

DECISION

ON CAPITAL ADEQUACY OF THE DEVELOPMENT BANK OF MONTENEGRO

(OGM 094/25 of 12 August 2025, 028/26 of 4 March 2026)

I. GENERAL PROVISIONS

Subject Matter

Article 1

This Decision governs types and features of elements to be included in own funds, the method of calculating own funds, the calculation of total exposure to risk, capital requirements relating to credit risk, operational risk, and market risk, the methods and approaches for calculating capital requirements and the method of calculating capital adequacy ratios of the Development Bank of Montenegro (hereinafter: the Development Bank).

Meaning of terms

Article 2

The terms used in this Decision shall have the following meaning:

- 1) own funds instruments mean capital instruments issued by the Development Bank that meet the requirements for Common Equity Tier 1 instruments, Additional Tier 1 instruments, or Tier 2 instruments;
- 2) share premium account has the same meaning as under the applicable accounting framework;
- 3) other reserves mean reserves within the meaning of the applicable accounting framework that are required to be disclosed under the applicable accounting standard, excluding any amounts already included in accumulated other comprehensive income or retained earnings;
- 4) applicable accounting framework means the accounting standards to which the Development Bank is subject under the regulations governing its accounting;
- 5) accumulated other comprehensive income has the same meaning as under the applicable accounting framework;
- 6) profit has the same meaning as under the applicable accounting framework;
- 7) retained earnings means profits and losses brought forward as a result of the final application of profit or loss under the applicable accounting framework;
- 8) distribution means dividend or interest payment in any form;
- 9) intangible assets have the same meaning as under the applicable accounting framework and includes goodwill;
- 10) financial sector entity means:
 - credit institution;
 - investment firm;
 - financial institution;

- ancillary services undertaking included in the consolidated financial position of an institution;
 - insurance undertaking;
 - third-country insurance undertaking;
 - reinsurance undertaking;
 - third-country reinsurance undertaking;
 - insurance holding company, which means a parent undertaking which is not a mixed financial holding company and the main business of which is to acquire and hold participations in subsidiary undertakings, where those subsidiary undertakings are exclusively or mainly insurance or reinsurance undertakings, or third-country insurance or reinsurance undertakings, at least one of such subsidiary undertakings being an insurance or reinsurance undertaking;
 - insurance undertaking excluded from the scope of application of regulations governing the operations of insurance undertakings due to its size;
 - third-country undertaking with a main business comparable to any of the entities referred to in indents 1 to 9 of this item.
- 11) non-financial sector entity means a business undertaking other than a financial sector entity, except a business undertaking that is not a financial sector entity but performs the operations deemed by the Central Bank of Montenegro (hereinafter: the Central Bank) to represent:
- a type of banking services;
 - ancillary services;
 - lease operations, factoring, management of investment funds, management of data processing services, and similar operations.
- 12) indirect holding means any exposure to an intermediate entity that has an exposure to capital instruments issued by the financial sector entity, or to liabilities issued by the Development Bank where, in the event the capital instruments issued by the financial sector entity or the liabilities issued by the Development Bank were permanently written off, the loss that the Development Bank would incur as a result would not be materially different from the loss the Development Bank would incur from a direct holding of those capital instruments issued by the financial sector entity or of those liabilities issued by the Development Bank;
- 13) exposure means an asset or off-balance sheet item of the Development Bank laid down in accordance with Article 20 of this Decision;
- 14) conversion factor means the ratio of the undrawn amount of a commitment from a single facility that could be drawn from that single facility from a certain point in time before default and therefore outstanding at default to the undrawn amount of the commitment from that facility, the extent of the commitment being determined by the advised limit, unless the unadvised limit is higher;
- 15) derivative contracts mean interest-rate contracts, foreign-exchange contracts and contracts concerning gold, and other contracts of similar nature underlying other items or indices, including, as a minimum, instruments such as: options, futures, swaps, forward rate agreements and any other derivative contracts relating to securities, commodities, financial indices or financial measures which may be settled physically or in cash, and financial contracts for differences;
- 16) central government means bodies of the government administration, government agencies and other entities whose authorities refer to the entire territory of Montenegro, a Member State or a third country, and which are, in accordance with the regulation governing the statistical reporting, classified as the central government.
- 17) public sector entity means a non-profit body responsible to the central government, or local self-government, or to authorities that have the same powers as local self-government, or a non-profit undertaking that is owned by or set up and sponsored or guaranteed for by the central government or local self-government;

