Impact of Prospectus Directive on Croatian Capital Market Act

Čulinović-Herc, Edita

Edita Čulinović Herc
University of Rijeka, Faculty of Law, Rijeka, Croatia

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Key words: public offer of securities, prospectus, European law, Croatian Capital Market Act, joint stock company, emission of shares

ABSTRACT

In order to facilitate widest possible access to European capital market a complete renewal of the Community provision on prospectuses is called for. Therefore Listing Particulars Directive from 1980, was recently replaced by Directive from 2001 and Public Offer Prospectus Directive from 1989 is in now in parliamentary procedure. The main changes incorporated in Directive amended proposal are: introduction of enhanced disclosure standards in line with international standards for the public offer of securities; introduction of special Community rules for securities designed to be traded by professionals; introduction of new prospectus format for frequent issuers and duty to update the information on issuers at least once a year; replacing concept of mutual recognition of the prospectus by concept of simple notification of the prospectus approved by the home competent authority and extensive use of "comitology". In the light of current trends in European law, Croatian legislator should reconsider re-implementation of criterion of nominal value of the issue. Issues targeted only to qualified investors should be treated separately. Newly proposed format of the prospectus should be examined and wider use of information technologies should be encouraged.

1. INTRODUCTION

The leading idea of the modern market is the protection of investors. By observing this principle in the narrower context - that is the context of securities issued by joint stock companies - one can transform it in the protection of the shareholders on one hand and protection of company's creditors on the other, since both categories could be considered as "investors" in the wider sense. Here, two dimensions of investor protection should be differentiated.

The first becomes prominent while deciding whether to invest or not in company's shares. In that phase the investor has to be given insight to all relevant data about the joint stock company. The main instrument enabling this evaluation is prospectus. The prospectus is a document published by the issuer of securities, which must contain all information necessary to enable investors to make an informed assessment of the assets

and liabilities, financial position, profit and losses, and prospects of the issuer and the rights attaching to securities.[1] In fact it is identity card of the issuer. Hence, such information, which needs to be sufficient and as objective as possible concerning the financial circumstances of the issuer and the rights attaching to the securities, should be presented in an easy analyzable and comprehensible form.[2]

Croatian law essentially differentiates IPO (Initial Public Offering) prospectus[3] from the listing prospectus, the second being issued when securities are admitted to trading / admitted to official listing on the stock exchange[4]. There is also an abridged prospectus, when issue is not public but rather targeted to private investors. Subject matter of this paper is public offer prospectus, primarily its mandatory contents, approval and publication. But also other legal issues deserved the attention as e.g. placements with foreign element, the question of so called exempted placements, and especially the question of liability arising from the prospectus. All these issues are covered on the cross-reference basis, in order to enable comparison between Croatian and European point of view. Speaking about European law, author refers not only to the existing rules but also taking into account forthcoming harmonization instruments.

2. STATE OF THE ART IN EUROPEAN AND CROATIAN LAW

If one have in mind investor's protection when investing into company's shares, it is obvious that those rules, especially one on disclosure could partly be found in company law but also in capital market law. Or if we put it in another way a hearth of disclosure is prospectus, and disclosure is at the crossroad between company and capital market law. Since these two bodies of law sometime overlap, there is a need for the conflict of law rules, in order to answer which body of law would take a precedence.

Mandatory content and publication of prospectus for the each issuer, being joint stock company or not, are regulated in the Law on Securities Market (hereinafter: LSM) which has recently replaced the Law on the Issuance and Sale of Securities. This body of law is *lex generalis* for issuance of all kind of securities /issuers. Besides that, issuance of prospectus during so called successive foundation of joint stock company is regulated by Company Law (hereinafter: CL) which is the *lex specialis* for that particular emission of shares. Moreover, art. 32. LSM goes on when regulating what particular issues of the joint stock companies are exempted from duty to prepare the prospectus.

