

## **BANK SUPERVISION DEPARTMENT**

### **FREQUENTLY ASKED QUESTIONS IN 2007**

#### ***I. Decision on the Classification of Bank Balance Sheet Assets and Off-Balance Sheet Items ("RS Official Gazette", No. 57/06), hereinafter: Decision on Classification***

**Q1.** Should a bank:

- classify into category A overdrafts, i.e. loans on current accounts, that are not higher than the three-month average monthly payment of regular personal income to the current account,
- classify unauthorized overdrafts on current accounts into relevant categories depending on the length of the period during which the account is continuously in unauthorized overdraft?

**A1.** Receivables from natural persons that constitute lending are to be classified in conformity with Section 10 of the Decision on Classification, by applying the criterion of timeliness or past due status referred to in Section 7 of the Decision on Classification in settling obligations towards a bank during the preceding 12-month period and assessment of the borrower's ability to timely meet its obligations towards a bank, conducted on the basis of documentation referred to in Section 14 of the Decision. Untimely settlement of contractual obligations by natural persons shall be classified into categories referred to in Section 7 of the Decision on Classification, subject to criteria specified therein. Delay in the collection of receivables from a client will be calculated as of the original maturity date. (6 March 2007)

**Q2.** Please provide your opinion with respect to implementation of Section 12, paragraph 4 of the Decision on Classification. Namely, does the first-time restructuring of receivables subject to conditions specified therein also refer to refinancing of loans to natural persons, i.e. does the above paragraph 4 of Section 12 of the Decision refer to legal entities only or can it also refer to natural persons?

**A2.** In conformity with Section 12, paragraph 4 of the Decision on Classification, restructured receivables mean receivables contracted to replace the balance of all receivables from a borrower on account of aggravation of the borrower's financial standing, if there was a significant change in terms and conditions under which such receivables were originally approved and, at the same time, if an adequate programme of financial consolidation of the borrower has been adopted. As a natural person cannot adopt a programme of financial consolidation, we hold that the provision from Section 12, paragraph 4 of the Decision on Classification does not refer to natural persons. (1 June 2007)

#### ***II. Decision on the Uniform Manner of Calculating and Disclosing the Effective Interest Rate on Loans and Deposits ("RS Official Gazette", No. 57/2006) – hereinafter: Decision on EIR and Guidelines for Implementing the Decision on the***

***Uniform Manner of Calculating and Disclosing the Effective Interest Rate on Loans and Deposits (“RS Official Gazette“, No. 57/06 and 88/06) – hereinafter: Guidelines.***

**Q1.** Section 8 of the Decision on EIR sets out that bank is required to notify the client in writing of any change in elements that form the basis for calculation of EIR. Please provide your opinion on whether such notification in writing is necessary if the agreement already contains an article stipulating a variable interest rate which shall enter into force following amendment to the decision on the interest rates of the bank. As we have a large number of loan clients and it would be very difficult to send so many notifications, we believe that sending of individual notifications is only justified in case there is no bilaterally signed agreement with the client.

**A1.** A contractual article stipulating a variable interest rate cannot be deemed to constitute a notification in writing referred to in Section 8 of the Decision on EIR. In conformity with Section 8 of the Decision on EIR, the bank shall notify the client in writing of any change in the effective interest rate resulting from a change in elements that form the basis for calculation of EIR (in this specific case, the change in the nominal interest rate), prior to the start of application of the changed effective interest rate. (6 March 2007)

**Q2.** The bank should present Annex 1 – General Data on Deposit/Loan to all its potential clients and store it chronologically in a relevant organizational section. If after a time a potential client decides to become a client of our bank, such client will be presented with the agreement and Annex 3 – Deposit Payment Schedule. In this connection, please explain whether the bank is required to move the Annex 1 from the centralized archive of potential clients into the client's personal file, especially since one and the same client can be a potential client in one branch office and conclude agreement with the bank in another one.

**A2.** A bank's loan/deposit offer should contain elements specified in Section 5 of the Decision on EIR. It is up to the bank to decide where to store Annex 1 – in the borrower's credit file or a centralized archive in a relevant organizational section. (6 March 2007)

**Q3.** Is the bank required to issue a deposit payment schedule for special-purpose accounts, e.g. deposit accounts that serve as collateral under performance guarantees of natural persons?

