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Guide to Doing Business  
Croatia

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## Guide to Doing Business Croatia

**Prepared by Nexia member firm,  
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# Contents

## **Croatia — 4**

- People & Location of Croatia — 4
- Environmental Protection — 4
- Religion & Language — 5
- Currency — 5
- Transportation & Communication — 5

## **Establishing Legal Presence in Croatia — 8**

- Forms of Business Entities — 8
- Liability — 8
- Formation — 9
- Corporate Governance — 11
- Branch and Representative Offices — 15

## **Accounting and Auditing — 19**

- Accounting — 19
- Audit — 20

## **Taxation — 24**

- General — 24
- Corporate Tax — 24
- Personal Income Tax — 27
- Social Security Contributions — 29
- Intrastat — 31

## **Employment — 34**

- Legislative Structure — 34
- Employment Contract — 34
- Probationary Period — 35
- Temporary Employment Agencies — 35
- Working Time — 35
- Holidays, Days Off and Vacation — 36
- Salaries — 36
- Termination of Employment — 37

## **Regulating Stay and Work of Foreigners in Croatia — 40**

- Categories of Foreigners — 40
- Nationals of EEA Member States and Their Families — 40
- Third-Country Nationals — 41
- Temporary Residence — 42

# Croatia

## People & Location of Croatia

Do you want to hear a story about a magnificent country with 1,246 islands, impressive natural and cultural heritage and a story about its rich history? Croatia is located in South-eastern Europe between Bosnia and Herzegovina, Slovenia, Hungary, Serbia and Montenegro and the Adriatic Sea, and has a maritime border with Italy. The Croatian Adriatic coast is one of the most indented in the world: it has 1,246 islands and islets with a total coastline of 4,058 km, the total length of the mainland coast being 1,777 km. The largest island is Cres; other large islands include Krk, Brač, Hvar, Pag and Korčula. *Interesting fact: The White House in Washington, D.C. was built with stone brought from the island of Brač.*

The largest peninsulas are Istria and Pelješac, and the largest bay is Kvarner Bay.

Croatia has a 1,011 km border with Bosnia and Herzegovina, a 670 km border with Slovenia, a 355 km border with Hungary, a 317 km border with Serbia (entirely with its Autonomous Province of Vojvodina) and a 25 km border with Montenegro. Croatia's islands and coastal areas have a Mediterranean climate, while inland areas have a temperate continental climate with hot summers and low overall humidity levels, but frequent rain showers and cold, snowy winters. The local terrain is quite diverse given the size of the country (56,594 km<sup>2</sup>).

According to the 2011 census, the population of Croatia was 4,284,889 people, 1,107,623 of whom live in the capital city, Zagreb. The majority of the population is Croatian, and other ethnic groups include Serbs, Bosnian Muslims, Hungarians, Slovenians, and Czechs.

## Environmental Protection

The right to a healthy environment is a constitutional prerogative of the Republic of Croatia. In the 2007 State of the Environment Report of the Republic of Croatia, it was concluded that good progress had been made in certain segments, for example, in air protection, as reflected in the considerable reduction in CO<sub>2</sub> emissions; and in the establishment of a monitoring, control and information system and in waste management; however, there are still some preconditions and key measures to be taken in order to generally improve the state. The Croatian Environmental Agency was founded in late 2002 as a central body for the collection and processing of environmental information and cooperation with relevant EU institutions. The Environmental Protection and Energy Efficiency Fund were established in 2003 to

provide funding for environmental protection and for internalisation of a portion of the environmental pollution costs. The Republic of Croatia ratified and signed many international treaties in the field of environmental protection, a list of which may be found at [www.mzopu.hr](http://www.mzopu.hr).

## Religion & Language

The Croatian language is today the official language of the Republic of Croatia. There are three principal dialects: Shtokavian, Chakavian, and Kajkavian. Many people speak Italian, German and English as a second language.

Croatia is predominantly a Roman Catholic country. According to recent statistics, nearly 90% of the population defines itself as Catholic, nearly 3% as Orthodox, 2.1% atheist and only 1.1% Muslim.

## Currency

The Croatian monetary unit is the kuna. In English, 'kuna' means marten; in medieval times marten pelts were used as a unit of trade. The Croatian National Bank (HNB) determines the value of the kuna in relation to other currencies in accordance with the stipulated trade and foreign currency rates on the market of foreign exchange payments. On 1 January 2017, US\$1 equalled HRK 7.168536, while on 21 August 2017, it dropped to HRK 6.296589. At the same time, €1 equalled HRK 7.557787, and dropped to HRK 7.392195 on 21 August 2017.

## Transportation & Communication

Transportation in Croatia relies on several main modes – road, rail, water and air. Road transport incorporates a comprehensive network of state, county and local routes, supplemented by a network of motorways for long-distance traveling. Water transport can be divided into sea and river transport. Croatia has 9 civil airports, five of which are international. The country also has several airlines, of which the most notable is Croatia Airlines. Rail transport is fairly developed.

The international dialling code for Croatia is +385. 4G mobile coverage is widespread with the majority of the country having GSM coverage. GSM operators have active roaming agreements with most international networks. ADSL/Optical broadband is common in Croatia with Internet cafés available in all major cities. Croatia has a national postal service with post offices in most cities, towns and villages.

## Did you know Croatia invented double-entry bookkeeping?

The first known manual on bookkeeping was *'Della mercatura e del mercante perfetto'* (On Merchantry and the Perfect Merchant), written in 1458 by Benedictus de Cotrullis, born in Dubrovnik, Croatia. It is also the oldest known manuscript on double-entry.



## Establishing Legal Presence in Croatia

### Forms of Business Entities

The principal law governing business organizations in Croatia is the Companies Act (CA). The statute is modelled on German and Austrian laws.

The CA introduces five types of commercial entities:

- general commercial partnership;
- limited partnership;
- joint stock company;
- limited liability company; and
- economic interest grouping.

