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Croatia

3rd Compliance Report

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LIST OF ACRONYMS

AML/CFT	Anti-money laundering and combating financing of terrorism
CC	Criminal Code
CCP (CPA, CPC)	Code of Criminal Procedure
CDD	Customer Due Diligence
CTR	Cash transaction report
DNFBP	Designated Non-Financial Businesses and Professions
EU	European Union
EUR	Euro
FATF	Financial Action Task Force
FIU	Financial Intelligence Unit
FT	Financing of Terrorism
KYC	Know your customer
LEA	Law Enforcement Agency
MER	Mutual Evaluation Report
ML	Money Laundering
MLA	Mutual legal assistance
NPO	Non-Profit Organisation
NRA	National Risk Assessment
SAR	Suspicious Activity Report
SR	Special recommendation
STR	Suspicious transaction report
UN	United Nations
UNSCR	United Nations Security Council resolution

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3rd Compliance Report submitted by Croatia

Note by the Secretariat

Introduction

1. The purpose of this paper is to introduce Croatia's 3rd Compliance Report to the Plenary concerning the progress that it has made to remedy the deficiencies identified in the mutual evaluation report on the 4th round assessment visit (MER).
2. Croatia has submitted its 3rd Compliance Report to the MONEYVAL Secretariat in November 2018. As per the 4th Round Rules of Procedure¹, countries must have implemented those FATF Recommendations that are considered to be Core² and Key³ at a level essentially equivalent to a "compliant" (C) or "largely compliant" (LC). The Plenary may retain some limited flexibility with regard to Key Recommendations if substantial progress has been made on the overall set of recommendations that were rated "partially compliant" (PC) or "non-compliant" (NC).

A. Background information

3. The onsite visit to Croatia took place from 19 to 24 November 2012. MONEYVAL adopted the 4th round MER of Croatia at its 42nd Plenary meeting in September 2013. As a result of the evaluation, Croatia was rated PC on 16 Recommendations⁴, including two Core, five Key and nine other Recommendations, as indicated in the table below:

Core Recommendations rated PC (no Core Recommendations were rated NC)
Recommendation 1 (Money laundering offence) Recommendation 5 (Customer due diligence)
Key Recommendations rated PC (no Key Recommendations were rated NC)
Recommendation 3 (Confiscation and provisional measures) Recommendation 23 (Regulation, supervision and monitoring) Recommendation 35 (Conventions) Special Recommendation I (Implementation of United Nations instruments) Special Recommendation III (Freeze and confiscate terrorist assets)
Other Recommendations rated PC (no other Recommendations were rated NC)
Recommendation 6 (Politically exposed persons) Recommendation 7 (Corresponding banking) Recommendation 12 (DNFBPs – R.5, 6, 8-11) Recommendation 16 (DNFBPs – R.13-15 and 21) Recommendation 17 (Sanctions) Recommendation 22 (Foreign branches and subsidiaries)

¹ MONEYVAL, *Rules of Procedure for the Fourth Round of Mutual Evaluations and for Follow-up as a Result of the Third Evaluation Round*, as revised in September 2017, available at <https://rm.coe.int/rules-of-procedure-for-the-4th-round-of-mutual-evaluations-and-for-fol/1680760775>

² The core Recommendations, as defined in the FATF procedures, are R.1, R.5, R.10, R.13, SR.II and SR.IV

³ The key Recommendations, as defined in the FATF procedures, are R.3, R.4, R.23, R.26, R.35, R.36, R.40, SR.I, SR.III and SR.V

⁴ It should be pointed out that the FATF Recommendations were revised in 2012 and that there have been various changes, including their numbering. Therefore, all references to the FATF Recommendations in the present report concern the version of these standards before their revision in 2012.

Recommendation 32 (Statistics)

Recommendation 33 (Legal persons – beneficial owners)

Special Recommendation VIII (Non-profit organisations)