**A3.** Section 2, paragraph 1, indent 3) of the guidelines defines 'deposit' as, inter alia, the sum of money that a depositor – legal entity or natural person – deposits in a depository bank. Deposits can be special purpose or general purpose deposits. At the time of concluding a deposit agreement, the bank shall be required to give the client a copy of the deposit payment schedule, in conformity with Section 7, paragraph 1 of the Decision on EIR. (6 March 2007)

**Q4.** While preparing Annexes 1 and 2 for household lending purposes, we found that the section that refers to data to be included in the calculation of the effective interest rate does not foresee data on the level of the deposit made (as precondition to loan approval) or the level of interest rate on such deposit. In that context, please inform us if a change in the above annex forms is to be expected.

**A4.** Data on the level of the deposit made should not be specified individually in Annexes 1 and 2 but should be included in aggregate data on the effective interest rate in these annexes – for loans approved against provision of deposit. It can also be specified in the section “Type of loan” (e.g. loan against 20% deposit). (6 March 2007)

**Q5.** In the event of change in interest rates in conformity with a concluded loan agreement, does the new loan repayment schedule need to be signed by the client? If this is not necessary, it would very much facilitate the procedure.

**A5.** Section 8 of the Decision on EIR sets out that the bank shall notify the client in writing if the effective interest rate changes due to a change in elements that form the basis for its calculation. We believe that the notification in writing should contain data that enter into the calculation of the EIR. If the bank makes a new loan repayment schedule, it is necessary for the client to sign such schedule. (6 March 2007)

**Q6.** In the event of change in any element that forms the basis for the calculation of the effective interest rate, should the bank, along with the written notification thereof, send to the client a new List of Important Elements of Loan Repayment, Loan Repayment Schedule or Deposit Payment Schedule, or it suffices to deliver only the notification of change in the level of the EIR applied to a specific bank product/service, and to specify therein the new amount of the loan instalment?

**A6.** Section 8 of the Decision prescribes an obligation for banks to notify their clients in writing of any change in the effective interest rate due to change in elements that form the basis for the calculation of the EIR, prior to the start of application of the changed EIR. We hold that the bank should specify the reasons behind the change in the written notification of change in the EIR, as well as submit to the client a new Loan Repayment/Deposit Payment Schedule.

**Q7.** If a new Loan Repayment Schedule/Deposit Payment Schedule is to be sent to the client, are the elements from the initial loan/deposit agreement that have remained unchanged used in calculating the EIR or is the new EIR calculated based on the current loan/deposit balance?

**A7.** Loan Repayment/Deposit Payment Schedule submitted to the client along with written notification on change in the EIR is based on the current loan/deposit balance, which means that the Schedule should refer to the period remaining until full loan repayment/deposit payment.

**Q8.** Is it necessary to calculate the new EIR and notify the client thereof if a change in the bank’s business policy refers to the level of the fee payable by the client to the bank on loan approval, as this data too represents an element of EIR calculation?

**A8.** If a change in the EIR occurred due to a change in the bank’s business policy regarding the level of the fee payable by the client to the bank as a one-off fee which the client pays on loan approval, we hold that the bank does not have the obligation to submit to the client a written notification of change in the EIR, as the abovementioned change does not affect the client’s payment obligation to the bank over the remaining of part of the loan repayment period. (30 April 2007)

### ***III. Law on Banks (“RS Official Gazette“, No. 107/05) – hereinafter: Law on Banks***

**Q1.** Are we right in assuming that a member of a bank's executive board that obtained prior approval of the National Bank of Serbia to his/her appointment does not need to obtain another approval of the National Bank of Serbia in order to be appointed chairman of the executive board, since the procedure for issuing approval of appointment is the same for both chairman and members of the bank's executive board?

**A1.** Section 29 of the decision of the National Bank of Serbia on implementing the provisions of the Law on Banks relating to granting of a provisional bank founding permit and subsequent issuing of a full operating licence to a bank, as well as on implementing specific provisions relating to granting approvals of the National Bank of Serbia ("RS Official Gazette", No. 51/2006) sets out detailed procedure for granting prior approval of appointment of members of executive board of a bank. As no difference is made between executive board chairman and members, banks can independently decide on the appointment of executive board chairman, choosing between members that were already granted prior approval of the National Bank of Serbia.