There are two principle types of business organizations – commercial partnerships and corporations. Both commercial partnerships and corporations are legal entities. Among commercial partnerships, the law distinguishes between general commercial partnerships and limited partnerships. The two types of corporations are the joint stock company and the limited liability company.

The CA also recognizes economic interest groupings. The rules on economic interest groupings implement European Community law (EC Directive on European Economic Interest Groupings). It defines an ‘economic interest grouping’ as a legal person set up by two or more natural persons or legal entities for the purpose of:

- facilitating or promoting their business activities; and
- promoting or increasing the effect of these activities. An economic interest grouping may not retain profits.

Investors can generally choose between these types of business entities. However, certain enterprises must take on a particular form. Banks, for example, can only be organized as joint stock companies.

### Liability

#### PARTNERSHIPS

In a general commercial partnership, partners are jointly and severally liable to creditors of the partnership. In a limited partnership, at least one partner is personally liable for the obligations of the partnership (the general partner) and at least one partner is not liable for the debts of the partnership if he/she has paid in a contribution (the limited partner). The limited partner may be held liable for the partnership’s debts incurred before registration.

#### CORPORATIONS

In the limited liability company and the joint stock company shareholders are not liable for the company’s debts. There are exceptions to this general rule:

- a shareholder may be held liable for the company’s debts in cases of abuse;
- company promoters are liable for debts incurred before the company’s registration; and
- statutory rules may lead to a shareholder’s liability for the company’s debts (in the context of groups of companies).

### Formation

#### PARTNERSHIPS

General commercial partnerships and limited partnerships are established on the basis of a partnership agreement. A partnership is not established until it is registered in the register of the relevant local commercial court. Registration is made upon filing the application containing particulars required by law together with the partnership agreement.

There are no minimum capital requirements for the formation of a general commercial partnership. If not otherwise provided by the partnership agreement, partners are obliged to make equal contributions. Contributions may be made in cash, kind, labour or services.

Registration is not conditional upon partners having made their contributions. Failure to make a contribution can lead to liability for partnership debts.

The same applies to the general partners of limited partnerships. Limited partners are not obliged to pay in their contribution before the company is registered. The limited partner is not personally liable for debts of the partnership if he/she has paid the contribution undertaken in the partnership agreement in full. However, failure to pay the contribution in full gives rise to the limited partner’s joint and several liability along with the general partners for the debts of the partnership, but only up to the outstanding amount of the contribution.

## **CORPORATIONS**

A limited liability company is established on the basis of notarized Articles of Association. The company may be established by one shareholder on the basis of a notarized Deed of Incorporation. The company is established by registration in the court register upon application to the competent local court. The minimum share capital of a limited liability company is HRK 20,000 (approximately EUR 2,615). Contributions to the share capital may be made in cash or in kind. Prior to registration, each founder must pay in:

- 100% of its contribution in kind; and/or
- at least 25% of his/her cash contribution, provided that the total amount of all cash contributions paid in before registration is no less than HRK 10,000 (approximately EUR 1,307).

The CA also provides for the possibility of establishing a 'simple limited liability company' with a minimum share capital of HRK 10 (approximately EUR 1.30) and not more than three shareholders. Contributions to the share capital of such a company may only be made in cash and have to be paid in full prior to registration. There are specific prescribed forms that are used when setting up a simple limited liability company. This type of business entity was primarily introduced into legislation to encourage start-ups.

A joint stock company is established on the basis of notarized Articles of Association which the founders adopt. The company may be established by one shareholder on the basis of a Deed of Incorporation. A joint stock company may be established by way of simultaneous incorporation or successive incorporation. In the former, promoters undertake all shares, adopt and execute the Articles of Association and declare the establishment of the company.

In the latter, promoters adopt the Articles of Association, undertake a part of the shares and issue a public prospectus for the subscription of shares. In both simultaneous and successive incorporation, the company is established by registration with the court upon application by the members of the management board and the supervisory board.

The minimum share capital of a joint stock company is HRK 200,000 (approximately EUR 27,000). Rules for contributions are similar to those applicable to limited liability companies.

However, unlike the formation of a limited liability company, promoters must submit a report on the company's incorporation to the court.

In addition, the members of the Management Board and of the Supervisory Board, or Executive Directors and members of the Board of Directors, must audit the company's formation. In certain cases, the formation of the company must also be audited by independent auditors appointed by the court.

## **Corporate Governance**

### **PARTNERSHIPS**

Partnerships do not have bodies entrusted with management or representative authorities. Each partner of a general commercial partnership is authorized and obliged to manage the partnership unless otherwise provided by the partnership agreement. The authority to manage the partnership extends to all actions normally taken in the course of conducting business. An action cannot be taken if a partner authorized to manage the partnership objects to the action. Actions outside normal business can only be taken with the consent of all partners.

The same rules apply to general partners in a limited partnership. Limited partners are excluded from management. They can only object to decisions made and actions taken by general partners outside the normal course of business.

Each partner of a general commercial partnership is authorized to represent the partnership, except where the partnership agreement states otherwise. Such restrictions have no effect on third parties. The same applies to general partners of limited partnerships. Limited partners are excluded from representation.

### **CORPORATIONS**

The mandatory governing body of a limited liability company is the management board / managing director(s).

The management board of a limited liability or joint stock company consists of one or more directors (with the exception of simple limited liability company which may only have one director). In a limited liability company, management board members are appointed at the shareholders' meeting, unless the Articles of Association provide otherwise. They can be revoked or removed at any time. Unless otherwise provided by the company agreement, the members of the

management board shall represent the company jointly. A legal person (i.e. company) is not allowed to be appointed as a managing director.

Only directors are authorized to represent the company. The Articles of Association may restrict the representative powers of directors; however, such restrictions are only internal and are ineffective towards third parties.

In a joint stock company, management board members and the chairman of the board are appointed by a supervisory board for a term of office not exceeding five years. Appointments may be renewed. Management board members can only be changed by the supervisory board for material cause, including:

- a gross breach of duty;
- the inability to conduct company business; or
- a vote of no-confidence at the shareholders' meeting, unless such vote was made for manifestly arbitrary reasons.