- 18) retail exposure means an exposure that meets the conditions set out in Article 29 paragraph (1) of this Decision;
- 19) financial institution means a legal person, other than a credit institution or an investment firm, the principal or predominant activity of which is to acquire holdings in capital or to pursue one or more principal financial services set forth in item 20) of this paragraph, including a financial holding company, a mixed financial holding company, a payment institution, an asset management company, but excluding insurance holding companies and mixed-activity insurance holding companies;
- 20) core financial services mean:
- taking deposits or other repayable funds;
 - lending, including: consumer loans, mortgage loans and non-banking loans for financing of commercial transactions, purchase of receivables, factoring with or without recourse, including export financing based on purchase at a discount and without recourse of long-term receivables secured by financial instruments (forfeiting);
 - financial leasing;
 - providing payment services, in accordance with a separate law;
 - issuing guarantees or other sureties;
 - trading for own account or for the account of clients in:
 - a) money market instruments (cheques, bills of exchange, certificates of deposit),
 - b) transferable securities,
 - c) foreign means of payment, including foreign exchange operations,
 - d) financial futures and options,
 - e) exchange and interest-rate instruments;
 - lending-related services, such as: data collection, developing analysis and providing information on creditworthiness of legal persons and entrepreneurs;
 - issuing other payment instruments and administering such instruments, insofar as the provision of such services is not deemed to be the provision of services referred to in indent 6 of this item;
 - safe deposit box services;
 - money market broking;
 - participation in financial instruments issues and the provision of services relating to financial instruments issues, in accordance with regulations governing the capital markets;
 - client's asset management and advice related to such asset management;
 - custody services, in accordance with regulations governing the capital markets;
 - advice to legal persons on capital structure, business strategy and related issues and the provision of services relating to status changes, acquisition of shares and participation in other undertakings;
 - issuing electronic money; and
 - investment and ancillary services and activities in accordance with the law governing the capital markets not being services referred to in indents 1 to 15 of this item.
- 21) marking to market means the valuation of positions at readily available close out prices that are sourced independently, including exchange prices, screen prices or quotes from several reputable brokers;
- 22) recognised exchange means an exchange which is a regulated market or a third-country market that is considered to be equivalent to a regulated market and it has a clearing mechanism;
- 23) nominated external credit assessment institution (ECAI) means an external credit assessment institution nominated by the Development Bank;
- 24) credit risk mitigation means a technique used by the Development Bank to reduce the credit risk associated with an exposure or exposures which the Development Bank continues to hold;
- 25) funded credit protection means a technique of credit risk mitigation where the reduction of the credit risk on the exposure of the Development Bank derives from the right of the Development

Bank, in the event of the default of the counterparty or on the occurrence of other specified credit events relating to the counterparty, to liquidate, or to obtain transfer or appropriation of, or to retain certain assets or amounts, or to reduce the amount of the exposure to, or to replace it with, the amount of the difference between the amount of the exposure and the amount of a claim on the Development Bank;

- 26) unfunded credit protection means a technique of credit risk mitigation where the reduction of the credit risk on the exposure of the Development Bank derives from the obligation of a third party to pay an amount in the event of the default of the borrower or the occurrence of other specified credit events;
- 27) market value of immovable property means the estimated amount for which the immovable property might be exchanged on the date of valuation between a willing buyer and a willing seller in an arm's-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion;
- 28) trading book means all positions in financial instruments and commodities held by the Development Bank either with trading intent, or in order to hedge positions held for trading intent.
- 29) third country, within the meaning of this Decision, is a foreign country that is not an EU Member State.

