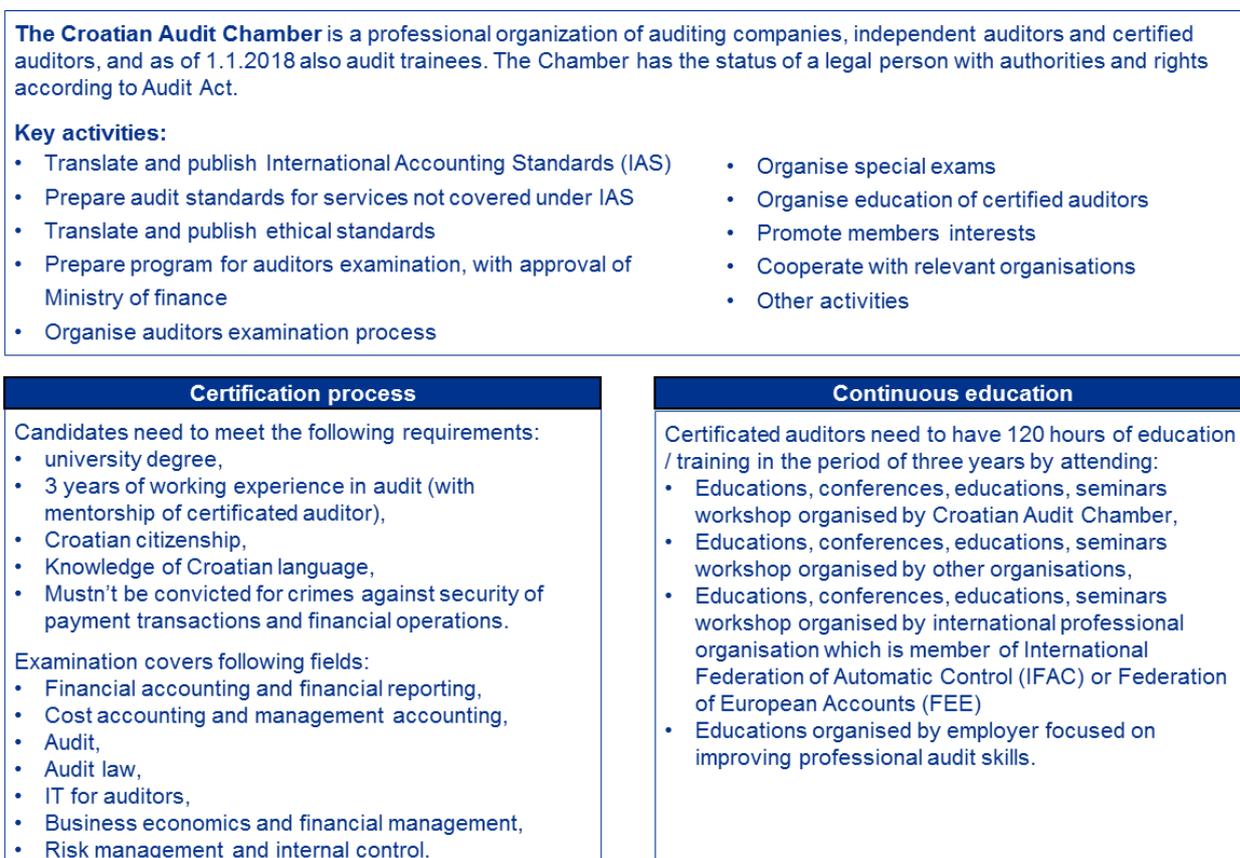
- Case study 1: Croatian Audit Chamber;
- Case study 2: ACCA ([Association of Chartered Certified Accountants](#)) insolvency licence in UK.

(i) Case study 1: Croatian Audit Chamber

The necessary pre-requirement for an audit certificate is minimum three years of experience in auditing financial statements (under mentorship of certified auditor) so to have at least three years of experience in real-life audit cases before being certified as an auditor.

