

Ordinance No. 7

of 22 December 2006

on the Large Exposures of Banks

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Chapter One

General Provisions

Subject

Article 1. (1) This Ordinance shall define the permissible limit of overall exposure concentration risk for a bank or a bank group.

(2) The main purpose of this Ordinance is to limit the loss sustained by a bank or a bank group from concentration of exposures.

Exposure

Article 2. (1) An exposure to an individual person or economically connected persons within the meaning of Article 44, paragraph 2 of the Law on Credit Institutions shall be:

1. all balance sheet assets set forth in Chapter Four *Standardized Approach* of BNB Ordinance No. 8 of 2006 on the Capital Adequacy of Credit Institutions (hereinafter referred to as BNB Ordinance No. 8) prior to the application of risk weights;
2. off-balance sheet items under Appendix 2 *Classification of Off-balance Sheet Items* of BNB Ordinance No. 8 prior to the application of risk weights and conversion factors.

(2) The following shall be executed from the exposures under paragraph 1:

1. exposures set off against the bank's capital base under Chapter Two *Supervisory Requirements*, Section I *Own Funds (Capital Base)* of BNB Ordinance No. 8;
2. exposures incurred in the ordinary period for settlement of foreign exchange transactions within 48 hours following the payment under the transaction;
3. exposures incurred in the usual period for settlement of trades in securities within the first five working days after the payment or delivery of securities, whichever is earlier.

Large Exposure

Article 3. (1) A large exposure, within the meaning of Article 44, paragraph 3 of the Law on Credit Institutions, shall be established on solo or consolidated basis as the sum total of exposures to an individual person or economically connected persons.

(2) The decisions under Article 44, paragraph 4 of the Law on Credit Institutions resulting in a large exposure to an individual person or economically connected persons shall be made prior to the occurrence of the exposure.

(3) A large exposure is in place where it results from:

1. reduction of own funds (capital base) as provided for in BNB Ordinance No. 8;
2. newly arising relatedness between individual persons, or an individual person and economically connected persons, which the bank is already exposed to;
3. change in the market prices or other factors influencing the value of the bank's existing exposures.

Trading Book Exposures

Article 4. (1) Banks calculating capital requirements for market risk shall measure and report large exposures incurred to an individual person or economically connected persons as the sum total of the exposures in their trading and non-trading books.

(2) An exposure to a single person or economically connected persons in a bank's trading book shall include:

1. the positive balance between long and short positions on all financial instruments issued by a single person or economically connected persons, whereas the net positions for each instrument are calculated in the manner defined in Article 277 of BNB Ordinance No. 8;
2. in case of underwriting of a debt or equity instrument issue the resulting net exposure is calculated according to Article 295 of BNB Ordinance No. 8;
3. exposures calculated pursuant to Articles 242, 244 and 273 of BNB Ordinance No. 8 in relation to transactions or agreements incurring settlement risk or counterparty risk.

(3) Exposures to a group of economically connected persons incurred in a bank's trading book shall be calculated by adding up all individual exposures to each person in the group.

Special Exposures

Article 5. In case of a syndicated loan or joint underwriting of issues, including on NIF and RUF transactions, the participating bank shall report an exposure corresponding to its share thereof, or in compliance with the terms of the contract.

Banks' Internal Rules

Article 6. (1) Banks/bank groups shall develop and maintain adequate administrative and accounting procedures and adequate internal control mechanisms for the purposes of identifying and recording all large exposures and any subsequent changes therein, and for monitoring such exposures in accordance with the bank's policy.

(2) In their lending rules, adopted pursuant to Article 73, paragraph 3 of the Law on Credit Institutions, banks/bank groups shall provide for the cases of overall risk for the bank caused by higher credit concentration due to newly emerged relatedness.

(3) In their lending rules, banks shall impose restrictions on concentration of exposures to specific economic sectors and/or geographic regions.

(4) Banks shall analyze their exposures to collateral issuers to find any concentration risk, and where concentrations over 10% of own funds are found out, they should take steps and report these circumstances to the BNB.

(5) Banks shall submit to the Bulgarian National Bank, Banking Supervision Department, a copy of the rules under paragraph 2 within 10 days after their adoption, amendment, respectively.

