

Pursuant to Article 15, paragraph 1 of the Law on the National Bank of Serbia (RS Official Gazette, Nos 72/2003, 55/2004 and 44/2010), and with reference to Article 28, paragraph 7 and Article 31, paragraph 3 of the Law on Banks (RS Official Gazette, Nos 107/2005 and 91/2010), the Executive Board of the National Bank of Serbia hereby issues the following

## **DECISION ON THE CLASSIFICATION OF BANK BALANCE SHEET ASSETS AND OFF-BALANCE SHEET ITEMS**

### **Introductory provisions**

1. This Decision specifies the balance sheet assets and off-balance sheet items subject to classification and the criteria for the classification of bank exposures, for the purpose of adequate and efficient management of credit risk that a bank is exposed to in its operation.

Bank exposures subject to classification as determined herein shall be balance sheet assets from Section 3, paragraph 1 and off-balance sheet items from Section 4, paragraph 1 of this Decision.

2. For the purposes hereof, the following terms have the following meaning:

1) *materially significant amount* is an amount higher than 1% of a single account receivable of the bank, but not lower than 10,000 dinars in case of a natural person borrower or 50,000 dinars in case of a legal person borrower;

1a) *financial difficulties* are difficulties experienced or about to be experienced by the borrower in repayment of its obligations which are assessed at the level of the borrower and/or of a group of borrowers within the scope of consolidation for the purpose of compiling consolidated financial statements if the borrower belongs to a group of related persons;

2) *forbearance* is the granting, due to the borrower's financial difficulties, of concessions relating to repayment of an individual exposure, which would not have been granted had the borrower not been experiencing such difficulties, regardless of whether any given amount of such exposure has matured, whether such exposure has been found impaired or whether default occurred in respect of such exposure in accordance with the decision governing bank capital adequacy, in at least one of the following ways:

– by changing the terms under which the exposure occurred, particularly if such subsequently agreed terms of repayment are more favourable than the initial terms (reduction of the interest rate, write-off of a

part of principal entailing a de-recognition of such part in the balance sheet, write-off of a part of accrued interest, change in the maturity date of principal and/or interest, etc.) or than the terms which would have been approved to another borrower with the same or similar risk profile at that time;

- by refinancing the exposure;

3) *residential real estate property* is a house, an apartment and parts of a residential building intended for dwelling, a garage or a garage place associated with an apartment, as well as a plot of land with a building permit for house construction; vacation homes shall not be considered residential real estate property;

4) *authorised valuer* is a person who, in line with the law governing the profession of real estate valuers, is authorised to perform the valuation of real estate, as well as a body which, in line with the law governing tax proceedings and tax administration, is competent for conducting tax proceedings; this person shall not be a person related to the borrower in the manner set forth by the Law on Banks and shall not be involved in the process of loan approval or sale of real estate;

5) *market value of real estate* is the estimated amount for which the property should exchange on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction wherein the parties had each acted knowledgeably, prudently and without compulsion; this value shall be transparently and clearly documented and shall be determined by an authorised valuer;

6) *entrepreneur* is a natural person registered in accordance with the law governing the registration of business entities;

7) *farmer* is a natural person – holder or member of an agricultural joint household within the meaning of the law on agriculture and rural development;

8) *probation period* is a period of minimum two years from the date the forborne exposure is classified as performing;

9) *refinancing of exposures* means the occurrence of a new bank exposure in respect of a loan approved by a bank to ensure total or partial repayment of the borrower's obligation to the bank or to another legal person to which the exposure to such borrower has been assigned;

10) *materially significant portion of total debt* is the amount of at least 6% of principal of a housing loan exposure with changed terms of repayment or an exposure that refinanced the bank's housing loan exposure and/or 8% of principal of an exposure in case of other exposures.

2a) *A non-performing loan* means the stock of the total outstanding debt under individual loans (including the amount of arrears):

- where the payment of principal or interest is past due over 90 days, in accordance with the provisions of this Decision,

- where 90 days (and more) of interest payments have been attributed to the loan balance, capitalized, refinanced or delayed,
- where payments are less than 90 days overdue, but the bank assessed that the borrower's repayment ability has deteriorated and doubts that the payments will be made in full.

### **Balance sheet assets and off-balance sheet items subject to classification**

3. Balance sheet assets to be classified within the meaning hereof shall include:

- due and undue short- and long-term loans;
- deposits with banks;
- interest and fees;
- long- and short-term securities not included in the trading book;
- bank's participation in the capital of other legal persons, except participation deductible from capital pursuant to the decision governing bank capital adequacy;
- assets acquired through collection of receivables in accordance with Section 21a, paragraphs 4 and 5 of this Decision;
- balance sheet assets included in the trading book in respect of which no capital charges are calculated by the bank for market risks within the meaning of the decision governing bank capital adequacy;
- other balance sheet assets, except balance sheet assets specified in paragraph 2 hereof.

