Pursuant to Article 44 paragraph (2) item 3) of the Central Bank of Montenegro Law (OGM 40/10, 6/13, 70/17), Article 118 paragraph (2), and in conjunction with Article 220 of the Law on Credit Institutions (OGM 72/19), the Council of the Central Bank of Montenegro, at its meeting held on 28 December 2020, passed the following

# DECISION
# ON THE CRITERIA AND THE MANNER OF CLASSIFICATION OF ASSETS AND CALCULATION OF PROVISIONS FOR POTENTIAL LOAN LOSSES OF A CREDIT INSTITUTION

## I. BASIC PROVISION

### Subject matter

### Article 1

This Decision prescribes the criteria and the manner of classification of balance sheet items and off-balance sheet items, including their valuation, as well as the calculation of provisions for potential credit losses.

## II. VALUATION OF BALANCE SHEET ITEMS AND OFF-BALANCE SHEET ITEMS

### Implementation of International Accounting Standards/International Financial Reporting Standards

### Article 2

(1) A credit institution shall value and disclose balance sheet items and off-balance sheet items in accordance with International Accounting Standards, and International Financial Reporting Standards, respectively.

(2) The following balance sheet items and off-balance sheet items are valued in accordance with the provisions of this Decision:

1) financial instruments that are in accordance with International Financial Reporting Standard 9 - Financial Instruments (hereinafter: IFRS 9), allocated to the following portfolios:
   - financial assets measured at amortised cost;
   - financial assets measured at fair value through other comprehensive result, other than equity instruments;
2) financial instruments which represent:
   - lease receivables,
   - loan commitments,
   - liabilities under financial guarantee contracts; and
3) other exposures covered by IFRS 9, for which credit losses are determined.

## Methodology

## Article 3

(1) A credit institution shall determine a methodology for valuing and impairing financial assets in accordance with IFRS 9.

(2) The application of methodology referred to in paragraph (1) of this Article should ensure the following:

1) all analyses, assumptions, estimates and other procedures in the process of estimating the amount of impairment of balance sheet items and probable loss on the basis of off-balance sheet items are explained and documented in detail;
2) the assessment of the amount of impairment of balance sheet items and probable loss on off-balance sheet items is based on accurate and up-to-date information and that it takes into account all significant internal and external factors that may affect the collectability of receivables.

(3) A credit institution shall consistently apply the methodology referred to in paragraph (1) of this Article, review it at least once a year and, if necessary, adjust it to the results of the review, and adjust the assumptions on which the methodology is based.

## Frequency of valuation

## Article 4

(1) A credit institution shall assess the quality of assets at least quarterly, determine whether there is an objective evidence of impairment of balance sheet items or probable loss related to off-balance sheet items, and calculate the adequate amount of such impairment, and/or probable loss.

(2) Objective evidence of impairment of balance sheet items or probable loss related to off-balance sheet items, within the meaning of paragraph (1) of this Article, shall be the information on one or more events that have an adverse effect on the debtor's ability to regularly meet its obligations towards the credit institution.

## Treatment of collateral when performing impairment

## Article 5

(1) When calculating the amount of impairment of balance sheet items and probable loss related to off-balance sheet items, a credit institution may also take into account cash flows on the basis of collateral referred to in Articles 6, 7, 8 and 32 paragraph (2) of this Decision.

(2) When estimating future cash flows based on the realisation of collateral referred to in Article 6 of this Decision, a credit institution shall determine the appropriate impairment factors of market value of certain types of collateral, expressed as a percentage, as well as adequate internally estimated deadlines for realisation of those types of collateral.

(3) The determination of impairment factors and deadlines referred to in paragraph (2) of this Article should be based on the practice and experience of the credit institution in the realisation of collateral, conditions in the economic and legal environment in which the credit institution operates and appropriate collateral characteristics.

(4) In determining the amount of the impairment factor and the length of deadlines referred to in paragraph (2) of this Article, the credit institution shall take into account that different types of collateral reflect different levels of risk of realisation.

(5) The impairment factors and deadlines for realisation referred to in paragraph (2) of this Article may not be less than the minimum benchmarks given in Annex 1, which constitutes an integral part of this Decision.

(6) A credit institution shall, at least once a year, review the validity of assumptions about the initially determined term of realisation of collateral and correct them if necessary.

(7) A credit institution may reduce the period of realisation of collateral on a quarterly basis in accordance with the passage of time, if:

1) it has undertaken actions for the realisation of collateral and if it estimates that the realisation of the collection of receivables is taking place in accordance with the previously estimated deadline; and
2) the credit institution can prove and adequately document the certainty of cash flows and if the final deadline for the realisation of collateral and the total amount of cash inflows that the credit institution will realise on that basis can be reliably determined.

(8) The methodology referred to in Article 3 of this Decision shall also determine the manner of valuation of the collateral for which the credit institution estimates the cash flows, as well as the expected deadline for the realisation of that collateral.