Therefore, we agree with the opinion set out in your question that no prior approval of the National Bank of Serbia is necessary with regard to the appointment of executive board chairman. (17 January 2007)

**Q2.** The Business Registers Agency refused to register the bank's branch office and explained this by saying that banks can have branches, but not branch offices. We were then told that we should submit to the Agency the decision of a competent organ on setting up a branch and the decision on appointing a representative of such branch, as well as the approval of the National Bank of Serbia to found such branch.

**A2.** The requirement to register branch offices has been regulated in the Law on the Registration of Business Entities ("RS Official Gazette", No. 55/2004 and 61/2005). Since in Article 88 of the Law on Banks the legislator mentions the opening of branches or other forms of organization in the territory of the Republic of Serbia, it can be concluded that the bank can, in addition to branches, found other forms of organization which are also subject to registration requirement.

In compliance with Article 89, paragraph 1 of the Law on Banks, the National Bank of Serbia issues approval of the decision to found a branch abroad. When it comes to founding a branch or another form of organization in the territory of the Republic of Serbia, a bank does not need approval of the National Bank of Serbia, as Article 88 of the Law on Banks prescribes only that banks should notify the National Bank of Serbia of the opening of a branch or another form of organization in the territory of the Republic of Serbia in a set timeframe. (26 January 2007)

**Q3.** Can the board of directors authorize the executive board to issue prior approval of a legal transaction of the bank with a related party of the bank in between two meetings of the board of directors, with the obligation to verify such approval on the first next board meeting?

**A3.** We believe there are no grounds for transactions coming under the remit of the board of directors to be transferred to the remit of the executive board or any other organ of the bank, as the Law on Banks does not leave a possibility for the board of directors to transfer any of its competences to another organ of the bank. Irrespective of this, the

prior approval from Article 38, paragraph 2 of the Law on Banks can be issued as a general prior approval, with a clear specification of the terms and conditions under which a legal transaction with a related party can be entered into, and subject to the obligation to inform the board of directors on concluded legal transactions with a related party on its first next meeting. (25 April 2007)

**A4.** Please provide clarification of Article 78 of the Law on Banks, which requires members of the bank's board of directors and executive board to submit statements on their property. Namely, do these provisions refer to all property worldwide or in Serbia only; what happens if a person is unaware of all proprietary rights of distant family members, particularly if family members refuse to disclose such information; who assesses the value of the abovementioned proprietary rights; in case of cash holdings, it necessary to specify the business name of the bank where such cash is held and the account number?

**Q4.** The statement should contain data on the property whose market value exceeds EUR 10,000, owned by members of the bank's board of directors and executive board, and their family members, irrespective of the territory on which the property is located. Hence, the statement should contain data on the property owned by such persons both in the Republic of Serbia and in other countries. The person submitting the statement will be required to specify all prescribed data that are available to it in the statement. The value of proprietary rights of members of the board of directors and executive board and their family members will be assessed with reference to market value. At the time of issuing the statement on the amount of cash holdings, it is not necessary to specify the business name of the bank and the number of the bank account on which such funds are kept. (20 April 2007)

#### ***IV Guidelines on Reporting Requirements for Banks ("RS Official Gazette", No. 57/06 and 116/06)***

**Q1.** With respect to disclosing provisions for estimated losses in item 1.7 (Special provisions for estimated losses as a deductible) in the DEV report (Daily report on bank foreign exchange risk ratio), please explain:

1) is it possible to "enter" not only special provisions for estimated losses, but also total provisions in item 1.7;

2) is this possibility temporary in character and when is it expected to be abolished, i.e. limited only to special provisions in item 1.7;

3) can the bank, because it has only "retained" special provisions in its report on the foreign exchange risk, again enter "total" provisions in item 1.7, in order not to have to sell foreign exchange, the sale of which will not be necessary anyway after shareholders' meeting is held? Consequently, if this is at all possible, is the bank supposed to "retroactively" adjust the reports it has sent since 27 January to date?

**A1.** 1) In the DEV report (Daily report on bank foreign exchange risk ratio), item 1.7 will include as deductibles only special provisions for estimated losses calculated for assets from items 1.1 to 1.6 of the DEV form. Item 1.7 does not include provisions for general banking risks.

2) As it is not possible to include provisions for general banking risks in item 1.7, we cannot discuss the temporary character of this option or the time of its abolishment.

3) If total provisions are taken to include provisions for general banking risks, these provisions will not be included in item 1.7 as a deductible. (8 March 2007)