



Factoring

Legal Framework in Croatia

Dubrovnik, 18 May 2015

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Croatian Financial Services Supervisory Agency (HANFA)

- The Croatian Financial Services Supervisory Agency (Hanfa) is a supervisory body whose scope of activities and competence cover the supervision of financial markets, financial services and supervised entities providing those services.
- Hanfa is an independent legal person with public authority within the scope of its activities and competence laid down in the Act on the Croatian Financial Services Supervisory Agency and other laws.
- Established on 1th January 2006 with the entry into force of the Act on the Croatian Financial Services Supervisory Agency.
- It is accountable to the Croatian Parliament.

Supervised Entities

- stock exchanges and regulated public markets, authorized securities companies and issuers,
- investment, privatization investment and pension funds management companies; investment funds; privatization investment funds; pension funds; Fund of the Croatian Defenders of the Homeland War and Members of their Families; and the Retired Persons' Fund,
- brokerage companies, brokers and investment advisers,
- the Central Depository and Clearing Company,
- the Central Register of Insured Persons (REGOS),
- insurance companies, pension insurance companies, insurance brokers and representatives,
- leasing companies and **companies providing factoring service**, unless the banks perform them within the scope of their registered activities.

Objectives and Principles

Principal objectives:

- fostering and safeguarding the stability of the financial system,
- supervising the legitimacy of supervised entities' operations.

In achieving its objectives, HANFA is governed by the principles of:

- transparency,
- building confidence among financial market participants and
- reporting to consumers.

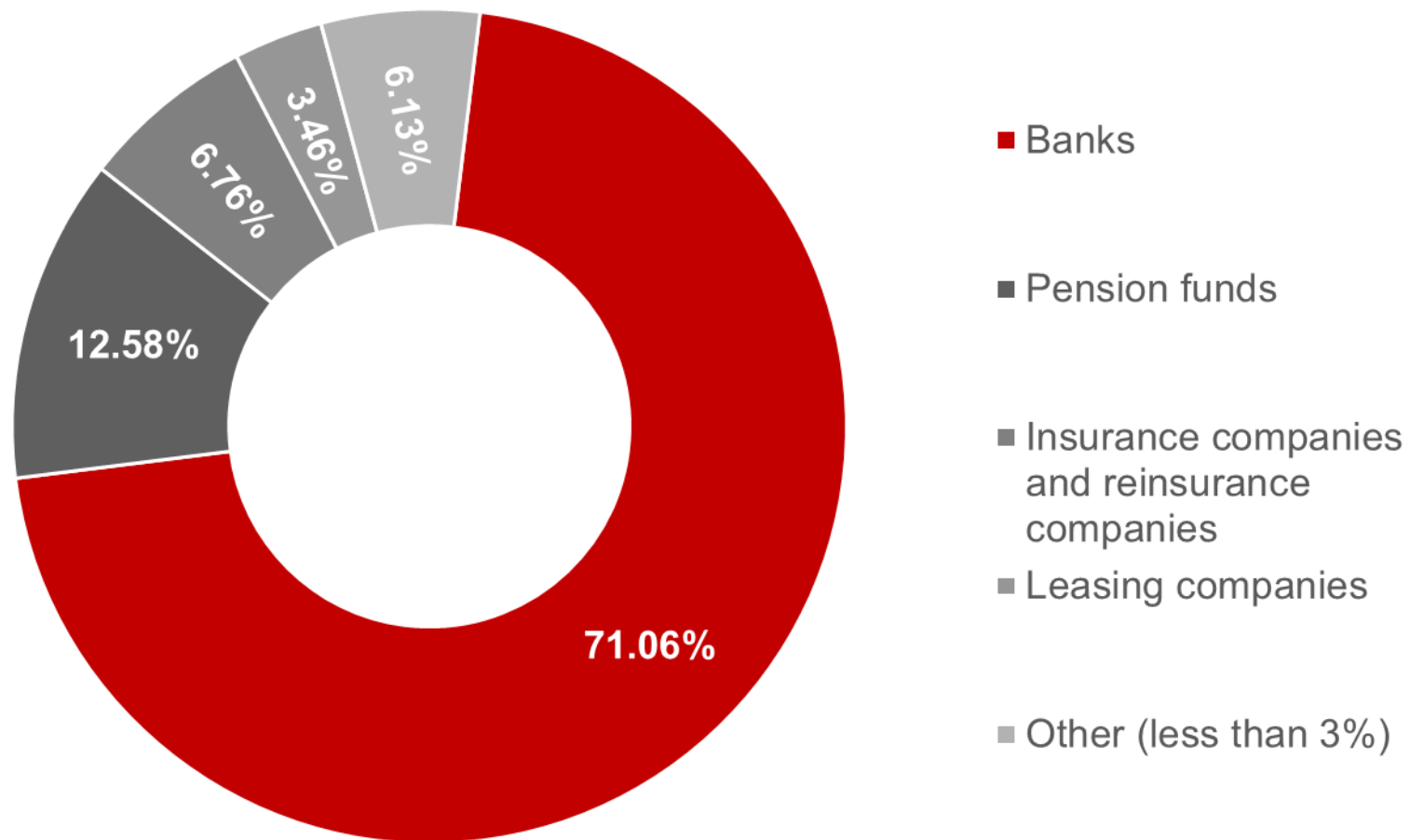
Overview of the Factoring Market in Croatia (as at 31 December 2014)