II. OWN FUNDS

Own funds

Article 3

Own funds of the Development Bank shall be a sum of Tier 1 capital and Tier 2 capital.

Tier 1 capital

Article 4

Tier 1 capital of the Development Bank shall be the sum of Common Equity Tier 1 capital and Additional Tier 1 capital of the Development Bank.

Common Equity Tier 1 capital and Common Equity Tier 1 capital items

Article 5

(1) Common Equity Tier 1 capital of the Development Bank shall consist of the Common Equity Tier 1 items as established in paragraph (2) of this Article reduced by deductible items referred to in Article 10 of this Decision.

(2) Common Equity Tier 1 capital of the Development Bank shall consist of the following items:

- 1) capital instruments, provided that the conditions referred to in Article 6 of this Decision are met;
- 2) share premium accounts related to instruments referred to in item 1) of this paragraph;
- 3) retained earnings;
- 4) accumulated other comprehensive income; and
- 5) other reserves.

(3) The items referred to in paragraph (2) items 3) to 5) of this Article shall be recognised as Common Equity Tier 1 capital only where they are available to the Development Bank for unrestricted and immediate use to cover risks or losses as soon as these occur.

Common Equity Tier 1 instruments

Article 6

(1) Capital instrument shall qualify as Common Equity Tier 1 instruments only if all the following conditions are met:

- 1) the instruments are issued directly by the Development Bank based on the decision of the Development Bank's Shareholders Assembly or, where permitted under applicable regulations, the decision of the competent bodies of the Development Bank;
- 2) the instrument is fully paid up and the acquisition of ownership of that instrument is not funded directly or indirectly by the Development Bank;
- 3) the instrument qualifies as capital, it is classified as equity in accordance with the applicable accounting framework;
- 4) the instrument is clearly and separately disclosed on the balance sheet of the Development Bank;
- 5) the instrument is perpetual;
- 6) the principal amount of the instrument may not be reduced or repaid, except in the case of the cessation of operation of the Development Bank;
- 7) the provisions governing the instrument do not indicate expressly or implicitly that the principal amount of the instrument would or might be reduced or repaid other than in the cessation of operation of the Development Bank, and the Development Bank does not otherwise provide such an indication prior to or at issuance of the instrument;
- 8) compared to all the capital instruments issued by the Development Bank, the instrument absorbs the first and proportionately greatest share of losses as they occur, and each instrument absorbs losses to the same degree as all other Common Equity Tier 1 instruments;
- 9) the instrument ranks below all other claims in the event of cessation of operation of the Development Bank;

(2) For the purposes of paragraph (1) item 2) of this Article, only the part of a capital instrument that is fully paid up shall be eligible to qualify as a Common Equity Tier 1 instrument.

(3) Indirect funding of capital instruments for the purposes of Article 6 paragraph (1) item 2) of this Decision shall be the funding that is not direct.

(4) Direct funding shall refer to a situation where the Development Bank grants a loan or funds it in any other form for the purchase of its capital instruments.

Consequences of the conditions for Common Equity Tier 1 instruments ceasing to be met

Article 7

The following shall apply where a Common Equity Tier 1 instrument ceases to meet the conditions laid down in Article 6 of this Decision:

- 1) that instrument shall immediately cease to qualify as a Common Equity Tier 1 instrument;
- 2) the share premium account related to that instrument shall immediately cease to qualify as a Common Equity Tier 1 item.

