

28 November 2006

Screening report

Croatia

Chapter 9 – Financial services

Date of screening meetings:

Explanatory meeting: 29-30 March 2006

Bilateral meeting: 4-5 May 2006

I. CHAPTER CONTENT

The *acquis* covered by this chapter includes rules for the authorisation, operation and supervision of financial institutions and regulated markets. Financial institutions covered by the *acquis* can operate across the EU in accordance with the ‘European passport’ and the ‘home country control’ principle either by establishing branches or by providing services on a cross-border basis.

In the field of **banks and financial conglomerates**, the *acquis* sets out requirements for the authorisation, operation and prudential supervision of credit institutions, as well as requirements concerning the calculation of capital adequacy requirements applying to credit institutions and to investment firms. The two relevant directives have recently been recast to incorporate the new capital requirements framework based on the Basel II Accord. The *acquis* in this sector also lays down rules relating to supplementary supervision of financial conglomerates and to the taking up, pursuit of and prudential supervision of the business of electronic money institutions. Credit institutions are required to join an officially recognised deposit guarantee scheme, which must provide for a minimum protection of €20,000 per depositor. The *acquis* lays down rules regarding the annual and consolidated accounts of banks and other financial institutions. It also harmonises certain provisions concerning the reorganisation and winding up of credit institutions with branches in more than one Member State.

In the field of **insurance and occupational pensions**, several directives set out rules concerning the authorisation, operation and supervision of life assurance and non-life insurance undertakings. Specific provisions exist in the non-life sector for co-insurance, tourist assistance, credit insurance and legal expense insurance. The *acquis* establishes rules for the supplementary supervision of insurance groups. It also incorporates a prudential regulatory framework for reinsurance activities in the Community aiming removing barriers to the pursuit of reinsurance business, such as the obligation for the reinsurance undertaking to pledge assets. The directive on insurance mediation establishes a legal framework for the taking-up and pursuit of the activities of insurance and reinsurance mediation by natural and legal persons operating in the Community. In the field of motor insurance, several directives harmonise requirements concerning insurance against civil liability in respect of motor vehicles with a view to facilitating the free movement of goods and people, in particular by abolishing frontier controls on motor insurance. Directive 2003/41/EC regulates the activities and supervision of institutions for occupational retirement provision. The *acquis* lays down rules regarding the annual and consolidated accounts of insurance undertakings. It also harmonises certain provisions concerning the reorganisation and winding up of insurance undertakings with branches in more than one Member State.

In relation to **financial market infrastructure**, the directive on financial collateral arrangements aims to reduce and harmonise the formal requirements and procedures to create and enforce collateral across the EU, while the directive on settlement finality aims to reduce the systemic risk linked to the insolvency of a participant in payment and securities settlement systems.

In the field of **securities markets and investment services**, the directive on markets in financial instruments (MiFID) and its implementing measures set out a comprehensive regulatory regime covering the authorisation, operation and supervision of investment firms and regulated markets. The prospectuses directive and its implementing measures reinforce the protection for investors by guaranteeing that all prospectuses, wherever in the EU they are issued, provide them with the clear and comprehensive information they need to make investment decisions. The *acquis* also prescribes minimum transparency requirements for listed companies concerning both periodic and ongoing information. The directive on market abuse and its implementing measures introduce a harmonised and comprehensive administrative regime for prohibiting and

prosecuting insider dealing and market manipulation. The *acquis* also requires that Member States ensure that at least one officially recognised investor compensation scheme is established offering compensation up to €20,000. The legislation on investment funds (UCITS) sets out common basic rules for the authorisation, supervision, structure and activities of investment funds to facilitate the cross-border distribution of units of funds in the EU and to ensure adequate investor protection.

II. COUNTRY ALIGNMENT AND IMPLEMENTATION CAPACITY

This part summarises the information provided by Croatia and the discussion at the screening meeting. Croatia indicates that it can accept the *acquis* regarding financial services. Croatia indicates that it does not expect any difficulties to implement the *acquis* by accession.

II.a. Banks and financial conglomerates

The Croatian Banking Act (Official Gazette 84/2002) regulates banks, the Act on Housing and Savings and State Incentives for Housing Savings (OG 109/97, 117/97, 76/99, 10/01, 92/05) regulates housing savings banks and the Act on Saving and Loan Co-operatives (OG 84/02) regulates savings and loan co-operatives. The latter are sometimes referred to as "credit unions". Housing savings banks are sometimes referred to as "building societies".

As regards the requirements for the **taking up and pursuit of the business of credit institutions**, the Banking Act and related implementing measures regulate *inter alia* the conditions for establishment, authorisation, operations and termination of operations of banks and housing savings banks, as well as their supervision.

Banks need an authorisation from the Croatian National Bank (HNB) for their establishment and operation in Croatia. The Banking Act provides for an exhaustive list of circumstances in which the HNB shall refuse an application for authorisation. Similarly, the Banking Act lays down an exhaustive list of circumstances in which a bank's authorisation may be withdrawn or revoked. Branches of foreign banks need an authorisation from the HNB for their establishment. Croatian legislation does not condition the authorisation to perform banking business to an economic needs test. Authorisations to provide other financial services, such as leasing & factoring, trading in money market instruments and other transferable securities, administering pension or investment funds are separate but can be granted simultaneously with a banking authorisation.

The initial capital to set up a bank amounts to HRK 40 million (€ 5.5 million). Lower initial capital requirements apply for housing saving banks (HRK 20 million, € 2.7 million) and for savings and loan co-operatives (HRK 0.1 million, € 0.015 million). The Banking Act also includes transitional provisions – expiring on 31 December 2006 – concerning the initial capital requirements for savings banks which obtained authorisation under the Banks and Savings Banks Act (OG 46/97, 89/98).

The acquisition of qualifying holdings in a Croatian bank, as well as subsequent increases in qualifying holdings above specified thresholds, are subject to HNB authorisation. A qualifying holding is defined as 10% of a bank's capital or of its voting rights or less than 10% if the holding allows the investor to exercise significant influence over management.

According to the Banking Act, banks must have a management board consisting of at least two members. Board members have to meet fit and proper criteria and have to have

sufficient professional experience. The HNB has to notify a refusal to the applicant together with its reasons.

The Banking Act incorporates provisions concerning the right of establishment (branching) and the freedom to provide services (cross-border provision) for banks authorised in EU Member States. The entry into force of these provisions is deferred until the date of Croatia's accession to the EU.

Croatia applies prudential requirements related to the calculation of regulatory capital (own funds, which may not fall below the level of initial capital), capital adequacy ratio, management of credit risk, limitations on exposures including large exposures, liquidity and other risks, and holdings in non-financial institutions and assets. A bank may not invest more than 30% of its own capital in non-financial institutions and not more than 15% in a single entity. A bank's risk exposure to one counterpart must not exceed 25% of its own funds. Large exposure refers to risks which equal or exceed 10 % of a bank's own funds, while the aggregated amount of large exposures may not exceed 600% of a bank's own funds.

Credit institutions have to set up an internal audit system and to fulfil certain documentation requirements.