Financial Institutions Assets (as at 31 Dec 2014)

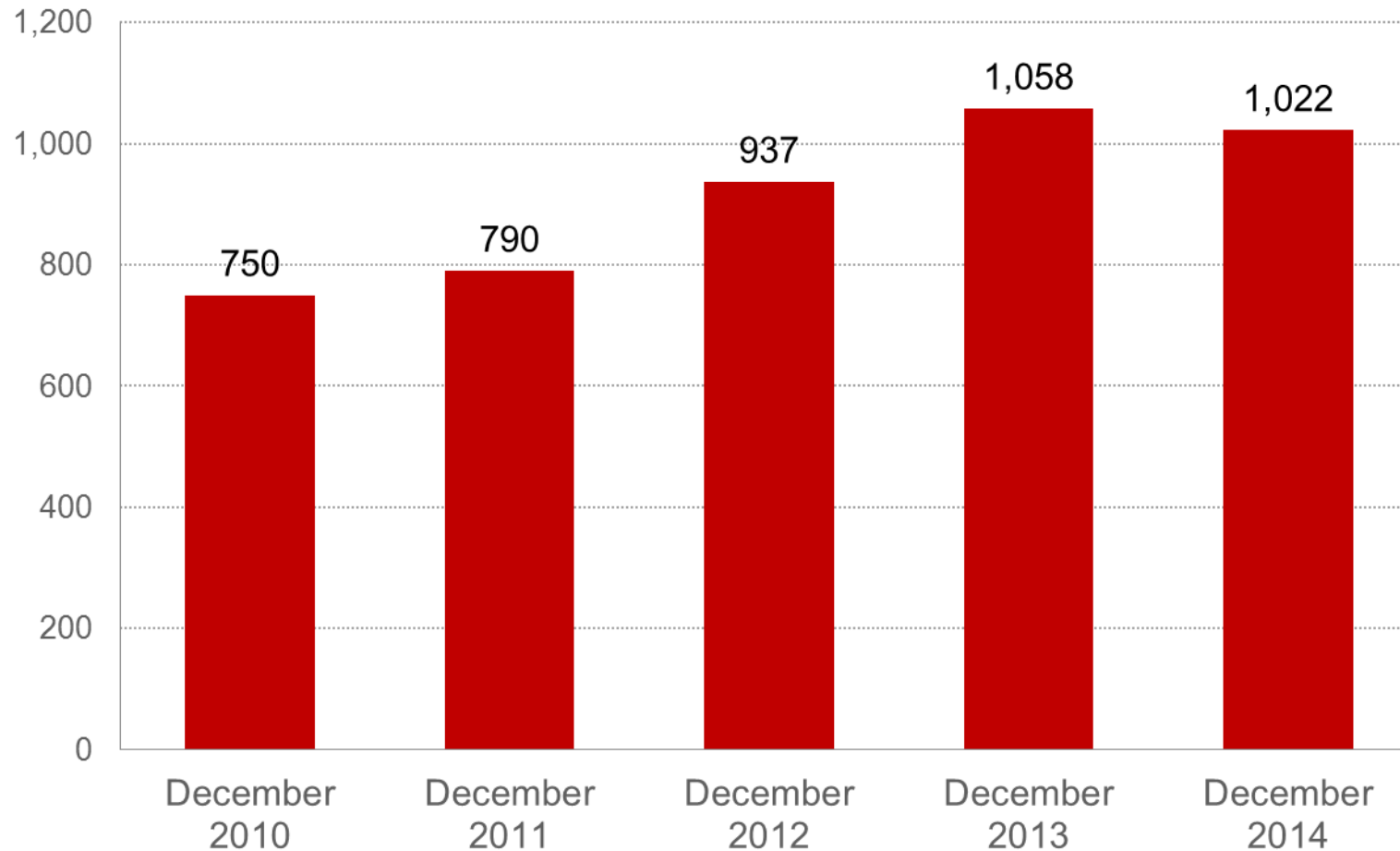
Financial institutions	Number	Assets (in EUR mil)	Share
Banks	29	51,263	71.10%
Pension funds	34	9,137	12.67%
Insurance companies and reinsurance companies	27	4,829	6.70%
Leasing companies	23	2,480	3.44%
Investment funds	111	1,958	2.72%
Factoring companies	17	1,049	1.46%
Housing savings banks	5	987	1.37%
Companies for the management of investment funds	23	135	0.19%
Credit unions	26	86	0.12%
Companies for the management of pension funds	6	85	0.12%
Pension insurance companies	1	52	0.07%
Investment firms	7	33	0.05%
Savings banks	1	2	0.00%
Total	310	72,097	100.00%

