

Pursuant to Article 63, paragraph 4 and Article 102, paragraph 7 of the Law on Banks (RS Official Gazette, Nos 107/2005, 91/2010 and 14/2015), Article 15, paragraph 1 and Article 64, paragraph 2 of the Law on the National Bank of Serbia (RS Official Gazette, Nos 72/2003, 55/2004, 85/2005 – other law, 44/2010, 76/2012, 106/2012 and 14/2015), the Executive Board of the National Bank of Serbia issues the following

DECISION ON DETAILED TERMS AND MANNER OF PERFORMING BANK SUPERVISION AND SPECIAL BANK AUDIT

Introductory provisions

1. This decision sets out detailed terms and manner of performing prudential bank supervision (hereinafter: bank supervision) in accordance with the Law on Banks (hereinafter: the Law) and other law entrusting to the National Bank of Serbia the authority to perform bank supervision, as well as detailed terms and manner of conducting special audit.

By bank supervision, the National Bank of Serbia shall assess the safety and soundness of a bank's operations, and/or the adequacy of a bank's market conduct, in particular:

- the financial condition, business policy and strategy of a bank, and/or the impact of changes in a bank's business policy, strategy or volume of operations on its financial condition and risk profile;
- the adequacy of a bank's governance and organizational structure, as well as the adequacy and reliability of a bank's system of internal controls;
- risks to which a bank is exposed or may be exposed in its operations, and the coverage and reliability of the established system for managing those risks, in particular the adequacy and reliability of the internal capital adequacy assessment process, consistency of its implementation and results of the assessment;
- a bank's capital adequacy vis-à-vis the risks a bank is exposed or may be exposed to in its operations and the established system for managing those risks;
- the adequacy and reliability of reports a bank submits to the National Bank of Serbia and accuracy and adequacy of data and information the bank is required to publish;

- whether a bank operates in compliance with the Law and regulations of the National Bank of Serbia adopted pursuant to the Law, as well as prudential banking standards;
- whether a bank operates in compliance with other law entrusting to the National Bank of Serbia authority for performing bank supervision and regulation adopted pursuant to that law or other regulation whose application by banks is supervised by the National Bank of Serbia;
- whether the human, material and other resources, as well as the bank's risk management system are set up so as to ensure that regulations are properly implemented when offering services to consumers and that consumers are treated with due professional care, i.e. in accordance with the principle of conscientiousness and fairness and good business customs.

Manner of performing supervision

2. The National Bank of Serbia shall exercise bank supervision as off-site and on-site supervision.

The National Bank of Serbia shall exercise off-site supervision by examining reports and other documentation that a bank submits to the National Bank of Serbia pursuant to regulations and/or at its request in accordance with the Law and other operational data of the bank available to the National Bank of Serbia.

The National Bank of Serbia shall exercise on-site supervision on a bank's premises – the head office and all organisational parts of the bank (branches, branch offices, facilities where certain equipment is stored, etc.), or premises of persons which are related by proprietary, management and business relationships to the supervised bank.

On-site supervision is conducted by inspecting business books and other documents of the bank or its clients, as well as by obtaining direct or indirect insight into data in the bank's IT system.

The data and documents from paragraph 4 of this Section may be copied.

Off-site and on-site supervision are also carried out by interviewing the bank's management and employees, and/or taking written statements from those persons.

The interview from paragraph 6 of this Section shall be audio recorded with the prior consent of the manager or the bank employee who is to be interviewed.

If the manager or the employee from paragraph 7 of this Section refuses to consent to the audio recording of the interview without a justified reason, the National Bank of Serbia may take this into account when assessing the bank's conduct in the supervision process within the meaning of Section 15 hereof, as well as within the assessment of the criteria from Article 116 of the Law.

The National Bank of Serbia may supervise any member of a banking group in the manner specified in this Section.

Findings of completed bank supervision, and/or irregularities in the bank's operations established in the supervision procedure, shall be presented in a report.

By way of exception to paragraph 10 of this Section, if in off-site supervision procedure a bank has notified the National Bank of Serbia of irregularities in its operations, the National Bank of Serbia shall not prepare a report referred to in that paragraph, but may take against the bank measures referred to in Article 110, paragraph 1 of the Law, and/or some of the measures referred to in Articles 113 to 115 of the Law, in accordance with the criteria laid down in Article 116 of the Law.

The provisions of this Decision pertaining to on-site bank supervision shall accordingly apply to the procedure following the preparation of a report on completed off-site supervision.

