



**NATIONAL BANK OF THE REPUBLIC OF NORTH MACEDONIA**

Pursuant to Article 47 paragraph 1 item 6 of the Law on the National Bank of the Republic of North Macedonia (Official Gazette of the Republic of Macedonia No. 158/10, 123/12, 43/14, 153/15, 6/16 and 83/18 and Official Gazette of the Republic of North Macedonia No. 110/21), Article 68 paragraph 1 item 2 and Article 69 paragraph 2 of the Banking Law (Official Gazette of the Republic of Macedonia No. 67/07, 90/09, 67/10, 26/13, 15/15, 153/15, 190/16, 7/19 and Official Gazette of the Republic of North Macedonia No. 101/19 and 122/21), and items 2 and 3 of the Decision on determining the order in which the Vice Governors replace the Governor while absent or prevented to perform their work obligations in 2023 No. 04- 43353/1 of 30 December 2022, the Council of the National Bank of the Republic of North Macedonia has adopted the following

**DECISION**  
**on the methodology for credit risk management**  
**(Official Gazette of the Republic of North Macedonia No. 57/23)**

**I. GENERAL PROVISIONS**

1. This Decision lays down the methodology for credit risk management and determining criteria for classification of on-balance and off-balance sheet items by risk degree and the method of determining impairment and special reserve, i.e. expected credit loss for credit exposures.

The methodology for credit risk management from paragraph 1 of this item shall include supervisory standards related to the loan approval method and the procedure for regulating overdue claims, the method of determining forborne and non-performing exposure to credit risk and the method of writing off claims and sale of overdue, non-performing and written-off claims from a credit agreement.

2. The terms used in this decision shall denote the following:

2.1 Credit risk shall denote risk of loss to the bank because of the client's inability to repay his/her liabilities in the agreed amount and/or within the contractual terms.

2.2 Exposure to credit risk or credit exposure shall include:

- on-balance sheet items which, in accordance with the National Bank of the Republic of North Macedonia regulation on the methodology for recording and valuation of the accounting items and for preparation of the financial statements, have the status of financial assets at amortized cost and financial assets at fair value through other comprehensive income, such as loans, deposits, investments in debt instruments, claims based on leasing contracts, purchased claims (factoring and forfeiting), payments made on the basis of guarantees, letters of credit, backing guarantees and other off-balance sheet items, interests, fees and charges, claims based on trade and other contracts with clients and other financial assets that expose the bank to credit risk;

- off-balance sheet items based on assumed liabilities for granting loans (undisbursed irrevocable lines of credit, undisbursed overdrafts and credit cards); unfulfilled assumed irrevocable liabilities for purchase of claims; issued uncovered guarantees; opened uncovered letters of credit; provided backing guarantees; provided acceptances and other off-balance sheet items that represent a potential liability for the bank with the exception of off-balance sheet lending obligations which, in accordance with the National Bank of the Republic of North Macedonia regulation on the methodology for determining capital adequacy, have a status of low-risk off-balance sheet claims.

The following items shall not be a part of the credit exposure:

- cash, gold and other precious metals, funds on the bank's account with the National Bank of the Republic of North Macedonia, investments in subsidiaries, associated companies and joint ventures, intangible assets, land, property and equipment, natural resources, foreclosed assets, means of operations and supplies;
- financial assets that expose the bank to market and/or other risks, other than credit risk: investments in equity instruments, investments in debt instruments measured at fair value through the income statement, and loans and claims measured at fair value through the income statement.

2.3 Client shall denote an entity subject to credit exposure.

2.4 Maturity date shall denote the day on which the client is required to pay a certain amount of money, according to the contract signed with the bank.

2.5 Overdue claims shall imply the amount of the bank's claims based on principal, interest and other claims payable by the client on the due date, as well as bank's claims for payments based on a guarantee, letter of credit or other off-balance sheet item referred to in sub-item 2.2 indent 2 of this item.

2.6 Increase in credit risk shall denote deterioration in credit quality (higher credit risk), as determined under the National Bank of the Republic of North Macedonia regulation on the methodology for recording and valuation of accounting items and for preparation of financial statements.

2.7 Credit exposure based on financing projects or project financing shall denote a credit exposure that the bank expects to collect from the cash flows generated from the project and that can be collateralized by the financed project (e.g. power stations, transport and telecommunication infrastructure, mines, apartment and/or office buildings, warehouses, hotels, railroads, etc.).

2.8 Joint credit obligations shall denote total exposure to two or more clients (co-borrowers) who are equally responsible for meeting the obligations arising from the joint credit exposure approved by the bank.

2.9 Eligible collateral instruments shall include collateral instruments from item 25 of this decision that are included in the calculation of the present value of the expected cash flows from credit exposures for the purposes of calculating impairment.

2.10 First-class collateral instrument shall include collateral instruments under item 26 of this decision.

2.11 Loan portfolio shall denote credit exposures that can be classified by similarity of their characteristics and the credit risk in consistence with item 28 of this Decision.

2.12 Expected credit loss shall denote expected credit loss on an individual basis from sub-item 2.13 of this item or expected credit loss on a group basis from sub-item 2.14 of this item.

2.13 Expected credit loss on an individual basis shall denote the difference between the carrying amount of the credit exposure and the present value of expected cash flows from that credit exposure.

2.14 Expected credit loss on a group basis shall denote a product of the rate of probability of default, the rate of loss given default and the credit exposure that is part of the loan portfolio.

2.15 Rate of probability of default shall denote the rate of 12 month probability of default or the rate of lifetime probability of default.

2.16 Rate of 12 month probability of default shall denote the probability that the credit exposure from the loan portfolio will become non-performing for a period of twelve months from the date of the determination of the rate.

2.17 Rate of life time probability of default shall denote the probability that the credit exposure from the loan portfolio will become non-performing during its life time, i.e. until the date of its maturity.

2.18 Rate of loss given default shall denote part of the non-performing or written-off credit exposures, which shall not be collected by the bank.

2.19 Credit exposure forbearance or forbearance shall imply modifying of contractual terms of an existing credit exposure or approving a new credit exposure for settling an existing credit exposure to a client who has financial difficulties in meeting his obligations, whereby there would not be any change or approval of a new credit exposure if the client can or could comply with the contractual terms of the existing credit exposure (hereinafter: existing contractual terms).

2.20 Forborne credit exposure shall imply a credit exposure subject to forbearance.

2.21 Restructuring of the credit exposure with a significant modification in the contractual terms (distressed restructuring) shall denote a change in contractual terms of an existing credit exposure to a client who is or is about to suffer serious financial difficulties which significantly reduce his financial obligation to the bank (diminished financial obligation), taking into account the provisions of item 56 of this decision.

2.22 Probation period shall denote a period of two years from the date of forbearance or the date when the credit exposure became eligible to be excluded from the category of forborne non-performing credit exposure in line with item 60 of this decision.

2.23 Defaulted credit exposure shall denote bank's credit exposure to a client who meets any of the following conditions:

- the amount of due claims to the client on any basis (principal, interest, other non-interest-bearing claims) has not been collected for more than 90 consecutive days from the date when the due amount exceeded the materiality threshold from sub-item 2.24 of this item (hereinafter: exceeding the materiality threshold);
- it has been determined that the client will not be able to settle their obligations to the bank in full, without recourse by the bank to actions such as realizing collateral (hereinafter: unlikeness to pay).

By way of derogation from paragraph 1 indent 1 of this sub-item, for exposures to natural persons, the bank may determine defaulted credit exposure at the level of individual credit exposure, if provided for in its internal acts, taking into account the provisions of item 48 and item 62 sub-item 62.2 of this decision.

2.24 Materiality threshold shall denote fulfillment of the absolute and relative components of sub-items 2.25 and 2.26 of this item. The materiality threshold shall be considered exceeded if both materiality threshold components are exceeded.

2.25 Absolute component shall denote the total amount of all due claims. The absolute component shall equal to:

- Denar 6,000 or an equivalent amount in another currency, for clients - natural persons,
- Denars 30,000 or an equivalent amount in another currency, for clients - legal entities (including small companies).

2.26 Relative component shall imply percentage ratio between the total amount of all due claims and the gross amount of all bank's balance sheet exposures to a client, i.e. without impairment and accumulated depreciation. The relative component shall equal 1%.

2.27 Non-performing credit exposure shall denote:

- defaulted credit exposure from sub-item 2.23 of this item;
- exposure impartially proven to be impaired under the the National Bank of the Republic of North Macedonia regulation on the methodology for recording and valuation of accounting items and for preparation of financial statements;
- credit exposure classified in D and E risk categories;
- credit exposure eligible under item 58 of this decision;
- off-balance sheet item from sub-item 2.2 paragraph 1 indent 2 of this item with likelihood to be called or used, where the on-balance exposure that will arise with its calling or utilization will become eligible to become non-performing credit exposure, in accordance with this sub-item.

2.28 Non-performing loan rate shall denote the ratio of total bank non-performing loans (principal) to total gross loans (principal) i.e. without taking into account impairment/special reserve and accumulated depreciation.

2.29 Non-performing credit exposure rate shall denote the ratio of total bank non-performing credit exposure to total gross credit exposure i.e. without taking into account impairment/special reserve and accumulated depreciation.

2.30 Sale of credit exposure with a significant loss shall denote a sale of a credit exposure that incurred a significant loss, determined in accordance with item 55 of this decision.

2.31 Net exporter shall denote a resident whose foreign currency inflow from exports in the previous twelve months has exceeded its foreign currency outflow for imports.

2.32 DSTI (debt service-to-income) ratio shall imply borrower's total monthly liabilities based on credit exposures of all banks and savings houses to such borrower and borrower's total monthly liabilities to other financial institutions -to- borrower's total monthly income.

2.33 TDTI (total debt-to-income) ratio shall imply borrower's total liabilities based on credit exposures of all banks and savings houses to such borrower and total borrower's liabilities to other financial institutions -to- borrower's total annual income.

2.34 LTV (loan-to-value) ratio shall imply credit exposure to natural person -to- value of real estate pledged as collateral for such credit exposure.

2.35 Green finance shall denote credit exposure intended to improve energy efficiency of households and corporations, to support investment in green technologies, materials etc., to support investment in renewable energy sources, and to control and prevent pollution, protect environment, mitigate climate risks, etc.

3. Issues not defined in this Decision shall have the meaning of the terminology defined in the Banking Law and the bylaws adopted on the basis of this law.

4. The bank shall classify credit exposures by applying the provisions of section II of this Decision and determine impairment and special reserve, i.e. expected loan loss for credit exposures by applying the provisions of section III of this Decision.

The National Bank of the Republic of North Macedonia (hereinafter referred to as: the National Bank) shall check the client's classification made by the bank, as well as the model for determining expected loan loss on a collective basis and may require from the bank to change the risk category and/or the model for determining the expected loan loss on a collective basis, i.e. the amount of the expected loan loss.