Note: Data for the banking sector refers to date 30.06.2014

Financial Institutions Assets (as at 31 Dec 2014)



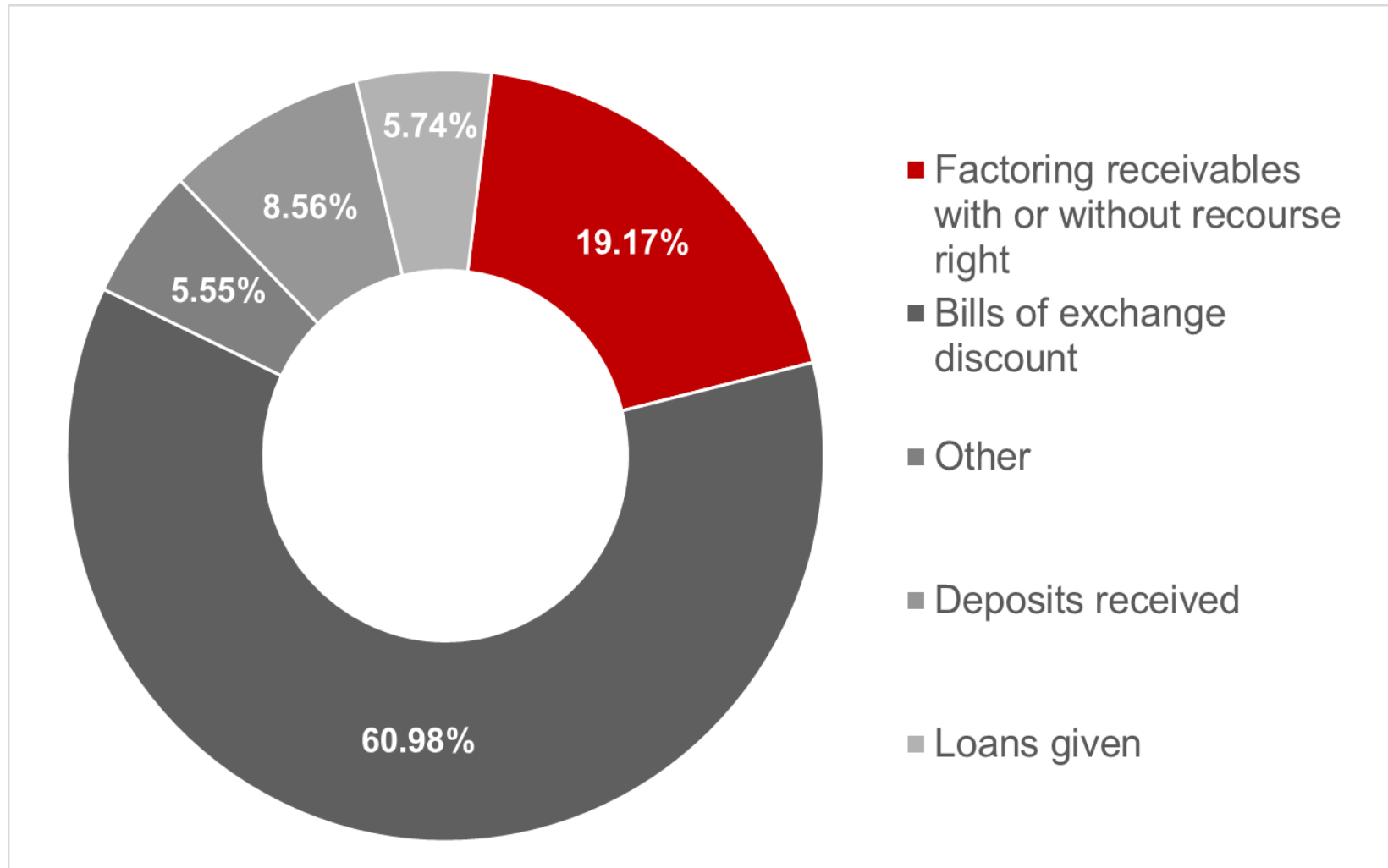
Total Assets of Companies Providing Factoring Service (as at 31 Dec 2014, *EUR million*)