**Treatment of collateral in the form of immovable property**

**Article 6**

(1) A credit institution may consider collateral in the form of immovable property when valuing assets, if it has documentation from which it can be concluded that the immovable property represents an efficient and adequate secondary source of collection of receivables.

(2) Collateral in the form of immovable property shall be considered an efficient and adequate secondary source of collection of receivables, within the meaning of paragraph (1) of this Article, if the credit institution has evidence that there is a market that allows fast and efficient realisation of collateral at an adequate price.

(3) When assessing cash flows, and after determining the net present value of receivables for which impairment is determined in accordance with the provisions of this

Decision, a credit institution shall take into account the part of collateral value in the form of immovable property remaining after deducting all receivables secured by that immovable property, and that is registered in the immovable property cadastre as mortgages of a higher priority ranking, in relation to the claims of the credit institution.

(4) The value of collateral in the form of immovable property shall be the assessment of the market value of the immovable property made by an independent appraiser in accordance with a special regulation governing the assessment of the value of property.

(5) For collateral in the form of immovable property, a credit institution shall have:

1) documentation on the registration of a mortgage or fiduciary transfer of ownership rights over a certain immovable property;
2) an updated excerpt from the cadastre of immovable property, with a registered mortgage or fiduciary transfer of property rights;
3) an insurance policy of a certain immovable property that is assigned in favour of the credit institution (except when the immovable property is land on which there is no facility built that would serve as collateral); and
4) documentation on the valuation by an independent appraiser or the purchase contract for that immovable property, whichever is applicable.

(6) A credit institution shall monitor the value of collateral in the form of immovable property that serves as collateral for the duration of the contractual relationship, as follows:

1) commercial property, at least once a year;
2) residential property, at least once in three years;
3) in deadlines shorter than the deadlines from items 1) and 2) of this paragraph, if market conditions are subject to significant changes.

(7) A credit institution may use statistical methods to monitor the value of collateral in the form of immovable property and to determine the need for revaluation.

(8) If a credit institution, based on monitoring the value of collateral in the form of immovable property using statistical methods, determines that there could be a significant decrease in the value of collateral compared to general market prices, it shall provide a revaluation of the collateral value by an independent appraiser.

(9) Notwithstanding paragraph (6) of this Article, for exposures exceeding 5% of the credit institution's own funds or exceeding EUR 500,000 (whichever is lower), the credit institution shall provide an appraisal of the value of collateral in the form of immovable property by an independent appraiser, at least every three years.

### Treatment of collateral in the form of movable property

### Article 7

(1) A credit institution may use movable assets as collateral to calculate the amount of impairment of balance sheet items and probable loss related to off-balance sheet items,

if:

1) there is a liquid market that enables fast and efficient realisation of collateral at an adequate price;
2) market prices are available for the corresponding movable property;
3) the operational conditions for the sale of that property are met;
4) the pledge agreement enables collection from collateral within a reasonable period of time determined in accordance with the internal act of the credit institution;
5) there is a right of priority in the order of collection in relation to other creditors;
6) the value of collateral is adjusted to market prices at least once a year, and more often if necessary;
7) the agreement on approved on-balance sheet or off-balance sheet exposure contains a description of collateral;
8) the credit institution has determined eligible types of collateral in the form of movable property and defined in its internal acts the procedures for determining eligible collateral, including the acceptable ratio between the value of receivables and collateral;
9) the credit institution has established in its policies the rules of exposure towards the debtor, the requirements regarding the timely realisation of collateral and regarding the adequacy of the price or market value of collateral;
10) the initial assessment of the value of movable property and all subsequent assessments of the value of movable property as a whole take into account the impairment of its value and the need for re-assessment;
11) the pledge is registered in accordance with the law governing the pledge as a security instrument; and
12) movable property is secured by an insurance policy in favour of the credit institution.

(2) A credit institution shall ensure that movable property with the value exceeding EUR 500,000 at the moment when negotiating collateral is assessed by an independent appraiser at least every three years, in accordance with the regulation referred to in Article 6 paragraph (4) of this Decision.

(3) Notwithstanding paragraph (2) of this Article, a credit institution may, for other collateral in the form of movable property, use the purchase value of that property minus the depreciation, the value of movable property from the insurance policy, or the market value that is readily available, transparent, and determined in accordance with the standards of the profession.

## Other types of collateral

## Article 8

(1) A credit institution may, in addition to the collateral referred to in Articles 6 and 7 of this Decision, use the following types of collateral:

1) security instruments referred to in Article 32 paragraph (2) of this Decision;
2) debt securities of institutions that do not have a credit assessment by external

credit risk assessment institutions, if all conditions from Article 216 paragraph (5) of the Decision on Capital Adequacy of Credit Institutions (hereinafter: Decision on Capital Adequacy) are met;
3) credit insurance policies against non-payment risk and life insurance policies with redemption value;
4) other instruments whose quality on the basis of appropriate evidence can be equated with the quality of security instruments from items 1), 2) or 3) of this Article.

