FICIL 20

TOMORROW IS THE CONSEQUENCE OF NOW

Position Paper No. 7

30 May 2019

FICIL's Position Paper by the Investment Protection and Court Efficiency Work Group

1. Summary

In 2018 and 2019, the Foreign Investors' Council in Latvia (hereinafter – FICIL) has continued to work on identifying the issues and offering solutions for the security, predictability and further improvement of the investment environment and improving the efficiency of the court system in Latvia.

FICIL's Investment Protection and Court Efficiency Work Group has been active, participating in working groups and discussions, preparing publications and organising meetings with the Ministry of Justice, the Enterprise Register and other State administration institutions. FICIL representatives also participate in the activities of the Commercial Law Amendments Working Group.

FICIL's recommendations for 2018 and 2019 cover the following areas:

1) improving the quality of the legislative process;
2) improving the efficiency of the court system;
3) ensuring good governance and compliance;
4) improving the regulation of commercial rights and further development of capital markets;
5) other recommendations for improving the investment environment in Latvia.

The report provides specific proposals for solutions to identified problems that create barriers, delays or hinder the pursuit of business in Latvia for foreign and local investors. Grounds are also provided for each recommendation, both based on the experience of FICIL members and analysed in the context of reviewing foreign best practices.

FICIL would like to emphasise that it appreciates the current cooperation with the Ministry of Justice on matters relating to the legal policy, development and improvement of Latvia's court and legal system.

2. Recommendations and rationale of recommendations

2.1. Transparency and predictability of the legislation process

FICIL considers it essential to work on further alignment of the legislation process at legislator level, which would prevent the passing of rushed and unconsidered initiatives for approval by the

Parliament. It should be noted that the legislator has the highest power in the adoption of laws and regulations, which subsequently affect every resident of Latvia.
Accordingly, the adoption of laws and regulations should be subject to special care and should not allow a situation where laws and regulations are those proposals directed by stakeholder groups, which have not been properly documented and for which there are insufficient grounds.

In order to avoid this problem, amendments to the Parliament Rules of Procedure should be proposed, imposing an obligation for all submitters of draft laws to prepare:

1) a clear written annotation for each draft law;
2) written grounds for each proposal submitted before the second or third reading of the draft law, including also information on consultations that have taken place during preparation of the proposals;
3) a written summary regarding each draft law.

It is also necessary to adopt and in practice accredit a clear principle that proposals unrelated to the purpose of the draft law shall not be included in the third reading in Parliament. It should be made clear that, at this stage of the legislative proposal, only technical amendments are allowed for the alignment of the text of the draft law and for language corrections, which shall in no way affect the substance of the draft law. A similar approach to the third reading also exists in other countries, such as Estonia and France.

A transparent and predictable legislative process and a qualitative outcome is an essential part of a constitutional State. These proposals will provide an opportunity to clarify the will of the legislator, provide an appropriate assessment of the impact of the law, as well as the identification of persons who have participated in the drafting of the law. In addition, these recommendations will ensure uniform application of the rule of law and help the interpretation of the law in contentious cases.

The aim of these recommendations is to promote legislative practices that would have a positive impact on the investment environment in Latvia and improve the overall quality of laws and regulations. These proposals are also included in the 2018 position paper of FICIL's Investment Protection and Court Efficiency Work Group. FICIL reiterates the significance of these proposals in this position paper.

2.2. Court system efficiency

FICIL emphasises the need to further improve the efficiency of the court system in Latvia. Specific solutions are proposed to achieve the objective, namely further specialisation of courts and judges, as well as improvements in procedural efficiency through the introduction of bifurcation of court procedures.

Court specialisation. It is clear that not all legal proceedings need unified procedures and equal resources.

FICIL considers it necessary to promote the efficiency of the court system as one of the methods calling for further specialisation of courts and judges in the settlement of certain categories of cases. This can be addressed both by setting up specialised courts and by setting up special chambers or other structures at the existing courts. Specialisation would mean that certain courts would have limited and exclusive jurisdiction to settle specific matters.