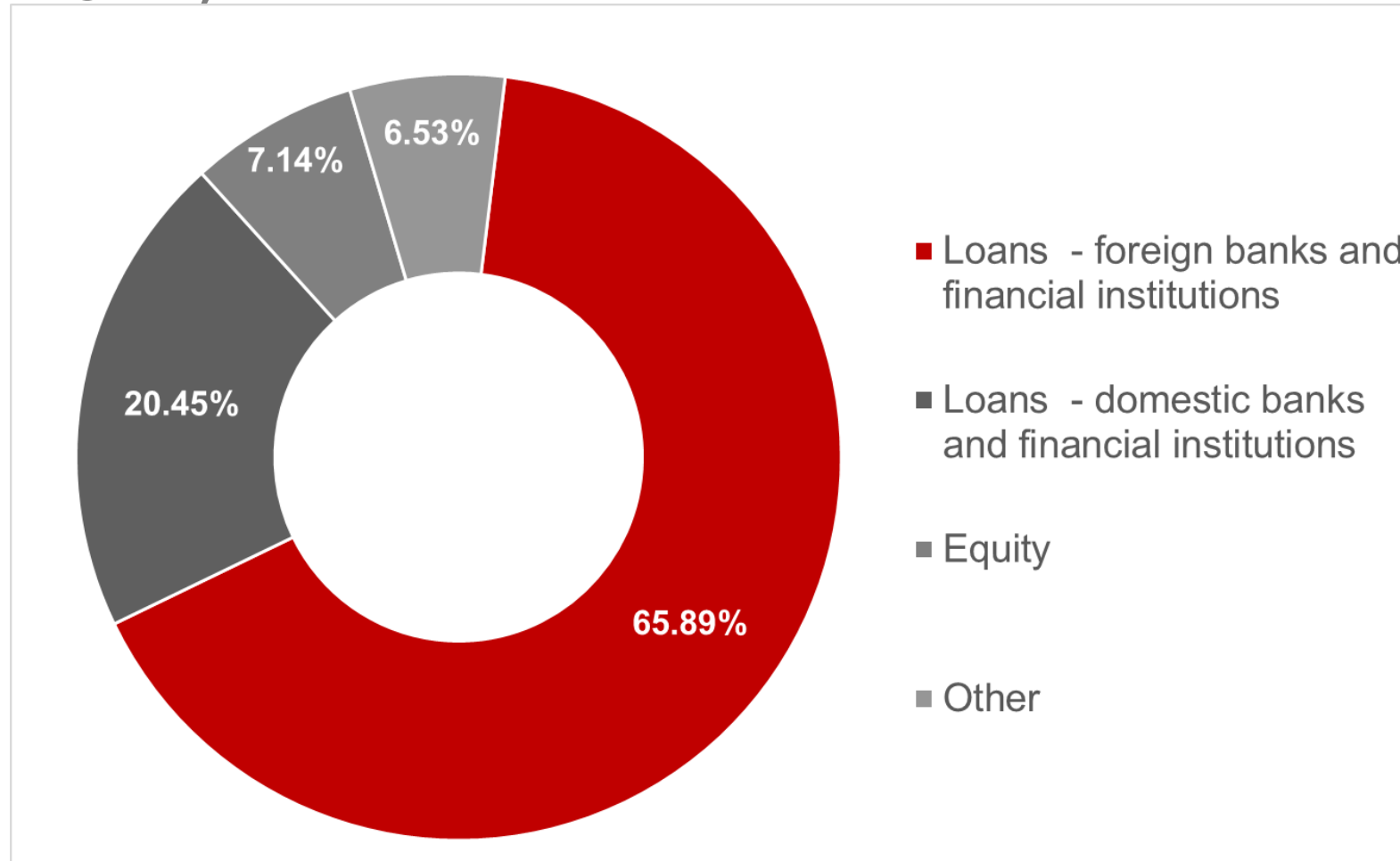
Ownership/Concentration

- 17 companies providing factoring services - 4 in direct and indirect non-resident ownership.
- The share of these 4 factoring companies in total assets of factoring companies stood at 72.8%.
- Out of 17 companies providing factoring services, 3 are part of the banking group.
- The Croatian factoring market is highly concentrated - the share of the top three companies accounted for 75.3% of total assets.