3. Irregularities in a bank's operations (hereinafter: irregularities) shall be bank's actions contrary to provisions of the Law, regulations of the National Bank of Serbia or other law and/or regulation, prudential banking standards and/or bank's actions otherwise jeopardising its soundness, and where measures referred to in Article 109 and Articles 113 to 115 of the Law are concerned, also when it is probable, due to rapidly deteriorating financial condition, including deteriorating liquidity situation, increasing level of leverage, non-performing loans or concentration of exposures, that the bank is likely to soon act contrary to the provisions of the Law, regulations of the National Bank of Serbia and/or other regulations.

4. On-site bank supervision shall be conducted by employees of the National Bank of Serbia designated by the decision of the Governor of the National Bank of Serbia (hereinafter: the Governor) or the person authorised by the Governor.

The bank and/or other supervised persons, as well as the subject of supervision, shall be stated in the decision referred to in paragraph 1 hereof.

The decision referred to in paragraph 1 hereof may also designate a person other than the employee of the National Bank of Serbia to take part in the on-site supervision procedure if the expertise of such person can assist the employees from that paragraph.

Bank on-site supervision procedure shall be initiated by adoption of the decision referred to in paragraph 1 of this Section.

The Governor or a person authorised by the Governor may supplement and/or amend the decision referred to in paragraph 1 of this Section during on-site supervision.

Authorised persons of a foreign regulatory authority which supervises activities of members of the same banking group that the bank is a member of, may take part in bank on-site supervision procedure, in accordance with the memorandum of understanding concluded between the National Bank of Serbia and such authority.

Employees of the National Bank of Serbia referred to in paragraph 1 of this Section and authorised persons referred to in paragraphs 3 and 6 of the same Section (hereinafter: authorised persons) shall prepare a report on the findings of completed bank supervision.

Reports, other acts and their submission

5. The National Bank of Serbia shall deliver the report referred to in Section 2, paragraph 10 of this Decision to the supervised bank, which may file its objections within 15 business days from the receipt of such report.

Once the decisions, reports, other acts and other communications in connection with the exercise of bank supervision are submitted to the bank, they shall be considered to have been submitted to the members of the bank's management bodies and no proof to the contrary shall be admissible.

The bank shall file to the National Bank of Serbia the objections to the report referred to in paragraph 1 of this Section, signed by presidents of its managing and executive boards.

If upon verification of the statements presented in objections referred to in paragraph 3 of this Section it is established that the factual state is materially different from the one stated in the report, the National Bank of Serbia shall prepare a supplement to the report on supervision to be delivered to the bank within 15 business days following the submission of objections to the report.

The National Bank of Serbia shall not consider the bank's objections to the report on supervision relating to factual changes that occurred after the completion of supervision (cut-off date), but may take them into account when imposing measures under this Law.

The National Bank of Serbia shall render a conclusion on termination of the supervisory procedure if no irregularities have been established in the report on supervision, or if less important irregularities have been established, or if the bank, in its objections submitted within the timeframe specified by the Law, has successfully disputed all findings in the report on supervision or has successfully disputed some of the findings so that the remaining irregularities represent less important irregularities.

The National Bank of Serbia may issue a Conclusion on termination of the supervision procedure if, within the timeframe specified for submitting objections, the bank provides evidence that the identified irregularities have been removed, and the remaining irregularities represent less important irregularities.

Decision on temporary measures

6. If the National Bank of Serbia takes a decision on temporary measures pursuant to Article 109 of the Law, such decision shall be effective until the imposing of measures referred to in Article 110, paragraph 1 or Article 113 of the Law, or until the rendering of a conclusion on termination of the procedure under such decision, and/or until the termination of the supervisory procedure.

The decision on temporary measures may be amended and/or supplemented if the National Bank of Serbia assesses that there are justifiable reasons for that or that new facts emerged following its adoption.

Letter of warning

7. A letter of warning referred to in Article 111 of the Law (hereinafter: letter of warning) shall be issued to a bank in whose operations irregularities were detected that have not had a significant and direct impact on its financial condition, but may have such impact unless eliminated.

In case of the supervision of the legality of a bank's operations in accordance with the Law on the Protection of Financial Services Consumers and the Law on Payment Services, i.e. supervision of a bank's market conduct, it shall be deemed that the identified irregularities from paragraph 1 of this Section could influence the bank in the way specified in that paragraph,

particularly if these irregularities are of systemic character and if they include or may include a large number of consumers and/or which may have significant material effects on consumers, or may jeopardise their rights and interests in another way.

