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EMERGING LITIGATION TRENDS AND RECENT DEVELOPMENTS IN BULGARIA

Cases of state liability for violations of EU law are rapidly increasing in Bulgaria, having already formed extensive case law on that matter. Below is a brief preview of some of the latest cases resolved by Bulgarian courts of law and having its legal ground in Art. 4, § 3 TEU with the most interesting conclusions related thereto:

1. KMB Bulgaria vs. the Supreme Administrative Court (Case 51/2020, Sofia Appellate Court)

In a recent case, the competent Bulgarian court awarded a local entity against the Supreme Administrative Court for a violation of EU law due to the **incorrect application** of Art. 168 of *Directive 2006/112/EC* relating to the right to refund of VAT and *Art. 267 TFEU*, according to which the national court is always required to refer the matter to the CJEU for interpretation if a question is raised before it in a pending case and the decision thereon would be final.

The case had been initially brought by the claimant KMB Bulgaria in connection with the refusal of the Bulgarian tax authorities to recognize the right to refund VAT to the company in a specific case, which is explicitly regulated in the Bulgarian tax legislation. The refusal of the authorities was confirmed by the competent Bulgarian administrative courts, where the last instance – the Supreme Administrative court also, in interpreting the relevant provision, refused to grant the applicant's request for a preliminary ruling by the CJEU on the relevant provision concerning the right to VAT refund, even though at the time there already were several controversial decisions of the same court on similar matters.

In the following case based on art 4, para 3 TEU the court held that the Supreme Administrative Court had misinterpreted the applicable VAT directive, and in particular art. 168 (“*In so far as the goods and services are used for the purposes of the taxed transactions of a taxable person, the taxable person shall be entitled, in the Member State in which he carries out these transactions, to deduct the following from the VAT which he is liable to pay*”) in the sense that the concept of EU law about the legal institute of VAT, and in particular the right to tax credit on receipt of taxable supplies to use them to carry out the economic activity of the taxable person receiving the supplies, remained unclear in its entirety.

Moreover, the court held that, even without a referral to the CJEU, the Supreme Administrative Court could have reached a correct interpretation of the relevant EU law had it use the conclusions of the CJEU on similar preliminary requests, made by other Bulgarian courts in the past.

The decision rendered by the Sofia Appellate Court and then fully confirmed by the Supreme Court of Cassation, is seen as an example for other local courts as it examines and justifies in detail the **prerequisites** for engaging state's liability for violation of EU law, stating that this principle is also applicable where the infringement stems from a **decision of a national court**.

2. State enterprise "Izgreve" vs the National Assembly and the the Public Enterprises and Control Agency (Case 2415/2020, Supreme Court of Cassation)

Similarly, in another recent case, a local entity has been awarded against the Bulgarian Parliament and the Public Enterprises and Control Agency (former Privatization Agency) for material violation of EU law - the **inaction** of the Bulgarian Parliament **to repeal** a legal rule and its continuous application by the respective state agency. The legal rule in question is § 8 of the Transitional Provisions of the Privatization and Post-Privatization Control Act (PPP). It enabled the State, through the Privatization Agency, to establish a legal mortgage on the assets of the privatized company for outstanding obligations of the buyer under a privatization contract.

It is indeed because of this provision that the European Commission initiated infringement procedure against Bulgaria as early as 2012 because it overruns the right to free movement of capital and can affect any future investor. Despite the threat of sanctions, national Parliament had been delaying its repeal for three years, with the draft bill put on hold for two years without any ground.

The court under the following case for infringement of EU law held that such rule has led to **inequalities** between the Bulgarian State and other individuals and therefore to violation of the rule of Art. 63 TFEU on the *free movement of capital* and the provision of Art. 49 TFEU on the *freedom of establishment*. The court further held that the principle applies where the national legislator is liable for the alleged failure to fulfil an obligation, which in the present case is the failure of the Parliament to repeal the rule contrary to fundamental principles of EU law and the Bulgarian Constitution, even after the obligatory instructions of the European Commission.

3. Capital Leasing vs the Prosecutor's Office of Republic of Bulgaria (Case 1914/2020, Supreme Court of Cassation)

The case has been commenced by the local company Capital Leasing, dealing with car and other specialized equipment leasing. In 2010, this company was accused by the Prosecutor's Office of Republic of Bulgaria for being part of the organized crime in Bulgaria and a "money laundering hub", linked to particular persons arrested for organized criminal

activity in the case “Octopus” which gained great social attention at that time. In this regard, a huge number of documents have been seized from the company by the prosecutors in charge, including those directly related to the existence of its core business, such as company’s computers and periphery, original contracts and other documents, correspondence with customers and state institutions, etc. For several years, those evidence was unduly detained by the Prosecutor’s Office, despite persistent requests by the company for their return, which in practice led to the liquidation of the company’s business and its legal termination later.