(2) When estimating future cash flows based on collection from debt securities, a credit institution shall apply appropriate haircuts with respect to the market price taking into account the volume and frequency of trading in those debt securities, collection experience, as well as economic conditions, and regulations applicable in the country where the issuer has a head office, where the haircut may not be less than 10% for debt securities referred to in paragraph (1) item 2) of this Article, or less than 20% for instruments referred to in paragraph (1) item 4) of this Article.

**Assessment of impairment of balance sheet items on an individual basis**

**Article 9**

(1) A credit institution shall perform individual assessment of impairment of balance sheet items and probable loss related to off-balance sheet items in respect of individually significant receivables.

(2) An individually significant receivable, within the meaning of paragraph (1) of this Article, shall be the total gross exposure of a credit institution to one person or a group of connected persons exceeding EUR 300,000.

(3) Notwithstanding paragraph (2) of this Article, a credit institution may, in its internal act, determine a lower amount of total exposure to a single person or a group of connected persons as a threshold beyond which the exposure shall be considered an individually significant receivable.

(4) The individual assessment of impairment of balance sheet items shall include determining the existence of objective evidence of impairment, estimating the present value of future cash flows, and calculating the amount of that impairment, for each individually significant receivable included in the assessment.

(5) It shall be considered that there is an objective evidence of impairment of balance sheet items on an individual basis, if:
1) the financial condition of the debtor indicates significant problems in its operations;
2) there is information on default, frequent delays in the repayment of principal and/or interest, or non-compliance with other contractual obligations;
3) the credit institution, due to the financial difficulties of the debtor, significantly changes the terms of repayment in relation to the originally agreed, or

4) it becomes certain that bankruptcy proceedings, reorganisation or other similar proceedings will be opened against the debtor.

### Determining impairment amount for balance sheet items

### Article 10

(1) The amount of impairment of balance sheet item shall be determined as the difference between the carrying amount of the receivable and the present value of expected future cash flows from that receivable.

(2) Notwithstanding paragraph (1) of this Article, if deadline for a specific receivable in which future cash flows are expected is shorter than one year, a credit institution shall not calculate the present value of expected future cash flows, but may determine the amount of impairment of that balance sheet item as a difference between the carrying amount of the receivable and the expected future cash flows on such receivable.

### Assessment of the probable loss related to off-balance sheet items

### Article 11

(1) The assessment of the probable loss related to off-balance sheet items on an individual basis includes assessment of future cash outflows that can be recovered for each off-balance sheet liability and a calculation of the amount of probable loss for each individual off-balance sheet item included in this assessment.

(2) Future non-recoverable cash outflows shall be the nominal amount of expected cash outflow related to off-balance sheet obligations less the amount reasonably estimated to be recovered by the counterparty or to be compensated by the realisation of collateral.

### Amount of probable loss related to off-balance sheet items

### Article 12

(1) The amount of probable loss related to off-balance sheet items shall be equal to the present value of expected irrecoverable future cash outflows under those items.

(2) By way of derogation from paragraph (1) of this Article, if it is estimated that cash outflows will occur within a year following the calculation date of probable loss related to off-balance sheet items, a credit institution may determine the amount of cash outflows to equal those outflows.

### Collective assessment

### Article 13

(1) A credit institution shall perform collective assessment of balance sheet items for impairment and/or probable losses related to off-balance sheet items for all receivables

where the impairment or losses may not be directly linked to those receivables, but which may be estimated, based on experience, to exist in the loan portfolio.

(2) A credit institution shall perform collective assessment for the following receivables:

1) those where individual assessment showed no objective evidence of impairment, or probable loss or if no amount of impairment of balance sheet assets or probable loss related to off-balance sheet items has been determined at individual level;
2) those that do not represent individually significant receivables referred to Article 9 paragraph (2) of this Decision.

(3) A credit institution may perform individual assessment of impairment of balance sheet assets and probable losses related to off-balance sheet items for receivables that do not represent individually significant receivables.

(4) When performing collective assessment, a credit institution shall group receivables based on similar characteristics of credit risk that reflect the debtor's ability to meet its obligations in accordance with the agreed terms by applying one or more criteria, such as: type of products, regularity in meeting the obligations, credit rating, geographical areas, economic sector, type of collateral, and the like.

### Accounting treatment

### Article 14

(1) A credit institution shall debit the amount of impairment loss calculated for balance sheet assets as expense and credit it to the allowances for the impairment.

(2) A credit institution shall debit the calculated amount of probable losses related to off-balance sheet items and credit it to the provisions for losses on off-balance sheet items.

## III. CLASSIFICATION OF BALANCE SHEET ITEMS AND OFF-BALANCE SHEET ASSETS

### Classification items

### Article 15

(1) A credit institution shall classify, at least once a month, balance sheet items and off-balance sheet items exposing the credit institution to credit risk and calculate loan loss provisions.