For example, cases regarding the annulment of decisions of capital companies (meetings of shareholders/stockholders) are examined by Jelgava Court and this has significantly reduced the number of cases of illegal takeovers of companies, which was still occurring just a few years ago. Court specialisation is also ensured in the handling of certain categories of cases in the field of child protection and in disputes relating to the protection of intellectual property rights. In cases where the courts examine specific categories of disputes, there are significant improvements in the speed of the proceedings (the judge spends less time settling similar cases), the number of errors is reduced and case law is created. Foreign practice shows that the judgments of specialised courts are more rarely appealed at the higher instance.[1] Therefore, creation of specialized courts could possibly reduce the traffic at the High Court, which, possibly could speed up the process of deciding whether the case is accepted for review by the High Court.

In FICIL's opinion, the specialisation of the courts in dealing with certain categories of cases is one way of ensuring that cases are settled qualitatively and in a timely matter. Both of these conditions are essential for safeguarding the rights that have been violated. FICIL calls for specialisation in the settlement of certain commercial disputes. A specialised court would have to deal with disputes relating to, for example, the following:

1) the application of the norms of the Financial Instrument Market Law;
2) application of provisions of the Group of Companies Law;
3) private claims raised on the basis of a violation of the norms of the Competition Law;
4) the application of the norms of the Financial Collateral Law;
5) means of guaranteeing collaterals entered in public registers (contesting their full or partial validity or applicability);
6) matters of the regulatory framework for investment protection, insofar as they fall within the jurisdiction of the Latvian courts;
7) large-scale claims in commercial disputes (requires an assessment of the characteristics of large-scale commercial disputes);
8) legal protection proceedings.

For the purposes of settling the disputes listed above, in FICIL's opinion specific expertise is required, regarding, for example, financial instruments, capital markets, competition rights, investment protection, the economy and finances.

Most Member States of the European Union have one or more specialised courts with exclusive jurisdiction on specific matters. Similarly, several countries have specialised courts on a variety of civil rights issues, such as commercial courts or courts under whose jurisdiction are employment or social welfare issues.[2]

There are several countries with old traditions of specialized courts, as well as countries, where such specialized courts are developed recently in response to the need of settling commercial disputes in a timely manner and qualitatively. The following provides only a brief insight into the experience gathered within the framework of FICIL's research.

Since the beginning of 2019 the Netherlands Commercial court has begun work and has already settled its first case.[3] This court has been created anticipating the consequences of Brexit to dispute

[1] For example, http://juristproject.org/what-we-do/specialized-courts-divisions
[2] Information on the countries indicated available at: https://e-justice.europa.eu/content_specialised_courts-19-en.do
[3] See more: https://www.rechtspraak.nl/English/NCC/Pages/default.aspx and https://netherlands-commercial-court.com/

settlement and developments in the field of arbitration as a good alternative in settling international commercial disputes. The Netherlands Commercial court hears commercial disputes with an international element, where the parties have agreed to settle the dispute in the particular court. Relations with the Netherlands is not a condition for hearing a case in this particular court, the court works in English and also applies laws of other countries. The judges of the Netherlands Commercial court are highly qualified in the field of commercial law and the first case was settled in about two months. The judgements of this court are recognized and enforceable both within and outside the European Union. In addition, state fees in all cases are around EUR 3000-4000, regardless of the amount of the claim.

Denmark has a number of specialised courts, such as the Maritime and Commercial Court (*Sø-og Handelsretten*), which has been investigating disputes related to maritime law and commercial law since 1862. The court's jurisdiction has been extended several times and the court is currently examining disputes arising from the Danish Trade Marks Act, the Design Law, the Marketing Law, the Competition Law, international trade rules and other commercial law issues. The same court also has a separate department examining bankruptcy, suspension of payments, mandatory debt settlement cases and debt repayment schedule review cases. Similarly, in Denmark, a separate Land Registration Court (*Tinglysningsretten*) was established in 2007, which both carries out the functions of the register (registration of real estate owners, registration of mortgages and other collateral, etc.) and deals with disputes arising from registration.

Germany has, among others, specialised financial courts, whose rulings may be appealed to the Federal Financial Court (*Bundesfinanzhof*). These courts have jurisdiction mainly in disputes relating to State fees, taxes and customs matters. In the first instance, three judges and two court members examine disputes.