Upon receiving the respective document from the National Bank (letter, decision, report or other document), the bank shall forthwith implement the amendments of paragraph 2 of this item.

## **II. CLASSIFICATION OF CREDIT EXPOSURE**

### **General requirements**

5. The bank shall classify the credit exposure based on an individual agreement in risk categories referred to in item 9 of this Decision, at least once a month as of the end of the month.

6. During classification of credit exposure upon its approval, the bank shall take into account:

- the client's creditworthiness, i.e. the project quality, in accordance with item 7 of this Decision and

- the regularity of repayment of liabilities, in accordance with item 8 of this Decision.

In each further classification of credit exposure, the bank shall take into account:

- the changes in client's creditworthiness, i.e. in project quality, in accordance with item 7 of this Decision and
- the regularity of repayment of liabilities, in accordance with item 8 of this Decision.

7. Client's creditworthiness, i.e. the change in his/her creditworthiness shall be assessed by applying at least the following criteria:

- client's status and economic characteristics and the quality and expertise of the management and supervisory bodies;
- whether the use of funds matches the agreed purpose of credit exposure;
- whether the use of funds from the credit exposure will cause cash flow to the client, in a scope and pace that matches the agreed method of repayment of liabilities;
- amount of capital, reserves and client's property condition, the realized cash flows of the client, as well as the ability to realize future cash flows;
- client's perspective and his/her activity;
- client's liquidity and profitable position;
- possible effects on client's creditworthiness by persons/entities connected to the client;
- macroeconomic or other indicators that may affect credit risk level (e.g. unemployment rate, property prices, price of client's product or service, etc.);
- political and economic situation of the client's domicile country;
- client's indebtedness level;
- method of repayment of loan liabilities and other forms of credit exposure to the bank, to other banks, liabilities to other legal entities and natural persons, etc., determined on the basis of internal and/or external data sources (e.g. Credit Registry of the National Bank, credit bureaus, etc.);
- client's credit rating, if any;
- internal risk category, if the bank has established internal risk categories;
- client's exposure to currency risk, interest rate risk and other risks, in terms of the impact that these risks have or would have on the client's ability to settle liabilities as agreed in the contractual terms, in conditions of change in the exchange rate, interest rate or other changes that tend to increase client's credit exposure. The evaluation of exposure to currency risk takes into account the provisions under item 81 of this decision.

In assessing project quality, i.e. change in project quality subject of the financial support, the bank shall take into account the criteria referred to in paragraph 1 of this item applicable to the project quality assessment, including the following criteria:

- project's financial capacity determined at least on the basis of the financial framework of the project and the corresponding financial indicators;
- manner of project delivery determined at least on the basis of: project contracts, probability and guarantees for timely project delivery and project location;
- previous experience and financial capacity of the contractor in the performance of similar projects;
- client's financial capacity, project importance for the client and previous experience in similar projects;
- financial support for the project by the client;

- legal environment, determined at least on the basis of the legal framework and the time required to provide the necessary documentation and licenses.

In assessing the client - natural person creditworthiness and the change in their creditworthiness, the bank shall take into account the criteria referred to in paragraph 1 of this item that match the characteristics of the natural persons.

The client's creditworthiness, i.e. project quality shall be assessed for changes:

- at least once every six months;
- more frequently if the criteria for increased credit risk are met, as defined in the internal acts in accordance with item 78 sub-item 78.4 of this Decision;
- in the case of modification of contractual terms.

Notwithstanding paragraph 4 of this item, the change in the creditworthiness of the client - a natural person shall be assessed at least in the case of modifications of the contractual terms.

Notwithstanding paragraph 4 indent 1 of this item, the creditworthiness of the client-legal entity may be assessed for changes at least once a year, if the bank's total credit exposure to that entity does not exceed Denar 6,000,000.

8. When determining the regularity in repayment of liabilities, the bank shall take into account:

- the days of delay in settling credit exposure, for the month of classification of credit exposure (hereinafter: current days of delay) and
- the days of delay in repayment of the credit exposure at least in the previous six months.

For the purposes of this Decision, the preceding six-month period does not cover the month subject of classification of the credit exposure.

## **Risk categories**

9. The Bank shall classify in the following risk categories:

9.1 Risk category A shall include:

- claims on the European Central Bank and the central governments and central banks of countries with 0% risk weight pursuant to the National Bank's regulation on the methodology for determining the capital adequacy;
- credit exposure to a client whose financial position and cash flows allow smooth operating and opportunity to cover current and future liabilities to the bank;
- credit exposure where no increased credit risk has been identified in accordance with item 78 subitem 78.4 of this Decision;
- credit exposure whose liabilities on the classification date are performed in line with the contractual terms, i.e. the current days of delay do not exceed 31 day;
- credit exposure whose liabilities in the previous six months have been repaid under the contractual terms, with a delay that does not exceed 31 day, or 60 days as an exception, if the delay is up to two times within the range from 32 to 60 days;

- part of credit exposure that is secured by first-class collateral instruments, as defined in item 26 of this Decision, if the instrument is launched within 90 days of the maturity date of the credit exposure;
- credit exposure that is in the last year of the probation period.

Notwithstanding paragraph 1, indent 4 of this subitem, the bank may classify in risk category A any credit exposure with current days of delay that exceed 31 day, if the total amount not collected for more than 31 day is lower than Denar 1,000 and the delay is no longer than 60 days.

#### 9.2 Risk category B shall include:

- credit exposure to a client/project that has financial weaknesses, but the financial situation enables its smooth delivery;
- credit exposure with current days of delay that do not exceed 60 days;
- credit exposure whose liabilities in the previous six months have been repaid with a delay that does not exceed 60 days, or 90 days as an exception, if the delay is up to two times within the range from 61 to 90 days;
- credit exposure with a status of forborne credit exposure, but only if the credit exposure did not have the status of forborne non-performing credit exposure or at least one year has passed since the credit exposure was excluded from the category of forborne non-performing credit exposure.

#### 9.3 Risk category C shall include:

- credit exposure to a client/project whose cash flows are unsuitable for regular repayment of liabilities;
- credit exposure to a client/project with an inadequate maturity structure between the sources of funding and its proceeds;
- credit exposure to a client with high debt to equity ratio and/or a client who has a significant debt to creditors;
- credit exposure to a client/project the latest updates of which are not known to the bank to make assessment of the client's creditworthiness, i.e. the project quality;
- credit exposure with current days of delay that do not exceed 120 days;
- credit exposure whose liabilities in the previous six months have been repaid with a delay that does not exceed 120 days, or 180 days as an exception, if the delay is up to two times within the range from 121 to 180 days;
- credit exposure to a client - non-financial entity that has claims based on financial loan on entity enjoying a credit rating equal to or lower than CCC+ (according to Standard & Poor's or Fitch) or Caa1 (according to Moody's);
- credit exposure to a client - non-financial entity that has claims based on financial loan on entity enjoying a credit rating higher than that referred to in indent 7 of this subitem, but its domicile country's credit rating equals to or is lower than CCC+ (according to Standard & Poor's or Fitch) or Caa1 (according to Moody's);
- credit exposure to a client - non-financial entity that has claims based on financial loan on entity who has not been assigned credit rating, but its domicile country's credit rating equals to or is lower than B- (according to Standard & Poor's or Fitch) or B3 (according to Moody's) or its domicile country's has not been assigned a credit rating.

Notwithstanding paragraph 1 of this subitem, the bank may not classify credit exposure to the client under paragraph 1, indents 7, 8 and 9 of this subitem in risk category C, if:

- the credit exposure is based on a customs guarantee or bid guarantee;



- the financial loan does not exceed Denar 31,000,000 (in the case of foreign currency financial loan, the Denar equivalent of the loan shall be taken into consideration);
- the financial loan is equal to or greater than Denar 31,000,000, and the bank's credit exposure is greater than the amount of financial loan and the bank has determined expected credit loss, at least in the amount exceeding 20% of the amount of financial loan, whereby the credit exposure or the client meets the criteria for classification in another risk category.

9.4 Risk category D shall include:

- credit exposure to a client that is illiquid;
- forbore non-performing credit exposure for which the client is past-due for more than 90 days or for which new forbearance has been approved;
- credit exposure with current days of delay that do not exceed 240 days;
- credit exposure whose liabilities in the previous six months have been repaid with a delay that does not exceed 240 days, or 300 days as an exception, if the delay is up to two times within the range from 241 to 300 days;
- credit exposure to a client (including governments and central banks) enjoying a credit rating equal to or lower than CCC+ (according to Standard & Poor's or Fitch) or Caa1 (according to Moody's);
- credit exposure to a client enjoying a credit rating higher than the rating referred to in indent 5 of this subitem, but its domicile country's credit rating is equal to or lower than CCC+ (according to Standard & Poor's or Fitch) or Caa1 (according to Moody's);
- credit exposure to a client that has not been given any credit rating, but its domicile country's credit rating is equal to or lower than B- (according to Standard & Poor's or Fitch) or B3 (according to Moody's) or its domicile country has not been given any credit rating yet.

Notwithstanding paragraph 1 of this sub-item, the bank may not classify the credit exposure of paragraph 1, indents 5, 6 and 7 of this sub-item in risk category D, in the case of off-balance sheet credit exposure based on customs guarantee or bid guarantee, or in the case of credit exposure to another bank, on the basis of FX accounts abroad.

9.5 Risk category E shall include:

- credit exposure whose liabilities are performed with a delay, that is not eligible for classification in risk category D, in accordance with sub-item 9.4 of this item;
- credit exposure to a client under a bankruptcy proceeding, except when there is a reorganization plan adopted for the client in accordance with law;
- credit exposure to a client that denies existence of any credit exposure (in litigation or arbitration).

10. The criteria for classification in risk categories defined in the item 9 of this decision shall be the minimum requirements that the bank is required to apply when classifying each credit exposure in a risk category.

In the policy or other internal acts from item 78 sub-item 78.6 of this decision, the bank may also specify other criteria for classification of credit exposures in the respective risk categories, the application of which cannot make a credit exposure to be reclassified in a better risk category than the one in which it would be classified, in accordance with the criteria defined in item 9 of this decision.

11. Non-performing loan exposure may not be classified in risk categories A or B.
12. Credit exposure eligible to be classified in two or more risk categories shall be classified in the worst risk category, as determined in this section.

### **III. CALCULATING IMPAIRMENT AND SPECIAL RESERVE**

#### **General requirements**

13. The bank shall determine impairment and special reserve for the credit exposures on the basis of determined expected credit loss on individual and/or cumulative basis, at least once a month.

The bank shall determine expected credit loss on an individual basis at least for:

- non-performing credit exposures;
- forborne credit exposures;
- credit exposures based on financing projects;
- credit exposures which may not be assigned in the loan portfolio or for which the bank does not hold data to determine the rates of probability of default and the rate of loss given default, as a basis for determining the expected credit loss on a group basis;
- significant credit exposures.