The Banking Act includes provisions on the consolidated supervision of banking groups, including requirements to report prudential indicators on a consolidated basis and a legal basis for co-operation between HNB and foreign supervisors.

Pursuant to the Banking Act, the Croatian National Bank may require banks to submit all reports and information, including accounting and other records maintained in electronic format, necessary to assess compliance with regulatory requirements. The Banking Act empowers HNB to perform both off-site and on-site supervision. The Act includes provisions requiring HNB staff and authorised persons to observe professional secrecy and exempting them from professional liability when performing their duties in good faith.

The Banking Act empowers HNB to adopt decisions and impose remedial measures if it detects violations of the banking regulations. Banks must implement corrective measures and report back to HNB within a specified deadline. The measures to be taken when banks fail to observe risk management policies or when the capital adequacy ratio falls below the statutory minimum are described in detail. The HNB may bring a bank under special administration *inter alia* if the bank fails to implement corrective measures to comply with capital adequacy requirements or if the bank's capital adequacy ratio falls below one quarter of the statutory minimum.

Croatia declared that the Savings and Loan-Cooperatives Act remains non-aligned with the *acquis*. A new Credit Unions Act will be adopted by the end of 2006 with a view to removing inconsistencies with the *acquis*. Some existing savings & loan co-operatives will restrict the range of services they provide and obtain authorisation under the new Credit Unions Act. Others will be able to transform into savings banks, whose establishment, operation and supervision will be regulated by the Credit Institutions Act, the adoption of which is foreseen for the first quarter of 2008.

Capital adequacy requirements for banks are included in the Banking Act and the Decision on the capital adequacy of banks (OG 17/2003, 120/2003, 149/2005), while the Securities Market Act (OG 84/02) and the Ordinance on minimal liquidity of brokerage companies (OG 118/03) incorporates capital adequacy requirements applicable to investment firms.

As regards banks, Croatia considers that the provisions concerning the position risk, settlement- and counter party risk, and the foreign exchange risk is almost fully taken into account for the calculation of the capital requirement. The capital adequacy ratio is defined as the ratio between a bank's regulatory capital and its adjusted risk-weighted assets. This ratio must be at least 10%. As regards investment firms, the provisions concerning initial capital requirements and those concerning market risk are not transposed in Croatian legislation. Croatia considers that provisions concerning the monitoring and control of large exposures are largely transposed, while it acknowledges that certain provisions concerning the scope, initial capital, disclosure, prudential supervision and the trading book remain to be transposed.

Croatia intends to align its legislation with the recast consolidated banking directive (2006/48/EC) and the recast capital adequacy directive (2006/49/EC) through the adoption of a new Act on Credit Institutions and a new Securities Market Act during 2008. According to the plans presented by Croatia, the new Credit Institutions Act transposing these directives will be adopted in March 2008, while implementing measures and operational instructions will be adopted in September 2008. The target implementation date is 1 January 2009 and all approaches to capital requirements calculation will be available immediately. No detailed milestones were provided concerning the transposition of the capital adequacy requirements for investment firms through the new Securities Market Act expected to be adopted in 2008.

Croatian legislation does not include rules on the supervision of **electronic money institutions**. Croatia intends to align its legislation with Directive 2000/46/EC through the adoption of a new Act in 2007.

Croatian legislation does not incorporate a comprehensive framework for the supplementary supervision of **financial conglomerates**, although both the recently adopted Insurance Act and the Act establishing the Croatian Agency for the Supervision of Financial Services (HANFA) provides for co-operation and exchange of information with other domestic and foreign supervisory authorities. Croatia intends to align its legislation with Directive 2002/87/EC in 2008 through the adoption of an Act on the Supplementary Supervision of Financial Conglomerates and through the amendment of the relevant sectoral acts.

Croatia has established an officially recognised **deposit guarantee scheme** pursuant to the Deposit Insurance Act (OG No 177/04). The scheme is administered by the State Agency for Deposit Insurance and Bank Rehabilitation (DAB).

Membership in the Croatian deposit guarantee scheme is compulsory for all Croatian banks, including housing savings banks, and for Croatian branches of foreign banks to the extent that their deposits are not covered by a scheme in their home country up to the insured amount foreseen in Croatian legislation. The scheme is financed on an ex ante basis through contributions from banks amounting to 0.3% of a bank's equity when commencing its business and 0.125% of the insured deposits each quarter. The Agency can request payment of differential premiums depending on the risk exposure of a particular bank. The scheme has a target size of 2.5% of the insured deposits but it has in practice been depleted due to the need to remunerate a large number of depositors as a result of the bankruptcies that arose following a banking crisis in the mid-1990s. Payouts to insured depositors were financed by a bond issue in 2000. Since then, premia have been used to service and eventually retire the bond, so that the fund has not been built up, and the 2.5% target has not yet been reached.

The DAB covers deposits of natural persons held with Croatian banks and with housing savings banks up to HRK 100,000 (€ 14,000). Deposits held of legal persons and those held with savings and loan co-operatives are not covered. Deposits of members of a bank's

management or supervisory board, deposits of shareholders with more than 5% of voting shares and anonymous deposits are not covered by the scheme. Funds which have been found by Court decision to arise from money laundering are also excluded. Croatia does not apply set-off rules to calculate the credit balance of a depositor. Joint accounts and the rules regarding compensation rights of joint account holders are not defined.

Payment of compensation under the scheme is triggered exclusively when a bankruptcy procedure has been declared against a bank. The time limit for the payment of compensation by the scheme is three months from the initiation of the bankruptcy procedure. This can be extended by a further 90 days pursuant to a decision of the DAB.

Croatia intends to align its legislation with Directive 94/19/EC through the adoption of a new Deposit Insurance Act by the end of 2007.

Bank and branch accounts are regulated by the Banking Act, the Companies Act, the Accounting Act, the Audit Act and the Act on Saving and Loan Co-operatives. (*See also Chapter 6 – Company law*).

Banks are required to draw-up their accounts in accordance with international accounting standards pursuant to the Accounting Act. Banks' financial statements have to be audited and published. The HNB prescribes the chart of accounts for banks and housing savings banks, as well as the forms and the contents of financial statements for supervision purposes, including publication requirements.

Croatia intends to align its legislation with the bank accounts directive and the branch account directive through the adoption of a new Act on Credit Institutions in 2008.

The **reorganisation and winding-up** procedures for banks are regulated the Banking Act (OG 84/02), the Bankruptcy Act (OG 61/04), the Companies Act (OG 118/2003) and the Act on Resolution of Conflicts of Law with Regulations of Other Countries in Certain Relations (OG 53/91).

The HNB is the competent authority concerning re-organisation and winding-up of banks. The HNB can place banks under special administration in certain circumstances specified in the Banking Act (see above). Croatian legislation also provides for voluntary and compulsory liquidation of banks. In the event that the HNB decides on compulsory liquidation, the State Agency for Deposit Insurance and Bank Rehabilitation (DAB) appoints one or more liquidation trustees. Branches of foreign banks have to be wound-up if a bankruptcy or liquidation proceeding was initiated in their home country.