There are separate courts in Ireland to deal with small claims (the amount of the claim does not exceed EUR 2000), as well as a separate Commercial Court. In essence, the court in question acts as a specialised Supreme Court body capable of dealing with cases immediately. The immediate examination of cases is achieved by means of special procedures which speed up the process of cases falling within the jurisdiction of that court. The court in question examines cases classified as "commercial matters"[4] in accordance with laws and regulations, such as:

- disputes arising from the Commercial Law;
- disputes arising from the Insolvency Law;
- disputes regarding intellectual property;
- construction disputes;
- administrative disputes;
- constitutional rights disputes.

In order for a claim to be accepted for examination by this court, the amount of the claim must be at least EUR 1 000 000 (with individual exceptions).

There are specialised commercial courts in Spain which have operated since 1st September 2004 and form part of the civil rights system.

There are commercial courts in Croatia which, in addition to the obligations laid down in other laws:

[4] Rules of the Superior Courts, Order: 63A, Commercial Proceedings : S.I. No. 2 of 2004. Available: http://www.courts.ie/rules.nsf/8652fb610b0b37a980256db700399507/71b5764f57d3440980256f340064227a?OpenDocument

- carry out registration and maintenance of court registers;
- decide on entries in the Register of Ships and Yachts, delegated to the jurisdiction of the court in accordance with the Maritime Code;
- decide on applications for the establishment, operation and exclusion of companies from the register;
- settle non-contentious matters specified in the Commercial Law;
- carry out procedures for the recognition and enforcement of judgments of foreign courts as well as arbitrary decisions in commercial disputes;
- provide evidence in disputes falling within its jurisdiction;
- apply law enforcement measures in court proceedings falling within its jurisdiction;
- decide on bankruptcy applications and implement bankruptcy procedures;
- provide international legal aid for obtaining evidence in commercial matters, etc.

Malta has a developed specialised court system. For example, at first instance there is a specialised court that supervises the notaries working in the country and notary archives as well as deciding on the accuracy of records in public registers. In addition, a special appeals court (tribunal) has been set up which deals with disputes on competition rights and consumer rights.

Although Austria operates on the principle that all courts examine different types of cases, there are also specialised courts in the major Austrian cities (Vienna and Graz).

In Vienna, there are five specialised courts dealing with civil, criminal, employment and social welfare matters, two of which deal with commercial rights cases. Commercial rights cases are primarily understood as being those civil matters where one of the parties is a merchant (with individual exceptions). Together with professional judges, a member representing the merchant shall also participate in the hearing in the first and second instance.

In Portugal, specialised commercial courts (*Tribunais de Comércio*) have been set up, covering the following matters:

- insolvency, where the debtor is a company, or a company included in the property connected to insolvency;
- decisions regarding the absence, invalidity and repeal of the articles of association and the memorandum of association;
- decisions regarding the suspension or revocation of decisions taken by companies;
- claims relating to industrial property and any of the cases provided for in the Industrial Property Code.

There are specialised courts in Finland, such as the Labour Court, the Social Insurance Court and the Market Court. The Market Court has jurisdiction over matters regulated by the Consumer Rights Protection Law, the Consumer Ombudsman Law and the Securities Markets Law. In addition, this court also examines cases related to the marketing and contract conditions, which are part of the Law on Contracts Between Credit Institutions and Entrepreneurs, as well as violations of the Law on Competition Restrictions.

The United Kingdom, in particular, England and Wales have specialised commercial courts (the commercial/mercantile courts) which examine commercial rights cases. There is also a specialised Technology and Construction Court in whose jurisdiction is the settlement of the respective cases.

Improving process effectiveness. In FICIL's view, a solution should also be considered to introduce in procedural laws the option of dividing the proceedings into several phases (bifurcation) with the

consent of both parties. That is, in cases where further progress is primarily dependent on the establishment of one or more circumstances (the existence of a violation or fact, etc.), the court could, with the consent of the parties, assign a separate hearing on one or more matters in the case, thereby saving the time and means of the court and the parties.