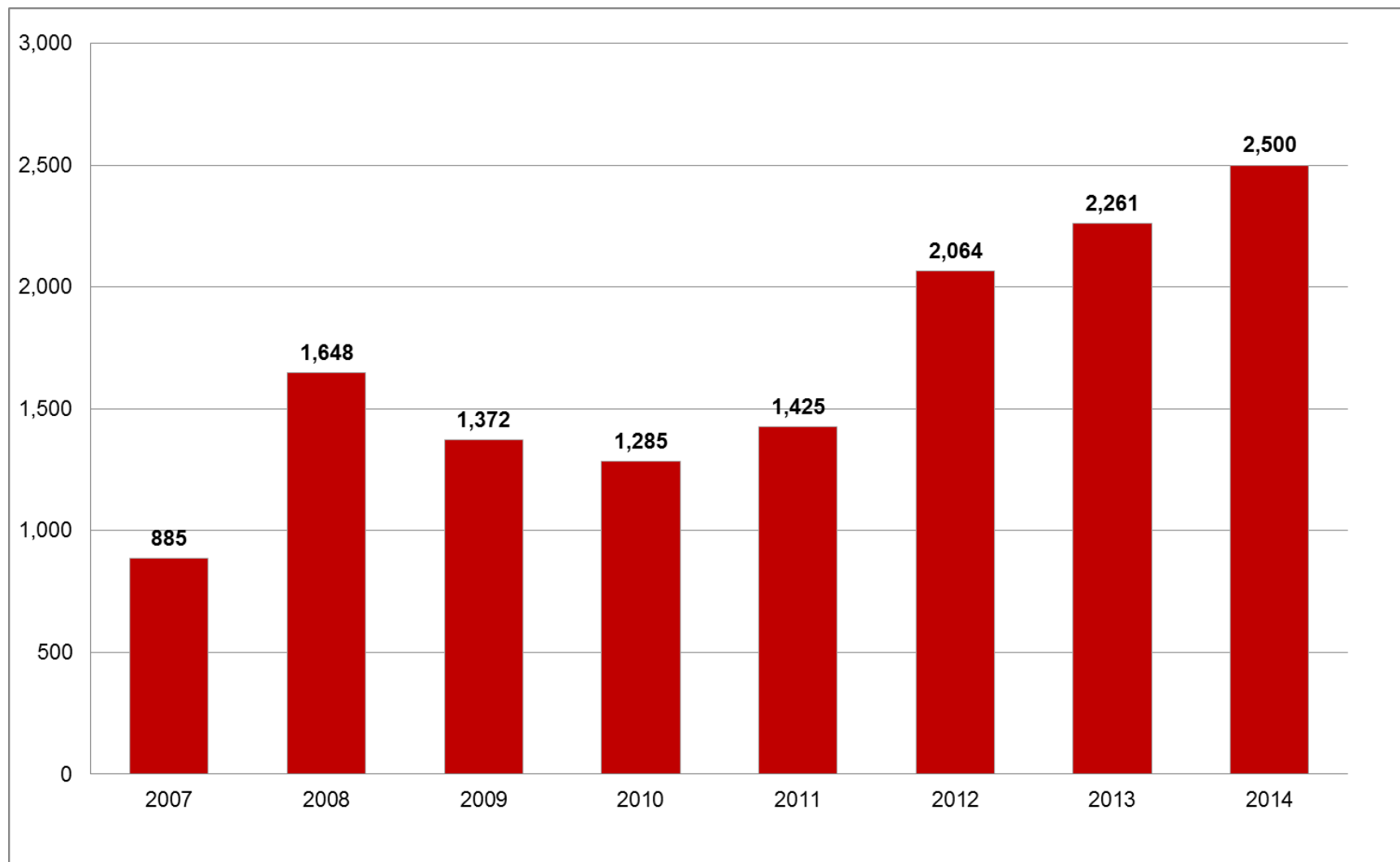
Assets Structure of Companies Providing Factoring Service (as at 31 Dec 2014)



Liability Structure of Companies Providing Factoring Service (as at 31 Dec 2014)



Transactions volume of Companies Providing Factoring Service (as at 31 Dec 2014, in EUR million)



Factoring Act

Factoring Act

- entered into force on 8 August 2014

The Act regulates the following:

- factoring agreement,
- rights and obligations of parties involved in factoring activities,
- terms and conditions for incorporation, operations and termination of operations of the factoring company,
- the conditions under which factoring companies with head offices outside the Republic of Croatia may provide factoring activities in the Republic of Croatia,
- reporting,
- supervision,
- risk management data.

Factoring Activity

- **Factoring activity** - a legal transaction in which companies providing factoring services, in accordance with the factoring agreement with the vendor and/or buyer, purchase outstanding receivables with or without recourse.
- **Receivable** - established by the invoice or any other document according to which a supplier of goods or services, or any other person instructed by him, charges for the supplied goods or services.
- **Factoring activity that incorporates bills of exchange purchase** - includes solely purchase of bills of exchange that are issued as a settlement instrument for the receivables arising from supplies of goods or services, domestic or foreign.

Factoring Agreement

- *Ordinance on the content of factoring agreements (Official Gazette 16/15)*
- Pursuant to the Article 14 paragraph 1 of the Factoring Act, the factoring agreement must contain the following provisions:
 - information regarding the contracting parties (company name or abbreviated company name, full name, main office or address and personal identification number – OIB),
 - specification of the factoring operations referred to in Article 8 of the FA,
 - description of the receivable,
 - description and the calculation of the interest expense,
 - description of the factoring commission, service charges and other expenses,
 - contracting parties authorized person signatures.
- Content of the factoring agreement shall indicate whether it is:
 - a domestic or foreign factoring,
 - with or without recourse.
- In the case of reverse factoring or factoring activity that incorporates bills of exchange purchase, this must be stated in the title of the agreement.
- In the case of factoring activity that incorporates bills of exchange purchase, factoring agreement must contain information regarding the bill of exchange (drawer, drawee, remitter, specific sum of money, place and time of issuing, maturity date, bill of exchange number) and the data on the bases of the formation of monetary claims.

Who is Allowed to Conduct Factoring Activities in the Republic of Croatia

- factoring company with the head office in the Republic of Croatia (RoC) - legal entity registered in the RoC and entered into the court registry on the basis of a license issued by HANFA.
- credit institution with the head office in the RoC - in accordance with the regulations governing the operations of credit institutions in the RoC.
- factoring company with the head office in an EU Member State fulfills the conditions laid down for mutually recognized services under the Credit Institution Act (ZOKI), can temporarily, directly or through a branch, provide factoring services.
- the branch of the factoring company with the head office in an EU Member State – has to acquire a license issued by HANFA.
- the branch of the factoring company with the head office outside the EU - has to acquire the license issued by HANFA.