The following balance sheet assets shall not be subject to classification:

- vault cash, gyro-account balances, gold and other precious metals;
- exposures to governments and central banks assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- exposures to territorial autonomies and local government units assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- exposures to public administrative bodies assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- exposures to international development banks and international organisations assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- fixed assets, investment property and intangible investments;
- assets acquired through collection of receivables where conditions under Section 21a, paragraphs 1–3 of this Decision are met;
- unpaid subscribed share capital;
- own shares;

- bank's participation in the capital of other legal persons constituting a deductible from capital pursuant to the decision governing bank capital adequacy;
- stocks;
- balance sheet assets included in the trading book, in respect of which the bank must calculate capital charges for market risks within the meaning of the decision governing bank capital adequacy.

4. Off-balance sheet items to be classified within the meaning hereof shall include:

- payment and performance guarantees issued,
- avals and bill acceptances,
- other forms of warranties,
- uncovered letters of credit,
- contingent liabilities,
- other off-balance sheet items in respect of which the bank may have to make payment.

The following off-balance sheet items shall not be subject to classification:

- exposure to governments and central banks assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- exposure to territorial autonomies and local government units assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- exposure to public administrative bodies assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- exposure to international development banks and international organisations assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- off-balance sheet items included in the trading book in respect of which the bank must calculate capital charges for market risks within the meaning of the decision governing bank capital adequacy;
- other off-balance sheet items not payable by the bank.

***Methodology for the assessment of balance sheet asset impairment and probable losses on off-balance sheet items***

5. A bank shall determine by its acts the methodology for the assessment of balance sheet asset impairment and probable losses on off-balance sheet items, i.e. recognition and measurement of expected credit losses (hereinafter: methodology), in accordance with the International Accounting Standards and/or International Financial Reporting Standards.

6. In its methodology, a bank shall:

- establish the procedures for the assessment of balance sheet asset impairment and/or probable losses on off-balance sheet items, as well as competences, obligations and responsibilities in that process;
- determine the methods and techniques for assessment of impairment at individual and collective level;
- establish models used for measurement of expected credit losses, including the measurement of impairment in case there is objective evidence of impairment;
- establish criteria for the classification of exposures into groups of exposures with similar characteristics for the purposes of assessment of existence of a significant increase in the credit risk and the amount of expected credit losses at collective level;
- establish procedures based on which to assess whether a significant increase in the credit risk of balance sheet assets and off-balance sheet items took place on the reporting date relative to the date of initial recognition;
- determine the definition of the default status of obligations used to determine changes in the default risk relative to the date of initial recognition of balance sheet assets and off-balance sheet items;
- establish the methods to determine whether balance sheet assets and off-balance sheet items have a low credit risk on the reporting date;
- establish criteria for the classification of balance sheet assets and off-balance sheet items by levels of impairment in the manner defined by the International Financial Reporting Standard 9 – Financial instruments (hereinafter: IFRS 9), including the criteria for the transfer of exposure from one level of impairment to another;
- make sure that all analyses, assessments and other procedures in the process of assessing balance sheet asset impairment and probable losses on off-balance sheet items are clearly explained and documented;
- make sure that the assessment of balance sheet asset impairment and probable losses on off-balance sheet items is based on accurate and current data, and that it takes into account all reasonable and substantiated information on past events, current circumstances and forecasts of future economic conditions, which is available without undue costs and burdens on the reporting date.

The moment when a bank determines that there is objective evidence of impairment, i.e. that the default status occurred in accordance with the definition under paragraph 1, indent 6 of this Section cannot be at the same time determined as the moment of a significant increase in the credit risk of balance sheet assets and off-balance sheet items relative to the day of initial recognition, within the meaning of indent 5 of that paragraph.

7. A bank shall apply the methodology consistently, and shall review it at least once a year, and if necessary more often, adjust the methodology and its underlying assumptions.

8. At least quarterly, a bank shall assess the quality of exposures, determine whether there is any objective evidence of impairment, and calculate an adequate amount of that impairment.

At least quarterly, a bank shall assess whether there has been a significant increase in the credit risk relative to the day of initial recognition and shall calculate the adequate amount of impairment in respect of expected credit losses.

9. In calculating the amount of impairment of balance sheet assets and probable losses on off-balance sheet items, a bank may take into account cash flows deriving from collateral instruments that secure the exposures.

In its methodology, the bank shall determine collateral instruments to be taken into account within the meaning of paragraph 1 hereof, the manner of determining their value, and the expected period within which they will be cashed in.

10. Objective evidence of impairment of balance sheet assets shall be evidence of one or more events that occurred and had a negative effect on estimated future money flows based on such assets.

In its methodology, the bank shall determine the circumstances whose occurrence will imply the existence of objective evidence of balance sheet impairment.

### **Classification criteria**

20. A bank shall classify all exposures to a borrower, except exposures referred to in Section 3, paragraph 2 and Section 4, paragraph 2 hereof, in categories A, B, C, D and E based on the following criteria: timeliness and/or delay in the performance of obligations to the bank, assessment of the borrower's financial position and/or creditworthiness, and quality of the collateral.