4. Upon adoption of the report, Croatia was placed under the regular follow-up procedure and was requested to provide, no later than two years after the adoption of the report, information on the actions it has taken to address the factors/deficiencies underlying any of the 40+9 Recommendations that are rated PC. Croatia was encouraged to seek removal from the follow-up process within three years after the adoption of the 4th round MER or very soon thereafter.
5. As a result, Croatia submitted 6 follow-up report discussed at the 48th, 50th, 52nd, 54th, 55th and 56th Plenary meetings. Due to the limited progress made with respect to Core and Key Recommendations at the 54th the Plenary, it was decided to apply the Step 1 of the MONEYVAL's Compliance Enhancing Procedures (CEPs). Croatia submitted its first Compliance Report at the 55th Plenary in December 2017.
6. At the 56th Plenary in July 2018, it was recognised that Croatia had adopted a new AML/TF Law which largely addressed deficiencies under R.6, R.7, R.17, R.22, R.32, R.33 and SR.VIII. However, the Plenary noted that Croatia had still a large number of outstanding deficiencies which relate to a number of Core, Key and Other Recommendations. This concerned notably R.1, R.3, R.5, R.23, R.35, SR.I, SR.III, R.12 and R.16. The Plenary decided that, should the respective amendments not be adopted by the time of the 57th Plenary (to which Croatia is invited to report back), it would consider the adoption of Step 2 of its CEPs.
7. Based on the 3rd Compliance Report submitted by Croatia on 14 November 2018, the MONEYVAL Secretariat prepared the present analysis of the progress made in relation to all recommendations rated PC in the MER.
8. On a general note concerning all follow-up and compliance reports: the procedure is a paper-based "desk review", and thus by nature less detailed and thorough than a MER. Effectiveness aspects can be taken into account only through consideration of data and information provided by the authorities. It is also important to note that the conclusions in this analysis do not prejudice the results of future assessments, as they are based on information which has not been verified through an on-site process and is not, in all cases, as comprehensive as it would have been during a mutual evaluation.

Overview of the progress made by Croatia since the adoption of the MER

A. Legislation, regulations and guidance

9. Croatia has undertaken measures for adoption of the number of legislative acts addressing some of the deficiencies identified in the 4th round MER.
10. Since the last Compliance Report in order to address the remaining deficiencies Croatia initiated revision of the recently adopted AML/TF Law (Official Gazette No. 108/17), of the Criminal Code (Official Gazette No. 56/15 and 61/15), of the Law on Insurance ("Official Gazette" no. 151/05, 87/08, 82/09, 54/13 and 94/14). All of these documents are yet in the different stages of the legislative process.
11. In addition to the above mentioned, Croatia has undertaken measures for adoption of the number of other legislative acts, such as:
 - The "Ordinance on Issuing Authorization to and on Acquisition of a Qualifying Holding in a Voluntary Pension Company" (Official Gazette 51/18);
 - The "Capital Market Act" (Official Gazette 65/18);
 - The "Payment System Act" (Official Gazette No. 66/2018);
 - The "Electronic Money Act" (Official Gazette No. 64/2018);

- The “Factoring Law” (“Official Gazette” no. 94/14).

B. Other developments

12. Croatia progressed with establishment of the Beneficial Owners Register initiated based on the Minister of Finance “Decision on forming an Inter-Institutional Working Group on harmonisation of Croatian AML/TF Law with the Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of ML or FT (4th EU AML Directive) and the FATF Recommendations (2012)” from 11 February 2016. The Beneficial Owners Register of Croatia is expected to be operational from January 1, 2019.

Review of measures taken in relation to Core and Key Recommendations

Recommendation 1 - Money laundering offence

13. With regard to Recommendation 1, Croatia advised that since the last Compliance Report, the working group for amendments of the criminal code discussed a proposal of addressing the remaining deficiencies regarding R.1. Amendments to the Criminal Code (Official Gazette No. 56/15 and 61/15) are still undergoing the legislative process in the Parliament of Croatia. Nevertheless, the Secretariat has not been provided with the translation of the draft provisions (as revised after the 56th Plenary) to consider these amendments. Therefore, the previous analysis of the Secretariat (as discussed during the 56th Plenary) remains unchanged for the time being.
14. Taking into consideration that no progress was demonstrated by Croatian authorities since July 2018, the previous analysis of the Secretariat as was discussed during the 56th Plenary remains unchanged. As was noted in the former analysis of the Secretariat, the majority of deficiencies identified in the 4th round MER would be addressed with the adoption of the draft Article 265 of the CC. Concerns remain however with regard to extending the subject matter of the actions of acquisition, possession or use to the pecuniary advantage “derived from criminal activity”, and about extending the definition of property to cover corporeal and incorporeal assets. Croatia should still seek to address these deficiencies during the on-going legislative process of amending the criminal code.