For the purposes of paragraph 2 indent 5 of this item, the bank shall determine expected credit loss on an individual basis for credit exposures which are determined as significant credit exposures at the time of their approval.

Notwithstanding paragraph 2 indent 1 of this item, the bank may determine expected credit loss on a collective basis for insignificant amounts of non-performing credit exposures.

14. The amount of impairment, or the amount of allocated special reserve for each risk category ranges within the following limits:

- from 0.01% to 5% for A risk category;
- over 5% to 20% for B risk category;
- over 20% to 45% for C risk category;
- over 45% to 70% for D risk category;
- over 70% to 100% for E risk category.

The amount of impairment, or the amount of allocated special reserve for credit exposure may not be lower than the lower limit provided for in paragraph 1 of this item for each risk category.

15. Notwithstanding item 14 paragraph 1 of this Decision, the bank may not calculate impairment, i.e. may not allocate special reserve for credit exposures in item 9 sub-item 9.1 indents 1 and 6 of this Decision.

16. For non-performing credit exposures classified in C risk category, the bank shall determine impairment, i.e. shall allocate special reserve of at least 30% of the amount of credit exposure.

17. The bank shall make impairment or allocate special reserve in the amount of 100% for credit exposure that meets at least one of the following criteria:

- there are strong expectations that the bank will not be able to collect any part of the credit exposure;
- liabilities based on credit exposure are repaid with a delay of more than 365 days and the bank has no eligible collateral instrument.
- liabilities based on credit exposure are repaid with a delay of more than two years and the bank has eligible collateral instrument.

18. The bank shall perform full impairment for the accrued interest on the date the interest-based claims were given a treatment of non-performing credit exposure.

### **Determining expected credit loss on an individual basis**

19. The bank shall determine the expected credit loss on an individual basis for each credit exposure by determining the present value of expected cash flows that will stem from that credit exposure.

When determining the expected cash flows, the bank shall include data on the expected changes in the creditworthiness of the client, i.e. the quality of the project, whereby the bank may also include the impact of macroeconomic or other indicators.

If the bank identifies a higher amount of impairment, i.e. a higher amount of special reserve than the amount prescribed in item 14 paragraph 1 of this Decision for the risk category the credit exposure is classified in, it shall reclassify the credit exposure in an appropriate risk category that fits the specified amount of impairment, i.e. the amount of special reserve.

20. The present value of on-balance sheet items, when determining the expected credit loss on an individual basis, shall be obtained by discounting the expected cash flows based on those claims using the effective interest rate as set by the National Bank's regulation on the methodology for recording and valuation of accounting items and for preparation of financial statements.

Notwithstanding paragraph 1 of this item, after the classification of credit exposure that consists of interest only and/or only of fees and commissions, the bank shall not be required to calculate the present value of expected cash flows, and the amount of impairment shall be determined in accordance with item 14 of this Decision.

21. The present value of off-balance sheet items, when determining the expected credit loss on an individual basis, shall be obtained by discounting the expected cash flows as a result of bank's payments on the assumed contingent liabilities and collections from the client, with the current market yield of low-risk securities issued in the same currency and with the same maturity as the currency and the maturity of the expected collection.

The present value of off-balance sheet items referred to in paragraph 1 of this item, shall be determined only in case of expected cash flows on the basis of assumed contingent liabilities.

Provided that there is no current market yield of low-risk securities with the same maturity as the maturity of the expected collection, the present value of the expected cash flows on the assumed contingent liability of the bank shall be determined on the basis of the

current market yield of low-risk securities with the closest maturity to the maturity of the expected collection.

22. Notwithstanding item 21 of this Decision, if the credit exposure based on one contract includes on-balance sheet and off-balance sheet items (e.g. used and unused overdrafts and loans based on credit cards, used and unused portion of irrevocable lines of credit, fee for off-balance sheet item and the off-balance sheet position itself, etc.), the bank shall apply the same percentage of impairment and special reserve for all items of the credit exposure.

23. Relating the non-performing credit exposures that the bank expects to foreclose, when determining the present value of the expected cash flows of those credit exposures, the bank may take into account the value of the eligible collateral instrument, in accordance with item 24 of this Decision.

24. Collateral which meets the requirements of item 25 of this Decision shall be included in the calculation of the present value of expected cash flows for non-performing credit exposures, in the amount that is equal to the lesser of the value of collateral determined in conformity with paragraph 4 of this item and the total credit exposure covered by collateral, while the discounting covers the period up to the date of expected recovery of credit exposure with collateral.

The bank may take into account the collateral under paragraph 1 of this item when determining the impairment only in instances when it has adequate documentation confirming that there is a market for the collateral where it will be able to quickly and efficiently sell the collateral at an appropriate price that will enable recovery of credit exposure.

The amount referred to in paragraph 1 of this item shall also include the expected costs of recovery through collateral that will be born by the bank.

The value of the collateral shall not be higher than:

- 100% of the fair value of the first-class collateral instrument and policies of item 25 sub-item 25.3 and 25.4 of this Decision;
- 100% of the value of the pledged claims on the central government of the Republic of North Macedonia;
- 80% of the estimated market value of the residential property of item 27 paragraph 1 indent 1 of this Decision;
- 70% of the estimated market value of commercial facilities and commercial premises of item 27 paragraph 1 indent 2 of this Decision;
- 60% of the estimated market value of precious metal and works of art of item 27 paragraph 1 indent 10 of this Decision, if stored in the bank depot, or 40% if not stored in the bank depot;
- 60% of the estimated market value of the product the price of which depends on the fluctuations in the price of that product on international markets of item 27 paragraph 1 indent 7 of this Decision;
- 50% of the estimated market value of the of unbuilt residential and commercial facilities of item 27 paragraph 1 indent 8 of this Decision;
- 50% of the estimated market value of the industrial facilities of item 27 paragraph 1 indent 3 of this Decision;

- 50% of the estimated market value of touristic facilities of item 27 paragraph 1 indent 5 of this Decision;
- 50% of the estimated market value of the agricultural land of item 27 paragraph 1 indent 6 of this Decision;
- 40% of the estimated market value of the agricultural facilities of item 27 paragraph 1 indent 4 of this Decision, and
- 40% of the estimated market value of construction, manufacturing, agricultural and other type of equipment of item 27 paragraph 1 indent 9 of this Decision.

For the needs of paragraph 4 indents from 3 to 12 of this item, the assessment of the market value of the collateral determined in accordance with item 27 of this Decision shall be taken into consideration.

The period to the date of expected recovery of the credit exposure with the collateral referred to in item 27 of this Decision, may not be shorter than three years from the date of calculation of the impairment.

The bank shall document the method of determining the value of collateral.

### **Eligible collateral instruments**

25. As eligible collateral instrument, the following shall be considered:

25.1 First-class collateral instrument of item 26 of this Decision.

25.2 Pledge of real estate and movable property in line with item 27 of this Decision.

25.3 Insurance policies for claims issued by the Development Bank of North Macedonia endorsed for the benefit of the bank.

25.4 Life insurance policies which, according to the National Bank's regulation on the methodology for determining the capital adequacy, are treated as credit risk mitigation instrument.

25.5 The pledge on claims on the central government of the Republic of North Macedonia, where the bank holds proper documentation for the established pledge, the pledge has been registered in a pledge registry and is given a precedence order of recovery against other pledge takers.

When determining the collateral of paragraph 1 sub-items 25.1 and 25.5 of this item, the central government shall also include public sector entities which, according to the National Bank's regulation on the methodology for determining the capital adequacy, are treated as central government.

The collateral of paragraph 1 of this item shall be considered a eligible collateral instrument only if during the entire validity of the contract, the credit exposure covered by the relevant collateral fulfills the terms under paragraph 1 of this item and the relevant terms of items 26 and 27 of this Decision.

26. First-class collateral instrument shall be considered the collateral that fulfills the following terms:

26.1 Cash deposit with the bank and possessory pledge on gold for the benefit of the bank, with the fulfillment of the following conditions:

- the date of payment of cash deposit is equal to or longer than the maturity date of the credit exposure specified in the credit contract;
- cash deposit or pledge may be withdrawn by the client only for the repaid portion of credit exposure;
- there is a relevant document (contract, statement, etc.) confirming the purpose of the deposit or the pledge as a collateral for credit exposure;
- in case of recovery through collateral, the bank shall be the only beneficiary of the cash deposit or pledged gold, and
- foreclosure occurs in circumstances when the client does not meet his/her liabilities arising from the credit exposure contract.

26.2 Securities issued by the European Central Bank and the central governments, central banks, multilateral development banks and international organizations for which, pursuant to the National Bank's regulation on the methodology for determining capital adequacy, a risk weight of 0% shall be applied;

26.3 Securities that the National Bank accepts as collateral in the conduct of monetary operations.

26.4 Debt securities (with the exception of Additional Tier 1 capital and Tier 2 instruments) issued by a bank having a long-term or short-term credit rating for which, in accordance with the National Bank's regulation on the methodology for determining capital adequacy, a risk weight of 20% shall be applied.

26.5 Debt securities (with the exception of Additional Tier 1 capital and Tier 2 instruments) issued by a bank having no long-term nor short-term credit rating, if in accordance with the National Bank's regulation on the methodology for determining the capital adequacy of the bank a risk weight of 50% shall be applied.

26.6 Unconditional guarantees payable on the first written call and issued by the entities under sub-item 26.2 of this item and by the entities established by the entities under sub-item 26.2 of this item, the operations and liabilities of which shall be fully covered by an explicit guarantee issued by these entities.

26.7 Unconditional guarantees payable on the first written call and issued by banks, to which, in accordance with the National Bank's regulation on the methodology for determining capital adequacy, a risk weight of 50% shall be applied.

When determining the credit rating for the purposes of paragraph 1 of this item, the rules in the National Bank's regulation on the methodology for determining capital adequacy shall be applied accordingly.

27. The pledge of the following types of real estate and movable property shall be considered a eligible collateral instrument if it meets the relevant conditions prescribed by this item:

- residential facility (apartment, house, and similar buildings), if they are completed and technically approved facilities;
- commercial facility and commercial premises (offices, shopping centers, warehouses, shops, car dealerships, etc.);

- industrial facilities (factories, plants and similar production facilities);
- agricultural facilities (mills, silos and similar production facilities);
- tourist facilities (hotels, apartments and similar facilities);
- agricultural land;
- products the price of which depends on fluctuations in the price of that product on international markets;
- unbuilt residential and commercial facilities for which a building permit has been issued by a competent institution, including construction land for which a building permit has been issued by a competent institution;
- construction, production, agricultural and other types of equipment;
- precious metals and works of art.