A letter of warning shall state the timeframe for eliminating the irregularities and the timeframe in which the bank is required to submit to the National Bank of Serbia the report on eliminated irregularities, with evidence enclosed.

The National Bank of Serbia shall examine if the bank removed the detected irregularities after the expiry of the timeframe referred to in paragraph 3 of this Section, or before the expiry of such timeframe if it receives a notification from the bank about the removal of irregularities.

The National Bank of Serbia shall terminate the supervisory procedure in a bank to which it issued a letter of warning when it has ascertained that the detected irregularities have been removed within the timeframe specified in the letter of warning, i.e. it may terminate the procedure if the irregularities have been removed or have been largely removed, whereas if they have not been removed or have not been largely removed, it shall take a new measure against the bank pursuant to Article 110, paragraph 1 of the Law, and/or some of the measures from Articles 113 to 115 of the Law, in accordance with the criteria laid down in Article 116 of the Law.

Decision on orders and measures

8. The National Bank of Serbia shall take a decision imposing orders and measures in accordance with Article 112 of the Law.

In case of the supervision of the legality of a bank's operations in accordance with the Law on the Protection of Financial Services Consumers and the Law on Payment Services, i.e. supervision of a bank's market conduct, it shall be deemed that the identified irregularities could jeopardise the bank's financial position, i.e. that the irregularities are subject to the decision from paragraph 1 of this Section – particularly if these irregularities are of systemic character and if they include a large number of consumers and/or have significant material effects on consumers.

The bank shall notify the National Bank of Serbia of the implementation of orders and measures referred to in paragraph 1 of this Section, in the manner and within the deadlines specified in the decision referred to in that Section.

The National Bank of Serbia shall supervise the implementation of orders and measures specified in the decision referred to in paragraph 1 of this

Section after the expiry of the deadline for their implementation, or prior to the deadline expiry if it receives the notification from the bank that the orders were implemented.

The decision referred to in paragraph 1 of this Section may also designate a management body or its member to be responsible for the implementation of orders and measures stipulated in that decision.

The Governor or a person authorized by the Governor may, by virtue of a decision, authorize some employees of the National Bank of Serbia to verify and monitor on a daily basis the implementation of orders and measures imposed by the decision from paragraph 1 of this Section.

9. If the National Bank of Serbia establishes that a bank has implemented all orders and measures referred to in Section 8, paragraph 1 of this Decision or that the irregularities based on which those orders and measures had been imposed were removed to such extent that the remaining irregularities represent less important irregularities, it shall terminate the supervision procedure, but if the irregularities were not removed, it shall take against such bank a new measure under Article 110, paragraph 1 of the Law, and/or some of the measures from Articles 113 to 115 of the Law, in accordance with the criteria laid down in Article 116 of the Law.

10. If the National Bank of Serbia establishes that the bank to which some of the measures referred to in Article 110, paragraph 1, indents 1) to 3) of the Law were imposed has committed a new irregularity or its financial condition deteriorated after the cut-off date, the National Bank of Serbia may take against such bank a new measure under Article 110, paragraph 1 of the Law, and/or some of the measures from Articles 113 to 115 of the Law, in accordance with the criteria laid down in Article 116 of the Law.

Early intervention measures

11. The National Bank of Serbia may, without prejudice to the undertaken measures referred to in Sections 7 and 8 of this Decision, take a decision imposing to a bank one or more measures referred to in Article 113, paragraph 1 of the Law, in accordance with the criteria laid down in Article 116 of the Law.

The decision referred to in paragraph 1 of this Section shall specify a deadline by which a bank is required to comply with those measures and to supply to the National Bank of Serbia appropriate evidence thereof.

Once it determines that the bank has timely complied with the measures from paragraph 1 hereof and that the irregularities based on which those measures had been imposed were removed to such extent that the

remaining irregularities represent less important irregularities, the National Bank of Serbia shall either terminate the supervision procedure or impose another measure from that paragraph, and/or one of the measures referred to in Article 110 in accordance with the criteria laid down in Article 116 of this Law.

Where a significant deterioration of a bank's financial condition has occurred or serious infringements of law, regulations of the National Bank of Serbia and other regulations or the bank's articles of association, and the National Bank of Serbia determines that other measures taken in accordance with Article 113 of this Law are not sufficient to remedy the bank's condition, it may require, by virtue of a decision, the removal of all or some members of the bank's management bodies, and/or the replacement of persons holding managing positions in the bank, in accordance with Article 114 of the Law.

