



HNB

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**Decision on  
foreign exchange risk exposure limits  
of credit institutions**

**(Official Gazette 38/2010)**

Pursuant to Article 161 paragraph (2) of the Credit Institutions Act (Official Gazette 117/2008, 74/2009 and 153/2009) and Article 43 paragraph (2) item (9) of the Act on the Croatian National Bank (Official Gazette 75/2008), the Governor of the Croatian National Bank hereby issues the

### **Decision on foreign exchange risk exposure limits of credit institutions**

#### **Article 1**

(1) This Decision determines the manner of calculation of total open foreign exchange positions of credit institutions, the maximum permitted exposure of credit institutions to foreign exchange risk and the time limits and the manner of reporting to the Croatian National Bank on foreign exchange risk exposure of credit institutions.

(2) This Decision shall apply to credit institutions with registered offices in the Republic of Croatia which have obtained authorisation from the Croatian National Bank and branches of third country credit institutions which have obtained authorisation to provide services from the Croatian National Bank (hereinafter: credit institutions).

(3) Notwithstanding paragraph (2) of this Article, this Decision shall not apply to electronic money institutions.

#### **Article 2**

For the purposes of this Decision, the following terms shall have the following meaning:

(1) Foreign exchange risk shall be the risk to which a credit institution is exposed when it has an open foreign exchange position in each foreign currency and gold which may lead to losses due to changes in cross-currency relations, changes in the value of the kuna against a foreign currency and changes in the value of gold.

(2) Own funds shall be the own funds defined under Article 2 paragraph (4) of the Decision on the capital adequacy of credit institutions (Official Gazette 1/2009, 41/2009, 75/2009 and 02/2010) which the credit institution has reported to the Croatian National Bank in the last submitted report. In case of a change in the own funds of a credit institution during a reporting period which can significantly change the exposure of a credit institution to foreign exchange risk (e.g. recapitalisation, reported loss), a new calculation of own funds shall be made and submitted to the Croatian National Bank without delay. If the Croatian National Bank has issued a decision, based on the supervision of the business of a credit institution, instructing the credit institution to make a new calculation of own funds, the credit institution shall immediately comply with this requirement in the calculation of exposure of foreign exchange positions to foreign exchange risk.

(3) Kuna assets whose value is calculated on the basis of the exchange rate of the kuna against an individual foreign currency shall be considered purchased call option on that foreign currency only in the case of the kuna depreciating against that foreign currency, while kuna liabilities whose value is calculated on the basis of the exchange rate of the kuna against an individual foreign currency shall be considered written call option on that foreign currency only in the case of the kuna depreciating against that currency.

(4) A call option on a currency shall be the option to buy a specific currency and a put option on a currency shall be the option to sell a specific currency.

(5) A working day shall be any calendar day except Saturdays, Sundays and national holidays.

### **Article 3**

A credit institution shall report under an open foreign exchange position in a foreign currency (and in gold) the following elements:

- 1) the net spot position in a currency (the difference between the assets and liabilities in this currency, including accrued interest and spot position in foreign exchange swaps and spot transactions which are concluded but not yet reported in the balance sheet) and the net spot position in gold;
- 2) the net forward position (the difference between all amounts to be received and all amounts to be paid under forward foreign exchange and forward gold transactions, including foreign exchange and gold futures and the nominal amount of foreign exchange swaps not reported under the spot position);
- 3) irrevocable guarantees, uncovered letters of credit and similar instruments that are certain to be called and likely to be irrecoverable;
- 4) net future income/expenses not yet accrued but already hedged in such a way that the hedge ratio complies with the requirements of hedge accounting in accordance

with International Accounting Standard 39, provided they are reported on a consistent basis;

5) the net delta equivalent of the total book of foreign exchange and gold options, calculated in accordance with Part 6.3 of Title III of the Decision on the capital adequacy of credit institutions (Official Gazette 1/2009, 75/2009 and 2/2010); and

6) the market value of other (non-foreign exchange and non-gold swaps) options whose underlying instrument is expressed in foreign currency.

#### **Article 4**

(1) A credit institution's calculation of spot position in an individual currency shall comprise:

- 1) all foreign exchange assets and liabilities;
- 2) assets and liabilities with a foreign currency clause;
- 3) spot foreign exchange purchase and sale transactions which have been agreed but have not been entered in the general ledger of the credit institution;
- 4) spot positions arising from foreign exchange swap agreements.

(2) Net spot position in an individual currency shall be long if the total assets under paragraph (1) of this Article exceed the total liabilities under that paragraph. Net spot position in an individual currency shall be short if the total liabilities under paragraph (1) of this Article exceed the total assets under that paragraph.

(3) Foreign exchange assets and foreign exchange liabilities shall include all foreign exchange assets and liabilities and assets and liabilities in kuna whose value in kuna is calculated on the basis of the exchange rate of the kuna against a foreign currency (hereinafter assets and liabilities with a currency clause).

(4) Net spot position shall not include impairment provisions arising from off-balance sheet liabilities nor any other on-balance sheet items which do not constitute assets or liabilities of a credit institution.