As far as European Law is concerned, two directives are in force, one relating to "listing prospectus" and the other relating to "public offer prospectus". By adopting Directive 2001/34/EC of the European Parliament and Council of 28 May 2001 on the admission of securities to official stock exchange and on information to be published on those securities, four former directives (with later amendments) were codified into

[1] Art. 20 LSM; art. 5/1 of the 1989 Directive
[2] čl 5/2 of the 1989 Directive
[3] čl.20. LSM
[4] čl.96/1 i 114/3 LSM

single one.[5] On the other hand, the Council Directive 89/298/EEC of 17 April 1989 coordinating the requirements for the drawing up, scrutiny and distribution of the prospectus to be published when transferable securities are offered to the public is still on force but substantial novelties will be introduced when new proposal will be adopted. When it comes into force it will provoke numerous implementing measures due to the new legislative technique that has been used.[6]

The reasons for the reform of European Law lay in the fact that the 1980 and 1989 Directives acknowledged the system of so called partial and complex recognition of prospectus between member states, which has put aside the idea of "single passport" prospectus. Single passport prospectus means prospectus suitable for cross-border circulation once it was approved by the competent domestic authority. On the basis of such a prospectus it should be possible to raise the necessary capital by means of a public offer in any of the member states. Consequently, the European legislators have considered necessary to extend the same system, adapt it to the current situation in time and incorporate it in one unified regulation.[7]

Amongst actions undertaken prior to the making of the Directive proposal the work of the Committee of Wise Men[8] appointed by the EU Council should be given and important place. In its initial report the Committee stressed out the lack of an agreed definition of public offer of securities with the results that the same operation is analyzed as a private placement in some Member States and not in others. According to the Committee's opinion, the current system discouraged firms from raising capital on an European wide basis and therefore from having real access to a large, liquid and integrated financial market.[9]

In its final report, the same Committee proposed the introduction of new legislative techniques named as "four level legislative technique". Namely, Level 1 encompasses the adoption of a set of framework principles. Level 2 is composed of an actively functioning network of national securities regulators, the European Commission and a new European Securities Committee to define, propose and decide on the implementing details of framework Directives and Regulations, determined in Level 1. Level 3 denotes strengthened cooperation among regulators during implementation. Finally, Level 4 consists of enforcement. In the directive proposal this "four level" approach is reflected in the way that Level 1 regulates the prospectus, the definition of public offer, the competence and authority and the issue of language, whilst all technical details and definitions of what is considered a detailed content of the prospectus (as per example is the content of prospectus for each specific kind of

[5] Council Directive 79/279/EEC (Listing Directive),
Council Directive 80/390/EEC (Listing Particulars Directive)
Council Directive 82/121/EEC (Interim Reports Directive)
Council Directive 88/627/EEC (Major Holdings Directive)

[6] Proposal for a Directive of the European Parliament and of the Council on the prospectus to be published when securities are offered to the public or admitted to trading, COM (2001) final 2001/0117/(COD); last change: COM(2002)460 final.

[7] About other trends in European Law regulating financial markets see: HOPT, K.J., *Europäisches kapitalmarktrecht - Rückblick and Ausblick*, in: Systembildung und Systemlücken in Kerngebieten des Europäischen Privatrecht, Mohr Siebeck 2000, p.324-327.

[8] The initial report was presented on 9 November 2002. The final report was presented on 15 February 2003. About other important segments of legislative activity in the European Law and particularly on timetable of their realization see: O'KEEFE/CAREY, *Financial Serveces and Internal Market*, in: FERRARINI/HOPT/WYMEERSCH (eds.) Capital Markets in the Age of the Euro, Kluwer, 2002, p. 9-13.

[9] Preambule of the Directive, under 3.

financial instruments, or the rules about advertising the prospectus) are regulated on the second level (so called comitology).

The latest modification of the Directive proposal has introduced a new set of rules for securities traded between institutional investors. There is no need for prospectus publication when an offer is made to qualified investors. Furthermore, the rules on prospectus advertising are not applied and in the case of application for admission of securities to trading on regulated market, the content of the prospectus is adapted to the trading of the qualified investors. Particularly, there is no need to make the summary of the prospectus. In order to draw the effective line between the market rules for professionals and the market rules for retail investors, taking into account that both are guarantied access to the exchange, the criterion of total nominal value of the emission has been introduced. When the total nominal value of emission exceeds a certain sum, more flexible approach towards institutional investors in needed. This does not affect the interests of retail investors.