Chapter 2

ESTABLISHING THE AMOUNT OF LARGE EXPOSURES

Calculation

Article 7. (1) For the purpose of calculation of the exposure to a single person or economically connected persons, the exposures under Article 2, paragraph 1, shall be summed up prior to applying any risk weights or conversion factors under BNB Ordinance No. 8.

(2) Banks calculating capital requirements for market risk measure and report existing large exposures to a single person or economically connected persons as the sum total of their trading and non-trading book exposures prior to application of risk weights and conversion factors.

(3) Determining an exposure as a large one shall be done by comparing the exposure to the own funds (capital base) of the bank/bank group.

(4) Exposures to derivatives under Appendix 1 *List of Derivatives* to BNB Ordinance No. 8 shall be calculated in accordance with one of the methods set forth in Chapter Eight *Treatment of Counterparty Credit Risk*, Section III *Method Selection* of BNB Ordinance No. 8.

(5) Where the BNB has authorized the application of Chapter Eight *Treatment of Counterparty Credit Risk*, Section IV *Internal Model Method* of BNB Ordinance No. 8, the models can be used to determine the value of the following exposures:

1. the contracts under Appendix 1 *List of Derivatives* of BNB Ordinance No. 8;
2. repurchase agreements;
3. securities lending/borrowing transactions;
4. margin lending transactions;
5. long settlement transactions.

Exposure Scope

Article 8. (1) Where individual persons are found to be connected on a consolidated or non-consolidated basis, the exposures to them shall be summed up and reported as one exposure.

(2) Where an exposure is directly and unconditionally guaranteed by a third party, or by collateral in the form of securities issued by a third party, the exposure shall be treated as an exposure to the third party, up to the amount of the secured portion, if the third party is not connected to the persons whose obligation it guarantees.

(3) The guarantees under paragraph 2 shall also include credit derivatives recognized under Chapter Six *Credit Risk Reduction* of BNB Ordinance No. 8 other than credit linked debt securities.

(4) Where the guarantee is denominated in a currency different from the currency of the exposure, the amount of the exposure deemed to be covered shall be calculated in accordance with the provisions on the treatment of a currency mismatch in a guarantee protection pursuant to Chapter Six *Credit Risk Reduction* of BNB Ordinance No. 8. The maturity mismatch of the exposure and of the protection shall be treated in keeping with the provisions of Chapter Six *Credit Risk Reduction* of BNB Ordinance No. 8.

Reductions

Article 9. (1) When calculating their large exposures as per Article 2 banks may include certain exposures of reduced amount by applying an adjusting 0% ratio to the following exposures:

1. exposures to central governments or central banks where unsecured exposures to these institutions would attract a 0% risk weight as per Chapter Four *Standardized Approach* of BNB Ordinance No. 8;

2. exposures to international organizations or multinational development banks where unsecured exposures to such institutions would attract a 0% risk weight as per Chapter Four *Standardized Approach* of BNB Ordinance No. 8;

3. exposures secured by unconditional guarantees of central governments, central banks, international organizations, multinational development banks or public sector enterprises where unsecured exposures to the person providing the guarantee would attract a 0% risk weight as per Chapter Four *Standardized Approach* of BNB Ordinance No. 8;

4. other exposures to or guaranteed by central governments, central banks, international organizations, multinational development banks or public sector entities where unsecured claims on the person, to which the exposure is attributable or by which it is guaranteed, would attract a 0% risk weight under Chapter Four *Standardized Approach* of BNB Ordinance No. 8;

5. claims and other exposures to central governments or central banks not listed in item 1, which are denominated and funded in the borrowers' national currencies;

6. exposures to regional governments and local authorities or guaranteed by them, which would attract a 0% risk weight as per Chapter Four *Standardized Approach* of BNB Ordinance No. 8.

7. other exposures secured by a collateral of debt securities issued by central governments or central banks, international organisations, multilateral development banks, Member States' regional governments, local authorities or public sector entities of Member States where the securities are claims on their issuers and the exposures to these issuers would attract a 0% risk weight as per Chapter Four *Standardized Approach* of BNB Ordinance No. 8.