Factoring Company

Factoring Company

- Legal entity registered in the RoC and entered into the court register on the basis of a license issued by HANFA.
- It can be incorporated as a joint stock company or Ltd.
- Bodies of factoring companies: management board, supervisory board, assembly.
- **Management board:** at least **two members** – must obtain approval of HANFA, must satisfy the criteria of competence, experience and good reputation as prescribed by the Factoring Act and Ordinance
- **Supervisory board:** at least **three members**, must satisfy the criteria of competence, experience and good reputation prescribed by the Factoring Act and Ordinance
 - *HANFA does not issue approval for members of the supervisory board*

Factoring Company Activities

- Besides the factoring activities, reverse factoring and factoring activity that incorporates bills of exchange purchase, FC can:
 - collect, create, analyse and provide information on the creditworthiness of legal entities and natural persons engaged in independent activities
 - manage customer claims arising from the sale of goods or services and consultation in connection with the above
 - carry out export financing based on the purchase at a discount without recourse long-term non-matured receivables collateralized with a financial instrument (forfeiting)
 - conduct repurchase of the matured receivables
 - issuing credit cover when performing foreign factoring.
- *Ordinance on conditions and manner of performing activities of the factoring company (Official Gazette 16/15)* prescribes limitations on activities that are directly / indirectly related to factoring and which may not exceed 25% of total reported assets of factoring activities and factoring activities which include the purchase bill of exchange.
- FC is not allowed to purchase overdue receivables from loans or purchase of the risks and benefits on the basis of overdue receivables from loans of the credit institution or the purchase of overdue receivables or redemption of the risks and benefits arising from such claims from financial services that have a financing as a core topic and purpose.

Capital Requirements

- Capital stock of the factoring company may not be lower than HRK 1 million and must be fully paid in before the leasing company requests entry of its incorporation in the court registry
- Factoring company shall maintain capital in an amount which must not be lower than HRK 1.0 mil.
- *Ordinance on the capital of factoring companies (Official Gazette 12/15)* lays down detailed criteria for the calculation of the FC capital:
 - the capital calculation does not include: earnings before the decision-making of the Assembly of the allocation of profit, revaluation reserves, intangible assets
 - FC is required to prepare internal documents regulating the actions of the FC in case of inadequate capital levels,
 - FC is required to report HANFA on a quarterly basis.
- *FC shall submit Report on equity to HANFA for the first time as of 30/09/2015 (method of delivery will be provided through technical instructions).*

License for Conducting Factoring Activities

- The request for licence is submitted by the founders of the FC, HANFA approval is issued within 60 days after the receipt of an orderly request.
- The licence is issued for an indefinite period and can not be transferred to another person and does not apply to the legal successor.
- In the case of a company which already performed factoring activities and whose factoring activity was registered in the court register at the moment of the entry into force of FA, must submit a harmonization report (instead of applications).

Acquiring a Qualifying Holding

- Every legal/natural entity intending to directly or indirectly acquire or increase a holding in a FC, which could result in equity participation/voting rights reaching or exceeding 10%, 20%, 30% or 50% or in FC becoming a subsidiary, is subject to prior approval for acquiring qualifying holding issued by HANFA.
- Prior to acquiring a qualifying holding in another legal entity, the leasing company must obtain an approval for acquiring qualifying holding from HANFA on the basis of which it exceeds 20%, 33% or 50% of the voting rights or of the capital stock of the other legal entity
- FC included in the acquisition, merger or division of the company, need to obtain approval from HANFA.
- *Ordinance on the acquisition of a qualifying holding in a factoring company or another legal person (Official Gazette 129/14)*

Acquiring Qualifying Holding

- When deciding on granting approval for the acquisition of a qualifying holding in the FC, HANFA evaluates the adequacy and the financial condition of the intended acquirer of a qualifying holding to the following criteria:
 - the reputation of the intended acquirer,
 - the reputation, experience and relevant skills of persons conducting business after the acquisition of a factoring company if there will be such a change,
 - the financial condition of the intended acquirer,
 - assessment of the possibilities of factoring companies to comply and continue to comply the provisions of the FA and other laws and regulations applicable to the business of FC,
 - the existence of legitimate reasons to believe that the acquisition of a qualifying holding would carry out or trying to carry out money laundering or terrorist financing, or could increase the risk of money laundering or terrorist financing.