The Banking Act requires the HNB to publish decisions to initiate compulsory liquidation procedures against a bank (in the Official Gazette and in two daily newspapers), but publication is not foreseen in the case of special administration. The Companies Act and the Bankruptcy Act foresee a duty to inform creditors of a company undergoing liquidation or bankruptcy proceedings.

The Croatian Bankruptcy Act stipulates that bankruptcy proceedings and their effect shall be determined according to the laws of the country in which the bankruptcy proceedings have been opened (*lex concursus*), subject to some exceptions. Moreover, the Bankruptcy Act foresees that Croatian courts shall have exclusive jurisdiction for conducting bankruptcy procedures against debtors registered in Croatia, as well as in cases when a debtor has established a business unit in Croatia that is not a legal entity (branches). The applicable law

in the case of liquidation follows similar principles and is determined by the Act on Resolution of Conflicts of Law with Regulations of Other Countries in Certain Relations.

Croatia intends to align its legislation with Directive 2001/24/EC by 2007.

As regards **administrative capacity**, banks and housing savings banks are supervised by the Croatian National Bank (HNB), while saving and loan co-operatives are currently supervised by the Ministry of Finance. As of the date of the screening meeting there were 34 banks (representing over 79% of financial sector assets), 4 housing savings banks (1.7% of financial sector assets) and 124 savings and loans co-operatives (0.5% of financial sector assets).

The HNB is an independent public legal entity, established pursuant to the Law on the Croatian National Bank (OG No 36/01). The Prudential Regulation and Banking Supervision Area is currently divided into 5 departments: the Prudential Regulation and Banking System Analysis Department; the Off-Site Supervision Department; the On-Site Risk Management Supervision Department; the Specialised On-Site Supervision Department; and the Licensing and Market Competition Department. As of the date of the bilateral screening meeting, the Prudential Regulation and Banking Supervision Area had 95 staff, of which 51 in the two on-site supervision departments and 20 in the off-site supervision department. The HNB performs risk-based supervision. From 2003 to 2005, the focus of on-site supervision has gradually shifted from full-scope towards targeted examinations. The HNB's on-site examinations covered 85% of the banking sector's assets in 2005.

The HNB has concluded Memoranda of Understanding with the home supervisors of the four countries whose banks have a significant presence in the Croatian market (Austria, Italy, Germany and Hungary) and intends to conclude one with the French authorities. HNB has, in its capacity as home supervisor of Zagrebačka Banka, also concluded a MoU with the Bosnian supervisory authorities.

At the domestic level, a Council of Financial Sector Supervisors was established in 2003 to enhance co-operation among domestic supervisory authorities. The HNB signed a MoU with HANFA on 28 September 2006. HANFA was established on 1 January 2005 through the merger of the three pre-existing non-bank supervisory authorities (see below).

The State Agency for Deposit Insurance and Bank Rehabilitation (DAB), which administers the only officially recognised deposit guarantee scheme, employs approximately 20 staff.

II.b. Insurance and occupational pensions

The basic Croatian legislation in relation to **life assurance and non-life insurance** is the Croatian Insurance Act, the Act on compulsory insurance within the transport sector (both OG 151/05) and the Act establishing the Croatian Agency for the Supervision of Financial Services (OG 140/05. The Insurance Act was adopted in 2005 and entered into force on 1 January 2006.

Croatian legislation differentiates between 18 insurance classes for non-life insurance and 5 main classes in the area of life assurance:

- Non- life insurance classes: accident, health, land motor vehicles, railway rolling stock, aircrafts, vessels, goods in transit, fire and natural disasters, other damage to property, motor vehicle liability, aircraft liability, vessels liability, other liability insurance, credit, suretyship, financial loss, legal protection, tourist assistance.

- Life assurance classes: life assurance, annuity insurance, supplementary insurance linked with life assurance policy, other life insurance lines (tontine, assurance with paid-up sum assured, insurance business which includes preservation of value of capital or payment of minimum interest), life assurances and annuity insurances linked with units of investment funds (unit-linked business)

Insurance undertakings need an authorisation from HANFA for their establishment and operation in Croatia. The authorisation can be limited to certain insurance classes. The Insurance Act specifies the information that has to be submitted together with the application for authorisation, as well as an exhaustive list of circumstances in which the application shall be refused or withdrawn. Domestic insurance undertakings need an authorisation in order to establish a branch abroad. Croatian legislation does not condition the authorisation to perform insurance business to an economic needs test.

Foreign insurance companies have to establish branches to operate in Croatia. Croatian residents are obliged to insure their activities in Croatia. Branches of foreign companies have to obtain an authorisation and to fulfil the same requirements as domestic insurers, in particular as regards capital requirements. The Insurance Act incorporates provisions concerning the right of establishment (branching) and the freedom to provide services (cross-border provision) for insurance undertakings authorised in EU Member States. The entry into force of these provisions is deferred until the date of Croatia's accession to the EU.

The transfer of an insurance portfolio requires a prior authorisation from HANFA. The calculation of premiums has to be notified to HANFA to verify their compliance with actuarial principles. An insurance undertaking may be established either as a joint-stock undertaking or a mutual insurance undertaking. Preference shares can comprise maximum 25% of the total shares.

The acquisition of a qualifying holding in an insurance undertaking and the acquisition of shares beyond certain thresholds require the permission of the supervisory authority. A qualifying holding is defined as 10% of an insurance undertaking's capital or of its voting rights or less than 10% if the holding allows the investor to exercise significant influence over management. The Insurance Act contains an exhaustive list of circumstances in which HANFA shall refuse the application for authorisation.

Insurance undertakings have to provide regularly various accounting, prudential and statistical information to the supervisory authority. This relates in particular to capital requirements, the solvency margin and technical provisions. The Insurance Act includes transitional provisions expiring in 2010 concerning the achievement of the necessary solvency margin, while HANFA may grant an insurance undertaking, at its request, an extension to the harmonisation period by a further two years. Equalisation reserves and mathematical provisions have to be established for certain types of insurance classes. The minimum guarantee fund consists of core capital and supplementary capital. It amounts to HRK 15 million (€ 2.1 million), if an undertaking is active in one non-life insurance class only, otherwise to HRK 22.5 million (€ 3.1 million). For life assurance the minimum guarantee fund is HRK 22.5 million (€ 3.1 million). Certain insurance classes require a higher solvency margin. Croatia defines investment rules which should ensure that investments are secure. Basically investments in securities from Croatia, EU-Member States and OECD countries within certain limits are allowed, unless otherwise approved by the supervisor.

The Croatian Insurance Bureau is a legal person which represents an association of insurance undertakings having their head offices in the Republic of Croatia. Membership is obligatory for insurance companies offering the compulsory traffic insurance (motor insurance).

Croatian legislation provides for relevant provisions on contract information to customers. The cancellation period (the so-called cooling off period) both for non-life and life insurance is 30 days. Advertising is not forbidden for insurance undertakings.

Croatia plans to align its legislation in this area, including in relation to the solvency margin requirements, by the end of 2008.

Croatia has certain regulations concerning the **specific non-life insurance classes** in place. This relates in particular to co-insurance and more limited to the legal expense- and credit insurance and tourist assistance. Croatia plans to align its legislation in this area by the end of 2008.