Recommendation 3 (Confiscation and provisional measures)

15. With regard to Recommendation 3, Croatia advised that since the last Compliance Report, the working group for amendments of the criminal code discussed a proposal of addressing the remaining deficiencies regarding R.3. As already indicated above, amendments of the Criminal Code (Official Gazette No. 56/15 and 61/15) are still undergoing the legislative process in the Parliament of Croatia. Nevertheless, the Secretariat has not been provided with the translation of the draft provisions (as revised after the 56th Plenary) to consider these amendments. Therefore, the previous analysis of the Secretariat (as discussed during the 56th Plenary) remains unchanged for the time being.
16. As was noted in the previous analysis of the Secretariat, the majority of deficiencies identified in the 4th round MER for R.3 have not yet been addressed. In particular, concerns remain with regard to: the concept of “pecuniary advantage” that adds supplementary features and an additional burden of proof, to determine proceeds of crime, property laundered and proceeds from ML, subject to confiscation regime; the confiscation of the instrumentalities that is conditioned by the supplementary element of the risk that they will be reused in another criminal activity; the absence of provisions on the confiscation of property of corresponding value of the instrumentalities; and the limited scope of the term “objects” used in the CPC. Croatia is urged to use the occasion that its criminal code is currently being amended to include revisions which would address the majority of outstanding deficiencies under R.3 which relate to technical compliance.

Recommendation 5 (Customer due diligence)

17. With regard to Recommendation 5, the authorities advised that new amendments are drafted to the recently adopted AML/TF Law (Official Gazette No. 108/17) to address the remaining deficiencies as described in the Secretariat analysis presented and discussed during the 56th Plenary.
18. Based on the provided information the Secretariat conducted analysis of the draft amendments to the AML/TF Law and concluded that:
 - (1) The deficiency on *the absence of requirements for financial institutions to obtain from customers information on a foreign legal person's or foreign legal arrangement's form, directors and powers to bind* is addressed by the provisions of the current AML/TF Law. However, as was indicated in the previous analysis of the Secretariat the AML/TF Law does currently not provide for similar requirements with regard to domestic legal entities to be fully in line with the FATF standards. This deficiency would be addressed with the adoption of the draft amendments to the AML/TF Law in their current form.
 - (2) The deficiency on *blanket exemptions from the CDD requirements where the risk of money laundering and terrorist financing is low, created by the AML/TF Law*, as was identified under the 4th round MER are addressed taking into consideration the new approach applied under the current FATF Methodology allowing the countries to apply exemptions while ensuring that appropriate risk mitigation measures are appropriately applied.
 - (3) The deficiency on *application of simplified CDD measures to overseas resident customers is not limited to countries which are in compliance with and have effectively implemented FATF Recommendations* would be addressed with the adoption of the draft amendments to the AML/TF Law in their current form.
 - (4) The Deficiency on *not extending a prohibition on the use of the simplified CDD measures to "specific higher risk scenarios" as required by the FATF Recommendations* would be addressed with the adoption of the draft amendments to the AML/TF Law in their current form.
19. In light of information provided by Croatia with regard to the application of R.5, it can be observed that with the adoption of the draft amendments to the AML/TF Law the remaining deficiencies as identified in the 4th round MER would be addressed. Hence, Croatia should seek adoption of the AML/TF Law as speedily as the legislative process allows and sufficiently in time before the 58th Plenary in July 2019.

Recommendation 23 (Regulation, supervision and monitoring)

20. With regard to Recommendation 23, Croatia informed that since July 2018, in order to address the deficiencies identified in the 4th MER the authorities have amended the Ordinance on Issuing Authorization to and on Acquisition of a Qualifying Holding in a Voluntary Pension Company (Official Gazette 51/18), adopted the new Capital Market Act (Official Gazette 65/18), Payment System Act (Official Gazette No. 66/2018), Electronic Money Act (Official Gazette No. 64/2018), and drafted amendments of the Law on Insurance which are not pass the Parliamentary procedures.
21. Based on the provided information the Secretariat conducted an analysis of the compliance of Croatia with R. 23 and concluded that:
 - (1) The deficiencies on *the requirement to obtain information on ultimate beneficial owners and, respectively, their criminal background for insurance companies and pension companies; the requirement to prevent criminals from holding shares or managerial positions in financial institutions; requirement to include criminal associates into the scope of the measures aimed at prevention of criminals from holding a controlling interest or management function in financial institutions* were further considered by Croatia while revising the legislation.

In particular, as concerns the insurance companies, the remaining deficiencies with respect to obtaining information on the beneficial owners, and prevention of criminal associates from holding a controlling interest or management function in insurance companies, Croatia stated

that these would be addressed by the draft amendments of the Law on Insurance after its adoption.