Management board members can only take management decisions jointly, unless the Articles of Association state otherwise. A decision based on a minority vote is not valid. Any restrictions to the representative powers provided in the Articles of Association are of an internal nature and are ineffective towards third parties.

Only the management board is authorized to represent the company. The management board represents the company jointly, unless the Articles of Association state otherwise.

There are no restrictions on the nationality of the directors of a limited liability or a joint stock company. The managing director does not have to be employed.

The Articles of Association shall determine whether or not the company shall have a supervisory board.

However, a supervisory board is a mandatory body in a limited liability company:

- if the average number of employees in one year exceeds 200;
- if specific statutes provide that a company carrying out certain activities must have a supervisory board; or
- if the share capital of the company exceeds HRK 600,000 (approximately EUR 80,500) and the company has more than 50 shareholders.

Joint stock companies can opt for a two-tier corporate governance structure (comprising a management board and a supervisory board) or a one-tier corporate governance structure (comprising only a board of directors which appoints one or more executive directors).

In a joint stock company, in the case of the two-tier system, members of the supervisory board are elected at the shareholders' meeting. However, the Articles of Association may provide that certain shareholders have the right to appoint members of the supervisory board directly. This right can only be granted to specific shareholders or holders of specific shares if the shares in question are ones whose transfer requires the company's consent. Only one third of the supervisory board may be appointed in this manner. Supervisory board members are elected or appointed for a term of office not exceeding four years and all may be re-elected or re-appointed.

The shareholders' meeting may remove an elected member of the supervisory board before expiration of his/her term of office. This resolution requires a majority vote of not less than 75% of the votes cast unless the Articles of Association provide for a larger majority or for additional requirements. If a shareholder made the appointment directly, he/she can revoke the appointed member of the supervisory board.

The supervisory board supervises the management of the company. It may inspect the business records of the company, treasury, securities and other matters. The board submits a written supervisory report at the shareholders' meeting. In addition, the board can call a shareholders' meeting, and must do so whenever it is in the interest of the company.

The rules governing the supervisory board of a joint stock company apply analogously to the supervisory board of a limited liability company.

In the case of the board of directors (i.e. one-tier system), the choice of the one-tier system of corporate governance should be expressly stated in the company's Articles of Association. The Articles of Association should also determine the number of members of the board of directors.

Members of the board of directors are elected at the shareholders' meeting and the duration of their term is determined by the Articles of Association (it cannot exceed 6 years). The Articles of Association may provide that certain shareholders have the right to appoint members of the board of directors directly. The appointment, revocation,



resignation and liabilities of the members of the board of directors, as well as the internal structure of the board of directors (e.g. the existence of particular committees) must comply with the rules of the supervisory board in the two-tier system.

The board of directors is competent for:

- steering the company;
- laying the foundations for performance of the company's activities;
- supervising management of the company; and
- representing the company towards executive directors.

The board of directors is obliged:

- to convene shareholders' meetings whenever necessary for the benefit of the company; and
- to file for bankruptcy in cases of insolvency and over-indebtedness. It is also responsible for ensuring the proper keeping of the company's business records. The board of directors also plays an important role in the adoption of the company's financial statements.

The board of directors appoints one or more executive directors of the company for a term defined in the Articles of Association which cannot exceed 6 years. If there are several executive directors, one shall be appointed as the chief executive director. Executive directors can be elected among members of the board of directors. However, members of the board of directors who are not appointed as executive directors must always remain in the majority within the board of directors. An executive director can be revoked by decision of the board of directors at any time. The revocation does not affect the contract entered into by and between the company and the executive director.

Executive directors manage and represent the company. The default rule is that the executive directors manage and represent the company collectively; however, a different solution can be prescribed in the Articles of Association. The statutory competences of the board of directors cannot be delegated to the executive directors. Provisions regulating the status and duties of the executive directors (e.g. their responsibilities and liabilities) generally refer to the rules governing the management board in the two-tier system.

## Branch and Representative Offices

The branch office is the minimal form of presence that allows the parent entity to conduct permanent business in Croatia. Branch offices may conduct activities that form part of the registered activities of the parent entity. A branch office is established by entry in the court register of the competent local court. The parent entity must adopt and notarize the resolution on establishment of the branch office. Details of this resolution are listed in the CA. A branch office is not a legal entity. Its operations, rights and obligations are acquired by and for the parent entity.

Foreign businesses can establish representative offices in Croatia for the purposes of market research, marketing, informational and representational activities. A representative office cannot conduct business in Croatia. The establishment of a representative office must be registered with the Ministry of Economy. Companies domiciled in one of the EU member countries to perform the mentioned activities do not need to establish a representative office. For such activities it is enough to register the company with the Croatian Health Insurance Fund and the Croatian Pension Fund and to employ employees.

Before starting to operate a business (by setting up a company or by employing employees for market research) it is necessary to obtain an ID number for foreign companies from the tax administration.

## Did you know Croatia invented the necktie?

However you may feel about the modern-day office noose, we have Croatia to thank for it, and it may very well be Croatia's most successful export. After all, it used to be called the cravat, and where did the word cravat come from? Croatia.

The origins of the necktie go all the way back to the 17th century, when Croatian mercenaries fought for the French in the Thirty Years' War, bringing their distinctively knotted neckwear along with them. From there it spread to other militaries, other countries, and, eventually, into the cubicles of modern-day offices and other fancy places. The knotting became distinctive enough that it simply became known as a tie, and here we are today.



## Accounting and Auditing

### Accounting

In order to harmonise the Croatian Accounting Law with the 2013/34/ EU Directive, a new accounting law was introduced in 2015. The majority of the provisions of the Accounting Act have been in force since 1 January 2016.

The accounting methods prescribed in the statute apply to all companies and business entities registered in Croatia. The accounting methods of various institutions, societies, civil associations and non-profit organizations are not subject to this statute, but are regulated by special laws.

