DEVELOPING FACTORING AS A FINANCING TOOL IN KOSOVO

Kosovo is one of the most disputed parts of the Western Balkans, with its status the source of controversy for over a decade. In February 2008, Kosovo unilaterally declared its independence from Serbia, which probably makes it one of the youngest countries in the world. In addition, according to government data, it is estimated that more than 65 per cent of the population is under the age of 30, and 50 per cent of the population classified as falling below the poverty line. It is therefore imperative that new financial products are developed to broaden the finance options available, as the development of a financial environment that serves small and medium-sized enterprises (SMEs) can promote inclusive growth, higher wages and a range of other positive outcomes. In addition, the job creation and opportunities are also likely to lead to a sense of belonging for the population.

AMMAR AL-SALEH
SENIOR COUNSEL, EBRD
AlsalehA@ebrd.com

Scarce finance and inadequate economic development stifle many small and medium-sized enterprises (SMEs). According to the EBRD-World Bank Business Environment and Enterprise Performance Survey, BEEPS V (2012-16) access to finance is one of the top three obstacles to doing business in 16 countries in the EBRD regions, with around 50 per cent of SMEs in the EBRD regions unable to access a loan when they required one. Furthermore, penetration levels for non-bank financing instruments such as factoring are less than half the level one finds in the EU (European Union) or OECD countries (3 per cent in the EBRD regions compared with 6 to 7 per cent in the EU/OECD) showing that there is potential for growth (based on World Bank Development Indicators database, 2016 data).

Kosovo has therefore taken an important step in the reform of its legal framework with the adoption of a new regulation on factoring by the Central Bank of Kosovo on 29 October 2018. Factoring is an area that was not previously regulated, and represents an attractive financial instrument which has not been sufficiently used in the country. With the recent entry into force of the regulation, the legal and regulatory framework for this activity will be significantly improved and aligned with international best practices. The adoption follows support by the Bank through its Legal Transition Programme (LTP) in preparation of the regulation.

Factoring is a financial service based on the sale of accounts receivable, and is a useful tool for capital-deprived SMEs with low credit standing. It unravels the potential of an asset that all SMEs have — their invoices – and supports SMEs in receiving capital faster and under more flexible terms than a conventional bank loan, rather than having to wait for customers to pay their invoices, thus easing their access to trade finance and promoting their inclusion in value chains.

In a new factoring environment such as Kosovo, it is not surprising that the biggest challenges are the absence of a supportive legal environment and the lack of awareness and understanding of factoring in the business community. For factoring to function it requires a legal environment that permits the sale or assignments of accounts receivables and enforces the underlying contracts. In this regard, a reference to factoring in the law, or even a "Factoring Act", which recognises it as a financial service, can clarify the nature of the factoring transactions and the ruling in case of default of sellers or customers.[1] Another driver of the legislative reform is Kosovo's process of EU accession which dictates alignment of financial sector regulation with EU directives.

Acknowledging the EBRD's track record working on factoring legal frameworks in the region, the Central Bank of Kosovo approached the Bank in 2017 with a request for technical assistance for developing its legal factoring framework.

On securing all of the necessary internal approvals and funding from the government of Luxembourg, the EBRD procured the services of local and international experts to assist the working group created by the central bank, with laying down the recommendations for improvement, drafting the factoring regulation and conducting outreach activities to promote factoring in the local market.

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Before drafting of legislation can commence there has to be a broad consensus among the relevant stakeholders on what the law has to achieve and how it can achieve it. Legislative reform was therefore undertaken in close coordination with market players, regulatory bodies and foreign experts in financial services. Coordination was reached by consultations at each stage of the process and provided stakeholders with the opportunity to comment on proposals and advise alternative solutions that, at a later stage, were transposed into legislation.

The preliminary stage involved preparation of a concept paper, which lays out international best practices on the regulation of factoring, accompanied by concrete recommendations tailored to the local market, looking in addition at what had been adopted and worked (or did not) in neighbouring countries.

In our reform process in Kosovo, the concept paper covered:

- types of factoring
- elements which enable a factoring framework – this included regulation of the industry, assignment of receivables, e-signatures and tax treatment
- review of factoring legislation locally, regionally and internationally.

The concept paper also serves to assist the authorities with future reform endeavours, as implementation of a new law is just as important as the passing of the law itself. Therefore follow-up activities to the project will include promoting factoring as an alternative financing tool for SMEs and ensuring that market participants are well-informed about the legislative changes.

As a result of the findings and the consensus for reform during the preliminary stages, the EBRD proceeded with drafting the provisions of the factoring regulation which were also presented and discussed at length with the working group members.

Bicycle producer plans ahead with factoring

Albimi SHPK is a company that was established in 1998 in the city of Gjilan, in Kosovo.

"It all started with a passion for bicycles and assembling bikes imported from different European countries," says Ibrahim Krivaca, the company's owner.

Thanks to a very dedicated and professional team, Albimi SHPK has grown and in 2008 it became an exclusive representative of the internationally renowned Shimano brand.

Albimi has also created its own brand, Pilot, which is very successful in the local market. Pilot is 100 per cent made in Kosovo: from design to the finished product.