The realization of single passport prospectus idea is based upon the abandonment of mutual recognition system and simultaneous adoption of the prospectus notification system. This means that approval of the prospectus is given to the issuer by the competent authority of the member state. In the case of a transnational public offer or in the case where the issuer seeks admission of the security on a regulated market in another member state, prospectus once approved, is accepted in all member states. The newly introduced notification system foresees that the competent authority of the member state in which the prospectus was initially approved notifies the competent authority of the member state in which application has been made for a public offer or the admission of the security to trading on regulated market has been sought.

The headline news of the Directive proposal is the introduction of the prospectus registration system on the Community level. In addition to the registration system, several new prospectus formats are introduced. A new prospectus can consist of one or separate documents. The first part of the prospectus is called the registration document and it consists of the information about the issuer. The second part is "securities note" and it consists of the data about the security. The summary of these two documents is provided for in the *ad hoc summary note.* This system considerably quickens the approval procedure of the new emissions. This is because in the case of a new emission only novelties are to be entered into the registration document once it has been approved, so the prospectus examination in the case of new emission is limited to the securities note. In accordance with the duty to disclose, annual updating of the registration document is requested in order to ensure the availability of new information. What information is necessary is determined by other regulations of the European legislation.[10] The introduction of the possibility to incorporate the information in the prospectus by reference to one or more documents also represents a significant novelty. In order to simplify the circulation of various documents that are an integral part of the prospectus, the use of the electronic media such as the Internet is stimulated. Furthermore, in order to overcome the language barrier and translation expenses, the member state in which the admission to trading on regulated market is

[10] So called Directive .34/2001), and other directives in the field of European Company Law.

sought could request only the prospectus summary to be translated in its official language, provided that the prospectus is drafted in a language customary in the financial field (usually English).[11]

3. COMPARISON OF EUROPEAN AND CROATIAN LAW ON PUBLIC OFFER PROSPECTUS

3.1. Public v. private offer

While the former Law on the Issuance and Sale of Securities omitted to define the concept of public offer and rather identified it with the prospectus, Art. 2 of the LSM defines public offer as *"an invitation addressed to an indefinite number of persons by means of public communication, whose objective is the subscription of securities"*. The indefinite circle of investors and means of public communication are the essential elements of this concept.

In regard to European Law, the 1989 Directive does not specifically address the definition of public offer. Namely, Art. 1 provides that the directive is applicable to *"transferable securities which are offered to the public for the first time in a Member State, provided that these securities are not already listed on a stock exchange situated or operating in that Member State".* On the contrary, art. 2 of the 2001 Directive proposal defines public offer as an *"offer, invitation or promotional message, in any form, addressed to the public, whose objective is the sale or subscription of securities including by placing securities through financial intermediaries."* Drawing the line between public and private offer is one of the most important issues when placement of securities is concerned, because they are subjected to different set of rules. This is also obvious from the short history of European legislature. The disparity of terms on the national level of the member states was an obstacle for the issuers to raise capital on the European wide basis.

In Croatian law, these terms were thoroughly revised. While according to the Law on Sale and Issuance of Securities, public offer implied the "full prospectus", and private offer the "abridged prospectus", according to the actual LSM, the private and public offer prospectuses do not differ much any more. Mandatory content of both prospectuses fully correspond, only the period of observance of relevant data is different. If it is private offer prospectus, the data on debt, financial condition and profit or loss of the issuer relate solely to the previous and current year, while for the public offer prospectus a period of observance except to the current year extends also to the last three years. This means that public offer and private offer prospectus are identical as far as their structure is concerned. In other words a demand for disclosure has been intensified for private placements of company's shares.
The essential difference between placement of securities by means of public or private offer can be observed in the fact that with public offer placement, the securities *have to* be issued as intangible (paperless) shares what implies that they are transferable

[11] About the problem of language choice when drafting the prospectus see: SCOTT, H.S. Internationalisation of primary Public securities Markets Revisited in: FERRARINI/HOPT/WYMEERSCH (eds.) Capital Markets in the Age of the Euro, Kluwer, 2002, p.313.

without limitations and they could not have serial number. Still, while doing a private placement, issuer is free to limit transferability of the share.

3.2. Format and content of prospectus

3.2.1. Croatian law

Mandatory content of the prospectus can be divided in the few thematic groups, depending on which investment aspect they relate to, depending on the security that is to be issued or depending on various issues about the legal and financial position of the issuer.