The Croatian Insurance Act contains provisions concerning **insurance groups**, including the definition of an insurance group and rules on reporting, risk management, capital requirements and supplementary supervision. The parent undertaking is responsible for the fulfilment of the obligations of an insurance group as a whole.

Croatia intends to align its legislation with Directive 98/78/EC in 2008.

Croatia does not have specific **re-insurance** provisions. However, the provisions applicable to non-life and life insurance companies in the Insurance Act also apply to re-insurance companies. Reinsurance companies are supervised by HANFA.

Re-insurance companies need an authorisation for their establishment and operation. A re-insurance undertaking can be established as a joint-stock undertaking only. Authorisations cover exclusively all types of re-insurance and differentiate between non-life- and life re-insurance. Technical reserves differ according to the type of business and have to fulfil certain security, profitability, marketability and diversification requirements. The Insurance Act determines particular categories into which an undertaking may invest such assets. Re-insurance activities require a minimum capital of HRK 22.5 million (€ 3.1 million). Croatia does not have collateral requirements between the re-insurer and the insurer. Foreign re-insurance undertakings are treated equally.

Croatia intends to align its legislation with Directive 2005/68/EC in 2008.

Motor insurance is regulated by the Act on Compulsory Insurance within the Transport Sector (OG 151/05) and the Insurance Act (OG 151/05).

Insurance undertakings offering compulsory transport insurance (accident insurance of passengers in public transport, motor vehicle liability insurance, insurance of the owner or user of an aircraft and motorboat or yacht against liability for damage caused to third parties) have to be member of the Croatian Insurance Bureau. The Croatian motor insurance is valid in all countries participating in the Green Card system. It has to be concluded with an insurance company licensed in the country. Croatia applies a bonus-malus system. Following the proper application of a claim, insurance companies have to compensate or properly inform the injured party within 30 days in the case of personal injuries and within 14 days in case of property damage.

The minimum coverage of a motor insurance is:

- In case of personal injuries:
 - for buses and freight vehicles, including trailers € 870,000
 - for vehicles transporting hazardous substances € 1,000,000
 - for damage caused by other vehicles and unidentified vehicles € 470,000
- In case of damage of property:
 - for buses and freight vehicles, including trailers € 470,000
 - for vehicles transporting hazardous substances € 540,000
 - for damage caused by other vehicles and unidentified vehicles € 200,000

The national guarantee fund compensates personal damage and damage to property in various cases including bankruptcy of an insurance undertaking and accidents caused by stolen, un-identified or un-insured vehicles. Claims representatives have to be appointed in order to settle damages in EU Member States or in Green Card member countries. The fund is financed by the insurance undertakings.

Croatia is member of the Green Card system. The Croatian Insurance Bureau carries out the activities of the National Green Card Bureau and at the same time fulfils the task of the guarantee fund. Systematic controls of motor vehicle insurance at Croatian borders are not carried out in respect of vehicles registered in an EU or EFTA country by virtue of the latter's membership in the Council of Bureaux (COBx) Multilateral Agreement on the abolition of border checks.¹

Insurance mediation is regulated by the Insurance Act. Insurance intermediaries are supervised by HANFA. Insurance mediation can be done by legal and natural persons whereas re-insurance mediation is only allowed for legal persons. Both legal and natural persons act either independently as an insurance broker or are tied to one or more insurance undertakings as an insurance agent selling non-competitive products. As the notion of non-competitive products is interpreted rather restrictively by HANFA, insurance agents may in practice sell insurance products of only one insurance company.

Croatian intermediaries are registered either in the judicial or the trade register after authorisation by HANFA. A separate register of insurance intermediaries has not yet been established. Insurance intermediaries have to fulfil fit and proper criteria. Appropriate knowledge and reputation is required. Information to the client has to be provided in writing and in a professional manner. The minimum requirement for the professional liability insurance for certain categories of insurance intermediary companies, which will be registered for the first time in 2006 according to the Insurance Act, will be HRK 7.500.000 (€ 1,000,000) and in annual aggregate HRK 11,250,000 (€ 1,500,000). For Intermediary companies registered before 1st January 2006 the Insurance Act regulates a gradual increase of the minimum requirement for the professional liability insurance: HRK 1.5 million (€ 206,000) as of 1 January 2007 increasing to HRK 3.5 million (€ 481,000) by January 2011.

¹ Systematic border checks on insurance against civil liability in respect of vehicles registered in Croatia were abolished by Commission Decision 2003/564/EC of 28 July 2003 on the application of Council Directive 72/166/EEC relating to checks on insurance against civil liability in respect of the use of motor vehicles (*Official Journal* Series L 192, 31.7.2003, p. 23).

The Insurance Act empowers HANFA to conduct both off-site and on-site supervision of insurance intermediaries. Sanctions for not complying with relevant provisions can lead to the withdrawal of the authorisation or to a penalty up to HRK 200,000 (€27,000).

Insurance accounts are regulated by the Insurance Act, the Companies Act, the Accounting Act, the Audit Act (OG 146/05) and several implementing measures issued by HANFA. (*See also Chapter 6 – Company law.*)

Insurance and reinsurance undertakings are required to draw-up their accounts in accordance with international accounting standards pursuant to the Accounting Act. The Insurance Act requires the leading insurance undertaking in an insurance group to prepare consolidated accounts. It also requires insurance and reinsurance undertakings to publish a summary of the audited annual report in the press, as well as to submit their annual report to HANFA within a certain deadline.

The Insurance Act empowers HANFA to issue detailed regulations prescribing the chart of accounts, as well as the type, form, layout, content and publication of financial reports.

Reorganisation and winding-up of insurance undertakings is regulated in the Insurance Act (OG 151/2005), the Companies Act (OG 118/2003), the Bankruptcy Act (OG 61/04) and the Act on Resolution of Conflicts of Law with Regulations of Other Countries in Certain Relations (OG 53/91).

HANFA is the competent authority concerning re-organisation and winding-up of insurance undertakings. Re-organisation measures include a wide range of instruments such as "extraordinary administration", capital increase and an increase of the solvency margin. Croatian legislation provides for voluntary and compulsory liquidation of an insurance undertaking. The latter is initiated by HANFA. The Insurance Act requires publication of measures related to compulsory liquidation and to the bankruptcy of insurance undertakings, but no publication is foreseen in the case of reorganisation measures. Croatian branches of foreign insurance companies have to be wound-up if a bankruptcy or liquidation proceeding was initiated in the home Member State of the insurance undertaking.

The provisions concerning the information of creditors and applicable law contained in the Companies Act, the Bankruptcy Act and the Act on Resolution of Conflicts of Law with Regulations of Other Countries in Certain Relations described in section II.a apply *mutatis mutandis* to insurance undertakings.

Croatia intends to align its legislation with Directive 2001/17/EC in 2008.

As regards **occupational pensions**, the Croatian pension system is based on three pillars. The first pillar is the mandatory social security system (pay-as-you-go system). The second pillar is a mandatory pension insurance comprising all employees and financed via individual capital savings. The third pillar is a defined benefit, voluntary system based on individual savings. Voluntary pension insurance schemes can be established as open-ended and closed-ended funds, where the sponsors of the closed-end funds can be companies, trade unions or self-employed persons. Both voluntary and mandatory pension funds are run and managed by pension companies. Pension funds are supervised by HANFA.

