

Pursuant to Article 161, paragraph (1) of the Credit Institutions Act (Official Gazette 117/2008) 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 large exposures of credit institutions

1 GENERAL PROVISIONS

Article 1

(1) This Decision prescribes:

- 1) the method of calculating and monitoring the credit institution's large exposures and concentration risk of exposures to collateral issuers and providers of unfunded credit protection;
- 2) the items included in exposures;
- 3) the indicators used to determine connected persons;
- 4) the explanations concerning the identification of persons in a special relationship with the credit institution, in particular persons who have concluded employment contracts with the credit institution under preferential terms;
- 5) the exemptions from large exposure limits;
- 6) the rules on exceeding large exposure limits; and
- 7) the method of reporting on large exposures, exposures to persons in a special relationship and collateral issuers and providers of unfunded credit protection.

(2) This Decision shall apply to:

- 1) credit institutions with registered offices in the Republic of Croatia, authorised by the Croatian National Bank; and
- 2) branches of third-country credit institutions, authorised by the Croatian National Bank to provide services.

(3) By way of derogation from paragraph (2) of this Article, this Decision shall not apply to electronic money institutions.

(4) Credit institutions shall comply with the provisions of this Decision on a consolidated basis if they are required to comply with the requirements on supervision on a consolidated basis for their groups of credit institutions in the RC as set out in Article 127 of the Credit Institutions Act.

Article 2

(1) A credit institution's exposure to a single person or group of connected persons shall be considered a large exposure where its value is equal to or exceeds 10% of its own funds.

(2) For the purposes of this Decision, the term 'own funds' shall be used as defined in Article 2, paragraph (3) of the Decision on own funds of credit institutions.

2 MONITORING OF LARGE EXPOSURES AND CONCENTRATION RISK OF EXPOSURES TO COLLATERAL ISSUERS AND PROVIDERS OF UNFUNDED CREDIT PROTECTION

Article 3

(1) Credit institutions shall establish and implement policies and procedures for identifying, recording and monitoring of large exposures to a single person or group of connected persons which arise on their non-trading books and trading books.

(2) Credit institutions shall establish sound administrative and accounting procedures, adequate information systems and adequate internal control systems for the implementation of policies and procedures referred to in paragraph (1) of this Article.

(3) Credit institutions shall establish internal control systems to temporarily transfer the exposures in question to another person, whether within the same group of connected persons or not, and undertake artificial transactions to close out the exposure during the 10-day period and create a new exposure.

Article 4

(1) Credit institutions shall establish and implement policies and procedures for identifying, analysing and monitoring of possible concentration risk of exposures to collateral issuers and providers of unfunded credit protection, and prescribe the procedures if such risk is determined.

(2) The terms used shall mean the following for the purpose of calculating the concentration risk referred to in paragraph (1) of this Article:

1) 'collateral' means credit protection set out in Part 4.2.1 of Title II of the Decision on the capital adequacy of credit institutions, with the exception of receivables, other physical collateral and leasing transactions set out in Article 338 of the same Decision, regardless of the credit quality step and the minimum requirements for recognition;

2) 'unfunded credit protection' means guarantees, counter-guarantees and credit derivatives set out in Part 4.3 of Title II of the Decision on the capital adequacy of

credit institutions, regardless of the credit quality step and the minimum requirements for recognition;

3) 'collateral issuer' means any person who issues and pledges securities to the credit institution or any person who pledges its deposits, real estate or other forms of collateral to the credit institution or allows fiduciary transfer of ownership; and

4) 'provider of unfunded credit protection' means any person set out in Part 4.3 of Title II of the Decision on the capital adequacy of credit institutions, regardless of the credit quality step of the provider.