21. Exposures shall be classified as set out below:

1) category A:

- exposures to a borrower with whom no collection-related problems are expected based on assessment of its financial position and/or creditworthiness,
- exposures secured by prime collateral, subject to Section 28, paragraph 3 hereof,

- exposures to a borrower who performs its obligations on time or with a delay of no more than 30 days;

2) category B:

- exposures to a borrower whose financial position, and/or creditworthiness is not fully satisfactory due to certain problems in operation, but does not suggest major deterioration in the future,

- 31 to 60 days past due exposures;

3) category C:

- exposures to a borrower whose financial position and/or creditworthiness is not satisfactory and suggests deterioration in the future,

- 61 to 90 days past due exposures;

4) category D:

- exposures to a borrower whose financial position and/or creditworthiness indicate significant collection-related problems – primarily exposures to a borrower that is illiquid or insolvent,

- 91 to 180 days past due exposures;

5) category E:

- doubtful or disputable exposures,
- exposures to a borrower in liquidation or bankruptcy,
- exposures to a borrower failing to act on the adopted reorganization plan as defined by the law governing bankruptcy,

- over 180 days past due exposures,

- exposures ineligible for classification in other categories from this Section,

- exposures to a borrower to which the bank had due exposures but had assigned them in the prior three years,

- exposures to a borrower – natural person (other than farmers and entrepreneurs) whose debt-to-income ratio, determined in accordance with Section 26, paragraph 1, indent 1 hereof, exceeds 60%.

21a. Property acquired through collection of receivables (foreclosure) shall not be classified during the period of three years following the maturity date of those receivables established in accordance with Section 23 hereof, provided the following conditions are met:

- that at the moment of acquisition the bank has an appraisal of the property's market value which is not older than a year;

- that the bank has the market value of the acquired property assessed at least once a year during the above period.

By way of exception to paragraph 1 hereof, if the bank acquired the assets referred to therein before the maturity date of the receivables in question, the period from that paragraph shall be calculated as of the date of acquisition of those assets.

Other assets acquired through collection of receivables shall not be classified during a one-year period following the date of acquisition provided that at the moment of acquisition the bank has an appraisal of their market value which is not older than a year.

The assets from paragraphs 1 and 3 hereof where the conditions from those paragraphs are not met shall be classified in category E.

The assets from paragraphs 1 and 3 hereof that the bank has neither alienated nor put to use in its business operations within the periods specified in those paragraphs shall be classified in category E.

Putting assets to use in its business operations referred to in paragraph 5 hereof means that the bank is using them as fixed assets or as investment property.

21b. Exposures to a borrower, other than a newly founded company, to which the bank assigned exposures shall be classified in accordance with the classification criteria set out in Section 20 hereof provided the following conditions are met:

- that at the moment of assignment the borrower to which the bank is assigning exposures is not past due on its obligations for more than 60 days;
- that the assessment of the financial position of the borrower assignee, which covers, inter alia, assessment of the impact of the assignment on the classification of exposures to that borrower and which is made based on the financial indicators prescribed by this Decision and the criteria for the assessment of financial position prescribed by the bank's internal acts, as well as based on the borrower's end-year financial statement and periodic financial statements during the one-year period prior to the assessment date – shows that following the assignment the borrower will be able to settle its obligations to the bank on time;
- that during the one-year period following the assignment of exposures the borrower settles its obligations to the bank on time, and/or with a delay of no more than 60 days.

Exposures to the borrower referred to in paragraph 1 hereof where the conditions stipulated in that paragraph are not met shall be classified in category E.

Exposures to the borrower to which the bank approved the loan by which it indirectly or directly settled a part or the entire amount of a loan approved by that bank considered non-performing within the meaning of this Decision, except for exposures to the borrower – newly founded company



within the meaning of Section 25 of this Decision, shall be classified in accordance with the criteria for classification referred to in Section 20 of this Decision if the following conditions are met:

- that at the moment of loan approval the borrower is not past due for more than 60 days under any loan approved by that bank;
- that the assessment of the financial position of the borrower to which the loan was approved, which was made based on financial indicators prescribed by this Decision and the bank's criteria for the assessment of financial position prescribed by the bank's internal acts, as well as based on the borrower's end-year financial statement and periodic financial statements during the one-year period prior to the assessment date – shows that following the approval of this loan the borrower will be able to settle its obligations to the bank on time;
- that during the one-year period following the approval of the loan the borrower settles its obligations to the bank on time or with a delay of no more than 60 days.

Exposures to the borrower referred to in paragraph 3 hereof where the conditions stipulated in that paragraph are not met shall be classified in category E.

Exposures to the borrower – newly founded company within the meaning of Section 25 of this Decision to which the bank assigned the exposure shall be classified in category E.

Exposures to the borrower – newly founded company within the meaning of Section 25 of this Decision to which the bank approved the loan by which it indirectly or directly settled a part or the entire amount of a loan approved by that bank considered non-performing within the meaning of this Decision shall be classified in category E.

Exposures to the borrower – newly founded company within the meaning of Section 25 of this Decision which is, within the meaning of the Law on Banks, considered a person related to the borrower to which the bank approved a loan considered non-performing shall be classified in category E.

21c. Forborne exposures considered performing by the bank, in accordance with Section 35f, paragraph 3 of this Decision, may not be classified in a category above the category in which they were classified at the forbearance date, and/or in which they would have been classified at such date, pending fulfilment of the conditions from paragraph 1 of that Section.