Deductible items from Common Equity Tier 1

Article 8

- (1) The Development Bank shall deduct the following items from Common Equity Tier 1:
- 1) losses for the current financial year;
 - 2) intangible assets;
 - 3) deferred tax assets that rely on future profitability;
 - 4) required provisions for estimated and potential losses for balance sheet and off-balance sheet items, as established in accordance with the regulation governing the criteria and the method of asset classification and calculation of provisions for potential loan losses of the Development Bank;
 - 5) direct and indirect holdings by the Development Bank of own Common Equity Tier 1 instruments, including own Common Equity Tier 1 instruments that the Development Bank is under an actual or contingent obligation to purchase by virtue of an existing contractual obligation;
 - 6) direct and indirect holdings by the Development Bank of the Common Equity Tier 1 instruments of financial sector entities that exceeds 10% of Common Equity Tier 1 of the Development Bank, established after application of deductions referred to in items 1) to 5) of this paragraph;
 - 7) the amount of qualifying holdings in persons engaged in non-financial business activity exceeding the limits prescribed in Article 36 paragraphs (1) and (2) of the Law on the Development Bank of Montenegro (hereinafter: the Law);
 - 8) any tax charge relating to Common Equity Tier 1 items foreseeable at the moment of its calculation, except where the Development Bank suitably adjusts the amount of Common Equity Tier 1 items insofar as such tax charges reduce the amount up to which those items may be used to cover risks or losses.
- (2) For the purposes of calculating the threshold referred to in paragraph (1) item 7) of this Article, Common Equity Tier 1 shall be determined after application of deductible items referred to in paragraph (1) items 1) to 5) of this Article.

Additional Tier 1 capital

Article 9

- (1) Additional Tier 1 items of the Development Bank shall consist of the following:
- 1) capital instruments, provided that the conditions referred to in Article 10 paragraph (1) of this Decision are met;
 - 2) share premium accounts related to instruments referred to in item 1) of this paragraph;
- (2) Instruments referred to in paragraph (1) item 1) of this Article shall not qualify as Common Equity Tier 1 or Tier 2 items.

Additional Tier 1 instruments

Article 10

- (1) Capital instruments shall qualify as Additional Tier 1 instruments only if all the following conditions are met:
- 1) the Development Bank has directly issued the instruments and they are fully paid up;
 - 2) the instruments are owned by the Government of Montenegro;
 - 3) the acquisition of the instruments is not funded directly or indirectly by the Development Bank;

- 4) the instruments rank below Tier 2 instruments in the event of the cessation of operation of the Development Bank;
- 5) the instruments are neither secured nor subject to a guarantee that enhances the seniority of the claims of the Development Bank or its subsidiary undertakings;
- 6) the instruments are perpetual and the provisions governing them include no incentive for the Development Bank to redeem them;
- 7) where the instruments include one or more early redemption options including call options, the options are exercisable at the sole discretion of the issuer;
- 8) the provisions governing the capital instrument require that, upon the occurrence of a trigger event, the principal amount of the instrument be written down on a permanent or temporary basis or the instrument be converted to Common Equity Tier 1 instrument;
- 9) the provisions governing the instrument include no feature that could hinder the recapitalisation of the Development Bank;
- 10) the instrument is not subject to a set-off or netting arrangement that would undermine its capacity to absorb losses.

(2) For the purposes of paragraph (1) item 1) of this Article, only the part of a capital instrument that is fully paid up shall be eligible to qualify as Additional Tier 1 instrument.

(3) For the purposes of paragraph (1) item 6) of this Article, incentives to redeem shall mean all features that provide, at the date of issuance, an expectation that the capital instrument is likely to be redeemed.

- (4) The incentives to redeem referred to in paragraph (3) of this Article shall include the following forms:
- 1) a call option combined with an increase in the credit spread of the instrument, if the call is not exercised;
 - 2) a call option combined with a requirement or an option to convert the instrument into a Common Equity Tier 1 instrument, where the call is not exercised;
 - 3) a call option combined with a change in reference rate where the credit spread over the second reference rate is greater than the initial payment rate minus the swap rate;
 - 4) a call option combined with an increase of the redemption amount in the future;
 - 5) a remarketing option combined with an increase in the credit spread of the instrument or a change in reference rate where the credit spread over the second reference rate is greater than the initial payment rate minus the swap rate where the instrument is not remarketed.