By applying such procedure for examining cases, only if it is established that, for example, the fact or violation exists, the court would move to the second phase and the matter of liability or the extent of damages would be examined. FICIL believes that such an approach would be particularly effective in complex cases, such as violations of competition rights and intellectual property rights disputes, as well as disputes regarding patent rights. At the same time, it should be noted that requests to examine matters separately should be decided at the very beginning of the proceedings, assessing whether the particular aspect can in fact be separated from the rest of the case, whether the evidence on the case to be examined does not overlap (wherewith consequently the procedural economy is only apparent), and whether there are indeed grounds to separate the matter from the rest of the case or whether the request has been initiated only to delay the proceedings. Where there are grounds to doubt the possibility of examining the case in question in separate proceedings, the court should reject such a request.

The main benefits of the possibility of bifurcation of proceedings should be the savings of the time and costs of legal proceedings.

State duties matters. FICIL has encouraged considering setting a "cap" on the State duty (fee), otherwise, as the amount of the claim grows, the State fee can grow to levels that create significant obstacles to access the court and can therefore create significant restrictions on the right to a fair trial.

In the case of claims not exceeding EUR 2134, a proportional fee of 15% of the amount of the claim, but not less than EUR 70, is applicable. On the other hand, for claims above EUR 2134, a total fee is set, the specific proportion of which depends on the amount of the claim. Following this method of application of the fee, claims for an amount above EUR 711435 are calculated as EUR 8715 plus 0,6% of the amount of the claim, without actually limiting the maximum amount of the State fee.

The existence of State fees is one aspect that limits access to courts. This observation was also made in the 2018 position paper of FICIL's Investment Protection and Court Efficiency Work Group, at the same time emphasising that a balance should be found to make sure that such limitations are commensurable. FICIL has pointed out that the absence of a cap on the State fee may unduly deny access to the court, particularly in large-scale monetary claims.

The problem in the absence of a fee cap is, for example, in the case of transaction claims, where the State fee is calculated on the basis of the amount of the transaction (Section 35, Paragraph one, Clause 11 of the Civil Procedure Law), but the observations made in practice show that the amount of the disputed transaction is not the most fair and reasonable criterion for calculating the State fee. For example, when challenging fictive transactions, the claimant must be able to pay the State fee from the amount of the transaction indicated by the parties of the disputed transaction.

Although Section 43 of the Civil Procedure Law provides for a list of cases where plaintiffs are exempted from payment of the State fee, in practice such claims are often required to be brought directly to persons who are not exempt from the State fee, moreover the exemption is not applicable to legal persons who, for financial reasons, may not be able to challenge the transaction if the

calculation of the State fee is related to the amount of the transaction. The financial burden imposed by the State fee on the plaintiff is reinforced by the fact that, in accordance with Section 34, Paragraph four of the Civil Procedure Law, when appealing the judgment of the first instance court on appeal, the State fee is payable at a rate calculated on the basis of the amount of the dispute before the first instance court.

In other countries, in contrast to Latvia's regulation, the maximum caps for State fees are set, and in claims for transaction disputes the amount of the fee is not connected to the amount of the transaction. For example, Section 59, Paragraph one, Clause 1 of the Estonian Law on State Fees states that a fee for claims of a financial nature depends on the amount of the claim. For claims of a financial nature straightforward fees are determined, which increase according to the amount of the claim, rather than being proportionate or total fees. In addition, a maximum State fee amount of EUR 3400 has been set, which is applicable to all claims exceeding EUR 500,000. In turn, in the case of claims of a transaction being null and void in Estonia, the amount of the State fee is calculated either as claims of a financial nature in accordance with the procedure laid down in Section 59, Clause 1 of the Law on State Fees, or determined as a straightforward fee of EUR 300 if it is not possible to determine the benefits of the plaintiff in the event of satisfying the claim.

Lithuania also has similar solutions for setting the maximum amount of the State fee, setting a maximum amount of EUR 15000, in Poland the State fee is no less than EUR 7 and no more than EUR 23245, in Italy the fee does not exceed EUR 1686 (for bringing a claim before the first instance court), in Sweden it usually amounts to EUR 87-270, but in certain claims EUR 512, while Finland has the highest fee of EUR 500. In France, the obligation imposed by the law of 30th December 1977 on the plaintiff to cover certain costs of the courts, called "*frais de greffe*", including the application fee, has been waived in full. The exception is commercial dispute courts, but the fees here are also relatively low. In Spain also since 2015, natural persons have not been charged the State fee for submitting a claim at all, and the fee is limited for legal persons to a maximum of EUR 300 (in 2007, in Spain the maximum amount of the State fee was EUR 6000).