Forborne exposures considered non-performing by the bank, in accordance with Section 35f, paragraph 4 of this Decision, may not be

classified in a category above category D or E (depending on the classification conditions met at the forbearance date), pending fulfilment of the conditions from Section 35d of this Decision, whereafter they may only be classified in a category which is not above category C, pending fulfilment of the conditions from Section 35f, paragraph 1 of this Decision.

If, simultaneously with or close in time, before or after, to the occurrence of a bank's exposure, the borrower makes payments of principal or interest in respect of another bank exposure which, at the time of such payment, was classified into category E, such new exposure may not be classified into a category above category E pending fulfilment of the conditions from Section 35d of this Decision, whereafter such exposure may only be classified in a category which is not above category C, pending fulfilment of the conditions from Section 35f, paragraph 1 of this Decision.

If the forborne exposure which is considered non-performing and has as such been classified into category D is re-forborne, such exposure may not be classified into a category above category E, pending fulfilment of the conditions from Section 35d of this Decision, whereafter it may only be classified in a category which is not above category C, pending fulfilment of the requirements from Section 35f, paragraph 1 of this Decision.

By way of exception to paragraph 4 of this Section, the exposure referred to in that paragraph shall not be classified into category E if it has been re-forborne in one of the following ways:

- pursuant to the law regulating consensual financial restructuring of companies;
- based on concluding an annex to the contract on a Swiss-franc indexed housing loan, pursuant to the decision on measures for preserving financial system stability in the context of foreign currency-indexed loans.

22. All exposures to a single borrower, except exposures secured as set out in Sections 28 and 29 hereof, shall be classified in one and the same category, i.e. the lowest category in which any of the exposures to that borrower is classified.

By way of exception to paragraph 1 hereof, doubtful and disputable exposures shall not determine the classification category of other exposures.

#### *Borrower's timeliness in the settlement of obligations*

23. Delay in the collection of receivables shall be calculated as of the latest agreed maturity date – this applies to the materially significant amount of exposures.

The assignment of exposures to another bank shall not affect the assignee bank's classification of those exposures according to the criterion of timeliness.

*Assessment of the borrower's financial position and creditworthiness*

24. By its internal acts, a bank shall regulate the procedures for the assessment of the borrower's financial position and creditworthiness, as well as the criteria and the manner of classification of exposures in categories from Section 21 of this Decision by taking into account the assessment in question and the documentation referred to in Section 30 of that Decision.

In regulating the procedures and criteria from paragraph 1 hereof, a bank shall also take into account the borrower's timeliness in settlement of obligations towards the bank over the past twelve months, stipulating however that bank exposures to a borrower who settled its obligations in the last twelve months with a delay of more than 90 days may not be classified in a category above category C.

25. A bank shall make an assessment of the financial position of a legal person borrower based in particular on the analysis of:

- profitability indicators;
- adequacy of the maturity structure of certain components of assets and liabilities;
- adequacy of cash flows from the aspect of debt servicing;
- financial structure indicators, notably the level of indebtedness;
- borrower's exposure to the foreign exchange-induced credit risk;
- business sector in which the borrower operates, the borrower's market position, borrower-specific features and other relevant indicators.

By way of exception to paragraph 1 hereof, the bank shall not be required to make an assessment of the financial position of banks if such banks have been assigned, under the decision on capital adequacy, credit quality step 3 or better.

By way of exception to paragraph 1 hereof, assessment of the financial position of a borrower founded during the two years preceding the date of classification (newly founded companies), as well as of a borrower founded for a special purpose, and/or implementation of a pre-determined project (project financing), shall be made in relation to the borrower's capacity to generate adequate cash flows that will ensure timely settlement of obligations in accordance with the agreed repayment schedule, the assessment being made in accordance with the bank's internal acts from Section 24 hereof.

The assessment from paragraph 3 hereof shall be made based on at least:

- analysis of the cost-effectiveness of investment for which funding was approved, and/or assessment of future cash flows generated by that investment (business plan, financial projections, estimate of the investment repayment period, analysis of project sensitivity to risk, etc.) in case of newly founded companies;
- analysis of the cost-effectiveness of the project for which funding was approved, and/or assessment of future cash flows generated by the project (business plan, financial projections, estimate of the investment repayment period, analysis of project sensitivity to risk, etc.), as well as on-going monitoring of project implementation in case of project financing.

Exposures to newly founded companies, as well as exposures arising from project financing, may not be classified in a category above category C – if the future cash flows are estimated as inadequate in respect of obligations to the bank during any settlement period, as well as in case of any major departure from the initial business plan, and/or planned implementation of the project during the repayment of exposures.

26. Assessment of the creditworthiness of a natural person borrower (other than farmer or entrepreneur) shall be performed based in particular on the analysis of:

- debt-to-income ratio, determined as the ratio of total monthly credit obligations and regular net monthly income, which ratio the bank shall determine when approving the loan, as well as thereafter in accordance with the manner and dynamics defined in its internal act;
- the currency structure of the borrower's total monthly credit obligations, particularly taking into account higher risk exposure of a borrower whose obligations are contracted in foreign currency or in dinars with a foreign currency clause.