As concerns the pension companies Croatia informed that in addition to the former legislative amendments described in the previous Secretariat analysis, the Ordinance on Issuing Authorization to and on Acquisition of a Qualifying Holding in a Voluntary Pension Company (Official Gazette 51/18) was recently adopted. This now additionally obliges any natural or legal person, or natural or legal person acting jointly (the proposed acquirer), intending to acquire or increase their holding in the pension company pursuant Article 79 and 84 of the Voluntary Pension Funds Act (Official Gazette 19/14, 29/18), to provide a list of his/her associates in order to receive authorisation on such acquisition or increase.

As concerns the investment firms Croatia informed that a new Capital Market Act (Official Gazette 65/18) prescribes that criminal or criminal associate cannot be a member of the managing body or the beneficial owner of the investment firm.

As concerns the payment institutions and electronic money institutions Croatia informed that newly adopted Payment System Act (Official Gazette No. 66/2018) and the Electronic Money Act (Official Gazette No. 64/2018) set out respective provisions to prevent criminals from holding shares or managerial positions in payment institutions.

Nevertheless it shall be noted that, the Secretariat has not been provided with the translation of any of the above listed respective (draft) provisions to verify the authority's statement, therefore no conclusion can be made on the actual progress demonstrated by the country to address these deficiencies.

Considering that there were some other developments reported by Croatia previously, this analysis shall be read in conjunction with the previous analysis of the Secretariat presented and discussed during the 56th Plenary, which remains valid.

- (2) The deficiencies on *the lack of legislatively defined licensing requirements and procedures for business entities engaged in factoring activities* as was indicated by the authorities already in 2014, is addressed by the adoption of the Factoring Law ("Official Gazette" no. 94/14) governing among other things the establishment, operation and termination of factoring companies. However, the Secretariat has not yet been provided with the full translation of that law to verify this.
22. Reflecting on the effectiveness of the implementation of supervisory measures, Croatia mentioned in particular that the CNB started the project on updating and aligning its risk-based supervision methodology with the European Supervisory Authorities' Joint Guidelines on the characteristics of a risk-based approach to AML/CTF supervision. The CNB is currently conducting a risk assessment of specific institutions, which would be considered when developing the supervisory plan. During the first half of the year 2018 CNB has performed 2 on-site supervisions.
23. Although steps were made to rectify technical deficiencies, concerns remain with regard to the implementation of measures on identification of the beneficial owners and prevention of criminals and their associates from holding a significant or controlling interest or management function in the financial organisations. Deficiencies in the Insurance Law still remain unaddressed. Progress made with the adoption of a number of legal acts as stated above could not be fully confirmed as the English translation of these acts were not submitted sufficiently in time before the distribution of this analysis. Consequently, the rating for R.23 is not yet up to a level equivalent to "largely compliant".

Recommendation 35 (Conventions)

24. With regard to Recommendation 35, Croatia provided no new information. According to the 4th round MER there is a considerable number of deficiencies indicated in relation to implementation of the relevant Conventions which are covered by the analysis of the measures adopted and implemented to ensure compliance of Croatia with R.1, R.3 and SR.II.

25. Taking into consideration that no progress was demonstrated by Croatian authorities since July 2018, the former analysis of the Secretariat as was discussed during the 56th Plenary, remains valid.
26. As was also noted in the former analysis of the Secretariat, it appears that R.1 and R.3 are not yet implemented up to a level equivalent to “largely compliant”. Hence the rating given to R.35 in the 4th round MER should remain unchanged.

Special Recommendation I (Implementation of United Nations instruments)

27. With regard to Special Recommendation I, Croatia informed that the Ministry of Foreign and European Affairs continued consultations with other competent authorities regarding drafting the necessary legislative amendments to the International Restrictive Measures Act to address the deficiencies identified in the 4th Round MER regarding freezing of terrorist assets.
28. Taking into consideration that no progress was demonstrated by Croatian authorities since July 2018, the former analysis of the Secretariat as was discussed during the 56th Plenary, remains valid.
29. As was noted in the former analysis of the Secretariat in light of information provided by Croatia concerns remain with regard to the narrow scope of the terms “terrorist” and “terrorist organisation”, derived from logical and systemic interpretation of different articles of the CC; ambiguities regarding the scope of provisional measures related to “funds” used or intended to be used in TF offense; and deficiencies under SR.III. Considering that, according to the Secretariat analysis, it appears that R.3 and SR.III are not implemented up to a level equivalent to “largely compliant”, the rating given to SR.I in the 4th round MER should remain unchanged.