The first group encompasses the data on securities to which the prospectus relates to and also the mode and conditions of their issuance.[12] It is now requested that the issuer highlights the purpose of raising funds by means of public offer, which was not the case with the former Law on the Issuance and Sale of Securities.

The second group encompasses the data on the issuer of securities.[13] Besides the terminological and editorial changes, the only novelty in this part is the duty to disclose the data about shareholders with more than 5 % of the total number of votes and the percentage of the votes they hold.

The data on the nature of the issuer's business are included in a separate group.[14] There are no changes with regard to the Law on the Issuance and Sale of Securities with exception of one addition - the data about the risk factors has to be entered. Those are risks to which the issuer is exposed, which could be of influence to the realization of rights from securities to which the prospectus relates to and on their market price.

When the data on property and debt, financial condition and profit or loss of the issuer are concerned,[15] the LSM has increased the transparency by stipulating that the data in question do not relate only to the period of last three years as has been provided for in the Law on the Issuance and Sale of Securities, but that it also embraces the current year conclusively with the last trimester prior to the submission of the application for approval of the securities prospectus. This solution is entirely in conformity with the principle of ongoing duty to disclose.

The next group includes the data on the responsible individuals of the issuer.[16] In its end, the prospectus also consists of a statement made by persons who sign the prospectus by which they guarantee that all the data in the prospectus are complete and accurate. The LSM did not change the data on the responsible individuals of the issuer, but it did introduce the duty of disclosing biographies of responsible individuals.

[12] Art.21/1/A LMS
[13] Art.21/1/B LMS
[14] Art.21/1/C LMS
[15] Art.21/1/D LSM
[16] Art.21/1/E LSM

However, the new Law did not specifically stipulate which is the individual who signs the prospectus, it only provided that the prospectus *must* be signed by responsible individuals of the issuer, while the persons who participated in drafting the prospectus or in the preparation of data *could* sign the prospectus. When the joint stock company is issuer, both members of the board and supervisory board must sign the prospectus.

If one of the responsible individuals refuses to sign the prospectus, the refusal must be explained in writing, and such explanation has to be published along with the prospectus. If such explanation is not made, the issuer has to highlight this in the prospectus. If one or several persons have issued a guarantee to meet obligations under the securities to which the prospectus pertains, the prospectus must also contain the data enumerated in Art. 21(1)(B) of the LSM.

3.2.2. European law

In Art 11 of the 1989 Directive the prospectus data are classified in following groups:
a) the data on the those responsible for the prospectus and declarations by them that to the best of their knowledge the information contained in the prospectus is in accordance with the facts and that the prospectus makes no omission likely to affect its import;
b) the data on the offer to the public and the transferable securities being offered;
c) the data on the issuer;
d) the data on the issuer's principal activities;
e) the data on the issuer's assets and liabilities, financial position and profits and losses;
f) the data on the issuer's administration, management and supervision;
g) the data on recent developments in its business and prospects.

The data have been elaborated in detail within each group. When roughly comparing LSM and the Directive in force, one could notice that the data enumerated within groups are mostly identical. There is only partial difference since the Law on Securities Markets includes some information not included in the Directive and vice versa.

One of the novelties in 2002 Directive Proposal is introduction of the new format of prospectus. Basically, the issuer has two options: to publish the prospectus as a single document or to publish the prospectus composed of separate documents. The prospectus composed of separate documents includes a *registration document, a securities note and a summary note*.

The content of each of these documents is stated in annexes I, II, III and IV of the Directive, whereby the first annex relates to a single document prospectus. It is in the Commission's competence to introduce the more detailed regulations on the data required for particular type of security or the particular issuer. Special flexible regulations should be expected in regards to the so called small and medium sized issuers (small and medium sized companies). Nevertheless, it is insisted upon the comparability with the IOSCO *International Disclosure Standards* for transnational public offers or admittance. In regard to the language, which is always delicate issue in the EU, the 2002 Directive proposal stipulates the rule according to which the

prospectus should be drafted in a language accepted by the competent domestic authority of the member state.
The registration document is filed with the competent authority and it should be updated on an annual basis. Member states should allow information to be incorporated in the prospectus by referring to one or more documents, which have been filed and published in accordance with the directive (*by reference*) with certain conditions. In the case of a new emission, the registration document, once approved, is not further examined and the examination is limited only to the *securities note*.