Total monthly credit obligations referred to in paragraph 1 hereof shall be the sum total of obligations in respect of loans – including loans under transaction accounts (overdrafts under transaction accounts) and obligations in respect of credit cards (monthly obligation of the total extended loan under a card) – loan warranties called and obligations under financial lease contracts. The bank may, however, in accordance with its internal acts, include in total monthly credit obligations some other obligations of the person from that paragraph.

#### *Quality of the collateral*

27. For the purposes hereof, collateral for the bank's exposures may, in terms of quality, be either prime or adequate.

28. Prime collateral shall include:

- cash deposit with a bank – provided it was agreed that such deposit would serve as collateral for certain exposures of the bank, as well as that its maturity matches the maturity of the corresponding exposures and that only the bank may dispose thereof;
- debt securities, as well as guarantees, other type of warranties, counter-guarantees and other similar instruments of unfunded credit protection issued by governments and central banks and assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- debt securities, as well as guarantees, other type of warranties, counter-guarantees and other similar instruments of unfunded credit protection issued by territorial autonomies and local government units and assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- debt securities, as well as guarantees, other type of warranties, counter-guarantees and other similar instruments of unfunded credit protection issued by public administrative bodies and assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- debt securities, as well as guarantees, other type of warranties, counter-guarantees and other similar instruments of unfunded credit protection issued by international development banks or international organisations and assigned a 0% credit risk weight pursuant to the decision governing bank capital adequacy;
- debt securities, as well as guarantees, other type of warranties, counter-guarantees and other similar instruments of unfunded credit protection issued by banks and allocated credit quality step 3 or better pursuant to the decision on capital adequacy;
- gold pledge.

Unfunded credit protection instruments, referred to in paragraph 1 hereof, shall be instruments used by a bank to mitigate its risk exposure, the mitigating impact arising from the obligation of a third party to make payment of a certain amount to the bank in the event of the borrower's default or occurrence of any other contracted event or circumstances which entitle the bank to employ the instruments.

Exposures secured by prime collateral from paragraph 1 hereof may be classified, up to the amount secured, in category A provided that:

- all requirements are met for the recognition of credit protection prescribed by the decision governing bank capital adequacy relating to the collateral;
- the borrower settles its obligations with a delay of no more than 90 days;

– the collateral issuer is not in bankruptcy, and/or the collateral issuer acts in accordance with the adopted plan of reorganization as defined by the law governing bankruptcy.

29. Adequate collateral shall include:

1) property mortgage provided:

– the mortgage is valid under the governing law and entered in the land books, cadastre or other appropriate register, and that the contractual provisions and the use of appropriate legal procedure ensure settlement of debt from the value of mortgaged property within a reasonable period of time,

– the bank regularly monitors the value of real estate property and, except in the case of mortgaged residential real estate property where the amount of the outstanding bank exposure does not exceed 40% of its value less the sum of all higher priority claims over such property, determines the market value of such property at least once every three years, or more often in the event of significant changes in property market conditions or physical changes to the property,

– the bank has prescribed in its policies, procedures and other internal acts the type of property eligible as collateral, as well as the terms and conditions of granting mortgage-secured loans,

– the bank has established clear and comprehensive procedures for monitoring and verification of the adequacy of insurance against the risk of damage to the property mortgaged,

– the financial position, and/or creditworthiness of the borrower is not significantly dependent on the value of mortgaged property or cash flows deriving from its use, but rather on the borrower's capacity to repay its debt from other sources of income,

– the value of mortgaged property is not significantly dependent on the borrower's financial position, and/or creditworthiness, without taking into account the macroeconomic factors affecting both the value of the property and the financial position, and/or creditworthiness of the borrower,

– the borrower settles its obligations secured by the mortgage with a delay of no more than 720 days,

– the owner of mortgaged property is not in bankruptcy, and/or the owner of mortgaged property acts in accordance with the adopted plan of reorganization as defined by the law governing bankruptcy,

– in relation to forborne exposures secured by such mortgage, the bank did not grant additional concessions pending fulfilment of the conditions for the bank to stop considering such exposures as non-performing and forborne,

– the market value of mortgaged property, less the sum of all higher priority claims over that property, is not lower than the total value of bank receivables;

2) pledge of warehouse receipt provided:

- the pledge was established in accordance with the law governing public warehouses for agricultural commodities,
- the value of exposures is not higher than the market value of stored agricultural commodities for which the warehouse receipt was issued, less the storage costs, and/or the value of exposures is not higher than the compensation amount specified in the insurance contract to which the bank is entitled in the event of destruction of those commodities,
- the maturity of exposures is no longer than the expiration date of warehouse receipt,
- the borrower settles its obligations secured by the pledge with a delay of no more than 180 days;

3) pledge of livestock that is marked and registered in accordance with the law on veterinary medicine, provided:

- that the pledge is established and entered into the register of pledges in accordance with the law governing the right of pledge over registered movables and that the bank is entered as the first priority creditor under that pledge, as well as that the contractual provisions and the use of appropriate legal procedure ensure the settlement of obligations from the value of the pledge object within reasonable time,
- that the pledge object is insured and that the insurance policy provides cover to the bank for at least the risk of death due to illness or accident, emergency slaughter and/or slaughter for economic reasons,
- that the value of the exposures does not exceed the market value of the pledge object, and/or that it does not exceed the compensation amount specified in the insurance contract in the event of destruction of the pledge object,
- that the bank regularly monitors changes in the market value of the pledge object and determines it in accordance with the dynamics envisaged by its internal acts, but no less than once a year,
- that the borrower settles its obligations secured by the pledge with a delay of no more than 90 days.