For the collateral of paragraph 1 indents 1, 2, 3, 4, 5, 6 and 8 of this item, the bank should have proper documentation for the pledge, such as:

- notarial deed with attachments for an established pledge, including an enforceability clause;
- title deed or other evidence from a public ledger for an established pledge issued by a competent institution;
- a valid real estate insurance policy endorsed for the benefit of the bank;
- a valid assessment of the market value of the facility made in accordance with this Decision;
- the established pledge shall be of a precedence order, and it may also be of a lower order if the pledge of a precedence order is with the same bank;
- and other relevant documentation.

For the collateral from paragraph 1 indent 7 of this item, the bank should have:

- notarial deed with attachments for an established pledge, including an enforceability clause;
- evidence from a public ledger for an established pledge issued by a competent institution;
- the established pledge shall be of a precedence order, and it may also be of a lower order if the pledge of a precedence order is with the same bank;
- a valid real estate insurance policy bound endorsed for the benefit of the bank;
- right to control and physical inspection of the subject of the pledge, on a regular basis;
- proof of regular monitoring of the market value of the pledged product on world stock markets;
- other relevant documentation.

For the collateral of paragraph 1 indents 9 and 10 of this item, the bank should have:

- notarial deed with attachments for an established pledge, including an enforceability clause;
- evidence from a public ledger for an established pledge issued by a competent institution;
- the established pledge shall be of a precedence order, and it may also be of a lower order if the pledge of a precedence order is with the same bank;
- a valid real estate insurance policy endorsed for the benefit of the bank;
- right to control and physical inspection of the subject of the pledge, on a regular basis;
- easy access to data on the market price of the collateral;
- proof that there are no obstacles to sell the collateral;

- proof that the collateral is determined as a mean of collateral in the credit exposure agreement;
- a valid assessment of the market value of the collateral made in accordance with this Decision;
- internal procedures for verification of the adequacy of the established pledge.

During the entire validity of the credit exposure agreement, the bank shall monitor the market value of the collateral from paragraph 1 of this item (e.g. through the application of statistical methods) at least once a year and shall provide an assessment of the current market value of the collateral at least once every three years, in accordance with the law.

Notwithstanding paragraph 5 of this item, the bank shall provide an assessment of the current market value of the collateral at least once a year, for the credit exposure that:

- exceeds 5% of the bank's own assets;
- is secured by a collateral instrument similar to collateral instruments the market price of which significantly dropped, or
- is secured by the collateral of paragraph 1 indent 8 of this item, taking into account the provisions of paragraph 7 of this item.

The assessment of the market value of the collateral from paragraph 1 indent 8 of this item should reflect the current value of the collateral, according to the stage of construction of the residential or commercial facility.

### **Determining the expected credit loss on a collective basis**

28. The bank shall assign credit exposures in loan portfolios by similarity of their characteristics and credit risk, having regard to the provisions of items 7 and 8 of this Decision.

The adequacy of loan portfolios shall be assessed at least on an annual basis.

Based on the determined expected credit loss, the bank shall classify exposures of the portfolios in the risk categories, in accordance with item 14 of this Decision.

29. When determining the rate of 12 month probability of default, the rate of lifetime probability of default of credit exposures and the rate of loss given default, the bank shall use a model prescribed in its internal acts. The model should include macroeconomic or other indicators that may have an impact on the calculation of the expected credit loss for the individual loan portfolios.

The Supervisory Board or the bank's Risk Management Board shall approve the model referred to in paragraph 1 of this item.

The bank may determine the rates referred to in paragraph 1 of this item, in accordance with items 30, 31 and 32 of this Decision.

The bank shall apply the rate of 12 month probability of default when determining the expected credit loss for the credit exposures which meet the criteria defined in item 9 sub-item 9.1 of this Decision, while for the other credit exposures the bank shall apply a rate of lifetime probability of default.



The rate of probability of default for non-performing credit exposures referred to in item 13 paragraph 4 of this Decision shall be 100%.

Impairment or allocated special reserve for credit exposures for which rate of 12 month probability of default is applied, may not be lower than 0.01% of the credit exposure, while for credit exposures for which rate of lifetime probability of default is applied, the impairment or allocated special reserve may not be lower than 5% of the amount of credit exposure.

The bank that does not hold enough data to determine the rate of loss given default for a certain loan portfolio, it shall apply the rate of loss given default which may not be lower than 90%.

30. The rate of 12 month probability of default may be determined as a multi-annual average of the annual rates of default. The annual rates of default shall be the ratio between the number of credit exposures that in the twelve-month period have become non-performing and the number of credit exposures in that portfolio at the beginning of that period.

When determining the rate of 12 month probability of default, the bank shall determine annual default rates for each loan portfolio for at least the last five years at least with monthly dynamics. The bank may assign greater weight to the more recent annual default rates, if identified that they more realistically show the probability of default and expected credit loss.

31. The rate of lifetime probability of default of the credit exposures from the portfolio may be determined as the ratio between the number of credit exposures that in the course of the average lifetime of the loan portfolio have become non-performing and the number of credit exposures from that portfolio at the beginning of that period.

If the bank does not hold data to calculate the rate of lifetime probability of default of the credit exposures from loan portfolio, the rate shall be calculated for a period of at least five years by including forecasts for the remaining average number of years.

32. The rate of loss given default for the credit exposure from the loan portfolio may be determined as the average loss for the bank arising from credit exposures that became non-performing credit exposures in a portfolio with similar characteristics as the portfolio for which the rate of loss given default is determined.

When calculating the rate of loss given default referred to in paragraph 1 of this item, the bank may include the recovery from non-performing credit exposures from loan portfolio that were written-off.

When calculating the rate of loss given default, the average loss shall be determined for a period of up to three years, including the recovery arising from the sale of collateral, where the data on the expected changes in the value of the collateral and the expected credit exposure recovery period can also be included.

When determining the rate of loss given default, the bank shall take into account the historical data on the realized loss from non-performing credit exposures with similar characteristics that became non-performing at most five years ago.

33. The bank shall evaluate the effectiveness (backtesting) of the model referred to in item 29 of this Decision at least on an annual basis or in case of significant change in its basic elements.

The evaluation the model should be carried out by the bank's organizational units that were not involved in the establishment of the model and/or by outsourcers.

#### **IV. OVERDUE CLAIMS**

34. The bank shall not, directly or indirectly, approve new credit exposure to refinance existing credit exposure, except in case of credit exposure forbearance. The following cases shall not be considered approving of new credit exposure to refinance existing credit exposure:

- approving a loan to a person who has due liabilities to the bank or has a liability to the bank that becomes due within 31 days, and the bank has provided documented evidence that the approved loan will not be used for repayment to the bank;
- approving a loan to a person to refinance any undue liabilities to the bank, while the approval the loan ensures more favorable conditions for the person;
- disbursement of approved unconditionally irrevocable credit lines, overdrafts and loans based on credit cards, while at the time of approval, the person has no due liabilities to the bank.

The bank shall take measures to make sure that the credit exposure from paragraph 1 indent 1 of this item will not be used for repayment of liabilities to the bank.

#### **V. FORBORNE CREDIT EXPOSURE**

35. The bank shall prescribe in the policy or the internal acts of item 77 of this Decision at least the following:

35.1 Procedures and rules for credit exposure forbearance, the method of decision-making on the restructuring and the persons, organizational units and/or bodies involved in the decision-making, as well as the documentation required to approve the restructuring;

35.2 Criteria for determining financial difficulties for repayment of liabilities (deteriorated financial standing of the client) and for determining whether the client can or could comply with the existing contractual terms, taking into account the provisions of item 37 of this Decision;

35.3 Cases considered as restructuring of credit exposure, taking into account the provisions of items 38 и 39 of this Decision;

35.4 Procedure and rules for assessing the sustainability of the credit exposure restructuring, in accordance with item 40 of this Decision;

35.5 Procedure and rules for assessing the effectiveness of the performed restructuring, in accordance with item 41 of this Decision, including the manner of determining and monitoring the rates under item 41 paragraph 2 of this Decision, as well as the level of these rates which indicate (non) effectiveness of the performed restructuring.

36. The bank shall perform every restructuring of the credit exposure on the basis of a decision of the Risk Management Board or a decision of another body or board in the bank.

When adopting the decision on restructuring credit exposure referred to in paragraph 1 of this item, the bank should take into account that the evaluation of the sustainability in the restructuring is in line with item 40 of this Decision, which should be an integral part of the analysis referred to in item 37 of this Decision.

37. When modifying the contractual terms of credit exposure, the bank shall make analysis and determine whether the client has or has not financial difficulties and whether he/she can or could adhere to the existing contractual terms without their modification.

For the needs of the analysis of paragraph 1 of this item, the bank shall also bear in mind the influence of:

- persons who together with the client create a group of connected persons;
- market conditions, if they indicate significant changes that may negatively affect the client's ability for repayment of liabilities.

The analysis of paragraph 1 of this items should not take into consideration the effect of the eligible collateral instrument on the recovery of credit exposure.

Notwithstanding paragraph 1 of this item, the bank shall not be required to make the analysis referred to in paragraph 1 of this item for credit exposure based on deposits in domestic and foreign banks, for off-balance sheet credit exposure and for credit exposure secured by a first-class collateral instrument referred to in item 26 of this Decision.

38. Foreborn credit exposure shall be considered at least the following cases:

- new contractual terms are significantly more favorable than the existing contractual terms, and based on the analysis under item 37 of this Decision, a deteriorated financial standing or inability for repayment of the liabilities according to the existing contractual terms has been determined;
- new contractual terms are significantly more favorable compared to the contractual terms that the bank currently offers to other clients with a similar risk profile, and based on the analysis of item 37 of this Decision, a deteriorated financial standing or inability for repayment of the liabilities according to the existing contractual terms;
- credit exposure where contractual conditions are modified or a new credit exposure is approved has the treatment of non-performing credit exposure;
- credit exposure would be treated as a non-performing credit exposure if contractual terms or the approval of a new credit exposure had not been modified, and based on the analysis of item 37 of this Decision, a deteriorated financial standing or inability for repayment of the liabilities under the existing contractual terms has been determined;
- new contractual terms include a full or partial reduction of credit exposure through write-off;
- on the date of approval of the credit exposure or in a period of 31 days prior to the approval of the credit exposure, the client repays other liabilities to the bank based on principal or interest of another credit exposure, which is treated as a non-performing

credit exposure, and the bank does not have documented evidence that the approved credit will not be used for repayment to the bank;

- on the date of approval of the credit exposure or in a period of 31 days prior to the approval of the credit exposure, the client repays other liabilities to the bank based on principal or interest of another credit exposure, which would have been treated as a non-performing credit exposure if those payments had not been made, and the bank does not have documented evidence that the approved credit will not be used for repayment to the bank, and based on the analysis of item 37 of this Decision, a deteriorated financial standing or inability for repayment of the liabilities according to the existing contractual conditions has been determined;
- new contractual terms include reduction of credit exposure through realizing the collateral.

For the purposes of paragraph 1 indents 6 and 7 of this item and item 39 indent 2 of this Decision, the cases where the modification of the contractual terms of an existing credit exposure includes the approval of an additional amount of credit exposure shall also be considered as approval of credit exposure.