3.3. Approval of the prospectus

3.3.1. Croatian law

Before it is published, the prospectus has to be approved by the CROSEC. When deciding about the approval of the prospectus the CROSEC follows the examination criteria which are rather of formal nature. It is examined, namely, whether the prospectus contains all the data required by law and whether the application for approval contains all required annexes.
By approving the prospectus, the Commission confirms that the prospectus contains all the data required by law and regulations of the Republic of Croatia and that it may be published. The issuer and the persons cited in the prospectus shall alone be liable for the accuracy of the information contained in the prospectus. If the Commission does not deliver a decision in prescribed period of examination, the prospectus should be deemed as approved.
Responsibility and liability for the accuracy of the prospectus lays primarily on the issuer and the persons "for whom it is established that they have used the prospectus to conceal or misrepresent material facts". At the level of the issuer, responsible are the persons who signed the prospectus (within boundaries of what they knew or could have known). A while deciding on the fact "could they have known", a standard of diligent businessman is to be applied.

3.3.2. Comparative experience in some EU member states

Comparative overview shows that the question of liability of the body that approves the prospectus is not insignificant one. In a recent case rendered by the Cassation Court of Italy[17] the liability of *Consob* (the Italian Commission for Securities) has been questioned.
The case involved an offer to subscribe shares in the limited liability company *(Hotel Villagio Santa Teresa HVST)*, which have been placed in public through the *Instituto Fiduciario Lombardo (IFL)*, who acted as fiduciary. As the IFL became insolvent, the HVST was liquidated so several investors filed a suit against *Consob* and its two officials before the *Tribunale di Milano*. The court of first instance denied the claim. While it's ruling was confirmed by the second instance, the Supreme court, however, overruled the decision of the appellate court. Investors challenged the truthfulness of the prospectus claiming that company's initial capital at the time of its placement was

[17] *Gatti e altri c. Consob*, Sezione I civile, 3 marzo 2001, n.3132, Societa, 2001, p.565 and further. For the case analysis see: FERRARRINI, G., *Liammissione a quotazione:natura, funzione, responsabilita e self listing*, CEDIF WP 1-2002, www.cedif.org, p 17 and further.

only 20 million lira instead of the announced 44 million; the hotel which was the final object of investment was property of a company whose shares were not transferred to the HVST (nor to the company which was supposed to transfer the shares to the HVST) and the hotel value was far below the promised amount of 44 million lira. The appellate court rejected the claims substantiating its decision with various arguments: that legislature of that period did not empower *Consob* to examine the truthfulness of data contained in the prospectus, that the inaccuracies in the prospectus were not the sole cause of damages, that the cause were rather the circumstances which were not even mentioned in the prospectus, namely that the proprietary claim was transferred to the bank what is common in the case of immovable property. The Cassation Court of Italy disagreed with the standpoint of the appellate court according to which *Consob* didn't have the authority to examine the truthfulness of the data and accepted the view presented by the prosecution in the appeal. According to the court's reasoning: "*Consob* had the authority to examine the truthfulness of the prospectus since it was by law given the role of supervisor that company acts legally, so in order to ascertain whether the data submitted were accurate and complete it also had the authority to request for additional submissions and/or to conduct an inspection or investigation."[18]

In Germany, the IPO prospectus is regulated by the *Verkaufsprospektgesetz.*[19] (This law is applicable in situations in which the issuer of securities makes the prospectus for the purpose of admitting the securities to official listing on the stock exchange.) When applying Art. 44 VProG, by analogy a conclusion could be drawn that, in the case of inaccurate (or false) prospectus, the person who has acquired the security can demand from issuer as well from every person "that stands behind" such prospectus, to buy back the security at the same price provided that this price does not surmount the initial price at the issuance of the security including the usual expenses related to legal transaction by which the security is acquired, but under condition that the act was made within the 6 months counting from the day public offer was made. This is the case of the liability *in solido* between the issuer and the persons "standing behind" the prospectus. An example of the liability of persons "standing behind" the prospectus would be the case where the mother company is to be held liable, when its daughter company was find liable from prospectus. For placements that do not fall under the scope of public offer or for investments not embodied in the form of securities, the doctrine of *culpa in contrahendo* is adopted in German court practices.[20] Untruthful or incomplete data in the prospectus have to be of essential significance.[21] Precisely, it is insisted upon the causality between the invalid prospectus and the purchase of the security to the detriment of the investor. There is no obligation for restitution of damages if the holder of the security knew of the untruthfulness or incompleteness of