In case of residential real estate property, in addition to conditions set out in paragraph 1, provision 1) of this Section, the following condition must be met: the owner of the property is living in the property or has a lease agreement signed with the tenant (or intends to live in it or to let it out on lease).

Regular monitoring of the value of real estate property from paragraph 1, provision 1), indent two of this Section means verification of such value on the basis of available data and information, including the use of statistical models, where the bank must conduct this verification at least once a year for

commercial real estate property and at least once every three years for residential and other real estate property.

The bank's exposures secured by adequate collateral may be classified one category above the category they would have been classified in otherwise.

*Borrower's credit file*

30. In its internal acts, the bank shall define procedures for establishing and continuous updating of credit files for each borrower.

The credit file should contain complete and accurate data needed to determine the borrower's financial position, and/or creditworthiness, and to assess the likelihood of collection of receivables and the quality of collateral, these data including in particular:

- documentation on the borrower's status (for a legal entity – excerpt from the register of business entities, for a natural person – photocopy of ID card or a form completed with data extracted from the electronic ID card, and/or passport, for an entrepreneur – excerpt from the register of business entities or a decision on setting up a business, for a farmer – excerpt from the register of agricultural households);
- assessment of the borrower's financial position and creditworthiness, including analysis of its exposure to foreign exchange risk;
- financial statements of the borrower for the two reporting periods preceding the date of occurrence of exposures, as well as for all reporting periods until full settlement of such exposures, including auditor's report for the borrowers for which such report is legally mandated, with the exception of borrowers in the initial stages of their operations;
- documentation on the settlement of obligations to the bank in the preceding twelve months, except for the new borrowers of the bank;
- report from the database on the borrower's total credit obligations and/or indebtedness and timeliness in settlement of obligations;
- bank's decisions on loan approval and other accounts receivable, as well as decisions on amendments to the terms and conditions thereof, if any;
- contract documentation relating to the borrower;
- data on the classification of exposures to the borrower at the moment of their occurrence and thereafter;
- correspondence and other documents proving contact between the bank and the borrower in connection with the exposure;
- documentation regarding collaterals used to secure exposures, which serves to prove compliance with the conditions set out in Sections 28 and 29 hereof;



– documentation relating to the collection of receivables and any action taken by the bank for the purpose of their collection.

In the event of assignment of exposures to another bank, the assignor bank shall submit the documentation from paragraph 2, indent 4 of this Section to the assignee bank.

If a bank assigns its exposures to a borrower to another bank, that borrower shall not be considered a new borrower of the assignee bank within the meaning of paragraph 2, indent 4 of this Section.

File on a borrower being a local government unit or organization of mandatory social insurance shall contain data specified in paragraph 2 of this Section, a copy of the decision to borrow as defined by the law on public debt, as well as bank analysis of the cost-effectiveness of investment for which funding was approved (business plan, financial projections, assessment of the investment repayment period and the analysis of project sensitivity to risk).

The borrower's financial statements referred to in paragraph 3 of this Section constitute an integral part of the rulebook on the manner of preparing, compiling and submitting final accounts of budget beneficiaries, and users of budgetary funds of the Republic of Serbia and local authorities.

File on a borrower – entrepreneur or farmer shall contain data from paragraph 2 of this Section, except data referred to in indent 3 of that Section, as well as evidence of the settlement of taxes over the preceding twelve months which the borrower is liable to pay as a tax obligor within the meaning of the law governing personal income tax. File on an entrepreneur paying lump-sum tax on revenues from self-employment as defined by the said law shall also contain data on the turnover recorded in the preceding twelve months, while files on entrepreneurs and agricultural producers using single-entry bookkeeping shall also contain the profit and loss account, and files on entrepreneurs and agricultural producers using double-entry bookkeeping shall also contain the balance sheet and the profit and loss account for the prior business year.

By way of exception to paragraph 7 hereof, the file on a borrower agricultural producer who is not a tax obligor within the meaning of the law governing personal income tax shall contain the data under paragraph 2 hereof, except data under indent 3 thereof, as well as evidence on the payment of contributions for pension and disability insurance and health insurance in accordance with the law governing the system of mandatory pension and disability insurance and mandatory health insurance.

File on a borrower natural person (other than farmer or entrepreneur) shall contain data from paragraph 2 of this Section, except data specified in indent 3 of that Section, as well as evidence of employment and earnings or pension income of such borrower in the preceding three months, issued and certified by the employer (pay slip), together with the borrower's statement confirming that they may be used for verification of tax and contribution payments, or data from the bank's records on the crediting of salary and/or pension to the borrower's account for that period, and, if the borrower is a tax obligor within the meaning of the law governing personal income tax, the file shall also contain data on the annual earnings of an employee and the liabilities set in relation to income tax and contributions to be paid therefrom.