39. The following indicators may denote a forbearance of credit exposure:

- at least once in the last three months before the modification of the contractual terms, the client was late for more than 61 days in the repayment of the liabilities based on that credit exposure, or would have been late for more than 61 days, if the contractual terms had not been modified;
- on the date of approval of the credit exposure, or in a period of 31 days prior to the approval of the credit exposure, the client repays other liabilities to the bank based on principal or interest of another credit exposure, on the basis of which the client was late for more than 31 days, at least once in the last three months prior to the approval of the new credit exposure, and the bank does not have documented evidence that the approved credit will not be used for repayment to the bank.

40. The bank shall evaluate the sustainability of the credit exposure restructuring, taking into account the following:

- the reasons for the identified deterioration of the client's financial standing or the inability to repay the liabilities under the existing contractual terms, and if applicable, also of the persons/entities connected to the client;
- the ability of the client to adhere to the new contractual terms, including the level of indebtedness of the client/project, that is, the possibility for the bank to fully recover the credit exposure;
- data on previous restructuring of the credit exposures to the client;
- cash flow forecast for the period that would be covered by the forbearance;
- data on the client's reorganization plan, if the client is subject to such a plan.

41. The bank shall evaluate the effectiveness of the performed forbearance the a regular basis, and at least every three months.

For the purposes of evaluating the effectiveness of the forbearance, the bank shall determine and monitor the following indicators for individual portfolios on a regular basis:

- recovery rate of the forborne credit exposures, including the written-off forborne credit exposures;

- the rate of forbore non-performing credit exposures excluded from this category, in line with item 60 of this Decision;
- write-off rate of forbore credit exposures.

On the basis of the evaluation of the effectiveness of the performed forbearance, the bank shall regularly review the forbearance rules and procedures.

42. The bank may perform capitalization of interest only if it is a part of the credit exposure restructuring.

Notwithstanding paragraph 1 of this item, the bank may perform capitalization of interest also during the project financing within the extended grace period, according to the contract.

43. The bank shall observe the criteria for classification of credit exposure arising from the forbearance, determined by this Decision.

44. The net effect of the credit exposure forbearance shall not increase the financial position of the bank, except in the case of reducing credit exposure as a result of recovery. Within six months upon forbearance, the bank shall not record income based on the release of impairment/special reserve, which is not a result of recovery of credit exposure.

45. Notwithstanding items 43 and 44 of this Decision, the bank may approve better risk category and/or calculate lower impairment/special reserve, only if the forbore credit exposure is secured by new first-class collateral instrument.

46. Credit exposure may be excluded from the category of forbore credit exposures if the following conditions are met:

- probation period has ended, and
- after the end of the probation period, all credit exposures of the client shall be classified in A risk category.

## **VI. NON-PERFORMING CREDIT EXPOSURE**

47. All credit exposures of the bank to one client shall become non-performing credit exposures if the client has a defaulted credit exposure according to item 2 sub-item 2.23 paragraph 1 of this Decision, unless:

- the bank decided to apply the exception under item 2 sub-item 2.23 paragraph 2 of this Decision, or
- exceeding the materiality threshold is the result of a technical error (errors in the data, delay in the execution of payment orders or there is a discrepancy in time between the payment made and its recording by the bank, etc.).

48. If the bank decides to apply the exception under item 2 sub-item 2.23 paragraph 2 of this Decision, it shall act accordingly for all exposures to natural persons.

In instances of paragraph 1 of this item, if the sum of the defaulted on-balance sheet credit exposures to client natural person of item 2 sub-item 2.23 paragraph 2 of this Decision exceeds 20% of the total on-balance-sheet credit exposure of the bank to that client, the bank

shall assign a treatment of non-performing exposures to all on-balance-sheet and off-balance-sheet exposures to that client.

Notwithstanding paragraphs 1 and 2 of this item, all credit exposures to the client, a natural person, become non-performing credit exposures, if the client meets the relevant indicators of unlikeliness to pay of item 54 and item 62 sub-item 62.8 of this Decision.

49. The bank shall consider as non-performing credit exposures all client exposures whose joint credit exposure meets the criteria for defaulted credit exposure. For the purposes of this item, the fulfillment of the materiality threshold in relation to the joint credit exposure shall be determined in accordance with item 2 sub-item 2.23 paragraph 2 of this Decision.

Notwithstanding paragraph 1 of this item, the bank may not consider as non-performing credit exposures the other credit exposures of clients with joint defaulted credit exposure, if:

- the delay in the repayment of the liabilities based on the joint defaulted credit exposure is the result of a court dispute between clients and there are no doubts about the deteriorated financial standing of individual clients,
- the joint defaulted credit exposure has a very small share in the total credit exposure of individual clients.

The bank shall not consider as non-performing credit exposures the joint credit exposures that individual clients have with other clients of the bank, who are not debtors on the basis of the joint defaulted credit exposure, but shall assess whether any of the indicators for unlikeliness to pay of item 54 and item 62 sub-item 62.8 of this Decision is met.

In the case of receiving information about an initiated bankruptcy procedure against a legal entity owned by a natural person, the bank shall determine whether, in relation to the exposures of the natural person, any of the indicators of unlikeliness to pay of item 54 and item 62 sub-item 62.8 of this Decision is met.

50. If it is an investment in securities that meets the criteria for defaulted credit exposure, all exposures to the client that issued the securities shall become non-performing credit exposures.

### **Exceeding the materiality threshold**

51. The bank shall monitor the fulfillment of the materiality threshold and its exceeding on a daily basis.

52. For the purposes of determining the exceeding of the materiality threshold:

- in instances when the credit exposure is based on an overdraft, the amount exceeding the approved limit shall be considered as due claims;
- in instances when the credit exposure is based on credit cards, the amount that the client was obliged to pay, in accordance with the agreement with which the credit card was approved, shall be considered as the amount of due claims;
- in instances when the repayment of the liabilities by the client is deferred or terminated in accordance with a regulation, the bank shall defer or stop determining the exceeding of the materiality threshold, but shall determine whether this client has met the

relevant indicators of unlikeliness to pay of item 54 and item 62 sub-item 62.8 of this Decision.

53. The bank may apply lower value for both components of the materiality threshold than those stipulated in item 2 sub-items 2.25 and 2.26 of this Decision, if considers and can prove that the lower values are better indicators of defaulted credit exposure, while the application of those lower values will not cause a significant amounts of exposure, which in a very short period after they are identified as defaulted credit exposures would meet the terms of item 59 of this Decision on excluding the non-performing credit exposures.

### **Unlikeness to pay**

54. The bank shall assess whether there is unlikeness to pay by the client, at least on the basis of the following indicators:

- sale of credit exposure of the client with a significant loss;
- restructuring of the credit exposure with a significant modification in the contractual terms as a result of which there is a significant reduction of the client's liabilities based on principal, interest or fees;
- a proposal to initiate a bankruptcy or other similar procedure against the client has been submitted, in accordance with the law;
- a bankruptcy or other similar procedure against the client has been initiated, in accordance with the law;
- the bank proceeded with foreclosure.

55. For the purpose of item 54 paragraph 1 indent 1 of this Decision, the loss arising from the sale shall be determined by using the following formula:

Loss =  $(E - P)/I \times 100$ , where:

E – total amount of credit exposure subject to sale

P – sale price.

The loss determined in accordance with paragraph 1 of this item shall be considered significant if exceeds 5% of the credit exposure.

In case of sale of the credit exposure with a significant loss determined in accordance with this item, the remaining exposures of the bank to the client receive the treatment of non-performing credit exposures, except if it is a client who is a natural person to whom the bank applies the exception of item 2 sub-item 2.23 paragraph 2 of this Decision, thereby applying item 48 of this Decision.

In case of sale of loan portfolio, the fulfillment of the term of paragraph 2 of this item shall be determined:

- on an individual basis for each loan, if the price of the entire portfolio is determined based on the individual prices of each loan in that portfolio;
- at the level of the entire portfolio, if the sale price is determined for the entire portfolio and in that case, if the limit under paragraph 2 of this item is exceeded, it is considered that all loans in the portfolio had treatment of non-performing credit exposures on the day of sale.

If the sale of the credit exposure is carried out for other reasons that are not related to the credit risk (for example: sale of credits for the purpose of providing additional liquidity, due to a change in the bank's business policy, etc.) and there is no objective evidence that that exposure is impaired, the sale of the credit exposure should not be considered as an indicator of unlikeness to pay, regardless of the amount of the realized loss.

The bank shall be required to provide adequate documentation to confirm the fulfillment of the terms of paragraph 5 of this item.

56. For the purposes of item 54 paragraph 1 indent 2 of this Decision the credit exposure shall be considered restructured credit exposure with a significant modification of the contractual terms if the amount of the client's liabilities after the restructuring of that credit exposure are significantly less than the amount of their liabilities before the restructuring.

The bank shall determine whether the client's liabilities have been significantly reduced by applying the following formula:

Diminished financial obligation =  $(NPV0 - NPV1) / NPV0 \times 100$ , where:

NPV0 – the present value of the expected cash flows in accordance with the existing contractual terms, discounted by the effective interest rate determined in accordance with the regulation of the National Bank on the methodology for recording and valuation of the accounting items and for preparation of financial statements,

NPV1 – the present value of the expected cash flows in accordance with the new contractual terms, discounted by the effective interest rate determined in accordance with the regulation of the National Bank on the methodology for recording and valuation of the accounting items and for preparation of financial statements.

The reduction of the client's liabilities in accordance with paragraph 2 of this item shall be considered significant, if it exceeds 1% of the present value of the expected cash flows in accordance with the existing contractual terms and that exposure is considered a restructured credit exposure with a significant modification of the contractual terms.

If the reduction of liabilities determined in accordance with paragraph 3 of this item does not exceed 1%, the bank shall evaluate whether the forborne credit exposure meets other indicators of unlikeness to pay, such as:

- bullet payment is approved;
- irregular repayments of the credit exposure are agreed, whereby the amounts to be paid in the initial period are far lower than those to be paid in subsequent repayment periods;
- a grace period longer than 24 months has been approved for the payment of the principal and/or interest;
- the client has or previously had other forborne credit exposures with a significant modification in contractual terms with the bank.

57. The bank can prescribe the following additional indicators of unlikeness to pay by credit exposure (type of product, client, geographical area):



- reduction of the client's income or reduction of their regularity due to which the client will not be able to earn regular income in a sufficient amount to repay the liabilities in accordance with the contractual terms;
- more frequent forbearance of the same credit exposure or multiple exposures to the same client;
- the level of client's indebtedness has significantly increased or it is expected its indebtedness to increase.

The bank shall take into account information about the client from external sources (information from the Credit Register of the National Bank, from the credit bureaus, macroeconomic indicators, financial reports, information in the public media and other publicly available information) that may indicate the unlikeness to pay, such as a delay in the repayment to other creditors of the client, financial problems in the business the client belongs to or its most significant contractual parties, etc.