#### **Article 5**

(1) A credit institution shall include in the calculation of the forward position and irrevocable guarantees and other similar instruments positions:

- 1) forward foreign exchange (and gold) purchase and sale transactions, including foreign exchange or gold futures and the principal of foreign exchange swap agreements not reported under the spot position;
- (2) irrevocable guarantees, uncovered letters of credit or similar instruments that are expected to be called in the future and are most likely to be irrecoverable (denominated in foreign currency or with a foreign currency clause).

(2) Irrevocable guarantees, uncovered letters of credit or similar instruments shall be reported under the long forward position in the net amount (nominal amount reduced by the formed provisions for identified losses).

### Article 6

(1) A credit institution shall calculate the value of the book of foreign exchange options in each currency. When calculating the value of the book of foreign exchange options, the options shall be reported in the delta equivalent of the notional amount of the option. By way of exception, credit institutions which pursuant to the Decision on the capital adequacy of credit institutions use a simplified method shall, when calculating the value of the book of foreign exchange options, report the options in the amount defined in Part 6.2 of Title III of the Decision on the capital adequacy of credit institutions.

(2) The delta equivalent of an option position shall equal the multiplication of its delta coefficient and the nominal value of that option. The delta equivalent (i.e. the amount determined by the application of a simplified method) of individual options by each currency shall carry the following signs in the calculation of the value of the book of foreign exchange options:

	BOUGHT	SOLD
CALL OPTION	+	-
PUT OPTION	-	+

(3) For exchange traded foreign exchange options, a credit institution shall apply delta coefficients determined by the exchanges. A credit institution may calculate delta equivalents by means of an internal model for option valuation approved by the Croatian National Bank.

(4) Notwithstanding paragraph (1) of this Article, where a credit institution has a small position in bought foreign exchange or gold options and calculates capital requirements in accordance with Part 6.2 of Title III of the Decision on the capital adequacy of credit institutions, the amount calculated in accordance with Part 6.2 of Title III of the Decision on the capital adequacy of credit institutions shall be added to the open foreign exchange position.

(5) Assets and liabilities with an embedded call option shall be summed up in their nominal amount, taking into account the sign they carry. The value of the assets and liabilities position with an embedded call option of an individual foreign currency shall be added to the previously calculated open foreign exchange position of the credit institution in an individual currency, taking into account the sign it carries.

(6) Notwithstanding paragraph (5) of this Article, a credit institution may calculate the value of the position in foreign currency of assets and liabilities with an embedded call option by means of an internal model in accordance with Part 6.3.3 of Title III of the Decision on the capital adequacy of credit institutions subject to prior permission of the Croatian National Bank.

(7) The market value of any other (non-foreign exchange and non-gold) options, whose price of the underlying is expressed in a foreign currency shall be calculated in such a way that market values of all such options are summed up, taking into account the sign they carry, and that their sum total is reported under a position in options on that currency.

(8) By way of exception, where a credit institution has entered into credit arrangements with the Croatian Bank for Reconstruction and Development whereby the foreign exchange risk of embedded call options on foreign currency arising from credit arrangements has been transferred to the final beneficiary of funds under the agreement and where all the conditions referred to in Article 558 of the Decision on the capital adequacy of credit institutions have been met, the credit institution may exclude these asset and liability items from the calculation of its open foreign exchange position.

## **Article 7**

(1) Open foreign exchange position of a credit institution in an individual currency may be long or short. A credit institution shall have a short foreign exchange position in an individual currency (or gold) when the sum of the elements referred to in Article 3 of this Decision in that currency (or gold) is negative. A credit institution shall have a long foreign exchange position in an individual currency (or gold) when the sum of the elements referred to in Article 3 of this Decision in that currency (or gold) is positive.

(2) Open position in an individual currency shall be calculated in that currency and converted into kuna by means of the midpoint exchange rate of the Croatian National Bank applicable on the reporting date.

(3) A credit institution shall also calculate open positions in currencies not shown in the exchange list of the Croatian National Bank. When calculating open positions in those currencies, the credit institution shall first convert such positions into euro or American dollars using the midpoint exchange rates of the benchmark markets and then convert them into kuna using the midpoint exchange rate of the Croatian National Bank applicable on the reporting date.

(4) For the purposes of calculating its open foreign exchange position in an individual currency, a credit institution may break down net positions in composite currencies into the component currencies according to the structure of the composite currency.

(5) For the purposes of calculating its open foreign exchange position under this Decision, a credit institution shall treat collective investment undertakings in accordance with Articles 559 and 560 of the Decision on the capital adequacy of credit institutions.

(6) The credit institution may exclude from the calculation of its open foreign exchange position in each currency all positions taken with the intent to hedge the credit institution's capital adequacy ratio against the adverse effects of exchange rate changes as well as all positions being deducted from own funds, provided that they are of a strategic nature, not traded by the credit institution, and excluded on a consistent basis. The credit institution may exclude the said positions only with prior permission of the Croatian National Bank. When applying for permission for exclusion, the credit institution shall state the reasons for the exclusion.

