

GOVERNOR

Reg. No: 994-091/091/21-1

Zagreb, 10 December 2021

**TO ALL LESS SIGNIFICANT
SUPERVISED ENTITIES**

Attention of: Management Board

Subject: Application of the Guidelines specifying the criteria to assess the exceptional cases when institutions exceed the large exposure limits and the time and measures to return to compliance (EBA/GL/2021/09)

Dear Sir/Madam,

We would hereby like to remind you that the European Banking Authority (hereinafter: the EBA) on 16 September 2021 published on its website the **Guidelines specifying the criteria to assess the exceptional cases when institutions exceed the large exposure limits and the time and measures to return to compliance (EBA/GL/2021/09)**; hereinafter: the Guidelines).

In accordance with Article 4, paragraph (1), item (3) of the Credit Institutions Act (Official Gazette 159/2013, 19/2015, 102/2015, 15/2018, 70/2019, 47/2020 and 146/2020; hereinafter: the Act), the Croatian National Bank (hereinafter: the CNB) shall make every effort to comply with those guidelines and recommendations issued by the EBA in accordance with Article 16 of Regulation (EU) No 1093/2010 (OJ L 225, 24.11.2010). In this regard, credit institutions are expected to apply the Guidelines as good practice while respecting the expectations contained in this Circular.

The purpose of the Guidelines is to ensure, based on current supervisory practices, a prudential and harmonised approach by providing guidelines to competent authorities specifying the criteria to assess the exceptional cases referred to in Article 396, paragraph (1) of Regulation (EU) No 575/2013 when a competent authority allows an institution to exceed the large exposure limits. According to the provisions of Article 395, paragraph (3) of Regulation (EU) No 575/2013, institutions shall at all times comply with large exposure limits. According to the provisions of Article 396, paragraph (1) of Regulation (EU) No 575/2013, if, in an exceptional case, exposures exceed the large exposure limits, a credit institution shall without delay report to the CNB as the competent authority, which may, where the circumstances warrant it, allow the credit institution a limited period of time in which to comply with the limit. Please note that the promptness of notifying about the breach is one of the criteria (paragraph 31(b) of the Guidelines) that may influence the competent authority's decision on the appropriate time to return to compliance.

The Guidelines define in detail the criteria to determine the appropriate time to return to compliance with the large exposure limits and the measures to be taken to ensure the timely return to compliance with these limits. The measures contain the key provisions regarding the compliance plan which is, under the provisions of Article 396, paragraph (1) of Regulation (EU) No 575/2013, mandatory for a period longer than three months. To ensure harmonised application, the Guidelines also introduce a minimum set of information to be provided to the competent authority in the case of breach of the large exposure limits. The key section of the Guidelines that defines all these provisions is Section 4.

The Guidelines apply from 1 January 2022 to all credit institutions, with the exception of gone-concern situations in which an institution is in the process of restructuring or undergoes a similar crisis-induced scenario, i.e. under resolution or undergoing winding-up proceedings. The Guidelines do not apply to the cases set out in Article 395, paragraph (5) of Regulation (EU) No 575/2013 as long as the institution fulfils the conditions laid down therein.

Special attention should be paid to the obligation of the credit institution to report to the CNB, as the competent authority, in case of a breach of the large exposure limits immediately after becoming aware of it and without delay. Given their nature, breaches of the large exposure limits are in the Guidelines treated as processes that require a case-by-case assessment, which is why we believe that the promptness and content of such reports are key for any further actions. In this regard, the CNB expects that the reports contain the minimum information specified in the Guidelines. In addition to the elements listed in paragraph 25 of the Guidelines, they should include all information and data that would specify the breach in detail and define its nature, complexity and impact on the credit institution, and thereby enable the CNB as the competent authority to make a timely and adequate decision on the appropriate time and proposed measures to return to compliance. For this reason, the CNB expects credit institutions to pay due attention to the content of such reports, i.e. the quality of information submitted to the CNB in order to optimise the time and steps to be taken to return to compliance with the large exposure limits. The CNB expects that the elements such as the description of available collateral referred to in paragraph 25(d) of the Guidelines contain all details that best describe the collateral in question, for example: the type of collateral, its market value, evaluation method, location, etc. When the institution assesses and specifies in the report presented to the CNB as the competent authority, in accordance with paragraph 25(g) of the Guidelines, that a period longer than three months is needed to return to compliance with the large exposure limits, it shall present a compliance plan together with the report.

The minimum content of a compliance plan is given in paragraph 41 of the Guidelines, with a description of all foreseeable risks or obstacles to the effective and timely execution of the compliance plan. Credit institutions are expected to pay due regard to the quality and content of the compliance plan. We draw attention to the provisions of Article 224, paragraph (1), item (21) of the Act giving the CNB the power to order a credit institution to present a plan to restore compliance with prudential requirements pursuant to the Act and Regulation (EU) No 575/2013 and set a deadline for its implementation, including improvements to that plan regarding scope and deadline. We believe that these provisions of the Act adequately address plans to restore compliance with the large exposure limits and expectations arising from the Guidelines in terms of assessing acceptability of the compliance plan, monitoring the accomplishment of the different milestones and the impact on timeframe corrections for its implementation.

Exceptionally, where objective circumstances prevent the credit institution to promptly prepare a compliance plan and present it to the CNB together with the report of a breach of the large exposure limits, the credit institution shall agree with the CNB on the timeframe to present the compliance plan.

The Guidelines specify the following three criteria as a minimum to determine the exceptional cases referred to in Article 396, paragraph (1) of Regulation (EU) No 575/2013: a rare event, inability to predict the breach and the institution's inability to prevent the breach. A quantitative element which may not qualify a breach of the large exposure limits as a rare event is a situation when an institution reports two breaches during the last 12 months that stem from the same origin or that concern the same client or group of connected clients. We also mention the reasons that may be considered to be beyond the control of the credit institution, which are listed in paragraph 22 of the Guidelines, including the unexpected and substantial decrease of the own funds of the credit institution. We are of the opinion that this does not include the situations when the own funds of the credit institution are reduced in the course of regular annual financial statements audit. Other listed reasons include unexpected regulatory, court or

administrative decisions and the merger of clients, but only in cases when the credit institution did not have timely knowledge of the merger. It should be particularly noted that a breach caused by an inappropriate application or misinterpretation of the large exposures framework should not qualify as a reason beyond the control of the credit institution.

The Guidelines in the English language are available on the EBA's website at the following link:

https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Guidelines/2021/EBA-GL-2021-09%20GL%20on%20large%20exposure%20breaches/1019615/Final%20Report%20on%20Guidelines%20on%20large%20exposures%20breaches%20and%20time%20and%20measures%20to%20return%20to%20compliance.pdf

The Guidelines in the Croatian language are available on the EBA's website at the following link:

https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Guidelines/2021/EBA-GL-2021-09%20GL%20on%20large%20exposure%20breaches/Translations/1023291/GLs%20on%20LE%20Breaches%20and%20Time%20Measures%20to%20Return%20to%20Compliance_HR_COR.pdf

Kind regards,

Boris Vujčić

Governor