To ensure adequate credit risk management, the bank shall determine in its internal acts the frequency of updating the borrower's credit file from paragraph 8 of this Section following loan approval and/or during loan repayment, which shall be at least once every three years or more often in the event of significant changes in the circumstances affecting the borrower's creditworthiness (e.g. a significant rise in the exchange rate, delay in repayment, etc.).

31. Any exposures to borrowers for which updated and complete data referred to in Section 30 hereof are not available to the bank shall be classified in category E, except when the partially incomplete or not updated data are less significant for determining the borrower's financial position, and/or creditworthiness and assessment of the collectability of receivables, in which case exposures to such borrowers shall be classified one category below the category in which they would have been classified otherwise.

By way of exception to paragraph 1 hereof, exposures to a natural person borrower for whom up-to-date data under Section 30 hereof are not available to the bank shall be classified one category below the category in which they would have been classified otherwise.

### **Reporting on classification**

35. The bank shall submit to the National Bank of Serbia quarterly reports on the amount and classification of its balance sheet assets and off-balance sheet items, on the forms prescribed by the decision governing reporting requirements for banks and the decision governing bank reporting on capital adequacy.

### **Classification for the purpose of additional asset quality monitoring**

35a. To monitor asset quality, the bank shall classify its balance sheet assets and off-balance sheet items from paragraphs 2 and 3 of this Section

(hereinafter: exposures) either in the group of non-performing exposures or in the group of performing exposures, with each of these groups also including a sub-group of forborne exposures.

Balance sheet assets classified for the purposes referred to in paragraph 1 of this Section include all debt instruments recorded in the balance sheet (due and undue short-term and long-term loans, other placements, deposits with banks, balances in accounts with the National Bank of Serbia, interest and fees, long- and short-term securities not included in the trading book and other debt instruments recorded in the balance sheet), other than instruments held for trading.

Off-balance sheet items classified for the purposes referred to in paragraph 1 of this Section include issued payment and performance guarantees, avals and bill acceptances, other forms of warranties, contingent liabilities, uncovered letters of credit and other off-balance sheet items in respect of which the bank may have to make payments, where only contingent liabilities may be classified as forborne exposures.

35b. The bank shall classify the exposures from Section 35a, paragraph 1 of this Decision as non-performing exposures if one of the following conditions has been met:

- the borrower is more than 90 days past due on such exposure,
- the bank's assessment of the borrower's financial position and/or creditworthiness indicates that the borrower will not be able to settle its obligations in full without realisation of collateral, regardless of whether the borrower meets its obligations timely or not;
- default on obligations has occurred, in accordance with the decision governing bank capital adequacy;
- an exposure is considered impaired in accordance with the IFRS 9 and is classified into Stage 3 by applying the criteria established in Section 6, paragraph 1, indent 8 of this Decision.

An exposure which is considered impaired in accordance with the IFRS 9, but is not classified into Stage 3 by applying the criteria established in Section 6, paragraph 1, indent 8 of this Decision shall be classified by a bank into the group of non-performing exposures if one of the conditions under paragraph 1, indents 1–3 of this Section is met.

The exposure from Section 35a, paragraph 1 of this Decision which does not meet any of the conditions from paragraph 1 of this Section, and the previously classified non-performing exposure which is not forborne but no longer meets any of the conditions from that paragraph, shall be classified as performing.

The following off-balance sheet items from Section 35a, paragraph 3 of this Decision shall be classified in the group of non-performing exposures, in their nominal amount:

- irrevocable commitments – if their withdrawal by the borrower would result in the occurrence of an exposure which the bank considers, on the basis of assessment of the borrower's financial position and/or creditworthiness, will not be settled in full without realisation of collateral;
- guarantees issued – if they are likely to be activated and in particular if the guarantee secures an exposure eligible to be considered non-performing.

35c. If a particular exposure to a borrower is classified in the group of non-performing exposures, the bank shall classify all exposures to such borrower in such group.

By way of exception to paragraph 1 of this Section, the classification of exposures in respect of fees in the group of non-performing exposures does not determine the classification of other exposures.

By way of exception to paragraph 1 of this Section, the classification of exposures to a borrower – natural person, farmer and entrepreneur, is performed at the level of individual exposures, unless the gross value of balance sheet exposures to such borrower that are past due by more than 90 days represents at least 20% of the gross value of all balance sheet exposures of the bank to such borrower, in which case all exposures to such borrower shall be classified as non-performing.

If the bank classifies exposures to a borrower belonging to a group of related persons as non-performing, the bank shall be required to consider whether circumstances leading to such classification also affect the classification of exposures to other members of the group.

35d. Within one year from the forbearance date, a forborne exposure which, in accordance with Section 35f, paragraph 4 of this Decision, was classified in the group of non-performing exposures may be re-classified in the group of performing exposures if the following conditions are met:

- no impairment amount from Section 35b, paragraph 1, indent four of this Decision has been found and default has not occurred in respect of such exposure;
- as at the classification date and following application of forbearance measures, the borrower settles its obligations timely and the bank, on the basis of analysis of the financial position and/or creditworthiness

of the borrower, assesses that the borrower will be able to settle its obligations in full in accordance with changed terms of repayment.