(2) Balance sheet asset items and off-balance sheet items which expose the credit institution to credit risk shall be balance sheet asset items which expose the credit institution to a default risk and off-balance sheet items representing contingent liabilities of the credit institution, and in particularly:

1) loans and receivables from credit institutions (including funds placed with credit

institutions, interests and fees);
2) loans and receivables from clients (including interests and fees, receivables based on lease, forfaiting and factoring);
3) financial assets carried at fair value through profit or loss (debt and equity securities not included in trading book, or included in trading book but the credit institution does not calculate for these items capital required for market risks in accordance with the Decision on Capital Adequacy;
4) securities measured at amortised cost and securities at fair value through other comprehensive income;
5) equity investments in other legal persons, excluding equity investments representing deductible item from credit institution's own funds in accordance with the Decision on Capital Adequacy;
6) guarantees issued;
7) credit obligations given (approved, unused loans);
8) bill of exchange security and bill of exchange acceptances;
9) other sureties;
10) uncovered letters of credit

(3) Balance sheet items and off-balance sheet items which do not expose the credit institution to a credit risk shall be the following:

1) cash and deposit account with central banks (cash and cash equivalents, which include cash and other short-term highly liquid instruments with original maturity up to three months, and for which there is low risk of change in value);
2) derivative financial assets used as hedging instruments;
3) investment properties, properties, plant and equipment and intangible assets;
4) equity investments in other legal persons representing deductible item from credit institution's own funds in accordance with Decision on Capital Adequacy;
5) financial assets included in trading book, for which the credit institution calculates capital requirement for market risks in accordance with the Decision on Capital Adequacy;
6) guarantees obtained;
7) credit obligations obtained;
8) written-off loans and receivables;
9) collateral obtained;
10) custody assets;
11) revocable off-balance sheet liabilities.

(4) The credit institution shall determine if all balance sheet items and off-balance items other than items referred to in paragraphs (2) and (3) of this Article expose it to credit risk, and it shall classify those items into the corresponding classification category in accordance with the provisions of this Decision.

**Classification criteria**

**Article 16**

During the contractual relationship, a credit institution shall assess the quality of credit exposure and classify those exposures into corresponding risk groups based on the following criteria:

1) debtor's creditworthiness;
2) debtor's regularity in meeting its obligations towards the credit institution and other creditors; and
3) other relevant factors for classification.

## Debtor's creditworthiness

### Article 17

(1) The assessment of debtor's creditworthiness is based on the assessment of the capacity and readiness of the debtor to completely and timely meet their obligations to the credit institution from primary sources of debt repayment.

(2) The primary sources of debt repayment mean, in particular, cash from debtor's operating and other activities.

(3) When assessing debtor's creditworthiness, a credit institution shall analyse:

1) assessment of the adequacy of the level of recorded cash flows with respect to its liabilities over the previous period;
2) assessment of future cash flows;
3) assessment of business indicators based on the indicators of profitability, liquidity, indebtedness, i.e. capitalisation, if the debtor is a company;
4) assessment of the quality of the investment plan and programme for the implementation of which the credit institution provides financial support, in the case of investment or project financing;
5) exposure to foreign exchange and interest rate risk based on receivables with a currency clause, receivables in foreign currency and receivables contracted with a variable interest rate, including off-balance sheet liabilities with a currency clause and off-balance sheet liabilities in foreign currency.

(4) The credit institution shall analyse credit risk for exposures referred to in paragraph (1) item 5) of this Article from the aspect of possible change in the financial position of the debtor, which could occur due to changes in the euro exchange rate against other currencies and changes in interest rates, that is from the aspect of debtor's ability to meet its contractually agreed credit obligations towards the credit institution in potentially changed circumstances.

## Delay in repayment

### Article 18

(1) Delay in repayment shall be calculated for matured receivables whose amount exceeds materiality thresholds (absolute and relative) as determined in Article 197 paragraphs (7) and (8) of the Decision on Capital Adequacy.

(2) Calculation of days past due shall be performed in line with Article 197 paragraph (14) of the Decision on Capital Adequacy.

## Assessment of other relevant factors

### Article 19

(1) Other relevant factors for classification of asset items shall include, in particular:
1) information on general economic cycle;
2) information on the condition and prospects of economic sector to which a debtor belongs;
3) information on loan concentration per economic sectors and certain group of loan beneficiaries;
4) debtor’s market position;
5) debtor’s ownership and status changes;
6) corporate governance and management’s capacity to implement the programme subject to financial support from the bank;
7) loan structure;
8) compatibility of the loan purpose with debtor’s activity, and
9) compliance of loan approval with the credit institution’s policies and procedures.

(2) When classifying balance sheet items, a credit institution shall take into account the relations within the group of connected persons and identify in its internal acts situations in which loans of other entities from the same group should be classified in the same category due to the classification of loans of one debtor from the group of connected persons into the category of non-performing loans.

## Classification groups

### Article 20

A credit institution, shall, depending on probability of incurring losses, classify balance sheet items into one of the following classification categories:
1) category A – “pass”;
2) category B – “special mention” with subcategories B1 and B2;
3) category C – “substandard” with subcategories C1 and C2;
4) category D – “doubtful”;
5) category E – “loss”.