Where the National Bank of Serbia has assessed that the removal and/or replacement of all or some members of the bank's management bodies, and/or the replacement of persons holding managing positions in the bank referred to in paragraph 4 of this Section is not sufficient to remedy the situation in the bank, the National Bank of Serbia may issue a decision on the appointment of one or more temporary administrators of the bank and introduce temporary administration in the bank, in accordance with the decision governing the conditions and manner of carrying out temporary administration in a bank.

Fine

12. For purposes of imposing a fine to a bank, a member of the bank's managing and/or executive board, in accordance with Article 117, paragraph 1 of the Law, the bank shall submit to the National Bank of Serbia, at its request, the data on division of authorities and responsibilities for activities falling within the scope of competence of the managing and/or executive board determined by the articles of association and internal regulations of the bank, the bank's income in the previous business year, average salaries of members of the managing and/or executive board for the period specified in the request of the National Bank of Serbia and other appropriate data.

13. A bank shall submit to the National Bank of Serbia a proof of payment of the fines referred to in Section 12 hereof by no later than within the timeframe defined in the decision imposing the fine, and/or eight days from the expiry of that timeframe, if the bank pays the fine instead of the members of the bank's managing or executive board, in accordance with Article 117, paragraph 9 of the Law.

If the bank fails to pay the fine referred to in paragraph 1 of this Section, the National Bank of Serbia shall directly enforce the collection by

transferring the amount of the fine from the bank's account held with the National Bank of Serbia.

Revocation of operating license

14. The National Bank of Serbia shall take a decision to revoke a bank's operating license in cases stipulated in Article 130, paragraph 1 of the Law, and/or may also take such decision in cases referred to in paragraph 2 of that Article.

Bank's actions in the supervision procedure

15. It shall be deemed that a bank failed to enable the National Bank of Serbia to exercise supervision if it failed to act in accordance with Article 104 of the Law, as well as in the following cases:

- if the bank fails to submit all required data or evidence within the specified deadline, in particular the data the bank is required to have according to law, secondary legislation or prudential banking standards;
- if the bank submits inaccurate or incomplete data deliberately or by gross negligence;
- if it fails to provide to the authorized persons the conditions required for conducting bank supervision and/or does not ensure that they are not disturbed by the bank's employees and other persons;
- if it fails to submit three consecutive reports it is mandated to periodically submit under the law or secondary legislation and if it fails to do so within the specified deadline at the repeated request of the National Bank of Serbia.

16. For the purposes of gathering, processing and analysing necessary data, the National Bank of Serbia may conduct a diagnostic examination of the bank's operations by carrying out direct insight into its business books and other documentation, in compliance with Article 101a of the Law.

The authorized persons shall prepare a report on completed diagnostic examination which shall not be delivered to the bank.

17. Provisions of this Decision shall accordingly apply to the supervision of a bank exercised by the National Bank of Serbia at the request and for the purposes of procedures of other competent domestic government authorities and institutions, on which the National Bank of Serbia shall prepare a report to be submitted to the authority/institution in question.

Detailed terms and manner of conducting special audit

18. If it assesses that specific data regarding a bank's business must be gathered, analysed and processed for the purposes of exercising supervision under this Law and these data are not covered by the report on the audit of the bank's annual financial statements, the National Bank of Serbia may require the bank to engage an external auditor to conduct a special audit of the financial statements of the bank and member of the banking group or specific parts thereof, as well as to conduct other types of audit, and/or examination of particular business processes and data on the operations of these persons (hereinafter: special audit).

The National Bank of Serbia shall determine the subject of special audit and in accordance with the subject it may determine additional criteria which the auditor from the list referred to in Article 52, paragraph 3 of the Law must fulfil so that the bank may select such auditor to conduct special audit, including the cost of engagement and operational, technical and staff capacities of the auditor.

The National Bank of Serbia may assess the fulfilment of criteria laid down in paragraph 2 of this Section on its own, or it may order the bank to engage an external auditor by applying those criteria.

Transitional and final provisions

19. Bank supervision procedures initiated before the effective date of this Decision shall be completed pursuant to provisions of the Law and the decision which were effective on the day of issuance of the National Bank of Serbia's act imposing a measure to a bank.

20. This decision repeals the Decision on Detailed Conditions and Manner of Conducting Bank Supervision (RS Official Gazette, No 43/2011).

21. This decision shall be published in the RS Official Gazette and shall enter into force on 1 April 2015.

NBS Executive Board No 19
26 March 2015

B e l g r a d e

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

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