[18] loc.cit

[19] from 9 September 1998, BGBI I p. 2701, replaced with *Gesetz weiteren Fortentwicklung des Finanzplatz Deutschland* or *Drittes Finanzmarktförderungsgesetz* vom 24 Marz 1998, BGBI I p.529. For the complete illustration of the institute according to the earlier regulation see: SCHAEFER, F.A. *Emission und Vertrieb von Wertpapieren nach dem Wertpapierverkaufsprospektgesetz*, ZIP 23-24/91, p.1557 and further. For the illustration according to the current regulation see: GRUNDMANN, S. *Das Emissiongeschäft,* in: SCHIMANSKY/BUNTE/LWOWSKI, *Bankrechtshandbuch*, Beck, München 1997, Band III, § 112, in particular Rn. 46-65. p.2948-2957.

[20] For the BGH judgments defining the scope of the civil-law liability see: HOPT, K.J. *Kapitalmarktrecht in der Rechtsprechung des Bundesgerichtshofes***,** in: 50 Jahre Bundesgerichtshof, Band II. Handels- und Wirtschaftsrecht Europäisches und Internationales Recht, München 2000, p.527 and literature cited thereby.

[21] CLAUSSEN, C.P., Bank- und Boersenrecht, Beck Verlag 2001, p.489.

data contained in the prospectus. While with earlier regulations, the holder could not call to account the issuer if his not knowing of the untruthfulness and incompleteness was due to gross negligence, now this is not the case with the *3. Finanzmerktförderungsgesetz.*[22] Decisive criterion for the issuer's liability is whether the holder knew of the untruthfulness and incompleteness of the prospectus. This criterion is different depending on the investor's level of expertise: whether he is the average individual or institutional investor. In any case, violations of the compulsory law on accountancy are considered significant.[23] As far as financial predictions in the prospectus are concerned, they are to be considered invalid if they are based on false facts.[24] On the other hand, the issuer could not be exempted from liability for data originating with third parties, as are, per example, the auditors who carry the audit of annual financial reports.

3.3.3. European law

The 1989 Directive foresees that the prospectus should be delivered to the competent authority of each and every member state before it is published, but it does not regulate in detail the competence of such an authority. On the other hand, the 2002 Directive proposal clearly defines that before published the prospectus must be approved by the competent authority.[25] The competent authority of the home member state should make a decision regarding the approval within the time limit of 15 days (with a few exceptions).
The Directive proposal also specifies the law applicable for determining the competent authority's liability for the approval of the prospectus. This question is to be governed solely by the national law of the member state in which the competent authority operates. With its regulations, the member state could exclude the competent authority's liability for approval of the invalid prospectus in its entirety. In regard to liability for information included in the prospectus the entire liability lies on the issuer or the persons guaranteeing for the issuer (art. 6(1)). The names and functions of those responsible for the prospectus must be clearly stated. Furthermore, their declarations that to the best of their knowledge the information contained in the prospectus is in accordance with the facts and that the prospectus makes no omission likely to affect its import are also necessary. On the other hand, the member states must ensure that those responsible will be liable according to the criteria of civil liability for damages. Still, those persons are not to be held liable solely on basis of the "summary" or its translation, unless the "summary" is misleading or inaccurate and it is not in conformity with other parts of the prospectus.