Mandatory and voluntary pension funds are regulated through the Mandatory and Voluntary Pension Funds Act (OG Nos. 49/99, 63/00, 103/03). Pension companies have to be established as a joint-stock company or a limited liability company. They need an authorisation from HANFA for establishment and operation. A voluntary pension fund has

to have at least 200 members. A mandatory pension fund has to have equity of HRK 40 million (€ 5.5 million), and a voluntary fund HRK 15 million (€ 2.1 million). A Croatian pension fund cannot be operated from a management company or a sponsoring undertaking outside Croatia. Members of the management or supervisory board of a pension company have to fulfil "fit and proper" criteria. Managers have to have a minimum professional experience and qualification.

The supervisory authority receives audited financial statements, information on sales and purchases of assets, fees and remuneration and salaries of the board and staff. Beneficiaries of a pension fund have to be provided with relevant information. Investments of voluntary pension funds have to respect certain principles to ensure the safety of the investment. These principles include investment diversity and an appropriate liquidity level. A pension fund should not invest more than 20% of its assets outside Croatia and not more than 5% in one type of investment. Furthermore, investments have to respect certain quality standards (ratings). Pension funds cannot invest in property, unlisted or not publicly traded securities, and in securities issued by a pension company, a custody bank or a related person. Croatian legislation does not allow for investments into risk capital markets.

Croatia intends to align its legislation with Directive 2003/41/EC through amendments to the Mandatory and Voluntary Pension Funds Act by the end of 2006.

As regards **administrative capacity**, the insurance and pension sector in Croatia is regulated and supervised by the Croatian Agency for the Supervision of Financial Services (HANFA), which is the legal successor of the two authorities previously competent for the supervision of insurance and occupational pensions, i.e. the Directorate for the Supervision of Insurance Companies (DINADOS) and the Agency for Supervision of Pension Funds (HAGENA). It is an independent public legal entity financed through fees of the supervised companies and deficits are covered by the state. In 2005, there was 25 staff working at DINADOS. A new organisation structure for insurance supervision was adopted in December 2005. It created separate teams responsible for on site supervision (7 people) and off site supervision (3 people). Also in 2005, there were 42 people working in HAGENA. The latter had 9 staff performing supervision of pension funds (both on and off site, with no specialisation). HANFA's organisation structure foresees specialised departments for on site and for off site supervision.

HANFA has a wide range of competences which include regulatory activities, licensing and on-site and off-site supervision of the entire non-banking financial sector in Croatia. The Agency can also impose sanctions such as the withdrawal of licenses, referral of cases to the judicial authorities and it can put undertakings in the finance sector under special administration. HANFA's President, members of its Board and employees are bound by professional secrecy and exempted from professional liability when performing their duties in good faith.

HANFA co-operates with the HNB as regards supervision. An agreement to that effect was signed on 28 September 2006.

Prior to the establishment of HANFA, DINADOS and HAGENA each concluded a Memorandum of Understanding with, respectively, the Slovenian Insurance Supervisory Agency and the Agency for the Supervision of the Fully Funded Pension Insurance of the former Yugoslav Republic of Macedonia.

In 2005, 26 companies were active in the Croatian insurance sector, including two re-insurance companies. 11 companies were foreign owned. The total annual premium volume

reached approximately HRK 7.4 billion (€ 1 billion) (HRK 1.9 billion (€ 261 million) life assurance, HRK 5.5 billion (€ 756 million) non-life insurance). Furthermore, 4 mandatory and 4 voluntary pension fund companies operated in Croatia. About 1.2 million persons were member in a mandatory pension fund scheme. Total assets of the mandatory fund were HRK 11.7 billion (€ 161 million) in 2005. About 56,000 persons were member of a voluntary pension fund and total assets amounted to HRK 228 million (€ 31 million).

II.c. Financial market infrastructure

Settlement finality in payment and securities settlement systems is regulated by the Act on the Croatian National Bank (HNB), the Securities Market Act, the National Payment System Act and relevant HNB decisions, which incorporate some provisions of the *acquis*.

Croatia has three settlement systems for securities which are the Croatian Large Value System (CLVPS), the National Clearing System (NCS) and the Central Depository Agency (CDA). The CLVPS is based on real time gross settlement. Participants are banks, the HNB and the CDA. Participants in the NCS are banks, the HNB and third parties. Net positions in banks' clearing accounts are settled at the end of the clearing day in the banks' settlement accounts with the HNB. The CDA acts as depository and central counterparty; it owns and operates the securities settlement system. Participants in the CDA system are brokers, custodians, money market participants and institutional investors. Settlement and clearing is based on the following principles: Contractual settlement (CS), trade for trade (TFT) and delivery versus delivery (DvD).

As regards the protection against insolvency of a participant, transfer orders entered into the system before the opening of insolvency proceedings are legally enforceable and binding on third parties. The decision to open an insolvency proceeding does not have retroactive effects on the rights and obligations of a participant. Transfer orders cannot be revoked after settlement.

Croatia intends to align its legislation with Directive 98/26/EC through a new act that will be adopted in 2007.

Croatia declared that it has not yet adequate legislation on **financial collateral**. However, some legislative acts, in particular the Securities Market Act cover some aspects of the directive. Croatia plans to align its legislation in this area through a new act in 2007.

Financial collateral providers/takers are certain public sector bodies (not defined in Croatian legislation), banks and credit institutions, insurance undertakings, UCITS and management companies, investment firms and brokerage houses. The CDA acts as settlement agent and clearing house. Securities as defined by the Securities Market Act such as shares, bonds, finance papers, treasury notes, commercial papers, certificates of deposit and other series securities (issued by the same issuer, simultaneously and giving the same rights) can serve as collateral. Money market deposits are not used in Croatia. REPOS are not regulated by law. Security financial collateral arrangements and title transfer of financial collateral are possible. In certain cases close out netting provisions of financial collateral are recognised in Croatia. The execution of the right of use of financial collateral is not allowed under Croatian legislation. There is no formal act required for perfection of an interest in financial collateral.

II.d. Securities markets and investment services

Croatian **markets in financial instruments** are regulated by the Securities Market Act (OG 84/02), whose scope is limited to transferable securities and money-market instruments. The Act does not include *inter alia* definitions of systematic internalisers, multilateral trading facilities (MTFs) nor of regulated markets. Croatian securities markets and investment firms are supervised by HANFA.

According to the Securities Market Act, only brokerage companies (which must be established as a private limited liability company or a company with share capital) and banks may perform transactions with securities. Both must obtain an authorisation from HANFA. The Securities Market Act and related implementing measures lay down *inter alia* the conditions for the establishment, authorisation and operation of brokerage companies. It specifies the information that must accompany the application for authorisation, which include neither a programme of operations nor an organisational structure. The Act further stipulates the circumstances in which HANFA shall refuse to grant the authorisation and lays down an exhaustive list of circumstances in which a broker's authorisation may be withdrawn.