58. Forborne non-performing credit exposure shall include:

58.1 The credit exposure which on the date of forbearance was treated as non-performing credit exposure or would become non-performing credit exposure if it has not been forborne;

58.2 The forborne credit exposure where during the probation period:

- the bank restructures the credit exposure with significant modification in the contractual terms,
- any of the indicators of unlikeness to pay referred to in item 54 and item 62 sub-item 62.8 of this Decision has been met or
- the client is past-due for more than 60 days based on forborne credit exposure.

58.3 The credit exposure subject to restructuring with significant modification in the contractual terms, including restructuring that meets some of the other indicators of unlikeness to pay referred to in item 56 paragraph 4 of this Decision.

### **Exclusion from non-performing credit exposure**

59. The credit exposure treated as a non-performing credit exposure may be excluded from this category if the following conditions have been met:

- at least 90 consecutive days have passed from the day when the criteria for defaulted credit exposure referred to in item 2 sub-item 2.23 of this Decision have ceased to be met;
- the bank conducts an analysis of the regularity of the client of repayment of their liabilities and their financial position which does not show that any of the indicators of unlikeness to pay referred to in item 54 and item 62 sub-item 62.8 of this Decision has been met, and
- the conditions referred to in indents 1 and 2 of this paragraph have been met also in terms of the new credit exposures approved to the client.

60. The forborne non-performing credit exposure referred to in item 58 of this Decision may be excluded from the category of non-performing credit exposures if all

conditions referred to in paragraph 2 of this item have been met and at least one year has passed from:

- the date of forbearance;
- the date when the credit exposure obtained treatment of a non-performing credit exposure, and
- the date when the grace period approved by the forbearance ended.

The bank shall make an analysis of the client's creditworthiness and the manner of repayment of their liabilities, which shall determine whether the following conditions have been met:

- the client regularly repaid their liabilities in accordance with the new contractual terms;
- the client has no liabilities based on credit exposure that are due for more than 31 days, in accordance with the contractual terms;
- through the regular repayment of liabilities in accordance with the contract, the client paid a substantial amount;
- any of the indicators of unlikeness to pay referred to in item 54 and item 62 sub-item 62.8 of this Decision has not been met;
- the client will be able to repay their liabilities in accordance with the contractual terms without taking activities for activation of the collateral, especially in the exposures with a bullet repayment or where larger payments are envisaged in the last periods of the terms of redemption;
- the conditions envisaged in the previous indents of this paragraph have been met also in terms of the new credit exposures approved to the client.

### **Management of non-performing credit exposures**

61. The bank shall establish an appropriate system for management of non-performing credit exposures, and especially for consistent application of the definition of non-performing credit exposures in the bank.

The bank shall regularly monitor and assess the impact of non-performing credit exposures on the own funds, profitability, liquidity and other indicators of the bank's operations.

62. For the purposes of item 61 of this Decision, the bank shall be obliged, in the policy and internal acts referred to in item 77 of this Decision, to encompass at least the following aspects:

62.1 To prescribe the manner of determining, monitoring and control of non-performing credit exposures, in accordance with the requirements of this Decision;

62.2 To define the approach of determining non-performing credit exposures for the clients - natural persons, at a level of a client or at a level of credit exposure / credit agreement;

62.3 To prescribe when the credit exposure to persons/entities with which the client - legal entity is connected, whose liabilities to the bank are treated as non-performing credit exposures becomes non-performing credit exposure;

62.4 To prescribe the application of item 49 paragraph 2 indent 2 of this Decision;

62.5 To prescribe the procedure for determining the significance of the loss which, in case of a sale of credit exposure, may be considered as an indicator of unlikeliness to pay, taking into account the provisions referred to in item 55 of this Decision;

62.6 To prescribe the procedure for determining significant modification in the contractual terms, taking into account the provisions referred to in item 56 of this Decision;

62.7 To prescribe the indicators on the basis of which it will determine that the forborne credit exposure where the reduction of the client's liabilities in case of modifying the contractual terms does not exceed 1% of the present value of the expected cash flows in accordance with the existing contractual terms (not considered forborne credit exposure with significant modification in the contractual terms) should be considered as non-performing, taking into account the indicators of unlikeliness to pay referred to in item 56 paragraph 4 of this Decision;

62.8 To prescribe the additional indicators of unlikeliness to pay, taking into account the provisions referred to in item 57 of this Decision, including the sources of data and information on their determining and monitoring, as well as the frequency of monitoring and reviewing these indicators;

62.9 To prescribe the procedure, criteria and data on the basis of which it decides on excluding the non-performing credit exposure and the forborne non-performing credit exposure in accordance with items 59 and 60 of this Decision, as well as to prescribe the manner of determining the substantial amount referred to in item 60 paragraph 2 indent 3 of this Decision;

62.10 To prescribe the signals of worsening of the quality of the credit portfolio of the bank for the purposes of determining an increased amount of non-performing credit exposures, in accordance with item 63 of this Decision;

62.11 To prescribe the procedure and rules for forced collection of non-performing credit exposures, including the criteria, procedure and manner of deciding on undertaking appropriate activities for activation and collection of the collateral.

63. The bank with an increased amount of non-performing credit exposures shall be obliged to determine:

63.1 Persons / organizational unit for management of non-performing credit exposures, who / which will be independent of the bank's organizational units that are competent for taking credit risk;

63.2 Strategy for management of non-performing credit exposures referred to in item 64 of this Decision, approved by the bank's Supervisory Board, which at least includes:

- instruments for reduction of non-performing credit exposures;
- quantitative thresholds for the amount of non-performing credit exposures in the short, medium or long term, and
- operational plan indicating the activities that the bank will undertake to reduce non-performing credit exposures, which is developed for a period from at least one to three years.

For the purposes of paragraph 1 of this item, the bank shall be considered to have an increased amount of non-performing credit exposures if:

- the rate of non-performing loans is equal to or exceeds 5%;
- the rate of non-performing loans is below 5%, but there is a high concentration of non-performing credit exposures (high rate of non-performing credit exposures by activity, connected persons/entities, etc.);
- there are signals of worsening of the quality of the credit portfolio (significant growth of the volume of non-performing credit exposures, exceeded early warning thresholds, etc.).

64. In the strategy for management of non-performing credit exposures, the bank shall determine one or more instruments for reduction of non-performing credit exposures, such as:

- forbearance of non-performing credit exposures and their retention in the bank balance sheet;
- sale, securitization or write-off of non-performing credit exposures;
- change in the type of collateral, foreclosure, conversion of credit exposure or its part into capital investment with the client, etc.;
- instigating bankruptcy procedure or other procedure for forced collection of credit exposure.

When laying down the strategy for management of non-performing credit exposures, the bank shall:

- assess the capacity to manage and reduce non-performing credit exposures, taking into account the main generators of the growth of non-performing credit exposures, having in mind the specificities of the various portfolios, as well as their mutual influence, the type and efficiency of the instruments for reduction of non-performing credit exposures in the previous period, the required human resources with appropriate experience and professionalism to implement the selected instruments, as well as the necessary IT support and the quality of data held by the bank to implement the strategy, which does not exclude the possibility of using outsourcing services;
- assess the characteristics of the current and the possible future environment in which the bank operates or will operate, including the indicators of the developments on the real estate market and the market expectations for the possibility for the purchase and sale of non-performing credit exposures and
- assess the impact of the strategy on the bank's operations, especially in terms of the required level of own funds, risk profile, profitability and the amount of impairment.

The strategy is part of the risk management process in the bank, especially in terms of the internal capital adequacy assessment process, the general framework for the risk appetite, as well as the recovery plan (when developing the recovery plan one shall take into account the activities, indicators and procedures defined in the strategy).

The bank shall be obliged at least once a year, or in case of a significant change in the risk management system, to examine the need for reviewing the strategy and if necessary to review it, in accordance with the risk appetite statement.

65. The bank's Internal Audit Department shall audit the management of non-performing credit exposures, in accordance with the annual internal audit plan.

## **VII. WRITE-OFF OF CREDIT EXPOSURE**

66. Bank shall write-off any credit exposure, fully or partially, when it does not expect its collection or when it has no right or in case of expired credit exposure collection rights.

Credit exposure shall be written off at least in the following cases:

- the bank is not entitled to future cash flows, i.e. the credit exposure collection rights have expired, regardless of the basis for their losing or expiration, which especially include: effective court decision stating that there is no legal ground for the bank's claim, effective court decision stating that the bank is not entitled to the claim, effective court decision on completed bankruptcy proceedings, effective court decision on the reorganization plan approved to a debtor in bankruptcy;
- the bank has no reasonable expectations for recovery of credit exposure, fully or partially;
- the bank has made a decision to discharge the debt in accordance with law, waiving a further recovery of the claim;
- in case of individually insignificant credit exposure.

Notwithstanding paragraph 2 of this item, the bank shall make mandatory transfer of the accounts for off-balance sheet records of credit exposures where twelve months have passed from the date when the bank was obliged to make impairment, or allocate special reserve of 100%.

The bank shall set the maximum amount of individually insignificant credit exposure referred to in paragraph 2 indent 4 of this item, by a decision of the Supervisory Board.

The bank may continue to recover the credit exposure referred to in paragraphs 2 and 3 of this item, unless it has waived or is not entitled to its further recovery.

67. The bank shall write-off credit exposure referred to in item 66 paragraph 2 indents 2 and 3 of this Decision, fully or partially, by a decision of the bank's Supervisory Board, on the basis of an elaborate for writing-off, which consists of the following:

- reason behind the proposal for the write-off;
- measures taken to collect the claim and the results of those measures;
- persons and bodies that participated in the credit approval;
- reason behind the absence or inadequacy of collateral;
- assessment of the observance of internal acts (rules, procedures, etc.) of the bank that determine the approval, monitoring, collection and write-off of credit exposure, and
- in cases of connection between the client and the bank, any person connected with the bank which, according to the Banking Law and bylaws adopted pursuant to this law, are regarded as connected to the client, shall be indicated.

68. The bank shall maintain off-balance sheet records of all credit exposures referred to in item 66 paragraphs 2 and 3 of this Decision at least for a period of 10 years from the date of the writing-off, i.e. from the transfer of credit exposure to the accounts for off-balance sheet records.

As an exception to paragraph 1 of this item, the bank shall not be obliged to maintain off-balance sheet records of individually insignificant credit exposures, as well as in the cases when the bank is not entitled to a certain claim, i.e. it requests certain amount incorrectly. The bank shall regulate the actions in such cases in the internal acts, taking into account the need to hold relevant data on the basis of which it will be able to assess the client's creditworthiness, to determine forbearance of credit exposures, to assess the client's unlikeliness to pay, as well as to ensure appropriateness of the information system and the reporting to the National Bank.