3.4. Publication of (public offer) prospectus

3.4.1. Croatian law

[22] See the explanation of the German Federal Government on *3. Finanzmerktförderungsgesetz,* BR-Drucks. 13/8933, See also: HOPT, K.J. *Das Dritte Finanzmerktförderungsgesetz, Börsen-und kapitalmarktrechtliche Überlegungen,* Festschrift für Drobnig, Mohr Siebeck, 1998, p. 546.
[23] CLAUSSEN, C.P. *op.cit,* p.490.
[24] BGH NJW 1982, p. 2823, 2826.
[25] art. 11 of the Directive Proposal

The prospectus must be published as a supplement in a daily newspaper sold regularly in the Republic of Croatia or in the form of a brochure available without payment on the territory of the Republic of Croatia. In that case, a notice must be published in the press, stating where this brochure can be obtained and the manner in which it can be ordered by mail without specific payment. The public offer prospectus must be available to investors at the place of seat of the issuer as well as in places of subscription of shares.

3.4.2. European law

Art. 15 of the 1989 Directive provides that the prospectus must be published or made available to the public in the Member State in which an offer to the public is made in accordance with the procedures laid down by that Member State. In addition, the prospectus must be published or made available to the public not later than the time when an offer is made to the public. The advertisements, notices, posters and documents announcing the public offer also must be must be approved prior to the publication.
The 2002 Directive proposal has thoroughly modernized the regulations on prospectus publication. Besides conventional means, the proposal has allowed the use of modern means of communication. The possibility of making the prospectus available on the issuer's web site is one of the most important innovations.
Regardless of the means of prospectus publication, the competent authority should make the prospectus available on its own web-site, or through a link to the issuer's web-site. Where the prospectus is made available by publication in electronic form, a paper copy must nevertheless, be delivered free of charge to the investor on request.

3. 5. Exempted emissions

3.5.1. Croatian law

The former Law on Issuance and Sale of Securities and the former Regulation on the contents of the abridged prospectus and conditions for private placement of securities provided that, in certain situations, the issuer does not have to submit the prospectus to be approved by the Commission or execute the abridged prospectus.[26] However, regardless of whether the issuers were allowed to issue securities without prior approval of the prospectus or whether they were exempted from the obligatory execution of the abridged prospectus, a summarized report about the completed issuance of securities should have been submitted to the CROSEC.

[26] According to the Regulation the duty to draw up a prospectus (and its prior approval) was amongst other things, related to the financial value of the total emission. Consequently, if the value of the entire private placement exceeds the amount of 2,000,000.00 kn, the issuer must execute and upon the approval of the Commission submit an abridged prospectus (Art. 26(1) of the Regulation). However, if the value of the entire private placement was between 200,000 and 2,000,000 kn, the issuer has the duty to draw up the prospectus, but it does not have to ask for prior approval. In certain cases the issuer is entirely exempted from the responsibility of executing an abridged prospectus (art. 27(1) of the Regulation)

The Law on Securities Market in its art.32, unified those exceptions into a single regime according to which either the issuer is obliged to execute and submit the prospectus for prior approval or it is exempted from this obligation all together. The issuer is not obliged to provide the prospectus in some emissions of shares.[27]
The value of the entire placement as criteria for deciding whether the prospectus should be provided was left out.

3.5.2. European law

Certain issues of securities are out of the scope of the 1989 Directive. Art. 2(1) (a-d) provides that the Directive shall not apply to certain types of issues, while Art. 2 (2) (a-l) of the same refers that the Directive shall not apply for certain types of securities. The first group encompasses some types of *placements* of securities. The second group provides that the Directive does not apply to some types of *transferable securities*.
The 2002 Directive proposal concisely defines the term of public offer and therefore, introduces clarity to this issue. This harmonizing effort was necessary in order to avoid gaps and ensure an equal treatment for all EU investors. In order to avoid the situation where Member states decide whether or not they will incorporate the exempted cases in their law, it was necessary to introduce a uniform system of exempted cases (in which there is no obligation of prospectus publication). The exempted cases according to 1989 directive were revised in a way that the exemptions were placed in two groups.
The first group encompasses situations in which certain types of securities are offered in return for existing securities or situations where certain types of securities relate to special operations for which the document equivalent to the prospectus is available to the public or to the shareholders. The second group of exemptions relates to the admittance of securities on the regulated market when specific transactions for which particular information are not necessary for investor protection, are concerned.