In the following case for damages against the Prosecutor’s Office of Republic of Bulgaria, the applicant stated that the seizure of all its documentation effectively deprived it of the opportunity to pursue its business, including to adequately protect its financial interests as a creditor under the leases concluded, to obtain insurance compensation for certain insurance events and to maintain the capital adequacy necessary to renew its business license as a financial institution. All this, according to the claimant, constituted a violation of Art. 63 TFEU establishing the free movement of capital and therefore violation of EU law. Along with this, the company claimed non-material damages, resulting from undermining the image of the company and loss of confidence by the investors due to the ungrounded accusations.

Both the first and the appellate instance rejected the claims as ungrounded, with the main argument based on the fact that the case does not represent infringement of art. 63 TFEU as the said provision applies *ratione loci* “worldwide”, i.e., to both capital movements within EU’s internal market and to movements from the internal market to third countries (and vice versa), while in the present case there was no such international link and it entirely concerned an “internal state”. It has been considered by the first and second instance courts that the so-called purely internal states do not, in principle, fall within the scope of the provisions of the Treaties concerning fundamental freedoms of movement (free movement of persons, goods, services and capital), so that the State cannot be held liable for a breach of EU law.

The second instance decision has been appealed and referred for review to the Supreme Court of Cassation, which, with a pioneer judgment dated 2 March 2021 repealed it and instead partially favored the claims lodged. In its final decision the Supreme Court found that “the searches and seizures carried out against the claimant under the investigation proceedings were unlawful, even though they have been carried out by a proper investigation authority within the scope of its competence and in accordance with the established legal procedure, as they did not comply with the principle of *proportionality* laid down in the EU (and national) law, according to which the restrictive measure taken on its content must be fit to achieve the legitimate objective pursued, necessary for its achievement and, most of all, to be *proportionate*, i.e. it shall not affect the legal sphere of the addressee to a greater extent than is necessary to achieve the objective”. Indeed the

principle of proportionality, as one of the general principles of EU law (its primary law), aims to grant rights to individuals and, accordingly, the direct effect as one of the necessary prerequisites for engaging the state's liability.

Finally, the Supreme court found that the actions of the Prosecution Office disproportionately affected the claimant's right to conduct business; especially since no evidence of the expected effectiveness of the measures imposed or empirical evidence of the likelihood of its success has been provided in the case. As such, the Prosecutor's Office of Republic of Bulgaria had manifestly and severely exceeded the limits of his discretion and has therefore committed a sufficiently serious breach of the legal principle of proportionality laid down in EU law, which is intended to grant rights to individuals, the latter enabling state's liability for breach of EU law.

In each of the above cases, the Bulgarian Supreme Court has precisely and comprehensively formulated the **criteria** for engaging state liability for a violation of EU law through the characteristics of the individual case:

- (1) the subject-matter of the infringed EU rule relates to the grant of rights to individuals;*
- (2) the breach of the rule is sufficiently material;*
- (3) there is a direct causal link between the infringement and the damage suffered by individuals; and*
- (4) the national court which committed the alleged infringement acted as a last instance.*

Furthermore, the Supreme court concluded that the actions by which the State has infringed EU law need not to be carried out intentionally or negligently to engage its liability, i.e., without the need of establishing guilt. Where the violation was committed intentionally or negligently, the prerequisite 'sufficiently substantial' shall be always presumed to exist. However, the latter may also exist, despite the due diligence, in cases where the public authority had no discretion to decide the respective matter, the rule infringed was clearly and precisely formulated, in the event of failure to make a reference for a preliminary ruling before CJEU, etc. Finally, the court found that EU law may be infringed not only where national legislation, containing a rule which does not comply with European Union law, has been applied, but also where EU law has not been applied or applied inaccurately, the applicable rule being misinterpreted, and also where it was not applied, irrespective of whether it is expressly regulated or can be derived from national legislation (i.e., objectively existing in another form in national law).

The increasing number of cases for breach of EU law also raised the question of which **procedural order** should be applied, since the Bulgarian legislation did not contain explicit rules at that moment. For a certain time, due to the novelty of the issue, this has led to the formation of controversial case law. Finally, the Bulgarian legislator intervened and adopted in 2019 new **explicit provisions** of the applicable Liability for Damages Incurred by the State and the Municipalities Act, dealing with cases for infringement of EU law, providing that they should be heard under the same existing procedural rules as the cases for damages from violations of the national law and enjoying the same procedural advantages for the claimants.

With more than 15 dedicated lawyers making up our Dispute Resolution Practice Group, DGKV has an extensive experience and capability of handling legal disputes stemming from infringements of both domestic and EU law by the State. We are at your disposal to provide more information on the above case law as well as credentials and list of our landmark cases in this area upon your request.

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