The statute classifies entrepreneurs into three categories:

- small;
- medium-sized; and
- large companies:

A 'small' company is a company that does not meet two of the following three conditions:

- total assets of HRK 30 million (approximately EUR 4 million);
- gross income of HRK 60 million (approximately EUR 8 million); and
- average annual number of employees of 50.

A 'medium-sized' company is a company that meets two conditions set for small companies, but does not meet two of the following three conditions:

- total assets of HRK 150 million (approximately EUR 20 million);
- gross income of HRK 300 million (approximately EUR 40 million); and
- average annual number of employees of 250.

A 'large' company is a company that meets more than two of the three criteria set for medium-sized companies. Moreover, the following types of entities are deemed to be large companies: banks, savings banks, building society institutions, electronic money institutions, insurance companies, leasing companies, investment and pension funds and their management companies, as well as pension insurance companies.

Companies generally have to apply *Croatian Financial Reporting Standards* (HSFI), which are adopted by the local Accounting Standards Board and are largely based on *International Financial Reporting Standards* (IFRS). All large companies, companies with listed shares or bonds or companies preparing for such public listings must apply fully with IFRS used in the EU.

Financial statements include: statement of financial position (balance sheet), statement of comprehensive income (income statement), cash flow statement, statement of changes in equity, and notes to the financial statements. Small companies must prepare and maintain only a statement of financial position (balance sheet), statement of comprehensive income (income statement) and notes to financial statements. Financial statements of banks, insurance companies, investment funds, pension funds and stockbrokers are subject to further special requirements and regulations. Holding companies within a group of companies must prepare and keep consolidated financial statements.

The default accounting period is the calendar year. However, based on special laws or for their own purposes, subject to special approval, companies may use alternative accounting periods.

Financial statements must be in Croatian and expressed in the domestic currency, kuna (HRK). They must be kept up-to-date and original documents must be archived on a permanent basis.

All companies must deliver their properly adopted financial statements to the Financial Agency within 6 months from the last day of the accounting period. Financial statements are kept in the publicly accessible Registry of Financial Statements. Annual consolidated financial statements have to be delivered to the Financial Agency within 9 months from the last day of the accounting period.

## **Audit**

According to the Accounting Act, as of 1 January 2016, a mandatory audit of the annual financial statements (FS) is required for the separate and consolidated financial statements:

(A) of all PIEs (public interest entities) as well as big and medium sized companies and other companies that are not PIEs,

(B) of limited partnerships and limited liability companies which on their balance sheet dates exceed the limits of at least two of the following three criteria:

- balance sheet total: HRK 15,000,000 (EUR 2,000,000),
- total income: HRK 30,000,000 (EUR 4,000,000),
- average number of employees during the financial year: 25.

(C) of companies for periods shorter than one year if such a period precedes status changes, i.e. liquidation or bankruptcy.

Limited liability companies and limited partnerships that do not

exceed the thresholds listed above may opt for a mandatory audit in their internal documents.

All audits must be in line with the International Standards of Auditing.

Presently, the Ministry of Finance recognizes the Chamber of Auditors as the only professional association of auditors in Croatia. Audits can be conducted by certified auditors within registered auditing firms as well as individual auditors provided they are licensed by the Chamber of Auditors. On the basis of reciprocity and in compliance with the CA, foreign audit companies may establish their branch offices in Croatia. The Chamber of Auditors is responsible for supervising audit standards and practices. The supervision of the Chamber of Auditors and of the auditors is vested in the Audit Public Oversight Committee.

The State Audit Office conducts audits of government accounts and operations and promotes sound financial management and accountability in the government, in compliance with the audit standards of the International Organization of Supreme Audit Institutions (INTOSAI). The Report of the State Audit Office is presented to the Croatian Parliament every year.

Enjoy the small and simple things in life...

Croatia indeed is a small country and according to the Guinness Book of World Records, the smallest town in the world is Hum, which is in Istria with a population of only 23 inhabitants. It was first mentioned in documents dating from 1102, at which time it was called Cholm, which is derived from the Italian name Colmo.



# Taxation

## General

The principles of the Croatian tax system are comparable to those of the tax systems of Western European Countries with developed, market-oriented economies. In Croatia, taxes are mainly levied on income, sales and specific transactions. Any business income subjects the business, regardless of its legal form, to the obligation of corporation tax. An income earned by individuals is subject to personal income tax. Generally, domestic sales and imports are subject to Value Added Tax (VAT), other taxes, excise duties and fees.

In most cases, taxes are self-assessed. The tax return should be filed and payment should be made by the taxpayer within the period set by law. The processing of tax returns, entering tax liabilities in tax records, collecting and refunding taxes is the responsibility of the Tax Administration. The administration of taxes in Croatia is vested in the Ministry of Finance.

## Corporate Tax

The following entities are subject to Corporation Tax:

- Companies or other legal or natural persons, resident in the Republic of Croatia, that perform their business activities independently, permanently or for the sake of achieving profit, income or revenue or other economic benefits,
- A business unit of a foreign enterprise in the country (non-resident),
- Natural persons who generate income according to the regulations on income taxation if they declare that they will pay profit tax instead of income tax,
- Natural persons who generate income through a sole proprietorship or activities equivalent to a sole proprietorship according to the regulations on income taxation:
  - (A) if in the previous tax period they generated a total revenue higher than HRK 3,000,000.00, or
  - (B) if they fulfil two of the following three conditions:
    - in the previous taxation period, they generated income above HRK 400,000.00,
    - they have long-term assets exceeding HRK 2,000,000.00,
    - in the previous taxation period they employed more than 15 employees on average.

- Exceptionally, state administration bodies, bodies of regional self-government, local self-government bodies, the Croatian National Bank, state institutions, institutions of units of regional self-government, institutions of units of local self-government, state institutes, religious communities, political parties, trade unions, chambers, associations, artistic associations, voluntary firefighter's associations, technical culture associations, tourist associations, sports clubs, sports associations and organisations, trust funds and foundations, if performing a business activity and if non-taxation of the activity would lead to the acquisition of unjustified privileges on the market, are subject to Corporation tax for those activities.
- Any entrepreneur who does not fall under the categories listed in items 1 to 5 above and who does not pay income tax according to the regulations on income taxation and whose profit is not taxed elsewhere.