The bank may assess that the borrower will be able to settle its obligations in full only if the borrower has paid, via its regular payments meaning payments made in the past twelve months in a timely fashion or with a delay of not more than 30 days, a total at least equal to the amount that was previously past-due (where there were past-due amounts) or that has been written-off (where there were no past-due amounts) under the changed terms of repayment, or if the borrower has otherwise demonstrated its ability to settle its obligations in accordance with changed terms of repayment.

35e. The bank shall classify exposures in the sub-group of forborne exposures in particular if:

- there has been a change in the agreed terms of repayment of non-performing exposures or exposures which in the absence of these changes would be classified in the group of non-performing exposures;
- there has been a change in the agreed terms of repayment of exposures resulting in total write-off or partial write-off of exposures in a materially significant amount;
- the bank has activated the agreed forbearance clauses based on which terms of repayment are changed due to the occurrence of specific events (embedded forbearance clauses) in respect of a borrower an exposure to which has already been classified in the group of non-performing exposures or would have been classified as such if such clauses had not been activated;
- simultaneously with or close in time, before or after, to the approval of a new bank exposure, the borrower made payments of principal or interest in respect of another exposure of the bank or of another legal person to which the exposure to the borrower has been assigned, that was classified or eligible to be classified in the group of non-performing exposures or would, in the absence of the new exposure, have been classified and/or been eligible to be classified as non-performing.

The bank shall consider whether an exposure should be classified in the sub-group of forborne exposures in particular if:

- in respect of exposures where terms of repayment were changed, but which were not classified in the group of non-performing exposures as at the date of such change, the borrower was more than 30 days past due on its obligations in the three-month period prior to such change in terms, or would have been more than 30 days past due had there been no such change;

- simultaneously or close in time, before or after, to the approval of a new bank exposure, the borrower made payments of principal or interest in respect of another exposure of the bank or of another legal person to which the exposure to the borrower has been assigned on which the borrower was, fully or partially, more than 30 days past due in the three-month period prior to the occurrence of the new exposure;

- agreed forbearance clauses based on which terms of repayment are changed due to the occurrence of specific events (embedded forbearance clauses) have been activated for 30 days past due borrowers or borrowers who would be more than 30 days past due without the exercise of those clauses.

If a bank assesses that, regardless of the occurrence of circumstances from paragraph 2 of this Section, an exposure is not to be classified in the sub-group of forborne exposures, it shall document such assessment in detail.

35f. The classification of an exposure as forborne shall be discontinued by the bank if the following conditions have been met at the end of the probation period from Section 2, indent 8) of this Decision:

- the forborne exposure is not classified in the group of non-performing exposures;
- through regular payments of principal or interest, the borrower has repaid a materially significant portion of total debt during at least half of the probation period;
- none of the obligations of the borrower to the bank is more than 30 days past due.

Where the conditions from paragraph 1, indents two and three of this Section are not met, the bank shall continue to classify the exposure in the sub-group of performing forborne exposures, and shall assess fulfilment of these conditions on at least a quarterly basis.

The exposure which, at the date of forbearance, was not classified in the group of non-performing exposures may continue to be classified in the group of performing exposures from the date of forbearance only if such forbearance did not result in the fulfilment of either of the conditions from Section 35b, paragraph 1 of this Decision.

The bank shall classify all forborne exposures meeting the conditions from Section 35b, paragraph 1 of this Decision in the group of non-performing exposures, and shall, regardless of the fulfilment of these conditions, also classify the following exposures in the group of non-performing exposures:

- exposures that were classified or were eligible to be classified in the group of non-performing exposures before forbearance;
- forbore exposures that have been reclassified out of the group of non-performing exposures to the group of performing exposures, and in relation to which the bank, during the probation period from Section 2, indent 8) of this Decision, makes additional concessions and/or if the borrower is more than 30 days past due on its obligations in respect of such exposure;
- exposures classified in accordance with paragraph 3 of this Section, in relation to which the bank makes additional concessions after re-forbearance.

### **Transitional and final provisions**

36. For property other than residential, as well as for property not being the subject of project financing – the conditions from Section 29, paragraph 1, provision 1), indents 5 and 6 of this Decision under which mortgage on that property is considered to be an adequate collateral – shall apply as of 31 December 2012.

37. Banks shall align the internal acts from Sections 5 and 24 of this Decision with the provisions of that Decision by no later than two months from its effective date and shall apply them in the classification of balance sheet assets and off-balance sheet items on their balance as at 31 December 2011.

Banks shall submit to the National Bank of Serbia the internal acts from paragraph 1 hereof, as well as any amendments and supplements thereto, within 15 days from their issue.

38. As of the effective date hereof, the Decision on the Classification of Balance Sheet Assets and Off-Balance Sheet Items of Banks ("RS Official Gazette", Nos 129/2007, 63/2008, 104/2009, 30/2010, 25/2011 and 45/2011) shall cease to be valid.

39. This Decision shall be published in the "RS Official Gazette" and shall enter into force on 31 December 2011.

NBS EB No 94  
12 December 2011  
B e l g r a d e

Chairman  
of the NBS Executive Board  
G o v e r n o r  
National Bank of Serbia

Dejan Šoškić, sign.