Croatian brokerage companies must notify HANFA if they establish a branch abroad. Foreign brokerage companies can establish a branch in Croatia subject to authorisation by HANFA.

The Securities Market Act lays down initial capital requirements for brokerage companies, which vary from HRK 200,000 (€ 27,500) to HRK 4 million (€ 550,000) depending on the activity performed by the broker.

As regards other authorisation and operation requirements, the Act does neither include a definition of qualifying holdings nor a requirement to seek authorisation for the acquisition of such a holding in a brokerage company. It does not require membership in an investor compensation scheme, nor does it require brokerage companies to take all reasonable steps to prevent conflicts of interest.

In relation to investor protection requirements, the Securities Market Act requires brokerage companies to publish their general conditions, to provide investors with true information, to execute orders without delay, to take care of their clients' interests and to act with due professional care. However, the Act *inter alia* does not contain rules concerning client categorisation, nor does it provide for a suitability and appropriateness test, neither comprehensive best execution requirements nor comprehensive rules on client order handling.

The Securities Market Act contains some limited provisions concerning pre-trade transparency (such as disclosure to clients of information concerning the order book), but does not incorporate comprehensive rules concerning market transparency and integrity. The Act requires investment firms to execute client orders through a stock exchange or a regulated market – the so called concentration rule.

The Act includes provisions concerning the authorisation and operation of securities exchanges and "regulated public markets" (which are a subset of the former). The initial capital of an exchange must be at least HRK 1 million (€ 137,000). The statutes and rules of a stock exchange must be approved by HANFA. However, the Securities Market Act does not incorporate *inter alia* rules concerning fit and proper criteria for managers of regulated markets, requirement concerning persons exercising significant influence over the

management of a regulated market, nor a requirement that regulated markets have sufficient financial resources available on an initial and ongoing basis. There are no rules (fit and proper criteria, etc.) concerning the admission of members and participants to a regulated market. Only brokerage companies that are members of an exchange may trade on that exchange.

Croatian stock exchanges have some regulating and self regulating powers concerning trading executions, fees, suspension of trading and quotation.

Croatia intends to align its legislation with Directive 2004/39/EC and its implementing measures through the adoption of a new Securities Market Act in 2008.

There is no officially recognised **investor compensation scheme** in Croatia. Croatia declared that it intends to establish such a scheme under the responsibility of the Central Depository Agency following the adoption of the new Securities Market Act in 2008.

Conditions for the admission to trading and transparency obligations of traded companies are regulated by the Securities Market Act. HANFA is the competent authority which supervises compliance with transparency obligations.

The Securities Market Act regulates the admission of securities to trading and empowers HANFA to lay down more detailed requirements concerning *inter alia* the issuers' initial capital and the minimum value of the securities subject to listing. All securities must be issued in dematerialised form. The Act does not provide HANFA with the power to reject an application for listing if the latter would be detrimental to investors' interests, nor to subject a listing to special conditions. There is no floor of € 1 million for the market capitalisation of shares for which admission is sought.

The Securities Market Act requires issuers of securities to publish certain periodic and ongoing information. As regards periodic reporting requirements, issuers listed in the 1st tier ("quotation one") of an exchange are required to publish annual, semi annual and quarterly financial statements. Public joint stock companies (which are subject to mandatory listing) are required to submit quarterly reports to HANFA, which makes them available to the public through its library and on its website. According to the mandatory listing requirement companies subject to an initial public offering, or having a capital of more than HRK 30 million (€ 4.1 million) and more than 100 shareholders have to be listed on a Croatian stock exchange.

As regards ongoing information, the issuer of securities has to promptly inform the public of all information relating to material facts, i.e. all information and facts that can influence the price of securities. Furthermore, information on the acquisition and disposal of major holdings crossing certain thresholds (10%, 25%, 50% and 75%) must be notified to HANFA or the issuer. After that the issuer has to inform the public. The deadlines for such notifications and for the publication of the information by the issuer are longer than foreseen in the acquis. Croatian legislation does not incorporate rules concerning officially appointed mechanisms for the disclosure of information to the public. However, in addition to financial reports, a number of documents pertaining to issuers are available in HANFA's library.

Croatia intends to align its legislation with the Directive 2001/34/EC, and with Directive 2004/109/EC and its implementing measures through the adoption of a new Securities Market Act in 2008.

The publication of **prospectuses** by issuers is regulated by the Securities Market Act. Issuers of securities are required to publish a prospectus (public offering) or to provide it to potential investors (private offering). Public joint stock companies (which are subject to mandatory listing) are only required to issue an abridged prospectus when listing shares on the relevant quotation. The Act includes exemptions from the obligations to produce a prospectus (certain types of capital increase, mergers, etc.) but these do not fully correspond to those set out in the directive.

HANFA supervises compliance with these requirements and must approve prospectuses. The deadlines for the approval and validity of prospectuses are not in line with the prospectuses directive.

The prospectus must contain complete, accurate and objective information on various business-relevant issues to allow a potential investor to make an objective assessment of the prospects and of the risks of an investment. There is no requirement to include a summary in the prospectus. The prospectus must be issued as a single document. The Securities Market Act provides for the publication of prospectuses as an insert in a daily newspaper or for the publication of an address from which the prospectus may be obtained. There is no provision concerning the publication on the websites of the issuers, the regulated market or the competent authority. The issuer and the persons who signed the prospectus are liable for its content.

Croatia intends to align its legislation with Directive 2003/71/EC and its implementing measures through the adoption of a new Securities Market Act in 2008.

Market abuse rules are included in the Act establishing the Croatian Agency for the Supervision of Financial Services, the Securities Market Act, the Investment Funds Act, the Takeover Act and the Companies Act. HANFA is the single competent authority for market abuse.

Croatian legislation covers both insider dealing and market manipulation. Inside information is defined as all non-public information which might be able to affect the value of capital market instruments. The realisation of gains on the basis of inside information is prohibited, as is the disclosure of such information to third parties. Issuers are required to disclose inside information to the public but are not required to draw up a list of persons having access to inside information. Market manipulation includes both transaction designed to manipulate prices and the dissemination of false information.

The Securities Market Act follows the main provisions of the acquis concerning the definition and public disclosure of inside information and the definition of market manipulation. The Companies Act follows the main provisions of the acquis concerning the exemptions for buy-back programmes. However, the Act does not contain comprehensive rules in line with the acquis concerning the fair presentation of investment recommendations and the disclosure of conflicts of interest.

Croatia intends to align its legislation with the Directive 2003/6/EC and its implementing measures in 2008, primarily through the adoption of a new Securities Market Act and a new Takeover Act.

Undertakings for collective investment in transferable securities are regulated by the Investments Funds Act (OG 150/05).

Investment funds can be established as a legal person or as a separate pool of assets.

Investment funds and management companies need to be authorised by the supervisory authority. There are both open-ended and closed-ended investment funds. For open-ended investment funds with a public offer, the application for authorisation must be accompanied by the investment objectives, the fund prospectus, the fund rules, the contract concluded between the management company and a depositary bank, and the name of the auditor. A management company shall exclusively be engaged in the establishment and management of investment funds, but it may perform certain ancillary activities. At least two members of its management board must meet fit and proper criteria. The minimum initial capital required to set up an investment fund is HRK 1 million (€ 137,000) and shall be larger if the value of the funds assets exceed HRK 1.875 billion (€258 million), with a ceiling of HRK 75 million (€ 10.3 million).