Considering the examples of other countries, a maximum amount of the State fee should also be set in Latvia in order to prevent disproportionate obstacles to the protection of the rights and lawful interests of a person in court. The amount of the State fee could, for example, be set at EUR 7000 to EUR 10000, which is a good deal higher than the amount of the State fee imposed in Estonia, but at the same time less than in Lithuania. At the same time, it should be considered in the framework of the Civil Procedure Law to provide for the payment of a single State fee for disputing several bogus transactions that are interconnected, as is the case in neighbouring Lithuania.

2.3. Ensuring good governance and compliance

Good governance and compliance. FICIL actively supports the introduction of good corporate governance and compliance systems in companies and institutions, particularly the capital companies of public persons (State and local government controlled limited liability companies and joint stock companies).

In order to ensure the compliance of the activities of a capital company controlled by the public sector in particular, it is necessary to implement and continuously improve such essential good governance and compliance systems as:

1) a general corporate governance system;
2) an internal audit system for the prevention of money laundering and terrorism financing;
3) a system for monitoring the risks of sanctions;

4) a system for the prevention of corruption and conflict of interests;
5) a personal data protection system;
6) an internal whistleblowing control system;
7) other compliance systems, taking into account the specifics of the company's activities and risk-based assessment.

It should be noted that some of these systems and procedures are already required by law to be introduced, while certain systems are optional but desirable. It should be stressed that each company needs appropriate control systems, procedures and policies for the specific situation, depending on the business profile of the company.

FICIL calls for a thorough assessment of the activities of public-owned capital companies in order to identify existing gaps in corporate governance of public-owned capital companies and to analyse which policies, guidelines, procedures or healthy internal control systems are necessary for them and their level of detail, as well as continuous monitoring of the actual compliance.

Good corporate governance and compliance systems should motivate company boards and councils to achieve objectives that are consistent with the interests of companies and their shareholders (stockholders) and encourage effective monitoring.

FICIL would like to point out that the formal existence of internal laws does not, in itself, provide good governance for the company. The relevant internal laws and regulations should be introduced into the company and assessed for improvements and amendments. Good corporate governance means that policies, procedures, guidelines or simple rules are tailored specifically for each company according to its situation and operational specifics.

It should be noted that the implementation of a good quality compliance system should also take into account the following aspects:
1) the implementation and maintenance of the system requires resources (including a responsible employee or employees);
2) it is necessary to implement the compliance system in practice by informing all stakeholders and regularly organising the training of employees;
3) a compliance system shall be monitored and the implementation thereof controlled.

In addition, it is also essential to ensure compliance whether the company council (if appointed) actually carries out the supervisory functions of the board, as required by law. One such example of the successful implementation of the control system of the board is the council's setting of measurable key performance indicators discussed with the board and its members.

Availability of information relevant to commercial activities. FICIL has continued a constructive dialogue with the Enterprise Register of the Republic of Latvia with a view to strike a balance between the need to ensure data protection and the public access to and availability of information relevant for the performance of commercial activities for the identification, verification and risk assessment of business partners.

In accordance with Paragraphs 12 and 49 of Cabinet Regulation No. 191 "Regulations Regarding the Issuing of Information and Other Service Fees of the Enterprise Register of the Republic of Latvia", electronically available documents from the holders of rights or legal facts shall not be released in the registers of the Enterprise Register from 1st August 2018 for re-use (the exception being annual accounts). This means that as of 1st August 2018, certain categories of data in the

Enterprise Register are no longer available for re-use by companies such as Lursoft and Firmas.lv. Information may be received from re-users of data in the Enterprise Register regarding registered officials and participants, however no documents in the registration file or documents in the Enterprise Register file or decisions taken by the Enterprise Register are available. For example, the Enterprise Register no longer transfers public documents such as articles of association, members' register divisions, incorporation resolutions (agreements), rules on the reduction or increase of share capital, reorganisation agreements, etc. for re-use.