## **VIII. SALE OF DUE, NON-PERFORMING OR WRITTEN-OFF CLAIMS FROM A CREDIT AGREEMENT**

### **Procedure and rules for sale of due, non-performing or written-off claims**

69. The bank shall sell due, non-performing or written-off claims from a credit agreement together with all secondary rights arising thereof.

Sale of due, non-performing or written-off claims from a credit agreement shall denote full or partial deviation of those claims from an individual credit agreement concluded with natural persons and non-financial legal entities (individual credit agreement) or deviation of several due, non-performing or written-off claims from credit agreements concluded with natural persons and non-financial legal entities (credit agreements portfolio).

With the contract for the sale of a due, non-performing or written-off claim, the bank shall transfer the rights and obligations, as well as the risks and the benefits of its claim to a third party, which leads to derecognition of the claim in the bank balance sheet, in accordance with the National Bank regulation on the methodology for recording and valuation of accounting items and for preparing financial statements.

70. If the bank sells due, non-performing or written-off claims, in the Credit Risk Management Policy or in the other internal acts for identification, measurement, control or reduction and monitoring of credit risk (rules, procedures, etc.) referred to in item 77 of this Decision, it regulates the procedure and the rules for sale of those claims, that should contain the following elements, in accordance with the types of sales made by the bank (sale of claims from an individual credit agreement or sale of a portfolio of credit agreements):

- the types of loans that can be covered in the sale of claims;
- the manner of determining the loans in the portfolio of credit agreements, which would be subject to sale;
- the manner of determining the claim selling price (in the amount of the claim or at a discount);
- the manner of selling that the bank will apply in the sale of claims (e.g. direct sale, auction system, securitization);
- the criteria for identifying potential buyers of claims;
- prepared draft-documents to conclude the sale (e.g. draft-contracts, memorandums for protection of confidentiality of data that are subject to negotiations, written approvals, etc.);
- the manner of providing an approval from the bank's clients to transmit data for the purposes of the sale of the claims;

- the criteria for identifying outsourcing service providers that could be involved in the process of negotiations and structuring of the sale and of the legal acts for selling of the claims from the credit agreement.

### **Contract for the sale of due, non-performing or written-off claims from a credit agreement**

71. Before concluding the contract for the sale of a due, non-performing or written-off claim, the bank shall be obliged to make an assessment of the effects of the sale of the claim and to assess the economic justification of the sale.

The assessment of the effects and the economic justification of the sale referred to in paragraph 1 of this item, shall include at least an assessment of the effects of the sale on the financial result, the risk exposure, the solvency and liquidity of the bank.

72. Before concluding the sales contract, the bank shall be obliged to provide to the person who intends to purchase a due, non-performing or written-off claim of the bank from a credit agreement, all information necessary for an appropriate assessment of the value of the claim, as well as for an assessment of the potential rate of collection.

73. The bank shall be obliged, in accordance with the type of the sale of a due, non-performing or written-off claim, to provide in the claim sales contract:

- clear demarcation of the rights and obligations between the bank and the buyer;
- provisions for inability to return the risks and the benefits of that claim;
- provisions for regulating the management and the collection of sold claims;
- a clause according to which the buyer of the claim will appropriately apply the consumer protection regulations in accordance with the law, if the subject of purchase and sale are claims on consumers;
- a clause according to which the buyer of the claim will appropriately apply the data protection regulations, in accordance with the relevant regulation on personal data protection;
- a clause with which the change in the interest rate of the claim from the credit agreement will not depend solely on the will of the buyer of the claim from a credit agreement, including a clause with which the changes in the other contractual terms will refer solely to providing more favorable conditions to the debtor whose obligation to the bank is subject of the sales contract;
- a clause for protection against the risks to the bank that may arise from the potential disputes in relation to the collection of sold claims.

### **Management and collection**

74. If on the basis of the concluded contract for the sale of due, non-performing or written-off claims, the bank has undertaken obligations to manage and collect sold claims, it shall be obliged to apply the internal acts and the business practices and procedures it applies in the collection of its claims, which should also be provided for in the claim sales contract.

If on the basis of the concluded sales contract, the buyer undertakes the obligation for management and collection of sold due, non-performing or written-off claims, the sales contract must contain a provision that will require from the buyer to respect and protect the

integrity of all debtors, and will not place them in a less favorable position than that as a contracting party in the credit agreement concluded with the bank.

## **IX. CREDIT RISK MANAGEMENT**

### **General requirements**

75. Credit risk management is a part of the overall bank's risk management system and meets the requirements for risk management defined by the Banking Law, the National Bank's regulation on the methodology for the risk management, as well as other bylaws adopted pursuant to this law.

76. In terms of credit risk management, the bank's organizational structure should enable:

- defined responsibilities and lines of accountability, especially in the process of decision-making for approval of credit exposures, for change in the contractual terms, for credit exposures forbearance, for use of collateral instruments, for definition and implementation of the strategy for management of non-performing credit exposures, etc.;
- cooperation and exchange of information on credit risk management;
- separation of the competences and responsibilities between the persons and organizational units of the bank responsible for the lending activity and who perform activities related to taking credit risk, on the one hand and the persons and organizational units that perform activities related to the credit risk management and the lending-related back office activities, on the other.

77. The bank shall design and apply credit risk management policy and/or other internal acts for identifying, measuring, controlling or mitigating and monitoring credit risk (rules, procedures, etc.), which at least include provisions for:

77.1 The approval and classification of credit exposures, taking into account items 78, 79, 80 and 81 of this Decision.

77.2 The manner of determining impairment / special reserve, including the manner of including the value of the collateral when determining impairment, taking into account items 82 and 83 of this Decision.

77.3 The method of stress testing of credit exposure, assumptions underlying the testing and method of reporting on the testing results.

77.4 The manner of managing foreborne credit exposures taking into account the provisions of Section V of this Decision.

77.5 The manner of managing non-performing credit exposures, taking into account the provisions of Section VI of this Decision.

77.6 The manner of writing off credit exposure, i.e. transferring credit exposure to the off-balance sheet records, including the criteria, the procedure, the bodies competent to make the decision, the documentation on the basis of which the decision is made, the manner



of deciding on full or partial write-off of credit exposures, as well as the manner of recording written off, i.e. transferred credit exposures to the off-balance sheet records, taking into account the provisions of Section VII of this Decision.

77.7 Procedure and rules for purchase and sale of claims and procedure for decision-making and organizational units / bodies / persons competent for deciding on purchasing and selling claims, whereby when selling due, non-performing or written-off claims one shall take into account the provisions of Section VIII of this Decision.

77.8 Contents and manner of keeping a credit file for bank clients/projects, taking into account item 84 of this Decision.

77.9 The volume and frequency of reporting to the Supervisory Board and the Management Board of the bank and to all other persons involved in the credit risk management, taking into account item 85 of this Decision.

77.10 The manner of collecting and processing personal data for the purposes of the assessment of the client's creditworthiness and monitoring the collection of credit exposures approved by the bank, taking into account the provisions of the law which regulates the personal data protection.

77.11 The manner in which the bank takes into account the impact of climate risks in the credit risk management.

## **Approval and classification of credit exposure**

78. In its internal acts, the bank shall be obliged to envisage the following aspects in terms of the approval and classification of credit exposures:

78.1 Criteria for approving loans and other forms of credit exposure, including criteria for approving credit exposures for financing projects.

78.2 Criteria for determining the creditworthiness of the client / quality of the project, i.e. the change in the creditworthiness of the client / quality of the project taking into account the minimum criteria from item 7 of this Decision, as well as defining the financial indicators that the bank will use when evaluating the financial capacity of the project.

78.3 Rules for deciding on the approval of credit exposure in the cases when the organizational units that perform activities related to the credit risk management, have failed to provide an opinion / approval or if the opinion of the organizational units that perform activities related to the credit risk management is different from the opinion of the organizational units of the bank responsible for the lending activity and which perform activities related to taking credit risk.

78.4 Criteria for determining the increase in the credit risk, which may differ for certain credit exposures or loan portfolios.

78.5 Criteria for determining the possible effects on client's creditworthiness of persons/entities connected to the client, as well as criteria for determining the possible effects of persons/entities with joint credit exposure.

78.6 Criteria for classification of credit exposures in the individual risk categories, taking into account the provisions of item 10 of this Decision, as well as the manner of deciding in terms of the classification of credit exposures.

78.7 Method for determining the level and type of interest rate and other fees and commissions.

78.8 Defining and monitoring internal credit exposure limits according to the structure of total credit exposure of the bank (e.g. by client, type of credit products, activity, currency, etc.).

78.9 Defining permissible exceptions, procedures for their approval and defining the acceptable level of credit exposure approved with permissible exceptions for a determined period (e.g. quarter).

78.10 Defining an acceptable level of repayment source, as well as the currency of credit exposure.

78.11 Defining an acceptable level and monitoring the level of debt service-to-income and total debt-to-income ratios and defining the individual elements of these ratios, taking into account the provisions of the National Bank regulation on borrower-based macroprudential instruments.

78.12 Defining the collateral that the bank accepts (for certain type of credit product or for certain currency of credit exposure), as well as:

- defining the necessary documentation for certain types of collateral referred to in item 27 of this Decision;
- defining the loan-to-value ratio by individual types of collateral;
- procedure, rules and frequency of monitoring and determining the market value of the collateral, including for the purposes of the calculation of the loan-to-value indicator;
- the procedure and deadlines for taking and/or selling collateral.

78.13 Method for determining and monitoring the regularity of debt repayment for the purposes of the classification of credit exposure.

78.14 Assessment of credit risk arising from currency risk the client is exposed to and establishment of criteria for granting foreign currency loans or Denar loans with FX clause, having regard to the provisions of item 81 of this Decision and the manner in which this assessment is taken into account in the classification of credit exposure.

78.15 Criteria for monitoring domicile country risk of the client - a foreign entity and for monitoring interest rate risk.

78.16 Assessment of the interest rate risk in terms of the impact that this risk has or would have on the possibility of the client to repay their liabilities to the bank, in accordance with the contractual terms, including determination of the impact of the interest rate risk on the bank's credit portfolio, within the regular stress-testing of the banks.

79. The bank shall, before granting the credit exposure, identify all factors that may have a significant impact on the risk of credit exposure, i.e. the client / project, taking into account the minimum criteria from item 7 of this Decision.

80. If the bank has developed internal risk categories, for the purposes of calculating the impairment, differing from the risk categories defined in item 9 of this Decision, the bank should enable their linking with risk categories provided for by this Decision and ensure their consistent application, for both granting credit exposure and its monitoring.

81. The assessment of credit risk arising from currency risk the client is exposed to, should refer at least to the monitoring, analysis and assessment of (mis)match of the currency position of the client and its impact on the client's ability to regularly repay their liabilities to the bank.