## Classification category "A"

### Article 21

(1) Loans shall be classified into the classification category “A” where highly documented evidence exist that they will be collected in full in accordance with the agreed terms and conditions.

(2) The following shall be classified into the classification category “A”:
1) loan granted to central governments, central banks, public sector entities, multilateral development banks and international organisations which receive a 0% risk weight pursuant to the Decision on Capital Adequacy;

2) loan which has the following characteristics:
   - loan is granted in accordance with the credit institution’s internal acts;
   - loan beneficiary is financially sound;
   - loan repayment is regular (as at maturity date or with small delay);
   - information and data on the fulfilment of obligations in prior period indicate that loan beneficiary met regularly its obligations; and
   - loan is secured by collateral, which in combination with debtor’s financial condition minimises risk of loan collection.

**Classification group "B"**

**Article 22**

(1) A loan shall be classified into the classification category “B” (subcategories “B1” and “B2”) if there is a small probability of incurring losses, but such loan must be subject to special watch of a credit institution, as the potential risk, if not adequately monitored, might result in poor perspective for its repayment.

(2) A loan classified into the classification category “B” (sub-category “B1” or “B2”) shall have some of the following characteristics:

1) financial information on loan beneficiary are incomplete;
2) loan has not been granted in accordance with the internal acts of the credit institution;
3) the assessment of financial value of collateral is incomplete or inadequately documented;
4) connected loan beneficiaries are not included in the loan analysis;
5) debtor’s financial situation is stable but it has some features that point to possible difficulties in future loan repayment;
6) debtor is over 30 days past due.

(3) A loan that is over 30 days past due may not be classified into higher classification category or sub-category other than sub-category “B1”, and a loan that is over 60 days past due may not be classified in higher classification category or sub-category other than sub-category “B2”.

**Classification category "C"**

**Article 23**

(1) A loan shall be classified into the classification category” C” if there is high probability of incurring losses due to clearly disclosed weaknesses jeopardising their repayment.

(2) A loan classified into the classification category “C” (sub-categories “C1” and “C2”) shall have some of the following characteristics:

1) primary sources of repayment are insufficient to repay debt and the credit institution must use secondary sources to collect debt, i.e. to foreclose the collateral, restructure debt, and the like;

2) current financial possibilities of the loan beneficiary or cash flows are insufficient for the repayment of maturing debt (customer is insufficiently liquid, significantly indebted or not well capitalised, it has critically low level of profitability or operates with loss);
3) negative trend in debtor’s operations exists;
4) there is an indication in short-term loans that loan beneficiary will not be able to convert assets into cash which will result in an inability of the borrower to repay debt when it becomes due;
5) credit institution does not possess required and updated financial information to determine financial ability of customer to repay the debt;
6) loan is over 90 days past due.

(3) A loan that is over 90 days past due may not be classified in higher classification category or sub-category other than sub-category “C1” and a loan that is over 150 days past due may not be classified in higher classification category or sub-category other than sub-category “C2”.

### Classification category "D"

### Article 24

(1) A loan shall be classified into classification category “D” if there is a low probability of the collection of loan in full, taking into consideration debtor’s credit capacity, value and possibility of realisation of collateral.

(2) A loan classified into classification category “D” shall have some of the following characteristics:

1) a business undertaking, which is loan beneficiary is illiquid with insufficient amount of capital, highly leveraged, non-profitable, has serious difficulties or shows permanent non-competitiveness without any perspective for further development, and the like;
2) bankruptcy proceedings have been initiated against the debtor;
3) there is significant credit risk, thus it is quite uncertain if the loan will be collected in full, but there are facts that indicate that there is real expectation for at least partial collection in near future (loan is in the process of collection, loan beneficiary has initiated the procedure of providing additional collateral which will fully secure the loan in case of its enforcement, the credit institution initiated foreclosure of additional instruments of security, and the like);
4) loan is over 270 days past due.

(3) A loan that is over 270 days past due may not be classified in higher classification category or subcategory other than sub-category of category “D”.

### Classification category "E"

### Article 25

(1) A loan shall be classified into classification category “E” if it is fully uncollectible or if

it will be collected in an insignificant amount.

(2) A loan shall be classified into classification category “E” if:
1) regardless of default, it contains at least one characteristic of doubtful assets, it is not fully secured and no facts exist indicating that there is real expectation for at least partial collection in near future;
2) loan is over 365 days past due.

## Classification of small loans

### Article 26

(1) A credit institution may classify loan that does not belong to a category of individually significant receivable referred to in Article 9 paragraph (2) of this Decision into appropriate classification category based on the information on debtor’s regularity in meeting its obligations to the credit institution.

(2) When there is default, loan under paragraph (1) of this Article shall not be classified into higher into classification category or sub-category other than:
1) sub-category “B1”, if the debtor is over 30 days past due,
2) sub-category “B2”, if the debtor is over 60 days past due,
3) sub-category “C1”, if the debtor is over 90 days past due,
4) sub-category “C2”, if the debtor is over 150 days past due,
5) subcategory “D”, if the debtor is over 270 days past due,
6) sub-category “E”, if the debtor is over 365 days past due.