3 EXPOSURE

Article 5

(1) For the purposes of this Decision, 'exposure of a credit institution' means the amount of its receivables, investments and off-balance sheet liabilities related to a single person or group of connected persons and includes:

- 1) the net amount of on-balance sheet items (the carrying value net of value adjustments);
- 2) the off-balance sheet items set out in Article 18 of the Decision on the capital adequacy of credit institutions and net of provisions, without the assignment of conversion factors and risk weights; and
- 3) the exposures due to the transactions, agreements and contracts set out in Part 6 of Title II of the Decision on the capital adequacy of credit institutions, such exposures being calculated in the manner laid down in Part 6 of the same Decision, without the assignment of risk weights.

(2) By way of derogation from paragraph (1) of this Article, the exposure shall not include:

- 1) spot foreign exchange transactions in the period up to the contractual settlement date which may not be longer than two working days from the trading date; and
- 2) spot transactions for the purchase or sale of securities in the period up to the contractual settlement date which may not be longer than five working days from the trading date.

(3) For the purpose of paragraph (2) of this Article, working days shall be days from Monday to Friday.

(4) The exposure shall be calculated by summing the exposures which arise on the non-trading book and the exposures which arise on the trading book. Where credit institutions calculate the capital requirement for position risks, they shall calculate the overall exposure to a single person or group of connected persons which arises on the trading book in accordance with Article 6 of this Decision.

(5) If credit institutions possess information about the structure and type of underlying exposures related to the exposure classes set out in Parts 2.2.13, 2.2.14 and 2.2.15 of

Title II of the Decision on the capital adequacy of credit institutions, they may treat these underlying exposures as exposures referred to in paragraph (1) of this Article and apply to them the provisions of this Decision.

Article 6

(1) Where credit institutions calculate the capital requirement for position risks, they shall calculate the overall exposure to a single person on the trading book by summing the following items:

- 1) the excess – where positive – of a credit institution's long positions over its short positions in all the financial instruments issued by the person in question, the net position in each of the different instruments being calculated in accordance with the methods laid down in Part 3 of Title III of the Decision on the capital adequacy of credit institutions;
- 2) the net exposure of a credit institution, in the case of the underwriting of a debt or an equity instrument, calculated by deducting those underwriting positions which are subscribed or sub-underwritten by third parties on the basis of a formal agreement from the amount of securities it became unconditionally committed to accept at an agreed price and reduced by the factors set out in Table 30 in Article 545 of the Decision on the capital adequacy of credit institutions; and
- 3) the exposures due to the transactions, agreements and contracts set out in Part 6 of Title II of the Decision on the capital adequacy of credit institutions, such exposures being calculated in the manner laid down in Part 6 of Title II of the same Decision.

(2) For the purpose of paragraph (1), item (2) of this Article, credit institutions shall be required to set up systems to monitor and control their underwriting exposures between the time of the initial commitment and working day one in the light of the nature of the risks incurred in the period in question.

(3) For the purpose of paragraph (1), item (3) of this Article, credit institutions shall not apply the provisions referred to in Part 3 of Title II of the Decision on the capital adequacy of credit institutions to the calculation of exposures.

(4) For the purpose of paragraph (1), item (3) of this Article, credit institutions may calculate the exposure value of repurchase transactions and securities lending or borrowing transactions in the manner prescribed in paragraph (1), item (3) of this Article only if the conditions referred to in Article 375 of the Decision on the capital adequacy of credit institutions are met. Where the conditions referred to in Article 375 of the Decision on the capital adequacy of credit institutions are not met, credit institutions shall report the exposure value of repurchase transactions and securities lending or borrowing transactions in the same manner as other on-balance sheet items in the non-trading book.

(5) The exposure to a group of connected persons on the trading book shall be calculated by summing the exposures to individual persons in a group, as calculated in paragraph (1) of this Article.

Article 7

For the purposes of this Decision and the calculation of exposures, the exposure to a branch of a third-country credit institution shall be treated as the exposure to any other credit institution.

4 CONNECTED PERSONS

Article 8

(1) When determining the connected persons in the manner referred to in Article 24, paragraph (1) of the Credit Institutions Act, credit institutions shall assess:

- 1) the relationship between parent undertakings and subsidiary undertakings or a similar relationship; and
- 2) the economic and financial interconnectedness.