Write down or conversion of an Additional Tier 1 instrument

Article 11

(1) For the purposes of Article 10 paragraph (1) item 9) of this Decision, the following provisions shall apply to an Additional Tier 1 instrument:

- 1) a trigger event occurs when the Common Equity Tier 1 capital ratio of the Development Bank falls below either of the following:
 - 6.5 %;
 - a level higher than 6.5%, where determined by the Development Bank and specified in the provisions governing the Additional Tier 1 instrument;
- 2) the Development Bank may specify in the provisions governing the instrument one or more trigger events in addition to that referred to in item 1) of this paragraph;
- 3) where the provisions governing the instrument require it to be converted into a Common Equity Tier 1 instrument upon the occurrence of a trigger event, those provisions shall specify either of the following:
 - the rate of such conversion and a limit on the permitted amount of conversion;

- a range within which the instrument will convert into Common Equity Tier 1 instrument;
- 4) where the provisions governing the instrument require its principal amount to be written down upon the occurrence of a trigger event, the write down shall reduce all the following:
 - the claim of the holder of the instrument in the in the event of the cessation of operation of the Development Bank;
 - the amount required to be paid in the event of the call or redemption of the instrument;
 - the distributions made on the instrument.

(2) The amount of Additional Tier 1 instruments recognised as Additional Tier 1 items is limited to the minimum amount of Common Equity Tier 1 items that would be generated if the principal amount of the Additional Tier 1 instruments were fully written down or converted into Common Equity Tier 1 instruments.

(3) The aggregate amount of Additional Tier 1 instruments that is required to be written down upon the occurrence of a trigger event shall be no less than the lower of the following:

- 1) the amount required to fully restore the Common Equity Tier 1 ratio of the credit institution to 6.5%;
- 2) the full principal amount of the instrument.

(4) When a trigger event occurs, the Development Bank shall do the following:

- 1) immediately notify the Central Bank;
- 2) notify the holders of the Additional Tier 1 instruments; and
- 3) write down the principal amount of the instruments, or convert the instruments into Common Equity Tier 1 instruments no later than within one month, in accordance with the requirement laid down in this Article.

(5) All necessary authorisations shall be obtained by the Development Bank at the date of issuance of convertible Additional Tier 1 instruments referred to in paragraph (6) of this Article and the Development Bank shall maintain at all times the necessary prior authorisation to issue the Common Equity Tier 1 instruments into which such Additional Tier 1 instruments would convert upon occurrence of a trigger event.

(6) Where the Development Bank has established that the Common Equity Tier 1 ratio has fallen below the level specified in paragraph (1) item 1) of this Article that activates conversion or write-down of the instrument, the management body or any other competent body of the Development Bank shall without delay determine that a trigger event has occurred and there shall be an irrevocable obligation to write down or convert the instrument.

(7) The amount to be written down or converted shall be determined as soon as possible and within a maximum period of one month from the day when it is determined that the trigger event has occurred pursuant to paragraph (6) of this Article.

(8) Where an independent review of the amount to be written down or converted is required according to the provisions governing the Additional Tier 1 instruments, or where the Central Bank requires an independent review for the determination of the amount to be written down or converted, the management body or any other competent body of the Development Bank shall see that this is done immediately. The independent review shall be completed as soon as possible and shall not create impediments for the Development Bank to write down or convert the Additional Tier 1 instrument and to meet the requirements laid down in paragraph (7) of this Article.

Consequences of the conditions for Additional Tier 1 instruments ceasing to be met

Article 12

The following shall apply where an Additional Tier 1 instrument ceases to meet the conditions laid down in Article 10 paragraph (1) of this Decision:

- 1) that instrument shall no longer qualify as an Additional Tier 1 instrument; and
- 2) the part of the share premium account related to that instrument shall immediately cease to qualify as Additional Tier 1 item.

