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CJEU RULES AGAINST CROATIAN LEGISLATION ON RETROACTIVE NULLITY OF LOAN AGREEMENTS

The Court of Justice of the European Union ("CJEU"), with its recent judgement, has set the course for the Croatian legislator attempting to intervene into existing contractual relationships. On 14 February 2019, the CJEU delivered a judgment concluding that a national law of an EU Member State cannot retroactively invalidate loan agreements that were deemed valid at the moment of execution. This is a rather expected outcome of recent controversial legislative intervention by the Croatian Parliament.

In July 2017, the Croatian Parliament passed the Act on Nullity of Loan Agreements with International Elements Concluded in the Republic of Croatia with Unauthorized Lenders ("Act"). Under the pretext of restoring order to the financial markets, the Act provided for automatic nullity of loan agreements, including all ancillary documentation, concluded on the territory of Croatia by foreign lenders without valid Croatian financial services authorizations or approvals. The practical consequence of the nullity is an obligation by each party to return the benefits received under such loan agreement, or to properly reimburse the other party if restitution is impossible. The consequences of the Act may not have even been so grave had the nullity encompassed those loan agreements executed after its enactment. However, the Act contained a catch-all clause, triggering nullity of loan agreements concluded before the Act had entered into force, by a retroactive, general and automatic rule.

Croatian borrowers with loans falling within this category took legal actions before Croatian courts, seeking a declaration of nullity of their loan agreements. A Croatian court hearing one of these disputes submitted a request to the CJEU for a preliminary ruling, asking whether this piece of legislation is compliant with the freedom to provide services in the internal market of the EU.

The CJEU held that the Act discriminates foreign lenders and that it precludes one of the four freedoms of the EU, the freedom to provide services in the internal market. The Croatian Government argued that the Act had been adopted as an avenue of last resort, in order to protect Croatian citizens, the public order and the proper functioning of the Croatian financial sector. The CJEU, however, stated that the Government had failed to

provide convincing arguments and evidence to justify those allegations, and concluded that the Act clearly goes beyond what was necessary to achieve the objectives the Government sought to pursue and that there were other less aggravating and prejudicial measures that could have been adopted.

Although the Act, formally speaking, remains in force, Croatian courts are obliged to adhere to CJEU's judgement. In their considerations on the (in)validity of loan agreements, Croatian courts will need to interpret the national laws in accordance with the CJEU's determination of EU law, not applying the controversial provisions of the Act. It remains to be seen whether and how the Croatian legislator will react to the CJEU's judgement.

The Act is also being scrutinized by the Croatian Constitutional Court for which the proceedings are still pending. Even though the Constitutional Court's decision may now be redundant from a practical point of view, from the standpoint of the Croatian internal legal order, the Constitutional Court's decision on the constitutionality of the Act will be relevant.

Such outcome of this legal matter is not entirely unexpected, considering that the Act was labelled as legally controversial from its adoption. Further developments and reactions from Croatian authorities are expected shortly.

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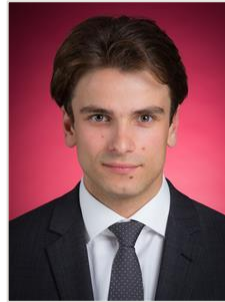


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