8. exposures secured by collateral of cash deposits placed with the lending bank or with a bank, which is the parent undertaking or a subsidiary to the lending bank;

9. exposures secured by collateral of deposit certificates issued by the lending bank or by a bank, which is a parent undertaking or a bank subsidiary, and placed with one of them;

10. claims and other exposures to institutions within the meaning of BNB Ordinance No. 8 with a residual maturity of up to one year where these are not included in the institutions' own funds;

11. bills of trade and other similar bills with a maturity of up to one year bearing the signatures of other banks;

12. covered bonds falling within the terms of Chapter Four *Standardized Approach* of BNB Ordinance No. 8;

13. holdings in insurance companies of up to 40% of the own funds of the bank that has acquired such holdings;

14. exposures to regional or central banks, with which the lending bank is associated in a network according to a legislative act and which are responsible, under the legislative act, for cash-clearing operations within the network;

15. equalised off-balance sheet items under item 4 of Appendix 2 *Classification of Off-balance Sheet Items* of BNB Ordinance No. 8 where the contract with an individual person or economically connected persons explicitly states that the exposure can be assumed only where this does not result in exceeding the limits of Article 44, paragraphs 5 and 6 of the Law on Credit Institutions.

(2) Where banks calculate large exposures under Article 2, they may include certain exposures of reduced amounts by applying a 20% adjustment ratio to the following exposures:

1. exposures to regional or local authorities or guaranteed by them where these claims would attract a 20% risk weight as per Chapter Four *Standardized Approach* of BNB Ordinance No. 8;

2. exposures to institutions with a residual maturity between 1 and 3 years where they are not included in those institutions' own funds.

(3) When calculating the large exposures under Article 2 banks may include certain exposures of reduced amount by applying an adjusting ratio of 50% to the following exposures:

1. debt securities with a residual maturity of above 3 years issued by institutions where those securities are subject to daily quotations and trading on recognized stock exchanges, or where their issuance is approved by the home competent bodies of the issuing institution. This treatment is not allowed where the securities are an element of the issuing institution's own funds;

2. off-balance sheet items in item 3 of Appendix 2 *Classification of Off-balance Sheet Items* of BNB Ordinance No. 8;

3. exposures falling under the terms of Article 39, paragraph 2 of BNB Ordinance No. 8;

4. exposures in relation to lease deals falling under the terms of Article 42 of BNB Ordinance No. 8 where the lessor retains ownership over the housing property for the period prior to exercising the right to final purchase by the lessee.

Chapter Three

EXPOSURES WITHIN A BANK GROUP

Subsidiaries of Member State Banks

Article 10. An exposure of a bank, which is a subsidiary to another bank licensed in a Member State, to the parent bank or to other subsidiaries in the group, shall not be included in determining the ratio under Article 44, paragraphs 5 and 6 of the Law on Credit Institutions where that exposure is not included in the own funds of the parent bank or of the subsidiaries.

Subsidiaries to Third Country Banks

Article 11. An exposure of a bank licensed in the Republic of Bulgaria, which is a subsidiary to a bank domiciled in a third country, to the parent bank or to other subsidiaries in the group, as well as to its own subsidiaries, where the exposure is not included in these companies' own funds, shall not participate in determining the ratio under Article 44, paragraphs 5 and 6 of the Law on Credit Institutions where the following conditions are in place:

1. the bank is licensed in a country of recognized equivalent supervision;
2. the bank is subject to consolidated banking supervision by the country where it was licensed;
3. there is a bilateral agreement for information exchange between the supervisory bodies of the two countries.

Chapter 4

NOTIFICATION AND REPORTING OF LARGE EXPOSURES

Notification of Connected Persons

Article 12. Each customer shall be required by the bank, prior to incurring an exposure, to submit information of the existence or absence of economic connection with other persons as well as of any newly occurred connections or changes in the existing one.

Notifications of Large Exposures

Article 13. (1) Banks shall submit to the Banking Supervision Department of the Bulgarian National Bank notifications under Article 71, paragraph 1, item 5 of the Law on Credit Institutions within 10 days following the decision resulting in incurring a large exposure.

(2) In case of occurrence of a large exposure to individual customers, banks shall submit notifications of the existence of economic connection between them.