The Management Board

- **At least one** of the members of the FC management board must **speak Croatian** well enough to be able to perform this function.
- Members of the management board must be **full-time** employees of the FC.
- Member of the management board of a FC may be only the person who has obtained an approval from the HANFA.
- *Ordinance on the requirements for membership in management and supervisory boards of a factoring company (Official Gazette 129/14)* regulates:
 - criteria for management board members, procedure for issuing approvals and documents accompanying the application for performing the function of management board of the FC
 - content of the operational program for the FC, procedure and criteria for evaluation of the program and candidates for the FC board member representing the program
 - conditions that need to be met by members of the supervisory board of the FC

Criteria for Membership in the Management Board

- Corresponding expertise, skills and experience necessary for conducting the FC operations
- The individual has not been a member of the SB, the management or the person at the other position of leadership in the FC and any another company when it entered bankruptcy proceedings, in time of the compulsory liquidation decision or revoked authorization, unless the competent authority assesses that the bankruptcy, liquidation or revocation of the operating license were not caused by the careless or negligent work of the individual
- Whose assets are not opened or entered into bankruptcy proceedings.
- Has a good reputation.
- Has not been convicted of criminal acts against values protected by international law or any other criminal deeds.
- Has not been convicted of a misdemeanor or a criminal act which constitutes a grave and sustained violations of regulations related to HANFA, CNB or other competent authority activities.
- The individual meets the criteria for management member pursuant to the the regulation governing the establishment and operation of companies.
- The individual is not a member of the management board, procurator in other company.
- Individual to who HANFA refused the approval to perform the function of FC management board can not be a member of the FC management board at least one year after the decision was adopted.
- Has not been relieved of duties of a FC management board by the HANFA.

Supervisory Board

- The FC supervisory board must have at least **three members**.
- The FC supervisory board member shall possess corresponding expertise, skills and experience necessary to supervise the FC conduct of business – regulated by the FA and the *Ordinance on the requirements for membership in management and supervisory boards of factoring company*
- In addition to the competences pursuant to the Companies Act, the supervisory board of the FC shall give approval to the management and:
 - adopt business policies of the FC,
 - adopt financial plans of the FC,
 - organize internal control systems,
 - adopt the annual plan of the FC.

Duties and Responsibilities of the Management and Supervisory Board

- In carrying out their activities or duties, has to act conscientiously and fairly in accordance with professional standards and the best interests of customers as well as to protect the integrity of the factoring market.
- Act with diligence of fair and conscientious professionals in carrying out their responsibilities.
- Obtain and effectively use the resources and procedures necessary for the proper performance of FC.
- Comply with the provisions of the FA and associated regulations or in accordance with other laws regulating the operations of FC, and regulations based on those laws.

The Risk Management System and Reporting Requirements

The Risk Management System

- Risk management is a comprehensive process and set of measures, methods and techniques designed to identify, measure and assess and manage the risks to which the FC is exposed or might be exposed in the course of performing its business activities, including the reporting of the same.
- FC shall establish a comprehensive and effective risk management system in accordance with the type, scope and complexity of its business:
 - strategies, policies, procedures and risk management measures,
 - techniques of risk measurement,
 - the division of responsibilities in relation to risk management.
- The criteria and the method of risk management can be prescribed in a separate ordinance issued by HANFA.

Internal Audit

- Way of conducting internal audits in FC is prescribed by the *Ordinance on internal audit in the factoring company (Official Gazette 12/15)*
- FC must organize internal audit that independently and objectively assess the internal control system, provides independent and objective opinion and advice to advance the management in order to improve the business of the FC by bringing a systematic and disciplined approach to evaluating and improving the effectiveness of risk management, control and corporate governance
- To carry out internal audits, the FC may: (1) have an employee in the company, (2) entrust the conduct of internal audit to natural person who is not employed by the FC, (3) entrust the conduct of internal audit to another legal entity.
- Internal Auditor - Call a certified auditor or a certified internal auditor acquired in accordance with the law governing audits, or acquired in accordance with the rules and program of the competent professional organization for professional education of Internal Auditors
- The person conducting internal audit may not perform other tasks in the FC.
- Internal audit must not be conducted by the board members of the FC
- The FC is responsible for conducting internal audits even in the case of entrusting the performance of internal audit to another legal entity.

Annual Financial Statements

- Annual financial statements of the FC must be audited by certified auditor.
- The financial reporting of FC shall be subject to the Accounting Act and IFRS.
- The same audit company shall conduct a maximum of seven consecutive audits of financial statement in the same FC and shall not simultaneously provide services in the field of finance, accounting, internal audit, valuation, consulting, etc. to the FC.
- FC shall deliver to HANFA audited annual financial statements within 15 days from the date of issuance of the audit report, and no later than 30 April of the current year for the year audit reports are prepared for.
- *If HANFA determines that the audit report of the FC financial statements has not been performed or that the audit report is not drawn up in accordance with legal regulations or if it finds that the audit report is not based on true and objective facts – it may reject the auditor's opinion.*

Financial and Additional Reports

- The structure and content of annual financial statements and additional reports is prescribed by the *Ordinance on the financial and additional reports and chart of accounts for the FC (Official Gazette 16/15)*
- *Financial Statements* (Statement of Financial Position, Statement of Comprehensive Income, Statement of Cash Flows, Statement of application of capital)
- *Additional reports:*
 - Report on portfolio structure – factoring (SP-F),
 - Report on portfolio structure – factoring activity that incorporates bills of exchange purchase (SP-FOM),
 - Report on portfolio structure – reverse factoring (SP-DF),
 - Report on portfolio structure by economic activities, sectors and size of companies providing factoring service and factoring related businesses (SP- DSV),
 - Report on portfolio structure – activities directly or indirectly related to factoring (SP-OP),
 - Statement of Changes in allowance (IV),
 - Report on the quality of the portfolio (KP),
 - Report on large exposures (VI),
 - Report on the sources of funding (IS),
 - Report on the currency structure of assets and liabilities (VS-IO),
 - Report on the maturity structure of assets and liabilities (RS-IO),
 - Report on the structure of other financial assets (OFI),
 - Report on the structure of financial liabilities (OFO).