In addition, newly certified auditors are required to attend ongoing education, i.e. at least 120 hours of education during the three year period, minimum two trainings / workshops annually (15 hours annually and approximately minimum 45 hours during three year period). For more details, please refer to Figure 30.

Figure 30



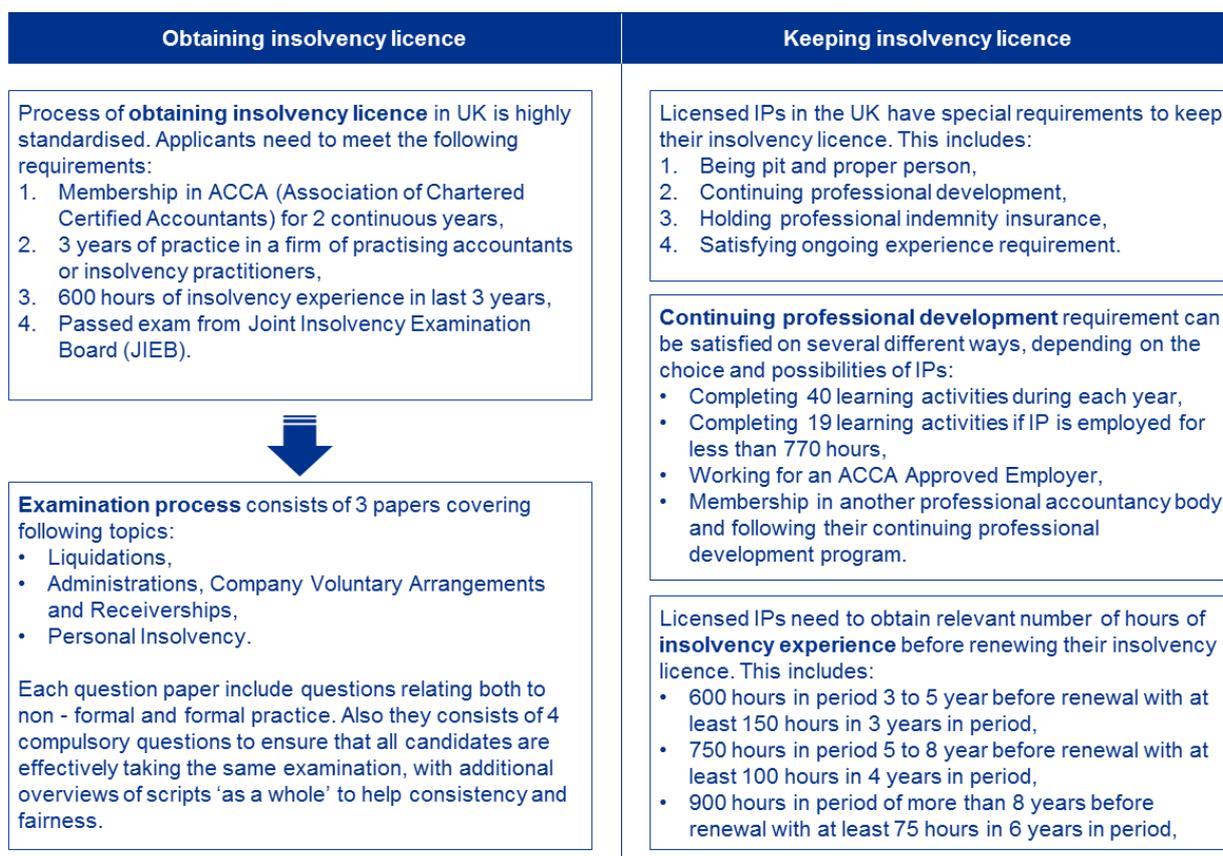
Source: Croatian Audit Chamber website

(ii) Case study 2: ACCA insolvency licence (UK)

Candidates applying for an IP licence need to be a member of a recognised professional body (in line with the Insolvency Act), e.g. chartered accountants, insolvency practitioners association, etc. Here is provided an example of ACCA insolvency licensing procedure as one of international best practice model.

The process of licensing and examination is highly standardised, with significant advance requirements. For more details on the process of obtaining (and maintaining) the ACCA insolvency licence, please refer to Figure 31.