(3) Banks shall notify of a large exposure, formed under the provisions of Article 3, paragraph 3, within 10 days of its occurrence.

Reporting of Large Exposures

Article 14. (1) Exposures to individual customers, which are economically connected within the meaning of § 1, item 5 of the Additional Provisions to the Law on Credit Institutions, are regarded as individual exposures to ‘economically connected persons’.

(2) When reporting large exposures, reductions under Article 9, shall be reported as an integral part of the overall report.

(3) Collaterals under Article 9, paragraph 3, items 3 and 4 shall be specified in their full amount in the report on large exposures.

(4) Interbank exposures shall be reported in their full amount.

Reporting

Article 15. (1) Banks shall draw-up and submit a report on the large exposures to the Banking Supervision Department of the Bulgarian National Bank by the 15th day of the month following the reporting quarter.

(2) The Deputy Governor of the Bulgarian National Bank heading the Banking Supervision Department shall give mandatory instructions on the manner of drawing up and submitting reports on large exposures.

(3) The Banking Supervision Department may require additional information on each individual exposure.

Consolidated Report

Article 16. Banks and bank groups shall also draw up a consolidated report on large exposures, according to the procedure established in a special BNB ordinance.

Chapter Five

CONTROL AND MEASURES FOR ELIMINATION OF VIOLATIONS

Control

Article 17. (1) Bank supervisory bodies of the Bulgarian National Bank shall conduct examinations of the correctness of large exposures reports, including on-site inspections and comparisons between the data in the reports and that from the accounting and the operative reporting of banks.

(2) The certified auditors under Article 76, paragraph 1 of the Law on Credit Institutions shall conduct an inspection and prepare an opinion on concentration of exposures.

Additional Provision

§ 1. Within the meaning of this Ordinance:

1. ‘NIF (note issuance facility)’ shall mean a loan transaction connected with the issuance of securities by a customer through the intermediation and under the management of the bank, where the bank sets a limit for the customer, up to which it accepts to buy back the securities issued by the customer on this transaction.

2. ‘RUF (revolving underwriting facility)’ shall mean a loan transaction, a version of NIF, where not a bank but a group of banks intermediates in the issuance of a customer’s securities, setting a limit, usually covering the full amount of the issue, up to which the group of banks accepts to buy the securities issued by the customer, in case the securities are not sold, and up to the amount of the announced issue which is not sold through the public subscription.

3. ‘Syndicated loan’ shall mean financing by a group of banks or financial institutions in which everyone individually participates in the total amount of the loan.

4. ‘Individual person’ shall mean each physical person or legal entity, as well as partnerships under civil law or other associations of such persons, with no legal personality, as well as central governments, regional or local authorities, in their capacity of individual obligors to the bank.

5. ‘Own funds (capital base)’ shall mean capital within the meaning of Ordinance No. 8 of the BNB.

6. ‘Directly and unconditionally guaranteed exposure’ shall mean an exposure for which a guarantee meeting the requirements below was issued:

a) the guarantee ensures an unconditional payment in favour of the bank upon first request with no possibility to object or arrange other formal conditions for payment; and

b) is irrevocable and with validity longer than the agreed term for the execution of the guaranteed obligation; and

c) the only condition for its claiming is the guarantor to receive a written request from the bank, in favour of which the guarantee is issued, containing a statement that the debtor does not honour the obligation covered by the guarantee; and

d) there are no other persons entitled to claim a payment under the guarantee; and

e) with the exception of the amount, there exists a complete correspondence between the obligation of the customer to the bank (secured receivable) and the obligation, specified in the guarantee, and the guarantee covers all types of failures to execute that obligation.

7. 'Trading' and 'non-trading books' shall mean books within the meaning of Ordinance No. 8 of the BNB.

Transitional and Final Provisions

§ 2. This Ordinance is issued on the grounds of Article 44 of the Law on Credit Institutions and, is adopted by Resolution 169 of 22 December 2006 of the Governing Council of the Bulgarian National Bank.

§ 3. This Ordinance shall be applied also for banks' exposures existing at the time of its coming into force.

§ 4. The Deputy Governor of the Bulgarian National Bank heading the Banking Supervision Department shall provide instructions with regard to the implementation of this Ordinance.