## Assessment of creditworthiness of loan beneficiary for investment projects

### Article 27

(1) In the process of classifying loan granted for the investment project, a credit institution may base its assessment of debtor’s credit capacity on the analysis of profitability of such investment project.

(2) Profitability analysis of the investment project shall include, as a minimum, the following:
1) assessment of reality of business plan and financial projections;
2) assessment of the period required for return on funds invested in the project;
3) project risk sensitivity;
4) assessment if cash flows arising from the project implementation ensure regular fulfilment of debtor’s obligations in accordance with the agreed loan repayment dynamics.

(3) Investment project, within the meaning of paragraph (1) of this Article, means the project from the production or services sectors aimed at promoting the existing activity of the loan applicant, introduction of new products and services, and the like.

(4) The classification of loans referred to in paragraph (1) of this Article may be performed only by a credit institution that has adequate methodology for the assessment of business plans set forth in its internal act.

(5) A credit institution shall regularly monitor projected implementation of the investment project, and based on the analysis of compliance of actual and projected implementation of the investment project and other criteria for asset classification, it shall classify loan into adequate classification category or subcategory.

**Multiple loan holder**

**Article 28**

(1) If one person holds more loans with a credit institution, and one or more of those loans are classified into category of non-performing loans, a credit institution shall classify all receivables to such a person into the lowest classification category or subcategory.

(2) By way of derogation from paragraph (1) of this Article, if more than 90% of total carrying amount of all loans referred to in paragraph (1) above, including outstanding interest, has been classified into the classification categories "A" or "B", a credit institution may keep such loans within the same classification category.

**Loan restructuring**

**Article 29**

(1) A credit institution is deemed to have restructured a loan if, due to deterioration in the debtor’s creditworthiness, it has:

1) extended principal or interest repayment dates;
2) reduced the interest rate on the granted loan;
3) acquired the debtor’s liabilities to a third party, either against full or partial repayment of its loan;
4) reduced the amount of debt, principal or interest;
5) capitalised interest on the loan granted to the debtor;
6) replaced the existing loan with a new loan (loan renewal), or
7) made other similar arrangements that alleviate the debtor’s financial position.

(2) The following shall not be considered to be loan restructuring:

1) change in conditions for principal repayment due to contingencies that are out of the debtor’s control (for instance, delays in project completion), provided that the effective interest rate remains the same as agreed, as long as the interest is paid on time;
2) reduction of interest rate or capitalisation of interest which are not the result of deterioration in the debtor’s credit capacity.

(3) In the procedure of loan restructuring, a credit institution shall:

1) analyse the debtor’s financial position in order to assess whether the debtor will

record cash flows sufficient for principal and interest repayment after the loan restructuring;

2) provide adequate information on the results of restructuring in accordance with the International Accounting Standards and/or the International Financial Reporting Standards, that is:
   – define and determine the fair value at which the credit institution will account for assets obtained in the process of loan restructuring and precisely recognise any loss associated with the loan restructuring, and
   – provide up-to-date accounting of all elements of transactions performed in the process of loan restructuring;
3) apply the concept of fair value assessment for assets acquired against debt collection, provided that:
   – when there is a stable market, the fair value assessment of assets shall be equal to their market value,
   – when the market is unstable or the value of acquired assets cannot be determined, a credit institution shall ensure the fair value assessment of such assets in accordance with professional standards.

## Classification of other balance sheet items

### Article 30

The classification of balance sheet items other than loans shall be performed in line with the applicable criteria referred to in Article 16 of this Decision, as well as based on other facts that are important for establishing the level of potential risk of loss arising from these asset items.

## Classification of off-balance sheet items

### Article 31

(1) The classification of off-balance sheet items that expose a credit institution to credit risk shall be performed in line with the loan classification criteria set out in this Decision by applying those criteria on potential debtor of the credit institution.

(2) The classification of agreed but undrawn loan shall be made if a credit institution was irrevocably obliged to meet outstanding liabilities for that loan arrangement.

## Provisioning

### Article 32

(1) A credit institution shall calculate loan loss provisions for balance sheet and off-balance sheet items by applying the percentages from the table below:

| No. | Classification categories and subcategories | Provisions in percentages |
|---|---|---|
| 1 | Category A – “Pass” | 0.5% |

| | | |
|---|---|---|
| 2 | Category B – “Special mention”<br>sub-category B1<br>sub-category B2 | <br>2%<br>7% |
| 3 | Category C – “Substandard”:<br>sub-category C1<br>sub-category C2 | <br>20%<br>40% |
| 4 | Category D – “Doubtful” | 70% |
| 5 | Category E – “Loss” | 100% |

(2) The base for calculating loan loss provisions in line with paragraph (1) of this Article for individual balance sheet item or off-balance sheet item shall be the carrying amount of such an item deducted by the amount secured by:

1) Cash deposit placed with the credit institution if it has been agreed that it will be used as collateral for certain receivables of the credit institution, and its maturity is not shorter than the maturity of receivable and it is solely at the disposal of the credit institution;
2) Pledge of gold;
3) Debt securities, guarantees, counter-guarantees, other forms of surety or other similar instruments of unfunded credit protection, whose issuers are:
   - Central governments and central banks that are assigned 0% credit risk weight in accordance with the Decision on Capital Adequacy;
   - International development banks and international organisations that are assigned 0% risk weight in accordance with the Decision on Capital Adequacy;
   - Credit institutions that would qualify for at least credit quality step 2 in accordance with the Decision on Capital Adequacy.