"Being present in all the cities of Kosovo and having contracts with more than 50 retailers, managing payment delays is very difficult," says Mr Krivaca.

But using factoring has made a huge impact on his business this year. Instead of waiting up to 100 days for an invoice to become due, the company gets paid by Raiffeisen Bank, which provides factoring services, shortly after making the delivery.

"With factoring I can plan my budget and foresee investments much more easily", continues Mr Krivaca. "It is a much-needed source of finance and development support for small and medium-sized businesses here in Kosovo." Now Mr Krivaca hopes that factoring will further develop across the country and will support local producers with international trade.

CONCLUSION

The legal and judicial environments play a key role in the success of factoring. The legal provisions of general laws such as the civil code do not necessarily recognise factoring as a financial service, nor are they tailored to the needs of factoring services. This can limit the scope of factoring transactions or increase factoring transaction risks, including creditors' priority rights for instance.

A factoring framework introduces meaningful oversight that guarantees the stability and legitimacy of the sector and its growth. It is thus advisable for regulators to create a sound, clear and predictable legal framework to encourage the development of factoring activities and avoid unnecessary disputes due to a lack of regulation.

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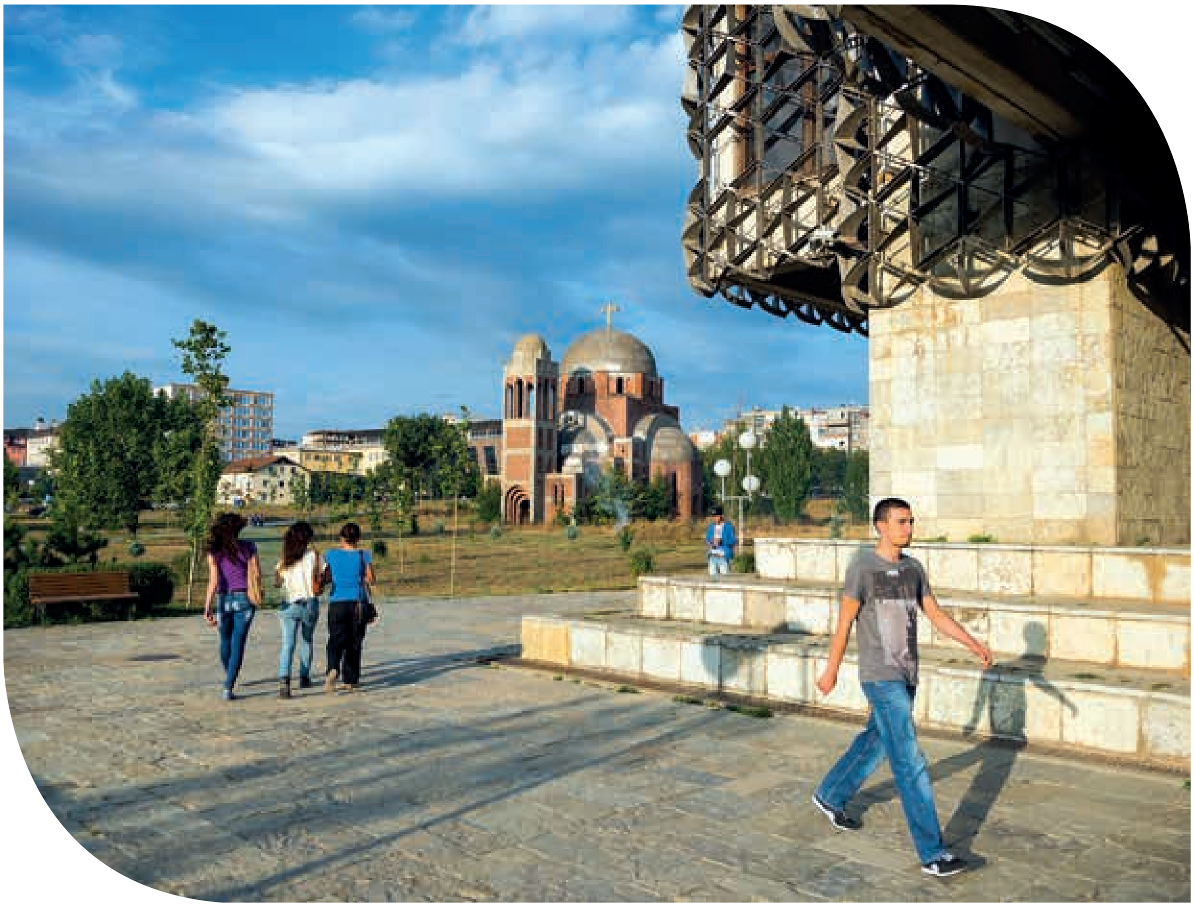

However, designing and implementing effective regulation, which balances financial stability and investor protection, represents a challenge for policymakers and regulatory authorities. A key take-away from the legislative reform process in Kosovo, which applies to any such process, is that a pre-condition for successful and functional reform is the involvement of all stakeholders from the start and their close cooperation throughout.

1 Source:
http://www.oecd.org/cfe/smes/New-Approaches-SME-full-report.pdf
(last accessed 27 December 2018).