(2) When determining the relationship of control which arises from direct or indirect relationship between parent undertakings and subsidiary undertakings, credit institutions shall apply the provisions of Article 18 of the Credit Institutions Act.

(3) When determining the relationship between any legal or natural person and a subsidiary undertaking, which is similar to the relationship of control between parent undertakings and subsidiary undertakings referred to in Article 21 of the Credit Institutions Act, credit institutions shall assess the following indicators of control:

- 1) the person has power to decide on crucial transactions such as the transfer of profit or loss;
- 2) the person has power to govern the financial and operating policies of another person;
- 3) the person has power to cast the majority of votes at meetings of the general assembly, management board or equivalent governing body where control of another legal person is exercised by that board or body;
- 4) the person has power to coordinate the management of a legal person with that of other legal persons in pursuit of a common objective; and
- 5) other relationships that are in their substance similar to indicators stated in items (1) to (4) of this paragraph.

(4) It shall be deemed that the control referred to in paragraph (3) of this Article exists if credit institutions determine the existence of the indicators of control, regardless whether the person for the time being actually does exercise its control or not.

(5) When determining the economic and financial interconnectedness between persons, credit institutions shall assess the following indicators of interconnectedness:

- 1) in the case when the lessor of a commercial property receives the majority of the rent from one lessee, which constitutes the majority of its income;
- 2) in the case when one person is the sole vendor of a product and the other person the only buyer of the same;
- 3) in the case when the operation of one person (e.g. producer) depends on one or more vendors which it would take time to substitute;
- 4) in the case when legal persons have an identical customer base, consisting of a very small number of customers and where the potential for finding new customers is limited;
- 5) in the case when legal persons use a common source of significant funding;
- 6) in the case when both of them are undertakings where the majority of the members of the management or supervisory boards or other governing bodies is identical; and
- 7) other relationships that are in their substance similar to indicators stated in items (1) to (6) of this paragraph.

(6) By way of derogation from paragraphs (2) and (3) of this Article, if the government is a direct or indirect holder of shares or holdings in two or more legal persons, these persons shall not be considered connected persons.

(7) A natural or legal person may not be included in more than one group of connected persons referred to in Article 24, paragraph (2) of the Credit Institutions Act, except in the following cases:

- 1) legal and natural persons may be included in the groups of each of their connected undertakings, provided that an interconnectedness has not been established for the same undertakings on the basis of indicators of control or economic and financial interconnectedness;
- 2) a majority holding in the capital or of the voting rights of an undertaking is held by one person on trust for another person and in this case it may be appropriate to include this undertaking in both groups;
- 3) it is necessary to include a legal person in which only two persons hold 50:50 participations (shares or holdings) in the groups of these two persons in case they exercise a common influence on that legal person.

5 PERSONS IN A SPECIAL RELATIONSHIP

Article 9

For the purposes of this Decision, employment contracts concluded with the credit institution under preferential terms referred to in Article 153, paragraph (1), item (3) of the Credit Institutions Act shall be the contracts the provisions of which imply that the persons with whom they are concluded have a significant influence over the operation of the credit institution and the contracts in which the remuneration for the work of certain

persons is determined in accordance with the special criteria, different from those applied to the persons who have concluded the standard employment contracts, where these persons are not referred to in Article 153, paragraph (1), items (1), (2) or (4) of the Credit Institutions Act.

6 EXEMPTIONS FROM EXPOSURE LIMITS

Article 10

(1) By way of derogation from Articles 150 to 152 of the Credit Institutions Act, the exposure limits shall not apply to a credit institution's holdings in credit and financial institutions if such holdings are items which are deducted from own funds referred to in Article 27, paragraph (1), items (1) and (3) of the Decision on own funds of credit institutions.

(2) The provision of paragraph (1) of this Article shall not apply to investments in subordinated and hybrid instruments of credit and financial institutions.