(3) Provisions in the amount of 0.5% shall be allocated to the gross carrying amount of balance sheet items and/or off-balance sheet items deducted in accordance with paragraph (2) of this Article.

**Treatment of provisions and allowances for impairment**

**Article 33**

(1) A credit institution shall determine the difference between the amount of provisions for estimated and potential losses calculated in accordance with Article 32 of this Decision and the sum of the amount of allowances for impairment for balance sheet items, calculated in accordance with Article 10 of this Decision and the amount of probable loss for off-balance sheet items calculated in line with Article 11 of this Decision.

(2) The positive difference between the amount of calculated provisions for estimated and potential losses and the sum of the amount of impairment for balance sheet assets and probable loss for off-balance sheet items, determined by individual sub-accounts,

shall be the provisions required for estimated and potential losses.

## IV. CLASSIFICATION OF ASSET ITEMS FOR THE PURPOSE OF ADDITIONAL MONITORING OF ASSET QUALITY

### Classification obligations

### Article 34

A credit institution shall, for the purpose of additional monitoring and reporting on asset quality, classify asset items into the group of performing or non-performing assets, as well as determine the status of restructured loans in accordance with Articles 35 to 37 of this Decision.

### Non-performing and performing assets

### Article 35

(1) A credit institution shall classify asset items as non-performing assets, if:

1) the debtor is over 90 days past due on that asset item;
2) the credit institution, based on the assessment of the financial situation, i.e. creditworthiness of the debtor, estimates that the debtor will not be able to settle obligations under that item in full without the realisation of collateral, regardless of whether the debtor settles its obligations on time or not;
3) the status of non-performance arises for that item in accordance with Article 197 of the Decision on Capital Adequacy; and/or
4) a receivable under that item is considered impaired in accordance with IFRS 9, and is classified in Stage 3 or represents an asset purchased or originated at impairment.

(2) An asset item for which some of the conditions from paragraph (1) of this Article are not fulfilled, shall be classified in the category of performing assets.

(3) An asset item shall be deemed to have ceased to be non-performing if:

1) the exposure is not considered impaired in accordance with IFRS 9 and does not have the non-performing status in accordance with Article 197 of the Decision on Capital Adequacy;
2) the debtor's position has improved in such a way that the credit institution can collect the receivable in full in accordance with the originally established or, if applicable, in accordance with the changed conditions; and
3) the debtor has no obligations from the maturity of which more than 90 days have passed.

(4) The classification of a non-performing asset as a fixed asset held for sale in accordance with IFRS 5 does not terminate its classification as a non-performing exposure.

## Classification of restructured loans into the category of performing loans

## Article 36

(1) A restructured loan that belongs to the category of non-performing assets may be classified by a credit institution into the category of performing loans following the expiry of a period of at least 12 months and provided that the conditions referred to in paragraph (3) of this Article have been met.

(2) A 12-month period referred to in paragraph (1) of this Article shall start from:

1) the moment of loan restructuring, if the restructuring arrangement has not specified grace period for loan repayment; or
2) the expiry of grace period specified under the debt restructuring arrangement, whereby grace period shall be the period during which no principal and interests are made or only interest payment is made.

(3) After the expiry of grace period referred to in paragraph (1) of this Article, the restructured loan may be classified into the category of performing loans only where the credit institution has determined that:

1) a restructured loan meets the requirements for its classification into the category of performing loans by applying the criteria referred to in Article 16 of this Decision;
2) a regular repayment of restructured loan was established in the period of at least 12 months and in accordance with amended repayment plan;
3) a debtor repaid a significant amount of debt within the meaning of Article 37 paragraph (3) of this Decision, or the analysis of debtor's financial situation determined its ability to repay the debt in full in accordance with the restructuring arrangement.

(4) A regular repayment of restructured loan, within the meaning of paragraph (3) item 2) of this Article, shall be the loan repayment that is not more than 30 days past due.

## Termination of the status of restructured loans

## Article 37

(1) A credit institution may stop treating the loan as a restructured loan if the following conditions have been met at the end of probation period:

1) restructured loan is classified in the category of performing loans;
2) a debtor has repaid a significant portion of debt through regular principal or interest payments during at least half of the probation period; and
3) there are no arrears in repayment longer than 30 days under any of the obligations to the credit institution.

(2) A probation period referred to in paragraph (1) of this Article means a period of two years that begins from the moment when a restructured loan is classified into the category of performing loans.