The tax base is determined in three ways:

- According to accounting principles, as a difference in income and expense, with prescribed increases and decreases;
- According to the cash principle, the difference in income and expense is increased or decreased for certain non-cash transactions and unrealized gains / losses and certain cash transactions and realized gains / losses). It is an option for taxpayers who fulfil the following cumulative conditions:
  - their income is less than HRK 3 million;
  - they calculate VAT according to the fees charged.
- Lump-sum – an option for non-profit organizations that are also taxed on the basis of economic activity, provided that the economic activity generates revenues less than the VAT threshold and if these revenues (based on which they are subject to corporation tax) are lower than 50% of total revenues (the lump-sum annual amount is determined by the Croatian Tax Administration)

### *Items that increase the tax base*

- 50% of entertainment expenses (food and drink, gifts with or without the company's printed logo or product brand and expenses for vacation, sport, recreation and leisure time, ren-

ting cars, vessels, airplanes and holiday cottages), up to the amount of the costs arising from a business relationship with a business partner;

- 30% (from 01.01.2018. 50%) of the cost, except for insurance and interest expenses, incurred in connection with own or rented motor vehicles or other means of personal transportation used by managerial, supervisory and other employees, unless the use of such means of transport is defined as a salary component;
- Personal expenses of shareholders and partners (withdrawals), as well as employees (entertainment, relaxation, sport and recreation costs) including value added tax;
- Fines imposed by competent bodies;
- Accrued penalty interest;
- Privileges and other economic benefits granted to natural persons or legal entities for the purpose of causing or preventing a certain event;
- Gifts in kind or cash made in Croatia for cultural, scientific, educational, health, humanitarian, sports, religious, environmental or other socially beneficial purposes to associations and other persons engaged in the above mentioned activities pursuant to special regulations, if they exceed 2% of the revenue generated in the previous year;
- Interest on loans received from a shareholder or partner holding at least 25% of shares or equity capital or voting rights in a taxable entity, provided that, in any tax period, these loans exceed the fourfold amount of such shareholder's or partner's share of the capital or voting rights, determined in relation to the amount and duration of loans in the taxable period, except for interest on loans from financial institutions (i.e. thin capitalization rule);
- Write-downs of inventories and financial assets.

*Items that decrease the tax base*

- Dividends received from other affiliated companies;
- Gains on the write-up of shares and interests in private companies (unrealised gains), if these were included in the tax base;
- Expenditure from previous periods which was included in the tax base;
- State support for training and development.

As of 1 January 2017, the corporation tax rate has been reduced from 20% to 18%, and taxpayers with annual income under HRK 3 million will be taxed at a rate of only 12%.

Tax losses may be carried forward for up to five consecutive years. Tax loss carry back, however, is not permitted.

A withholding tax is levied on certain payments by Croatian residents to non-resident legal entities, including payments of qualifying interest, dividends, capital gains, payments in respect of the use of intellectual property rights, services of market research, tax and business advisory audit and similar. A withholding tax is levied at the rate of 15%, except with respect to dividends and capital gains where the withholding tax is levied at the rate of 12%. Exceptionally, the rate is set at 20% for all services paid to persons having their permanent establishment or headquarters in countries other than the EU member states in which a general or average nominal profit taxation rate is lower than 12.5% and which are included in the list issued by the finance minister. Where a double tax treaty is applicable, such withholding tax may be decreased.

Croatia currently has a treaty for the avoidance of double taxation of income and property ratified and in effect with the following countries: Albania, Armenia, Austria, Azerbaijan, Belarus, Belgium, Bosnia and Herzegovina, Bulgaria, Canada, Chile, China, the Czech Republic, Denmark, Estonia, Finland, France, Georgia, Germany, Greece, Hungary, India, Indonesia, Iran, Ireland, Israel, Italy, Jordan, S. Korea, Kuwait, Latvia, Lithuania, Luxemburg, Macedonia, Malaysia, Malta, Mauritius, Morocco, Moldova, Montenegro, the Netherlands, Norway, Oman, Poland, Portugal, Qatar, Romania, Russia, San Marino, Serbia, Slovakia, Slovenia, South Africa, Spain, Sweden, Switzerland, Syria, Turkey, Turkmenistan, Ukraine, and the United Kingdom.

According to the law, the taxpayer has the obligation of making monthly advance payments based on the previous year's corporation tax return. The monthly payments may be adjusted by the Tax Authority. Upon its request, a company may be permitted to set its business/ financial year differently than the calendar year.

**Personal Income Tax**

Personal income tax is levied on the worldwide income of Croatian resident taxpayers and the Croatian source of income of non-resident taxpayers. Tax rates on income from employment are as follows:

MONTHLY INCOME	ANNUAL INCOME	TAX RATE
UP TO HRK 17,500	UP TO HRK 210,000	24 %
ABOVE HRK 17,500	ABOVE HRK 210,000	36 %

The taxpayer is entitled to a basic personal allowance of HRK 3,800 per month (approximately EUR 510). The allowance may be increased for dependants, spouse, children and disabled family members, i.e.

DESCRIPTION	RATE	AMOUNTS IN HRK
GROSS SALARY		6,842.63
SOCIAL SECURITY – PILLAR I	15%	1,026.39
SOCIAL SECURITY – PILLAR II	5%	342.13
TOTAL EMPLOYEE SOCIAL SECURITY CONTRIBUTIONS:	20%	
PERSONAL DEDUCTION		3,800.00
TAX BASE		1,674.11
INCOME TAX	24%	401.79
INCOME SURTAX (CITY TAX)	18%	72.32
TOTAL INCOME TAX & SURTAX		474.11
<i>EMPLOYER CONTRIBUTIONS</i>		
HEALTH INSURANCE CONTRIBUTION	15%	1,026.39
ACCIDENT INSURANCE CONTRIBUTION	0,5%	34.21
UNEMPLOYMENT BENEFIT CONTRIBUTION	1.7%	116.32
TOTAL EMPLOYER CONTRIBUTIONS	17.2%	1,176.92
<b>TOTAL NET SALARY</b>		5,000.00
<b>TOTAL SALARY COST</b>		8,019.55

The rates of tax levied on property income and income from proprietary rights are 12% and 24% respectively. Income from interest and income from grant of stock or stock options is taxed at 12%.