(3) By way of derogation from Articles 150 to 152 of the Credit Institutions Act, the exposure limits shall not apply to the exposures to credit institutions which arise from minimum reserves required by the Croatian National Bank and allocated by credit institutions to the accounts of other credit institutions, provided that these other credit institutions have allocated the same funds to the accounts held with the Croatian National Bank.

(4) By way of derogation from Articles 150 to 152 of the Credit Institutions Act, the exposure limits shall not apply to the exposures to credit institutions which arise from funds held by housing savings banks in their giro accounts with credit institutions.

Article 11

By way of derogation from Articles 150 to 152 of the Credit Institutions Act, the exposure limits shall not apply to the exposures to central governments, central banks, international organisations, multilateral development banks and public sector entities which, unsecured, would be assigned a 0% risk weight in accordance with the provisions of Part 2.2 of Title II of the Decision on the capital adequacy of credit institutions.

Article 12

(1) By way of derogation from Articles 150 to 152 of the Credit Institutions Act, where there are neither maturity nor currency mismatches, the exposure limits shall not apply to a part of the exposure secured by guarantees provided by central governments, central banks, international organisations, multilateral development banks and public sector entities if the equivalent unsecured exposures to these guarantors are assigned a

0% risk weight in accordance with the provisions of Part 2.2 of Title II of the Decision on the capital adequacy of credit institutions.

(2) By way of derogation from paragraph (1) of this Article, where there are maturity and/or currency mismatches between exposures and collateral referred to in paragraph (1) of this Article, credit institutions may calculate the value of collateral referred to in paragraph (1) of this Article in accordance with Articles 422 and 423 of the Decision on the capital adequacy of credit institutions.

(3) For the purpose of calculating the value of collateral in accordance with paragraph (2) of this Article, credit institutions shall prescribe the exposures to which the exemptions referred to in paragraph (1) of this Article shall apply and apply them consistently.

(4) For the purpose of paragraph (1) of this Article, the term 'guarantee' shall include credit derivatives recognised under Part 4 of Title II of the Decision on the capital adequacy of credit institutions other than credit linked notes.

Article 13

(1) By way of derogation from Articles 150 to 152 of the Credit Institutions Act, where there are neither maturity nor currency mismatches between exposures and collateral, the exposure limits shall not apply to a part of the exposure secured by the following collateral:

- 1) the exposures secured by securities issued by central governments, central banks, international organisations, multilateral development banks and public sector entities if the equivalent unsecured exposures to these issuers of securities are assigned a 0% risk weight in accordance with the provisions of Part 2.2 of Title II of the Decision on the capital adequacy of credit institutions; and
- 2) the exposures secured by cash on deposit held by the credit institution which calculates the exposure.

(2) For the purpose of paragraph (1), item (2) of this Article, the term 'cash on deposit' shall also include:

- 1) cash received under credit linked notes issued by credit institutions; and
- 2) loans and deposits received from other counterparties that are subject to on-balance sheet netting in accordance with the provisions of Part 4 of Title II of the Decision on the capital adequacy of credit institutions.

Article 14

Collateral for exposures referred to in Article 12 and Article 13 of this Decision shall meet the minimum requirements for the recognition set out in Part 4 of Title II of the Decision on the capital adequacy of credit institutions.

Article 15

By way of derogation from Article 13, paragraph (1) of this Decision, where there are currency mismatches between exposures and collateral, credit institutions may apply the exemptions referred to in Article 13, paragraph (1) of this Decision provided that the value of collateral referred to in Article 13, paragraph (1) of this Decision for the exposure or a part of the exposure to which the exemption is applied amounts to at least 120%.

Article 16

(1) Exceptionally, where credit institutions apply the methods referred to in this Article, they may apply the exemptions referred to in Article 13, paragraph (1) of this Decision even if there are maturity or currency mismatches between exposures and collateral.