#### **Article 8**

(1) The total short foreign exchange position of a credit institution shall be the sum of all short foreign exchange positions of the credit institution in individual currencies. The total long foreign exchange position of a credit institution shall be the sum of all long foreign exchange positions of the credit institution in individual currencies. The total open foreign exchange position shall be the higher of these two figures. The absolute open position in gold shall be added to the total open foreign exchange position.

(2) A credit institution shall adjust its total open foreign exchange position at the end of each day in such a way that its total open foreign exchange position (increased by the position in gold) does not exceed the amount which constitutes 30% of its own funds.

#### **Article 9**

(1) A credit institution shall submit to the Croatian National Bank daily reports on the total foreign exchange position referred to in Article 8 of this Decision. The reports shall be completed in the manner prescribed in the Instructions which constitute an integral part of this Decision.

(2) A credit institution shall submit the reports referred to in paragraph (1) of this Article on the next working day for the previous working day.

(3) For non-working days, a credit institution shall submit the reports referred to in paragraph (1) of this Article within two working days following the reporting non-working day.

(4) A credit institution shall keep the data used in the compilation of the reports referred to in paragraph (1) of this Article for a minimum period of three years.

### **Article 10**

(1) As of the date of its entry into force, this Decision shall repeal the Decision on the limitation of banks' exposure to foreign exchange risk and the Instructions for the implementation of the Decision on the limitation of banks' exposure to foreign Exchange Risk (Official Gazette 17/2003, 39/2006, 130/2006 and 25/2009).

(2) This Decision shall be published in the Official Gazette and shall enter into force on 31 March 2010.

No. 149-020/03-10/ŽR  
Zagreb, 22 March 2010

Croatian National Bank  
Governor  
Željko Rohatinski

**Instructions**  
**for the implementation of the Decision on foreign exchange risk exposure limits**  
**of credit institutions**

Article 1

Items which have been value adjusted in accordance with the International Accounting Standards shall be reported under the foreign exchange position in their recoverable amount.

Article 2

(1) A credit institution shall submit a Report on foreign exchange risk exposure by individual currencies (form VR-1) and a Report on the total foreign exchange risk exposure (form VR-2).

(2) A credit institution shall submit the forms VR-1 and VR-2 for non-working days within two working days following the reporting non-working day (e.g. if there are no national holidays during the week, data for Saturday, Sunday and Monday shall be submitted on Tuesday).

(3) For each individual currency, a credit institution shall report:

- 1) the spot position (columns 2 and 3 of form VR-1);
- 2) the forward position and irrevocable guarantees and similar instruments (columns 4 and 5 of form VR-1);
- 3) the option position (column 7 of form VR-1); and
- 4) the long or short foreign exchange position (column 8 of form VR-1).

Article 3

(1) The amount of option position, calculated in accordance with Article 6 of this Decision, shall be entered in column 7 of form VR-1.

(2) For each currency the sum total of the spot and forward positions shall be calculated (which is entered in column 6 of form VR-1). The obtained amount shall be adjusted for the option position, and the adjusted amount shall be entered in column 8 of form VR-1.

#### Article 4

(1) The total open foreign exchange position of a credit institution (option position excluded) that is entered in column 3 of form VR-2 shall represent the absolute amount of the sum total of all long or sum total of all short positions (calculated in columns 1 and 2 of form VR-2) by each currency, depending on which of the two sum totals is greater.

(2) The total open foreign exchange position of a credit institution (including the option position) which represents the absolute amount of the sum total of all long or sum total of all short positions (including option position) by each currency (listed in columns 4 and 5 of form VR-2), depending on which of the two sum totals is greater, shall be increased by the nominal amount of the gold position and entered in column 7 of form VR-2.

Croatian National Bank Republic of Croatia  Form VR-1 - Report on foreign exchange risk exposure by individual currencies	Name of credit institution:  OIB:  Contact person:  Balance as at:
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in HRK '000

Currency	Spot position		Forward position		Open foreign exchange position in an individual currency, without option position	Option position	Open foreign exchange position in an individual currency adjusted for the option position
	Assets	Liabilities	Long position	Short position			
(1)	(2)	(3)	(4)	(5)	(6) = 2-3+4-5	(7)	(8) = (6) + (7)

in HRK '000

Currency	Items determined in accordance with Article 2 paragraph (3) of this Decision	
	Assets	Liabilities
(1)	(2)	(3)

Name of method used to calculate the option position: \_\_\_\_\_

Croatian National Bank Republic of Croatia  Form VR-2 - Report on the total foreign exchange risk exposure	Name of credit institution:  OIB:  Contact person:  Balance as at:
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in HRK '000

Total long foreign exchange position (option position excluded)	Total short foreign exchange position (option position excluded)	Total foreign exchange position (option position excluded)	Total long foreign exchange position (option position included)	Total short foreign exchange position (option position included)	Position in gold	Total foreign exchange position
(1)	(2)	(3)	(4)	(5)	(6)	(7)

Own funds in HRK '000 (8)	
Percentage of foreign exchange position exposure (option position excluded) in relation to own funds ((3) / (8)) * 100	
Percentage of foreign exchange position exposure (option position included) in relation to own funds ((7) / (8)) * 100	