An individual resident taxpayer is required to file an annual tax return by the end of February of the next year for the previous year. Generally, an individual earning income solely from employment does not need to file a tax return. Of late taxpayers no longer have to file an annual tax return; they simply receive a decision about refund or payment from the Tax Authority at their home address. If they are entitled to a refund based on data that the Tax Authority doesn't have (e.g. if a child is not registered on a taxpayer's tax card) they have to file a request for a refund to the Tax Authority by themselves.

Besides income taxation, there is an obligation to pay surtax on income tax (i.e. city tax). The tax base for the surtax is the amount of income tax. Depending on population, cities can prescribe a surtax on personal income. Accordingly, the following major cities have local taxes:

- Zagreb = 18%
- Split = 10%
- Rijeka = 15%
- Osijek = 13%
- Pula = 12%
- Zadar = 12%
- Varaždin = 10%
- Dubrovnik = 10%

### Social Security Contributions

Compulsory social security contributions are a kind of direct tax used to finance the social security system, and hence, in a broader sense, form part of the tax system. These contributions fund the pension, health and unemployment insurance systems. Contributions are collected from the employee and the employer, and are the revenues of the following extra-budgetary funds:

- Croatian Pension Insurance Fund: contributions for Pillar I pension insurance;
- Croatian Pension Insurance Fund – Pillar II, paid to private insurance funds selected by the employee;
- Croatian Health Insurance Fund: health insurance contributions;
- Croatian Employment Service: contributions for accident and occupational health insurance.

The following is an example of the cost of a typical employee for an employer on the basis of a net salary amounting to HRK 5,000.

DESCRIPTION	FACTOR	MONTHLY AMOUNT	ANNUAL AMOUNT
BASIC PERSONAL ALLOWANCE	1,0	HRK 3,800	HRK 45,600
DEPENDANT SPOUSE PERSONAL ALLOWANCE	0,7	HRK 1,750	HRK 21,000
DEPENDANT FIRST CHILD PERSONAL ALLOWANCE	0,7	HRK 1,750	HRK 21,000
DEPENDANT SECOND CHILD PERSONAL ALLOWANCE	1,0	HRK 2,500	HRK 30,000
DEPENDANT THIRD CHILD PERSONAL ALLOWANCE	1,4	HRK 3,500	HRK 42,000



VAT taxpayers are individuals and legal entities providing goods and services on a regular basis. VAT is payable on the supply of goods and services within Croatia (including own consumption) and on the import of goods and services into Croatia. VAT registration is compulsory when annual turnover exceeds HRK 300,000 (approx. EUR 40,000).

A number of VAT exemptions exist, including: exports of goods and services, supplies of goods to free trade zones, supplies of goods and services to diplomatic missions and goods and services in transit. Certain types of services are VAT exempt, among them the services of banks, savings institutions, insurance companies, games of chance, etc.

Business transactions are taxed at 25%, 13% and 5%.

The 5% rate applies to the following:

- all kinds of bread and milk (except for fermented and certain other milk products);
- books of a professional, scientific, artistic, cultural and educational character and school textbooks (for primary, secondary and tertiary educational institutions, in all forms – i.e. printed paper and other media, CD ROMs, video cassettes, audio tapes, etc.);
- medicines determined by the List of Medicines of the Croatian Health Insurance Fund;
- scientific and scholarly journals;
- daily newspapers printed on paper, except those that wholly or mainly contain advertisements or are used for advertising;
- services rendered by cinemas.

The 13% rate applies to the following:

- services of accommodation with/without breakfast accommodation in all kinds of commercial hospitality facilities and on services of organised tourist stays;
- newspapers (except daily newspapers) and magazines printed on paper that are published periodically, except those that wholly or mainly contain advertisements or are used for advertising;
- edible oils and fats of vegetable or animal origin, in accordance with special regulations;
- child seats, baby food and processed cereal-based food for infants and young children, in accordance with special regulations;
- delivery of water, except water that is placed on the market in bottles or other containers;
- concert tickets;
- supply of electricity from another supplier or end-user, including charges related to such delivery;

- public utility for collection of mixed municipal waste, biodegradable municipal waste and separate collection of waste according to special regulations;
- urns and coffins;
- seedlings and seeds;
- fertilizers and pesticides, and other agrochemicals;
- feed for animals, except pet food.

The following are free from VAT taxation inside Croatia (main categories):

- lease or rent of housing space;
- banks, savings banks, credit-saving organisations and insurance company services;
- lotteries and other games of chance;
- postal stamps;
- delivery of used buildings and land (except construction land).

VAT returns must be filed by the 20th of the following month, while payment has to be made by the last day of the month following the end of the taxpayer's VAT accounting period. VAT accounting periods are normally monthly, but can be quarterly for some (smaller) taxpayers (up to HRK 800,000 annual income – approx. EUR 105,000).

### **Intrastat**

Intrastat discloses details of movements of goods between Member States which take place for commercial reasons, recording the movement whenever goods enter the territory of Croatia from other Member States or leave it to other Member States. A declaration must be filed monthly once the annual threshold is exceeded. Intrastat declarations can be submitted online. The due date for submission is the 15th day of the month following the reference period.

The Intrastat threshold for arrivals and dispatches is HRK 1,700,000 (approx. EUR 225,500).