4. OFFERS WITH FOREIGN ELEMENT FROM THE CROATIAN POINT OF VIEW

The Law on Securities Market regulates the position of the foreign issuer issuing securities by means of public offer in the Republic of Croatia, as well as the position of domestic issuers intending to issue securities on foreign markets.
A foreign issuer can issue securities in the Republic of Croatia by means of public offer only through a company authorized to act as agent or sponsor of the emission. The authorized company submits the application for approval of the securities prospectus in the name of the foreign issuer and it jointly and severally liable for truthfulness and completeness of the prospectus. For that reason, the contract between the foreign issuer

[27] Those are: when the initial capital is increased by means of transforming capital gain, reserves and withheld gain in the initial capital company; when the initial capital is increased for the purpose of company merger; when the initial capital is increased while all shares are subscribed and paid for by a shareholder with more than 75% of the votes; when the initial capital is increased with the partaking of only the institutional investors; when the company is transformed into a joint stock company; when transferable bonds are converted into shares provided that, with the issuance of transferable bonds, the prospectus was approved and published or distributed to the investors; when the initial capital is increased by converting the monetary claim into share.

and the company authorized to act as agent or sponsor of the emission, must be annexed to the application for the approval of prospectus.
It is not clear whether foreign issuers could offer securities in the Republic of Croatia by means of private offer. In that respect, considering that the concept of public offer relates to certain values of the total emission in European Law, it is possible that the issuer is not obliged to execute the prospectus according to European Law, while in Croatian Law this is necessary. In order to stimulate public offer by foreign issuers in Croatia, the strict rules on prospectus apply to foreign issuers in a more flexible manner. The Laws are, therefore, *in favorem* of European issuers, as well as those whose seat is in member states of the WTO.

5. SANCTIONS ACCORDING TO CROATIAN LAW

Stating false data in the prospectus and unlawful distribution of the prospectus are defined as criminal acts by Art. 151 of LSM. Corresponding criminal act is provided by art. 624 (1) (1) of the CL. There are also many misdemeanors according LSM.
Civil liability although not expressly mentioned comes into play according to the general principles of the liability pursuant to Article 154 of the Law on Obligation. The act causing damages would be the publishing of inaccurate or incomplete prospectus, and the damages must be related to the deficiencies of the prospectus.[28] The liability of the issuer should be differentiated from personal liability of persons who signed it and persons who have used the prospectus to conceal or misrepresent material facts (Art.23 ZTVP). Persons who signed the prospectus are held liable for truthfulness and completeness of data contained by the prospectus within boundaries of what they knew or could have known. With regard that the prospectus is signed by all members of the board of directors and the supervisory board they could be exempted by proving their due diligence (Art. 252(2) and Art. 272 ZTD). The CROSEC could not be liable for inaccurate prospectus (Art. 23(1) ZTVP).[29] In case of initial emission of shares, the

[28] German Law recognizes special liability for the issuer of listing particulars, which is analogously applied to the public offer prospectus. See § 13 Wertpapier Verkaufsprospektgesetz of 9 September 1998 and § 45 - 48 Börsengesetz of 21 June 2002.
[29] See, supra, under 3.3.2. For the details on national divergencies see ČULINOVIĆ-HERC, E., Prospekt pri javnoj i privatnoj ponudi vrijednosnih papira – Zakon o tržištu vrijednosnih papira i pravci razvoja u europskom pravu [Public and Private Offer Prospectus – Law on Securities Market and trends in European law], Zbornik Pravnog fakulteta u Rijeci, vol.24, 1/2003, p. 126 et. seq.

founders would be held liable for the inaccuracy of the prospectus, on the basis of *pre-society* doctrine (art. 6 CA).

7. CONCLUSION

Croatian LSM should be changed in the light of current trends in European law. First of all, the public offer should encompass criterion of nominal value of the issue. This approach would enable to subject small-scale issues (not exceeding 2 500 000 EUR) to more relaxed rules. On the other hand, big-scale issues (overall amount of at least EUR 50 000 per investor/ or nominal value of at least EUR 50000 per securities) should also be treated separately as well as issues targeted only to qualified investors (i.e. who have specific professional qualification or characteristic). There is also necessity to embrace physical persons in the definition of institutional investor, as European law suggest. Newly proposed format of the prospectus should be examined for its possible adaptation. Wider use of information technologies should be encouraged, for example by publishing the prospectus via issuer's web site.