(2) Where credit institutions use the Financial Collateral Comprehensive Method referred to in Part 4.2.1 of the Decision on the capital adequacy of credit institutions for the calculation of risk-weighted exposure amounts for credit risk, they may use the same method to calculate the value of collateral referred to in Article 13, paragraph (1) of this Decision. In this case, the value of collateral referred to in Article 13, paragraph (1) of this Decision shall be equal the C_{VAM} calculated in accordance with Article 380 of the Decision on the capital adequacy of credit institutions.

(3) Where credit institutions use the AIRB Approach referred to in Part 3 of Title II of the Decision on the capital adequacy of credit institutions for the calculation of risk-weighted exposure amounts for credit risk, they may use their own estimates of the effects of financial collateral on exposures to calculate the value of collateral referred to in Article 13, paragraph (1) of this Decision if the following conditions are met:

- 1) credit institutions are able to estimate adequately the effects of financial collateral on their exposures and separately from other LGD-relevant aspects; and
- 2) the methodology used for estimating the effects of financial collateral on exposures must be in concordance with the methodology used for estimating the LGD for the purpose of calculating risk-weighted exposure amounts for credit risk and comply with the minimum requirements for estimation of risk parameters referred to in Part 3 of Title II of the Decision on the capital adequacy of credit institutions.

(4) By way of derogation from paragraph (3) of this Article, where credit institutions use the AIRB Approach referred to in Part 3 of Title II of the Decision on the capital adequacy of credit institutions for the calculation of risk-weighted exposure amounts for credit risk and do not use their own estimates of the effects of financial collateral on exposures referred to in paragraph (3) of this Article, they may use the Financial Collateral Comprehensive Method referred to in paragraph (2) of this Article.

Article 17

Credit institutions shall prescribe in their internal bylaws the types of exposure to which the exemptions referred to in Article 13 and Article 15 and the methods referred to in Article 16 shall apply and apply them consistently.

Article 18

(1) Where credit institutions use the methods referred to in Article 16 of this Decision to calculate the value of collateral referred to in Article 13 of this Decision, they shall conduct periodic stress tests of their credit-risk concentrations, including in relation to the realisable value of any collateral taken.

(2) These periodic stress tests shall address risks arising from potential changes in market conditions that could adversely impact the credit institutions' adequacy of own funds and risks arising from the realisation of collateral in stressed situations.

(3) Credit institutions shall satisfy that the stress tests carried out are adequate and appropriate for the assessment of risks referred to in paragraphs (1) and (2) of this Article.

(4) In the event that a stress test indicates a lower realisable value of collateral taken than would be permitted to be taken into account under the methods referred to in Article 16 of this Decision, credit institutions shall adjust the value of collateral referred to in Article 13 of this Decision.

Article 19

Where credit institutions use the methods referred to in Article 16 of this Decision to calculate the value of collateral referred to in Article 13 of this Decision, they shall, at a minimum, adopt the following internal bylaws to address concentration risk:

- 1) policies and procedures to address risks arising from maturity mismatches between exposures and any credit protection on those exposures;
- 2) policies and procedures in the event that a stress test indicates a lower realisable value of collateral than taken into account under the methods referred to in Article 16 of this Decision; and
- 3) policies and procedures relating to concentration risk arising from the application of credit risk mitigation techniques, and in particular large indirect credit exposures, for example to a single issuer of securities taken as collateral.

7 NON-COMPLIANCE WITH LARGE EXPOSURE LIMITS

Article 20

If credit institutions at any time fail to comply with the limits referred to in Articles 150 to 152 of the Credit Institutions Act, they shall be required to act in the manner referred to in Article 155 of the Credit Institutions Act.

8 REPORTING ON LARGE EXPOSURES

Article 21

(1) Credit institutions shall report to the Croatian National Bank on all large exposure referred to in Article 2 of this Decision and collateral issuers and providers of unfunded credit protection referred to in Article 4 of this Decision.

(2) Credit institutions shall report on collateral issuers and providers of unfunded credit protection if the value of exposures covered by their collateral and unfunded credit protection exceeds 10% of their own funds.