## Enjoy the small and simple things in life...

The Church of the Holy Cross called 'the smallest cathedral in the world' is the most valuable preserved monument of early Croatian religious architecture and one of Nin's symbols. It dominates the area where it stands with its position and beauty. It was built in the 9th century, in the Early Christian period. It is 7.80 m long, 7.60 m wide, and 8.20 metres in height (inside measures) and the walls are 57cm thick. It was built on the remains of ancient houses which are visible even today. During the reign of the Croatian Kings it served as a Court chapel for the nearby Duke's Court. A number of medieval graves were discovered around the church. This small church, thanks to the position of its windows and the angle at which the light falls is a kind of calendar; the exact date of the equinox and solstice can be determined by the sun's rays. The first day of summer is the start of an interesting event called 'The Festival of Sun and Light'.

Spellbound by its beauty, the famous English architect, Thomas Jackson, called it 'the smallest cathedral in the world'.



# Employment

## Legislative Structure

The principal piece of legislation governing labour relations in Croatia is the Labour Code. In addition to this core legislation, labour relations are regulated by:

- additional Croatian statutes such as legislation on work safety;
- Collective labour agreements; and
- Work by-laws adopted by the employer.

The Labour Code provides all workers with minimum guarantees that cannot be superseded by any other agreement between the employer and the employee.

## Employment Contract

The employer is required to establish an employment relationship by means of an employment contract or through a confirmation of employment status. Both documents must be produced in writing. Preference should be given to the employment contract. Both the contract and the confirmation must contain particular information as mandated by the Labour Code. Failure to comply with this requirement is sanctioned by fines to the employer.

A short form employment contract is possible provided that the short form contract contains references to relevant provisions of the applicable statute, regulation, collective labour agreement or work by-laws as allowed by law. The freedom to contract is limited. Any provision that is contrary to mandatory law shall be invalid. If there is a discrepancy between different documents governing employment, the document containing rules most favourable to the employee shall prevail.

As a general rule, employment contracts are made for an indefinite period of time. As an exception, an employment contract may be concluded for a definite period of time ('fixed-term contract') for the establishment of an employment relationship the termination of which is determined in advance as a result of objective reasons that are justified by a specific deadline, performance of a specific task or occurrence of a specific event.

If the employee works at an alternative workplace – e.g. works at home, the employment contract must contain special clauses about using the worker's own equipment and machinery, reimbursement for using the worker's equipment, premises, and the method of training and educating the worker.

## Probationary Period

An employer has the right to establish a probationary period for a maximum of six months. The imposition of a probationary period must be specifically stated in the employment contract. If during the course of the probationary period the employer determines that the employee does not meet the criteria set for the position for which the employee was hired, the employer may dismiss the employee without payment of severance and with only seven days' written notice.

## Temporary Employment Agencies

As a possible alternative to the regular employment structure, employees may be hired through a temporary employment agency. In such cases, the temporary employment agency is considered to be the employer, and the employee is assigned to work at the assignee on the basis of a secondment agreement between the temporary employment agency and the assignee for which the work is to be performed. An individual may be seconded by the temporary employment agency to the assignee for up to a maximum of one year continuously, and cannot be rehired for at least one month by the same assignee.

## Working Time

As a default rule, regular working time is set at a maximum of 40 hours a week. In addition, an employee cannot work more than 6 days a week. The maximum regular working time is inclusive of a mandatory 30-minute daily break. This effectively means that, as a rule, an individual cannot work more than 37.5 hours in a five-day week or 37 hours in a six-day week. Any work in excess of the maximum regular working hours is considered to be overtime work.

Overtime work is subject to a special regime. The labour inspector must be notified of overtime work in particular cases defined by the Labour Code. The labour inspector is authorized to ban overtime work in cases when it is determined that the overtime work adversely affects the employee. Overtime work must be paid extra.

## Holidays, Days Off and Vacation

There are 14 national holidays and non-working days in Croatia, namely:

- New Year's Day (1 January);
- Epiphany (6 January);
- Easter Sunday;
- Easter Monday;
- Labour Day (1 May);
- Corpus Christi (9th Thursday after Easter Sunday);
- Anti-Fascist Struggle Day (22 June);
- Statehood Day (25 June);
- Homeland Thanksgiving Day (5 August);
- Assumption of the Virgin Mary (15 August);
- Independence Day (8 October);
- All Saints' Day (1 November);
- Christmas Day (25 December); and
- Boxing Day/St. Stephen's Day (26 December).

Employees working on a Sunday or public holiday are entitled to additional pay as defined by the employment contract, collective labour agreement and/or work by-laws.

Employees in Croatia are entitled to an annual leave of at least 4 weeks in a calendar year. An employee is entitled to use his/her annual leave (in full) once he/she has worked for an employer for at least 6 months. The employer must prepare an annual leave schedule no later than 30 June of the relevant calendar. The Labour Code further requires that the employer notify employees on the schedule of their annual leave at least 15 days before the annual leave is to start.

An employee whose employment contract is terminated shall be entitled to a proportion of annual leave in that calendar year.

## Salaries

Salaries must be paid to employees at least once a month. As a default rule, employers must pay the salary and other employment-related payments no later than the 15th day in the month for the preceding month. The salaries may not be lower than the minimum monthly salary established by applicable Croatian laws.

## Termination of Employment

Generally, an employment relationship may be terminated by:

- mutual agreement of the parties;
- the employer or
- the employee.

The employer may terminate the employment contract only on specific grounds provided in the Labour Code (including staff redundancy for business reasons, employee's repeated failure to fulfil his/her duties or employee's gross breach of duties). An at-will termination of an employment contract by the employer is not allowed.

When terminating employment for any reason, employers must strictly comply with specific procedures and requirements provided in the Labour Code. Except when employment is terminated due to a gross breach of an employee's duties, when terminating employment the employer is required to observe applicable notice periods and the employee's right to severance. The Labour Code provides for minimum notice periods and minimum severance pay that will prevail whenever the employee's rights are diminished by the employment contract.

## Have you heard of Dubrovnik?

The prosperity of the city of Dubrovnik was historically based on maritime trade. As the capital of the Republic of Ragusa, a maritime republic, the city achieved a high level of development, particularly during the 15th and 16th centuries. Dubrovnik became notable for its wealth and skilled diplomacy. Dubrovnik was once a city-state and some people say it was the first state to recognize the independence of the United States.