Consideration should also be made regarding the judgment of the Administrative Affairs Department of the Senate of the Republic of Latvia in Case No. 2019. A420322015, SKA-148/2019, in which a dispute was settled over whether the Enterprise Register, when publishing and transferring for re-use a police decision imposing an arrest on property, carried out unwarranted processing of personal data contained in the motive part, such as the data of the victims, and whether the legal obligations imposed on the Enterprise Register were justified in the disputed decision. In the specific case at the discretion of the Enterprise Register, it had a legal basis to transfer for re-use the full text of the police decision imposing an arrest on property, as one of the duties of the Enterprise Register is to ensure the issuance of information held by the Enterprise Register and Sub-paragraph 15.4 of Cabinet Regulation No 277 provides that the Enterprise Register shall issue electronic copies of documents in registration cases without a statement of compliance for persons with whom a contract has been entered into regarding the regular issuance of information, if they have been created during the term of the contract for the issue of information. In the opinion of the Senate, this does not exempt the Enterprise Register from the obligation to comply with the data protection requirements of individuals and does not justify the transfer of personal data contained in the motive part of the police decision to re-users.

Despite the fact that data is no longer available to re-users, anyone may request the necessary documents from the Enterprise Register. The Enterprise Register shall process such requests for information within five working days. Nowadays, such a deadline would be considered to be relatively long.

As can be seen from the above, there is currently a situation in which re-users of data are prohibited from using data from the Enterprise Register file or registration case, while equivalent tools for obtaining information are not yet available for use. At the same time, the Enterprise Register is taking action to address the situation. FICIL calls for the active continuation of this work and to ensure solutions for the availability of up-to-date information relevant to commercial activities.

2.4. Improving the regulation of commercial law and development of capital markets

Commercial law. FICIL welcomes the work on putting forward proposals in the framework of the Commercial Law (for example, employee options, notional capital, optimisation of different procedures and others) and continues to cooperate on further development of regulation (e.g. capital share categories, facilitation of reorganisation processes, problems with the transfer of shareholders' registers in closed stock companies, the continuous and balanced facilitation of capital raising procedures). FICIL proposes to develop more flexible rules of the Commercial Law applicable to capital shares and capital structure of limited liability companies (including the introduction of capital share categories and substantially relieving the procedures for conversion of limited liability company into the legal form of joint stock company). In general, the regulation of the development of the commercial laws shall be continued to facilitate implementation of legal and substantiated capital attraction and other financing projects for commercial companies.

On the development of laws for the improvement of capital markets. The development of capital markets has a major impact on the country's overall economic development. FICIL appreciates the progress made to date in the regulatory framework for capital markets. In order to encourage business owners and management to choose capital markets as a source of funding, it is necessary to continue to work both on improving the regulatory framework of existing legislation and on introducing a financial support instrument for the inclusion of companies in a regulated market, in line with competition and State aid rules.

Inclusion of public-sector capital companies in the regulated market. FICIL expresses its support for the development of capital markets in Latvia and for measures that would facilitate the raising of funding needed for business development in capital markets.

The 2018 position paper already pointed out that Latvian companies are mostly reluctant to raise funding by offering their shares in public circulation – only a few companies have done so in recent years.

In FICIL's view, the inclusion of capital companies controlled by the State and local governments in the regulated market would contribute significantly both to the effective management of these companies and to the development of capital markets in Latvia. The following are recommended to achieve these aims:

1) to carry out or actively pursue the assessment of capital companies belonging to public persons, including with regard to the suitability of the company's business model, capital structure, corporate governance for inclusion in capital markets;
2) to develop an appropriate action strategy for preparing the activities of companies eligible for capital markets for inclusion in the regulated market;
3) to identify key indicators that would show whether the company's progress on the capital market has been successful. For example, it would be necessary to identify results that can be achieved during the process, such as the minimum amount of capital to be raised, the minimum amount of institutional investor participation, the level of involvement of private investors, etc.

FICIL continues to be available for cooperation to improve the investment environment in Latvia.