The Investment Funds Act incorporates provisions concerning the right of establishment (branching) and the freedom to provide services (cross-border provision) for management companies authorised in EU Member States. The Act also includes rules concerning the “product passport.” The entry into force of these provisions is deferred until the date of Croatia's accession to the EU.

The Act specifies rules concerning eligible assets and portfolio diversification. Investment funds have to have a risk management system. The assets of a fund are kept by a depositary bank and cannot be pledged as a guarantee or seized by third parties. Activities of safe-keeping and other activities carried out by a depositary bank for the management company shall be separated, in terms of organisational structure, from the activities of the management company. The depositary bank must maintain the assets of each fund in a separate account.

An open-ended investment fund with a public offer may be authorised to distribute a simplified prospectus only, provided the latter does not differ from the terms and conditions of the full prospectus, that it contains a clear reference to the full prospectus and that the latter can be obtained upon request.

The prospectus and/or fund rules, which, in case of an open-ended investment fund may be in a simplified form, shall previously be delivered or made available to all buyers of units in an open-ended investment fund.

Half-yearly and audited annual reports must be submitted to HANFA.

Croatia declared that further alignment of the Investment Funds Act will be completed by the end of 2008.

As regards **administrative capacity**, securities markets and investment services in Croatia are supervised by the HANFA (see above), which is the legal successor of the former supervisory authority in this area, i.e. the Croatian Securities Commission (CROSEC). At the end of 2005, CROSEC had 22 employees, of which 7 in the enforcement department. There was no specialisation of staff for on site and off site supervision, although this is provided for in HANFA's statute.

CROSEC undertook 135 examinations (6 on-site) in 2005. It revoked various licenses of brokers and investment firms. The imposition of financial sanctions falls under the competence of the judiciary.

CROSEC has concluded Memoranda of Understanding with similar institutions from Austria, Bulgaria, Bosnia and Herzegovina (both the Federation of Bosnia and Herzegovina

and the Republic of Srpska), the former Yugoslav Republic of Macedonia, Turkey, Serbia, Montenegro and Romania

III. ASSESSMENT OF THE DEGREE OF ALIGNMENT AND IMPLEMENTING CAPACITY

Overall Croatia's legislation is satisfactorily aligned to the financial services *acquis*. Alignment has progressed further in the areas of banking and financial conglomerates, and of insurance and occupational pensions.

The necessary supervisory authorities are established. However, their competences need to be further strengthened. The co-operation with other Member States' supervisory authorities can be improved.

III.a. Banks and financial conglomerates

Croatian legislation in this area is sufficiently aligned with the *acquis*. The main gaps with respect to the *acquis* are the absence of certain capital adequacy requirements, especially for investment firms, the lack of a comprehensive framework for the supplementary supervision of financial conglomerates and the non-existence of rules for the supervision of electronic money institutions. The scope, level of guarantee and procedures of the Croatian deposit guarantee legislation will need to be adapted.

Croatian legislation on the **taking-up and pursuit of the business of credit institutions** is satisfactorily aligned with the existing consolidated banking directive (2000/12/EC). Croatia's provisions concerning the establishment, authorisation, operations and termination of operations of credit institutions, as well as their supervision, are largely in line with the *acquis*. The calculation of own funds, limits on large exposures and the capital adequacy ratio are partially aligned.

As regards **capital adequacy** requirements, Croatian legislation is partially aligned to the present *acquis* (Directive 2000/12/EC). The minimum capital adequacy ratio foreseen in Croatian legislation (10%) is higher than required by the directive. Provisions for banks regarding the calculation of capital requirements for position risk, settlement and counterparty risk, as well as foreign exchange risk, are largely transposed. Provisions for investment firms concerning initial capital and calculation of capital charges have not yet been incorporated in Croatian legislation. Capital requirements for saving and housing banks and savings and loan co-operatives (credit unions) are not aligned. As regards the latter, the Croatian authorities have indicated that they intend to request an exemption under Article 2 of Directive 2000/12/EC. Some savings and loans co-operatives may transform into fully licensed credit institutions. The Croatian authorities intend to require saving and housing banks to meet the full initial capital requirements under the directives (the average capital of the 5 institutions concerned amounted to about € 6 million at the end of 2005).

Croatian legislation is partially aligned with the recast consolidated banking and capital adequacy directives (2006/48/EC and 2006/49/EC). A number of definitions, including operational risk, need to be transposed. Provisions against risks, minimum own funds requirements for credit risk and operational risk and disclosure by credit institutions are not yet aligned with the recast directive. Initial capital requirements for investment firms need to be transposed as well as the provisions concerning the trading book.

Croatia has presented an action plan for the transposition of the provisions of the recast consolidated banking and capital adequacy directives applicable to credit institutions.

However, no detailed plans were provided concerning the transposition of the capital adequacy requirements applicable to investment firms via the new Securities Market Act to be adopted in 2008.

Croatia currently does not have rules on the supervision of **electronic money institutions** corresponding to Directive 2000/46/EC.

Croatian legislation does not incorporate a comprehensive framework for the **supplementary supervision of financial conglomerates**. In addition to the adoption of a specific Act, amendments to sectoral legislation, including the Insurance Act, are required to achieve full alignment.

Croatian legislation concerning **deposit guarantee schemes** is partially aligned with the *acquis*. An officially recognised guarantee scheme is in place. However, Croatian legislation does not comply with EC law on a number of points. The minimum level of guarantee is at present below the required level and deposits of legal persons are not covered. Neither the initial date for the calculation of the three month re-imburement period nor the discretionary powers of the DAB to extend this time limit are in line with the Directives. The financing of the DAB's scheme needs to be monitored.

Croatia indicated that, at the time of drafting of the new Deposit Insurance Act in the course of 2007, an analysis on the possibility of full application of the provisions of the Directive will be carried out.

The alignment of Croatia's legal framework with the directives on **bank accounts and branch accounts** is partial (see also Chapter 6 – Company law as regards the use of international accounting standards).

Croatian legislation concerning **re-organisation and winding-up** of banks is satisfactorily in line with Directive 2001/24/EC. Re-organisation measures do not need to be published in Croatia, contrary to the directive. The derogations from the principle of *lex concursus* are not fully in line with the directive. The directive's provisions on the principle of *lex rei sitae*, netting agreements and repurchase agreements are not fully incorporated in Croatian law.

The HNB's **administrative capacity** to supervise the banking sector has improved considerably during recent years. The HNB introduced risk-based supervision and reorganised its Prudential Regulation and Banking Supervision Area in response to the Financial Sector Assessment Programme (FSAP) report issued by the World Bank and by the International Monetary Fund in 2001. The changes resulting from the reorganisation include a greater specialization of the on-site officers on a particular area of banks' activities, e.g. credit risk, and an increased focus on operational risks. Together with organisational changes, banking supervision staffing has gradually been strengthened, especially in relation to on-site supervision.