Besides the criteria defined in accordance with item 78 of this Decision, when granting and monitoring the foreign currency loans and Denar loans with FX clause, the bank shall establish and apply other criteria defined in its internal acts (e.g. quantitative limits on the share of credit exposure in foreign currency and in Denars with FX clause in the bank's credit exposure, quantitative limits on debt service-to-income, total debt-to-income and loan-to-value ratios, etc.).

Within the regular stress testing, the bank shall determine the impact of exchange rate changes on bank's loan portfolio, at least once a year, through assessment of (mis)match of the currency position of the client and its impact on the client's ability to regularly repay their liabilities to the bank.

If the client's expected foreign currency inflows, foreign currency claims and claims in Denar with FX clause cover at least 80% of their total expected foreign currency outflows, foreign currency liabilities and Denar liabilities with FX clause, the client shall be considered to have matched currency position. It shall be considered that both net exporters and clients whose price of most common product depends on movements in the price of that product on international markets also have matched currency position.

The bank shall maintain records of clients with matched and mismatched currency position.

As an exception, the bank shall not apply the provisions of this item, for clients whose overall credit exposure amounts to Denar 200,000 for natural persons and small companies, or to Denar 600,000 for other legal entities.

When granting foreign currency loans or Denar loans with FX clause, the bank shall inform the client of all risks arising from the use of such credit products, including clients referred to in paragraph 6 of this item.

The bank's Internal Audit Department shall audit the assessment of the credit risk arising from the currency risk, in accordance with the annual internal audit plan.

## **Determining impairment / special reserve**

82. In its internal acts, the bank shall be obliged to envisage the following provisions with respect to the manner of determining impairment / special reserve:

82.1 Defining credit exposures for which expected credit loss on an individual and/or on collective basis is determined, including the manner of determining of significant credit exposure and insignificant amount for non-performing credit exposures.

82.2 Detailed description of the manner of calculation of the expected credit loss on an individual basis, i.e. of the determination of expected cash flows, the assumptions on which they are based, including macroeconomic or other indicators that may have an impact on the expected cash flows.

82.3 The criteria for forming loan portfolios and a detailed description of the model for calculating the expected credit loss for credit exposures from the loan portfolio, which includes:

- method for determining the rates of probability of default and the rate of loss given default, including information on the database used in the calculation of the rates and the time period to which the data refer;
- assumptions underlying the model for determining the rates;
- determination of the macroeconomic or other indicators that may have an impact on the calculation of the expected credit loss for the appropriate loan portfolio and the manner of their inclusion in the model;
- description of the manner and dynamics of making an independent evaluation of the effectiveness of the model, defining acceptable level of deviation of the results from the evaluation and defining activities that are to be undertaken by the bank's bodies in order to harmonize the model with the results from the evaluation of its effectiveness.

82.4 Manner of including the value of the eligible collateral instrument when determining the current value of the expected cash flows, which includes:

- the procedure and rules for determining the period until the date of expected recovery of the credit exposure with the eligible collateral instrument and for determining the percentage of the reduced value (haircut) of the eligible collateral instrument that is included in the determination of the expected credit loss for non-performing credit exposures,
- the procedure for assessment of the need for reviewing the manner of determining the value of collateral and the period to the date of the expected collection of credit exposure with collateral,
- the manner of monitoring the market value of collateral (e.g. by applying statistical methods), including the manner of confirming the effectiveness of the methods that the bank uses for monitoring the market value,
- the manner of determining that there was a substantial fall in the market prices of the eligible collateral instrument;
- the documentation on the basis of which one can confirm that there is a market in which the collateral can quickly and efficiently be sold at an appropriate price that will enable recovery of credit exposure,

- the manner of determining the expected costs of recovery through collateral that will be borne by the bank.

82.5 Method for determining the expected credit loss for investments in debt securities classified and measured at fair value through the other comprehensive income.

83. The bank's Internal Audit Department shall review the determination of impairment / special reserve, including the appropriateness of the manner of determining and monitoring the market value of collateral, in accordance with the annual internal audit plan.

## **Credit file**

84. The bank shall maintain a credit file on each client / project it finances.

The credit file shall contain all data based on which the bank will be able to determine the identity, creditworthiness of the client, quality of the project, regularity of repayment of liabilities and the quality of collateral.

In the client's credit file, the bank shall also keep the entire documentation related to the process of deciding on the approval of the credit exposure or its forbearance, the analyses made for the purposes of the forbearance or determining unlikeness to pay, the analyses made for the purposes of exclusion of the credit exposure from forborne and/or non-performing credit exposure, the forced collection procedures, the court disputes, etc.

The bank may maintain a credit file for each client, i.e. project in electronic form.

## **Reporting system**

85. The bank's reporting system shall provide data and/or information at least on:
- the structure of total credit exposure, by risk category and by activity / area of relevance to the bank's credit exposure (e.g. by sector, credit product, currency, total debt-to-income and debt service-to-income ratios, type of collateral, maturity, country, etc.);
  - total credit exposure of the bank to the connected persons/entities;
  - non-performing credit exposures, the reasons that affect the most the growth of non-performing credit exposures, the total amount of excluded non-performing credit exposures, as well as the reasons for their exclusion;
  - migration of credit exposures from one risk category to another, within a specified period on an aggregate basis;
  - credit exposures approved on the basis of the exceptions defined in the bank's internal acts;
  - the assessment and the results from the evaluation of the effectiveness of the model for determining the expected credit loss on a collective basis;
  - results of stress testing;
  - forborne credit exposures;
  - written-off credit exposures and credit exposures transferred to the off-balance sheet records, referred to in item 66 paragraphs 2 and 3 of this Decision;

- the level and movements in the expected credit loss at the level of total credit exposure and by specific activities / areas (e.g. sectors, currency, maturity, etc.);
- recovered non-performing credit exposures, recovered written-off credit exposures and recovered credit exposures transferred to the off-balance sheet records (structure, amount, recovery rate, etc.);
- green finances approved;
- claims sold.

## **X. CREDIT RISK MANAGEMENT ON A CONSOLIDATED BASIS**

86. Any bank subject to consolidated supervision shall apply this Decision on both individual and consolidated basis, at a level of the banking group.

87. The bank subject to consolidated supervision shall be obliged to ensure observance of the provisions of this Decision by all members of the banking group, and especially in terms of ensuring consistent application in the manner of defining and determining the forborne and non-performing credit exposures and the conditions for exclusion from these categories, defined in this Decision.

When assessing the unlikeness to pay of the client in accordance with item 54 of this Decision, the bank subject to consolidated supervision takes into account also the fact whether some member of the banking group submitted a proposal for opening a bankruptcy or other similar procedure against the client, in accordance with the law.

## **XI. REPORTING TO THE NATIONAL BANK**

88. The banks shall compile a report on the implementation of this Decision according to the accounting value at the end of each month and shall submit it to the National Bank.

The reporting deadline shall be 15 days after the expiration of the reporting period.

Notwithstanding paragraph 2 of this item, the reporting deadline as at 31 December shall be five working days after the deadline for submission of unaudited annual financial statement.

89. The bank shall report to the National Bank also on:

- the forbearance of the credit exposure considered to be large exposure in accordance with the Banking Law;
- the restructuring of the credit exposure with significant modification in the contractual terms;
- the write-off of the credit exposure, fully or partially, performed in accordance with item 66 paragraph 2 of this Decision,
- the mandatory transfer of credit exposures to the accounts for off-balance sheet records performed in accordance with item 66 paragraph 3 of this Decision;
- the prepared operational plan for taking activities for reduction of non-performing credit exposures;
- the deviation from the goals set in the operational plan for reduction of non-performing credit exposures;

- the assessment and the results from the evaluation of the effectiveness of the model for determining the expected credit loss on a collective basis;
- the sale of due, non-performing or written-off claims;
- green finances approved, and
- the recovery of the credit exposures that have previously been written-off in accordance with item 66 paragraph 2 and 3 of this Decision.

The deadline for submission of the notification referred to in paragraph 1 indents 1, 2, 3, 5, 6 and 7 of this item shall be ten days after: the decision for credit exposure forbearance, the decision to restructure the credit exposure with significant modification in the contractual terms, the decision to write off the credit exposure (fully or partially), the development of the operational plan for undertaking activities for reduction of non-performing credit exposures, the deviation from the goals set in the operational plan for reduction of non-performing credit exposures and the assessment and the results from the evaluation of the effectiveness of the model for determining the expected credit loss on a collective basis.

Notwithstanding paragraph 2 of this item, the bank shall submit an aggregate report on the performed write-offs of individually insignificant credit exposures referred to in item 66 paragraph 2 indent 4 of this Decision on a monthly basis.

The bank shall submit reports on the credit exposures transferred to the accounts for the off-balance sheet records referred to in paragraph 1 indent 4 of this item, the claims sold referred to in paragraph 1 indent 8 of this item, for the green finances approved referred to in paragraph 1 indent 9 of this item and for the collection of previously written-off credit exposures referred to in paragraph 1 indent 10 of this item on a monthly basis.

The reports referred to in paragraphs 3 and 4 of this item shall be submitted to the National Bank in accordance with item 88 paragraphs 2 and 3 of this Decision.

90. On special request of the National Bank, the bank shall compile a report as of another date and within another deadline different from the date and the deadline specified in items 88 and 89 of this Decision.

## **XII. TRANSITIONAL AND CLOSING PROVISIONS**

91. The Governor of the National Bank shall prescribe, with Instructions, the manner of and the procedure for submission of the report on the implementation of this Decision referred to in items 88 and 89 of this Decision, as well as the form and content of the forms.

92. The provisions of this decision that refer to banks shall apply to savings houses accordingly.

Foreign bank branches shall apply the provisions of this decision, taking into account the provisions of the Banking Law and bylaws derived from this law that regulate the operation of foreign bank branches in the Republic of North Macedonia.

93. The bank shall prepare the first report of item 88 paragraph 1 of this Decision, with the effect of the application of the new definition of non-performing credit exposures to the credit exposures, as at 31 January 2024 and shall submit it to the National Bank not later than the deadline specified in item 88 paragraph 2 of this Decision. The bank shall apply the new definition of non-performing credit exposures to the clients / credit exposures as of 1 January 2024 whose due amount is above the materiality threshold during the entire period from 1 October 2023 to 1 January 2024.

94. The implementation of this Decision shall supersede the Decision on the methodology for credit risk management (Official Gazette of the Republic of Macedonia No. 149/18 and Official Gazette of the Republic of North Macedonia No. 76/20, 116/20 and 83/22).

95. This Decision shall enter into force on the eighth day following that of its publication in the Official Gazette of the Republic of North Macedonia, and shall apply from 1 January 2024.

Notwithstanding paragraph 1 of this item, the provisions of item 77 sub-item 77.11 of this Decision shall apply from 1 January 2025.

**D No. 02-6835/6**  
**27 February 2023**  
**Skopje**

**Ana Mitreska**  
**Vice Governor and Chairman**  
**of the National Bank of the**  
**Republic of North Macedonia Council**