Financial and Additional Reports to HANFA

- *Ordinance on the financial and additional reports and chart of accounts for the FC (Official Gazette 16/15)*
- Instructions for filling out the report and the implementation of the Chart of Accounts – in process
- The method of delivery will be prescribed by the Technical instructions (xml. format).
- The first application for the quarterly reports as at 31/12/2015, that should be submitted to HANFA by 31/01/2016.
- The first application for the yearly reports as at 31/12/2015, that should be submitted to HANFA by 30/04/2016.

Reporting to HANFA– Other Information

- *Ordinance on the content of factoring companies' regular reports and reports submitted at the request of the Croatian Financial Services Supervisory Agency and on the manner and time limits for their submission (Official Gazette 140/14)*
- FC has to report on the following facts and circumstances:
 - entry and any change of data in the court registry,
 - assembly meetings and all decisions adopted,
 - shareholders of the FC and the acquisition or modification of qualifying stakes,
 - estimated opening, moving, closing or temporary terminating of branches or representative offices and/or other related changes,
 - investments based on which the FC acquired, directly or indirectly, qualifying stakes in another legal entity and all further investments in the same legal entity,
 - changes in the capital structure,
 - termination of certain factoring operations.

Supervision

Supervision

- **Supervision** means an inspection in order to establish whether the FC operates in accordance with the provisions of the FA, ordinances adopted pursuant to it, in accordance with other regulations, with the risk management regulations as well as in accordance with its own rules, standards and the codes of conducts in a manner that enables an orderly operation of the FC and the implementation of measures and activities aimed at eliminating the established violations and irregularities.
- the main **objectives of supervision** are checking the legality, security assessment and stability of the FC, in order to protect the interests of clients and the public interest, to contribute the stability of the financial system and to promote and preserve trust in the factoring market.
- HANFA has the authority to review parts of business with entities related to the FC, a shareholder of a qualifying holding in the FC and the person to to which the FC has outsourced certain business functions.
- HANFA may review the operations legal entity in cooperation with other supervisory body in Croatia and the EU Member States.

Supervision

- the direct supervision, in the premises of FC by examination of original documents, review and evaluation of the entire business, talking to members of management and other responsible parties.
- indirect supervision, in the premises of HANFA by analyzing reports which are submitted to HANFA by the FC within the prescribed deadlines, or at the request of HANFA.
- when determining the frequency and intensity of supervision for each FC HANFA takes into account the size, influence and importance of the FC, as well as the nature, type, scope, complexity and indicators of their business.

Supervision Measures

- In the case of illegalities and irregularities determined during the supervision HANFA can impose control measures to FC aimed at securing lawful and orderly operation and protect the public interest:
 - recommendations to management board,
 - pass the admonition,
 - eliminate unlawfulness and irregularities,
 - special supervision measures,
 - the abolition of license for conducting factoring activities.
- HANFA can impose special supervision measures in case:
 - FC has not acted in accordance with the decision of HANFA,
 - the capital of the FC is below the prescribed minimum,
 - in other cases when HANFA deems necessary.

Final annotations

Harmonization

- Legal entities that, on the day FA enters into force, conduct factoring activities and have been entered in the court registry shall continue operating as factoring companies in compliance with FA.
- Are obliged until 8 August, 2015 to:
 - Harmonize their factoring activities with provisions of the FA,
 - Harmonize their capital stock with Article 22 of the FA,
 - Harmonize their management with Article 46 and 47 of the FA,
 - Harmonize their board of directors with Articles 53 and 54 of the FA,
 - Harmonize their operations with other provisions of the FA, unless otherwise stipulated.
- If legal entities that conduct factoring activities on the day FA enters into force, does not align operations with the provisions of the FA within given time limit, shall cease to engage in factoring activities and delete factoring activity from the court registry.
- The procedure described in detail regarding the harmonization, can be found at www.hanfa.hr - *Notification regarding the proceedings of companies that meet the requirements of Article 117 para. 1 of the FA, in the process of their harmonization with FA.*

Final Annotations

- It is expected that the Factoring Act will allow:
 - greater legal security of all participants in the factoring market,
 - regulation of factoring companies that are not within the regulated banking / financial groups,
 - preservation of the financial stability of the entire financial market in the Republic of Croatia .

Thank you for your attention

www.hanfa.hr;

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