(3) The significant amount of debt, within the meaning of paragraph (1) item 2) of this

Article, shall be deemed to be repaid if the debtor has paid, in accordance with regular payments under the restructuring arrangement, total amount that is equal to the amount of previous outstanding debt (if any) or the amount that was written-off (where no outstanding liabilities existed) under the restructuring arrangement.

(4) If the requirement referred to in paragraph (1) item 1) of this Article has been met at the end of the probation period referred to in paragraph (2) of this Article, and any of the requirements referred to in paragraph (1) items 2) and 3) of this Article have not been met, the probation period shall be extended until the fulfilment of those requirements, and the loan shall be treated as a restructured loan that do not belong to the category of non-performing loans until the expiry of such a period.

(5) A credit institution shall check the fulfilment of the requirements referred to in paragraph (1) items 2) and 3) of this Article at least on quarterly basis.

(6) A credit institution may continue to classify a receivable that was classified into the category of performing loans in the moment of restructuring into the same category if the restructuring has not led to the fulfilment of the requirements for classifying such a receivable into the category of non-performing loans.

(7) In addition to the restructured loans classified into the category of non-performing loans in the moment of restructuring, the credit institution shall classify the following into the same category:

1) loans that met the requirements to be classified into the category of non-performing loans before the restructuring;
2) restructured loans from the category of non-performing loans that were classified into the category of performing loans in accordance with Article 36 paragraph (1) of this Decision and for which the credit institution made additional concessions for the debtor during the probation period referred to in paragraph (2) of this Article, or if the debtor repays obligations under such a receivable in arrears longer than 30 days;
3) loans classified in accordance with paragraph (6) of this Article for which the credit institution made additional concessions for the debtor after the second restructuring.

## V. REPORTING TO THE CENTRAL BANK OF MONTENEGRO

### Article 38

(1) A credit institution shall submit to the Central Bank of Montenegro (hereinafter: the Central Bank) reports on the classification of balance sheet items and off-balance sheet items, information on the amount of calculated loan loss provisions and information on non-performing assets and restructured loans in accordance with the decision governing the reporting of the credit institutions the Central Bank.

(2) If the Central Bank, as part of the supervision procedure, has ordered the credit

institution a stricter classification of balance sheet items or off-balance sheet items, it may require the credit institution to state the new classification also in the reports from the previous reporting period.

## VI. FINAL PROVISION

### Entry into force

### Article 39

This Decision shall enter into force on the day following that of its publication in the Official Gazette of Montenegro, and it shall apply from the date of application of the Law on Credit Institutions (OGM 72/19).

**THE COUNCIL OF THE CENTRAL BANK OF MONTENEGRO**

**CHAIRMAN**
**G O V E R N O R,**

**Radoje Žugić, m.p.**

No. 0101-7725-4/2020
Podgorica, 28 December 2020

**ANNEX 1**

**OVERVIEW**
**of collateral with impairment factors**
**and expected realisation period**

| No. | Collateral | Impairment factor (%) | Realisation period (years) |
|---|---|---|---|
| | **IMMOVABLE PROPERTY** | | |
| 1 | Residential buildings * | 10 | 2 |
| 2 | Residential buildings for sale and/or rent ** | 20 | 3 |
| 3 | Commercial facilities (shopping malls, warehouses, shops, car dealers…) | 20 | 3 |
| 4 | Business premises (offices) | 40 | 4 |
| 5 | Industrial facilities (factories, industrial plants, buildings, farms …) | 50 | 4.5 |
| 6 | Agricultural real estate (mills, silos...) | 40 | 3 |
| 7 | Construction land | 45 | 3 |
| 8 | Agricultural land | 50 | 4 |
| 9 | Built tourist facilitates in operation | 30 | 2 |
| 10 | Construction right | 50 | 3 |
| 11 | Unfinished commercial premises – commercial | 60 | 5 |
| 12 | Unfinished commercial premises – residential/mixed | 60 | 5 |
| 13 | Unfinished tourist premises | 60 | 4 |
| | **MOVABLE PROPERTY** | | |
| 14 | General purpose equipment and devices | 60 | 3 |
| 15 | Special purpose equipment and devices | 60 | 3 |
| 16 | Personal vehicles | 40 | 1.5 |
| 17 | Vehicles (commercial) | 40 | 1.5 |
| 18 | Ships and other vessels | 60 | 5 |
| 19 | Airplanes and helicopters | 60 | 5 |
| 20 | Inventories not under the control of the credit institution | 70 | 3 |
| 21 | Inventories under the control of the credit institution | 65 | 3 |
| 22 | Precious metals, works of art - not deposited with the credit institution | 60 | 3 |
| 23 | Precious metals, works of art - deposited with the credit institution | 40 | 3 |
| 24 | Construction machinery | 60 | 3 |
| 25 | Production machinery | 60 | 3 |
| 26 | Agricultural machinery | 60 | 3 |

<u>Note:</u>
* individual apartments
** provided that the building is completed and has a use permit
*** provided that they have a valid insurance policy
Encumbrances are deducted after determining the fair value