Special Recommendation III (Freeze and confiscate terrorist assets)

30. With regard to Special Recommendation III, Croatia informed that the Ministry of Foreign and European Affairs continued consultations with other competent authorities regarding drafting the necessary legislative amendments to the International Restrictive Measures Act to address the deficiencies identified in the 4th Round MER regarding freezing of terrorist assets.
31. Taking into consideration that no progress was demonstrated by Croatian authorities since July 2018, the former analysis of the Secretariat as was discussed during the 56th Plenary, remains valid.
32. As was noted in the former analysis of the Secretariat, the authorities have indicated that, following Croatia’s accession to the EU on 1 July 2013, the freezing mechanisms are applied exclusively through EU legislation. While some deficiencies identified under the 4th round MER are addressed to a certain extent through the application of EU mechanisms, concerns still remain as to whether Croatia is in a position to freeze the funds controlled indirectly by designated persons. Croatia has not also adopted any respective measures under the domestic framework. No further information was provided on additional guidance to the reporting entities, as recommended under the 4th round MER. Hence, the rating for SR.III is not yet up to a level equivalent to “largely compliant”.

Review of measures taken in relation to other Recommendations

Recommendation 12 (DNFBPs – R.5, 6, 8-11)

33. With regard to Recommendation 12, Croatia provided no new information on steps taken to address the remaining deficiencies.
34. Taking into consideration that no progress was demonstrated by Croatian authorities since July 2018, the former analysis of the Secretariat as was discussed during the 56th Plenary, remains valid.
35. As was noted in the former analysis of the Secretariat, the majority of technical deficiencies identified in the 4th Round MER are addressed. Concerns with Recommendation 5 described above are equally applicable to DNFBPs. In addition, doubts remain with respect to explicitly addressing the deficiencies of regulation of matters on non-face to face business relationships or transactions, as well as providing an appropriate guidance on identifying complex or unusually large transactions, and unusual patterns of transactions, which have no apparent economic or lawful purpose. Hence the rating for R.12 is not yet up to a level equivalent to “largely compliant”.

Recommendation 16 (DNFBPs – R.13-15 and 21)

36. With regard to Recommendation 16, Croatia provided no new information on steps taken to address the remaining deficiencies.
37. Taking into consideration that no progress was demonstrated by Croatian authorities since July 2018, the former analysis of the Secretariat as was discussed during the 56th Plenary, remains valid.
38. As was noted in the former analysis of the Secretariat, since Recommendations 13-15 and 21 were rated “largely compliant” in the 4th Round MER the rating PC for the Recommendation 16 was based on the effectiveness of implementation of respective provisions. However, except for information on trainings, the Secretariat has not yet been provided with other information on any progress made. Hence, the rating for R. 16 is not yet up to a level equivalent to largely compliant.

Conclusion

39. While Croatia has made some progress since the 56th Plenary in July 2018, a large number of deficiencies identified in the 2012 MER for the following key and core recommendations have not been fully addressed: R.1, R.3, R.5, R.23, R.35, SR. and SR.III.
40. Work on revising the newly-adopted AML/TF Law has begun aimed at addressing outstanding deficiencies under R.5 (as well as R.12 and 16). Currently the amendments to the AML/TF Law are pending the legislative procedure.
41. Amendments to the Criminal Code in order to address deficiencies with regard to R.1 and R.3 are still pending the legislative procedure. The authorities are urged to use the momentum of that legislative procedure and include outstanding deficiencies under both recommendations which may not yet have been included in the amendments.
42. No particular progress has been made with respect to SR.III and, as a consequence, with respect to R.35 and SR.I. Due to the fact that the Secretariat was not sufficiently provided with respective adopted legislation, progress on R.23 could not be verified.
43. Mindful of the fact that the deficiencies were already identified in the MER of 2012, the Secretariat notes that progress made by Croatia since the 56th Plenary (July 2018) falls short of the expectation by the Plenary (which had decided that, should the respective amendments not be adopted by the time of the 57th Plenary in December 2018, it would consider the adoption of Step 2 of its CEPs). The Secretariat therefore proposes that the Plenary discusses the application of Step 2 of CEPs, as provided in Rule 14 of MONEYVAL’s 4th round rules of procedure.

The MONEYVAL Secretariat
November 2018