Consolidated supervision was introduced in Croatia by the Banking Act adopted in 2002 and a supporting by-law was issued and came into force in mid-2003. There are currently six banking groups subject to consolidated supervision in Croatia.

The HNB reports good working-level co-operation with the home supervisors of EU banks that own subsidiaries in Croatia. There has been an increased focus on the need to enhance co-operation among domestic supervisory authorities since 2003, including through the establishment of a Council of domestic financial supervisors. Co-operation has been simplified and facilitated by the integration of non-bank supervision within the Croatian

Agency for the Supervision of Financial Services (HANFA). The co-operation agreement between HNB and HANFA was signed on 28 September 2006. However, there is a continuing need to enhance co-operation between HANFA and HNB, particularly to ensure the consistent future implementation of the *acquis*.

While good progress has been achieved over recent years, the HNB's administrative and institutional capacity should be further strengthened in view of the specific characteristics of the Croatian market, especially the potential for significant unhedged foreign exchange risks, the growing sophistication of the market, including the emergence of financial conglomerates, and the significant challenges that full alignment with the *acquis* will bring, in particular as regards the implementation of the new capital requirements framework.

III.b. Insurance and occupational pensions

The alignment in the insurance sector is satisfactory. The main gaps are the differences in the calculation of solvency margins and the absence of a comprehensive framework for the supervision of insurance groups and of reinsurance companies.

Croatia's alignment to **life and non-life insurance directives** is good. Most of the provisions concerning the establishment and operation of an insurance undertaking are largely aligned. This includes the separation of life insurance and non-life insurance business and also reporting and auditing requirements. The Croatian guarantee fund capital requirements are in line with the minimum capital requirements of the directive. The major gap between Croatian legislation and the *acquis* concerns the calculation of the solvency margin.

With regard to life assurance work is still needed to transpose provisions on certain investment rules (see also Chapter 4 – Free movement of capital and Chapter 17 – Economic and monetary union).

The alignment of Croatia's legislation on **specific non-life insurance classes** to the relevant directives is limited. Some provisions concerning co-insurance are in place. Provisions with regard to the legal expense insurance, the tourist assistance and the credit insurance are not aligned.

The alignment of Croatian legislation on **insurance groups** is limited. Some basic provisions are in place, such as the supervision of insurance as a group and reporting requirements. However, most of the relevant *acquis* still needs to be transposed.

Croatia's legislation on **re-insurance** is not aligned with the *acquis*.

Croatian **motor insurance** legislation is partially aligned to the *acquis*. Basic principles such as a guarantee fund, the bonus-malus system and claims representatives are in place. The minimum amounts of cover of the Croatian motor insurance are lower than in the directive.

Croatian provisions on **insurance mediation** are partially in line with the *acquis*. The professional liability insurance coverage is not yet adjusted to the required level and does not appear to cover all categories of intermediaries. Croatia has not submitted any commitments regarding the compliance with the minimum levels of the professional liability insurance. Moreover, the principles concerning the freedom of establishment and the freedom to provide services by intermediaries from other Member States need to be incorporated into Croatian law. The insurance representation business must be allowed for all categories of EU intermediaries (agents) and not be reserved only for tied insurance intermediaries as stated in the current law applicable to the Croatian intermediaries. Additionally, insurance

representation activities carried out at vehicle roadworthiness test garages must be allowed for all EU intermediaries and must not be reserved only for tied insurance intermediaries as it is the case today.

Croatian provisions on **insurance accounts** are at a good level of alignment with the *acquis*. The technical and basic mathematical provisions, the layout and the presentation of financial statements, publication requirement are largely in line with the directive. Croatia does still need to transpose important definitions such as insurance undertakings and activities of an insurance undertaking, valuation rules and publication requirements.

Croatian legislation concerning **re-organisation and winding-up** of insurance undertakings is satisfactorily in line with the *acquis*. Re-organisation measures do not need to be published in Croatia contrary to the directive.

The legislation on **occupational pensions** is satisfactorily in line with *acquis*. Provisions with regard to authorisation, certain definitions, separation between the sponsoring undertaking and the pension company, fit and proper requirements for managers and shareholders are satisfactorily aligned. However, rules on management and custody and the provisions concerning cross border operations need to be transposed. Moreover, Croatian legislation allows both open-ended and closed ended schemes, whereas only closed-ended voluntary pension insurance companies qualify as an IORP under Directive 2003/41/EC. Moreover, while Croatian legislation allows voluntary pension companies to operate direct benefit schemes, IORPs are only allowed to operate direct contribution schemes in accordance with the directive.

As regards **administrative capacity**, insurance companies and pensions funds are supervised by the Croatian Agency for the Supervision of Financial Services (HANFA). HANFA is an independent public legal entity. Its supervisory capacity has been strengthened. International co-operation could be further improved through conclusion of co-operation agreements. (See also section III.d.).

III.c. Financial market infrastructure

Croatia's legislation in the field of financial market infrastructure is at a low level of alignment.

The alignment of Croatian provisions on **settlement finality** in payment and securities settlement systems is limited. Several issues related to the settlement of transactions and the notification procedures in case of insolvency are not regulated.

Croatia's legislation on **financial collateral** is not aligned with the *acquis*

III.d. Securities markets and investment services

The provisions concerning investment services and security markets are partially aligned with the *acquis*. Further efforts are necessary as regards regulation and supervision of investment firms and regulated markets, prospectuses, market abuse and investment funds. Croatia needs to establish an officially recognised investor compensation scheme.

Croatian legislation incorporates some elements from the directive on **markets in financial instruments**. The Securities Market Act will need to be significantly revised in relation to definitions, the authorisation and operations of investment firms, investor protection rules, market transparency and integrity, as well as regulated markets. The concentration rule will need to be abolished.

Croatia's legislation on **investor compensation schemes** is not aligned with the *acquis*. There is currently no officially recognised investor compensation scheme in Croatia.

Croatian legislation is satisfactorily aligned with the *acquis* concerning **admission to trading** and **transparency obligations of traded companies**. However, HANFA's powers concerning the admission of securities to official listing will need to be strengthened. Moreover, the rules concerning the disclosure of regulated information will need to be enhanced.

The alignment to the **prospectuses** directive is limited. Numerous definitions are not transposed yet. Croatian legislation does neither foresee summary information, electronic publication, nor a supplement to the prospectus in case of significant new factors.

Croatian legislation is partially aligned with the directive on **market abuse**. Croatia has defined a single competent authority and rules on insider dealing and market abuse. However, various definitions and requirements as regards transparency are still narrower than in the directive. Market manipulation is not sanctioned. The powers of the competent authority (HANFA) need to be strengthened.

Croatian legislation concerning **undertakings for collective investment in transferable securities** is largely aligned with the *acquis*. Provisions concerning authorisation, investment policies, disclosure, custody and supervision are addressed in Croatian legislation. However, several implementing regulations remain to be drafted.

Administrative capacity in the field of investment services and securities markets continues to be strengthened. HANFA's creation should facilitate a more consistent and comprehensive approach in this area. However, the overall administrative and institutional capacity needs to be strengthened in view of HANFA's expanding responsibilities and to allow HANFA to assume the obligations from the *acquis*.