Figure 31



Source: ACCA Insolvency Licence website

For comparison, best practice IP licensing examples include the following:

- for a specific role (e.g. auditor, ACCA insolvency practitioner), working experience in relevant field is required (three or more years);
- training/education for obtaining the licence is longer and more comprehensive, if than currently for IPs in Croatia;
- post-licensing training (continued learning) is, again, more extensive than in Croatia for IPs with minimum 40 – 50 hours of training sessions per year;
- training/knowledge areas includes business, ethics, risk knowledge, etc.

3.13 Remuneration

Both the EBRD⁸² and the European Commission have identified remuneration as a key factor in developing the IP profession. In particular the European Commission has linked fees charged by IPs to the possibility for "timely and efficient resolution of procedures".⁸³

How IPs are remunerated for their work significantly affects whether the profession is attractive for prospective IPs and, as such, can have a measurable impact on the development of the IP profession.

If remuneration is insufficient, professionals may not be incentivised to join the profession. A competitive level of remuneration or professional compensation is therefore essential for the development of profession.

The remuneration system is also relevant for the creditors as fees of IPs are paid from the bankruptcy estate before settlement of claims of unsecured creditors.

In Croatia, the remuneration system of IPs is set out in the Decision on Criteria and Method of Calculation and Payment of Fees to Insolvency Practitioners. In each case the court determines the amount of the fees payable to an IP on the basis of criteria explained in the Table 2 below.

⁸² *Assessment of Insolvency Office Holders: Review of the profession in the EBRD region, 2014*, at: <https://www.ebrd.com/cs/Satellite?c=Content&cid=1395238712341&d=Mobile&pagename=EBRD%2FContent%2FContentLayout>

⁸³ Article 27 of European Commission, "Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU" COM(2016) 723 final.

Table 2

Type of insolvency proceedings	Fee	Amount of the gross fee (HRK)	Source of funds	Criteria for determining fee
pre-bankruptcy	lump sum fee	3,000 - 20,000	Debtor	complexity of the work of IP
preliminary bankruptcy proceedings	lump sum fee	3,000 - 20,000	advanced costs / bankruptcy estate	complexity of the work of IP
bankruptcy (liquidation)	fee	on the basis of a scale (max 630,000)	bankruptcy estate	value of liquidated assets
	additional fee	max 150,000	bankruptcy estate	level of recovery by creditors and additional efforts invested by the IP
	special fee	100 per examined claim (max 15,000)	bankruptcy estate	number of examined claims exceeding the threshold of 500 claims
Bankruptcy plan	fee	on the basis of a scale	bankruptcy estate	(i) value of the bankruptcy estate (ii) 20% higher fee is payable if bankruptcy plan is agreed within six months as from opening of bankruptcy
	fee for supervising implementation of the bankruptcy plan	3,000 - 30,000 per year	debtor	complexity of the work of IP

Given the often divergent interests of IPs and creditors with respect to remuneration, in most cases they have differently reported on the appropriateness of the current remuneration system.

While creditors whose recovery rates in Croatia are rather low feel that IPs fees should be capped at lower amounts, IPs feel that the remuneration for their services is insufficient considering the workload imposed onto them. This is particularly the case since IPs will not be remunerated in all insolvency proceedings in which they were appointed (as remuneration is dependent on the value of the bankruptcy estate and possibility to liquidate assets). Accordingly IPs see "higher" fees achieved in some of the cases as compensation for all other cases in which they invested a lot of efforts, but due to the nature of those cases, they did not receive a fee which would be appropriate to the workload.

IPs have particularly reported that they are in most cases not inclined to propose restructuring of the debtor in bankruptcy as they feel that, in most cases where restructuring would be appropriate, they can achieve same fee with less efforts if they simply liquidate the assets. Therefore, it should be considered whether to introduce further remuneration mechanisms (e.g. envisage an option for creditors to agree to pay an additional bonus for successfully concluded bankruptcy plans) to motivate IPs to support bankruptcy reorganisation where that would be appropriate.