(3) The group of connected persons referred to in Article 24 of the Credit Institutions Act shall also be deemed to be a single collateral issuer or provider of unfunded credit protection referred to in paragraph (2) of this Article.

Article 22

(1) When reporting on large exposures, credit institutions shall disclose separately the following items for the non-trading book and the trading book:

- 1) the name of each person or group of connected persons to which credit institutions have a large exposure;
- 2) the value of large exposure before and after taking into account the effect of exemptions referred to in Articles 10 to 15 of this Decision or the application of the methods referred to in Article 16 of this Decision;
- 3) the name of persons in a special relationship with credit institutions and persons connected with such persons referred to in Article 153 of Credit Institutions Act to which credit institutions have an exposure;
- 4) the value of exposures to persons in a special relationship with credit institutions and persons connected with such persons before and after taking into account the effect of exemptions referred to in Articles 10 to 15 of this Decision or the application of the methods referred to in Article 16 of this Decision; and
- 5) the type of exemption referred to in Articles 10 to 15 of this Decision.

(2) By way of derogation from paragraph (1), items (2) and (5) of this Article, for repurchase transactions and securities lending or borrowing transactions referred to in Article 6, paragraph (1), item (3) and paragraph (4) of this Decision, credit institutions

may disclose only the value of exposures calculated in the manner prescribed in that Article.

(3) When reporting on collateral issuers and providers of unfunded credit protection, credit institutions shall disclose the following items:

- 1) the name of collateral issuers or providers of unfunded credit protection;
- 2) the value of exposures covered by collateral or unfunded credit protection;
- 3) the type of collateral or unfunded credit protection; and
- 4) the market value of collateral or unfunded credit protection.

(4) For the purpose of paragraph (3), item (2) of this Article, where there are maturity and currency mismatches between exposures and collateral and where only a part of the exposure is collateralised, credit institutions shall calculate the exposure value or a part of the exposure value covered by collateral or unfunded credit protection in accordance with the provisions referred to in Part 4 of Title II of the Decision on the capital adequacy of credit institutions.

Article 23

(1) In accordance with Article 22 of this Decision, credit institutions shall report to the Croatian National Bank within the time limits and in the manner and form prescribed in the Decision on supervisory reports of credit institutions.

(2) Credit institutions shall report to the Croatian National Bank on each excess of the limits laid down in Articles 150 to 152 of the Credit Institutions Act and arising from trading book positions within the time limits and in the manner prescribed in the Decision on supervisory reports of credit institutions. In such cases, credit institutions shall in particular disclose the following items:

- 1) the amount of excess;
- 2) the date of exceeding the large exposure limits; and
- 3) the duration of excess where it arises from trading book positions.

(3) Credit institutions shall without delay report to the Croatian National Bank on all failures of internal control systems referred to in Article 3, paragraph (3) of this Decision.

Article 24

(1) Credit institutions referred to in Article 1, paragraph (4) of this Decision shall report to the Croatian National Bank on all large exposures, collateral issuers and providers of unfunded credit protection on a semi-annual and consolidated basis and within the time limits and in the manner and form prescribed in the Decision on supervisory reports of credit institutions.

(2) Where credit institutions use the IRB Approach to calculate the capital requirements for credit risk, they shall report their 20 largest exposures to a single person or group of connected persons on a consolidated basis referred to in paragraph (1) of this Article.

(3) Credit institutions shall include in their reports referred to in paragraph (2) of this Article the 20 largest exposures after taking into account the effect of exemptions referred to in Articles 10 to 15 of this Decision or the application of the methods referred to in Article 16 of this Decision.

9 TRANSITIONAL AND FINAL PROVISIONS

Article 25

This Decision shall be published in the Official Gazette and shall enter into force on 1 July 2009.

No.: 4-020/01-09/ŽR
Zagreb, 2 January 2009

Croatian National Bank
Council Chairman
Governor
Željko Rohatinski, m.p.