The hit HBO series Game of Thrones was filmed on the Dalmatian coast, in Dubrovnik and Split.

The fortified walls of Dubrovnik (where Game of Thrones was filmed) are the most preserved fortification system in Europe. Agatha Christie spent her second honeymoon in Dubrovnik and Split.



## Regulating Stay and Work of Foreigners in Croatia

The conditions for granting temporary or permanent stay to foreigners, as well as work permits, are regulated by the Foreigners Act (Official Gazette No. 130/2011, 74/2013, 69/2017) and accompanying by-laws.

### Categories of Foreigners

The Foreigners Act groups foreigners who wish to stay or work in Croatia into several categories. The documents submitted with the application depend on the category. Those categories are:

#### Nationals of EEA Member States and Their Families

Nationals of EEA member states or the Swiss Confederation and their family members, or family members of Croatian nationals intending to stay in Croatia longer than three months have to register temporary residence no later than eight days before the end of the three-month period with the competent police administration or police station depending on the address.

A certificate of registered temporary residence is issued in the form of a biometric residence permit valid for up to five years.

#### WORK OF EU MEMBER STATE NATIONALS AND THEIR FAMILY MEMBERS

Generally, nationals of EU member states and their family members can work and provide services in Croatia with no residence or work permit and no work registration certificate.

However, after accession of the Republic of Croatia to the European Union, some EU member states (12) implemented restrictions for employing Croatian citizens.

The following EU member countries have limited access to their labour market for Croatian nationals: Austria, Malta, The Netherlands, Slovenia and the UK (up to 01 July 2018 when they will decide whether or not to extend this limitation).

Based on reciprocity, restrictions apply for nationals of those EU member states and members of their families in accessing Croatia's labour market.

Consequently, foreigners from those countries can regulate their legal work status in the following manner:

- if they want to work up to 90 days a year based on a work registration certificate (for the purpose regulated by the Foreigners Act / this mostly applies to managing directors who periodically visit Croatia);
- if they want to work more than 90 days a year and are establishing labour relations in Croatia, they have to apply for residence and a work permit.

Despite these limitations, obtaining residence and work permits for key personnel, foreigners holding key positions in companies, foreigners transferred as part of internal staff transfers within companies, is just a procedural question.

### Third-Country Nationals

#### THIRD-COUNTRY NATIONALS WITH PERMANENT RESIDENCE IN AN EEA MEMBER STATE AND THEIR FAMILIES

Foreigners from this category can submit their temporary residence application to Croatia's diplomatic mission/consular post in the EEA member state where they have permanent residence or to the police administration/station in Croatia.

Temporary residence to a third-country national with permanent residence in another EEA member state will be approved if they:

- have a valid passport;
- have means of supporting themselves and their family members;
- have health insurance;
- meet the rest of the criteria for granting temporary residence given the nature of said stay.

#### HIGHLY-QUALIFIED THIRD-COUNTRY NATIONALS

##### *Issuing residence and work permits – the EU Blue Card*

Highly-qualified third-country nationals have to submit their application for work and residence permits to Croatia's diplomatic mission/consular post or to the police administration/station in their intended place of residence.

The EU Blue Card – residence and work permit – simultaneously grants temporary residence and work in Croatia.

The residence and work permit can be granted to third-country nationals who meet the criteria stated in Article 54 of the Foreigners Act (a valid passport, health insurance, proof they have means of subsistence) and enclose:

- a work contract or other corresponding contract for performing highly-skilled labour, lasting for at least one year
- proof of completed secondary school education or under graduate and graduate studies or integrated undergraduate and graduate studies or specialist graduate studies.

The residence and work permit (the EU Blue Card) is issued in the form of a biometric residence permit.

### **THIRD-COUNTRY NATIONALS**

Nationals of third countries are foreigners who are not nationals of European Economic Area (EEA) members. Regulating their stay or work depends on whether they have permanent residence in an EEA member state, whether they are family members of a national of an EEA member state, the Swiss Confederation, Croatian national, or do not fall under any of the abovementioned categories.

### **Temporary Residence**

May be granted on the following grounds:

- family reunification;
- secondary school education and university studies;
- scientific research;
- humanitarian grounds;
- work;
- work of posted workers or for other purposes.

Foreigners who do not need a visa to enter Croatia can submit their temporary residence application to the police administration/police station according to the intended place of residence, employer's location or place of work.

Foreigners who do need a visa to enter Croatia must submit their temporary residence or work and residence application to a Croatian diplomatic mission/consular post. Exceptionally, they can submit the application to the police administration/police station according to the intended place of residence if:

- they are coming for the purpose of regular undergraduate, graduate or postgraduate studies;

- they are coming for the purpose of scientific research based on a visiting contract;
- they are covered by Article 76, Paragraph 1, Items 12, 13, 14 and 15 of the Foreigners Act. These are foreigners working as part of youth mobility programmes run by the Republic of Croatia in cooperation with other states, scientific research and foreigners employed for scientific, scientific-teaching or other research work places in scientific legal entities, university professors, native speakers of foreign languages, foreign-language instructors and other lecturers invited by Croatian universities or registered foreign language schools, foreigners working pursuant to an international treaty, other than the treaty referred to in Article 79, Paragraph 1, Item 2 of the same Act.

The following must be enclosed with the application:

- a 35x45 mm colour photo;
- a copy of a valid passport;
- evidence of health insurance;
- evidence of sufficient means of subsistence;
- evidence of the reason for temporary stay (e.g. marriage certificate, university enrolment confirmation or other proof based on the purpose of the intended stay).

The documents enclosed with the application must either be originals or certified copies, while foreign documents have to be translated into Croatian and certified in line with special regulations.

The documents must not be older than six months.

Within 30 days of receiving the notification that their temporary stay has been approved, foreigners must report their residence to the police administration/station. Failing to do so within the specified time period will render the temporary stay/work and residence permit invalid.

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