Tier 2 capital

Article 13

(1) Tier 2 capital of the Development Bank shall consist of the following items:

- 1) capital instruments, provided that the conditions referred to in Article 14 of this Decision are met;
- 2) share premium accounts related to instruments referred to in item 1) of this paragraph;

(2) Item referred to in paragraph (1) item 1) of this Article shall not qualify as Common Equity Tier 1 or Additional Tier 1 items.

Tier 2 instruments

Article 14

(1) Capital instruments shall qualify as Tier 2 instruments, provided that the following conditions are met:

- 1) the instruments are directly issued by the Development Bank and fully paid up;
- 2) the instruments are owned by the Government of Montenegro.

(2) For the purposes of paragraph (1) item 1) of this Article, only the part of a capital instrument that is fully paid up shall be eligible to qualify as Tier 2 instrument.

Amortisation of Tier 2 instruments

Article 15

(1) The full amount of a Tier 2 instrument with a residual maturity of more than five years shall qualify as a Tier 2 item.

(2) The extent to which a Tier 2 instrument qualifies as a Tier 2 item during the final five years of maturity of the instrument shall be calculated by multiplying the result derived from the calculation referred to in item 1) of this paragraph by the amount referred to in item 2) of this paragraph:

- 1) the carrying amount of the instrument on the first day of the final five-year period of its contractual maturity divided by the number of days in that period;
- 2) the number of remaining days of contractual maturity of the instrument.

Consequences of the conditions for Tier 2 instruments ceasing to be met

Article 16

The following shall apply where a Tier 2 instrument ceases to meet the conditions laid down in Article 14 of this Decision:

- 1) that instrument shall immediately cease to qualify as a Tier 2 instrument;
- 2) the part of the share premium accounts that relate to that instrument shall immediately cease to qualify as a Tier 2 item.

III. CAPITAL REQUIREMENTS

Capital requirements

Article 17

(1) The Development Bank shall at all times meet the following capital requirements in accordance with Article 33 of the Law:

- 1) Common Equity Tier 1 capital adequacy ratio of 5.5%;
- 2) Tier 1 capital adequacy ratio of 7%;
- 3) total capital adequacy ratio of 10%;

(2) The Development Bank shall calculate capital ratios referred to in paragraph (1) of this Article, in accordance with the Law, as follows:

- 1) Common Equity Tier 1 capital adequacy ratio as the ratio of Common Equity Tier 1 capital of the Development Bank and the total risk exposure amount, expressed as a percentage;
- 2) Tier 1 capital adequacy ratio as the ratio of the Tier 1 capital of the Development Bank and the total risk exposure amount, expressed as a percentage;
- 3) total capital adequacy ratio as the ratio of own funds of the Development Bank and the total risk exposure amount, expressed as a percentage.

(3) Total risk exposure amount shall be calculated as the sum of the following items after accounting for the provisions laid down in paragraph (4) of this Article:

- 1) the risk-weighted exposure amounts for credit risk in respect of all business activities of the Development Bank, including the trading-book business activities in accordance with Article 49 paragraph (2) of this Decision;
- 2) the risk-weighted exposure amounts for counterparty risk calculated in accordance with Article 46 and 47 of this Decision for the following types of transactions and agreements:
 - derivative contracts;
 - repurchase transactions, securities or commodities lending or borrowing transactions based on securities or commodities;
 - margin lending transactions based on securities or commodities;
 - long settlement transactions;
- 3) capital requirements for operational risk calculated in accordance with Article 48 of this Decision.
- 4) capital requirements for foreign exchange risk calculated in accordance with Article 49 paragraph (3) of this Decision;

(4) For the purposes of paragraph (3) items 1) and 2) of this Article, the risk-weighted exposure amount shall be calculated by multiplying the amount of exposures of asset and off-balance sheet items, as

determined in accordance with Article 18 of this Decision, by a corresponding risk weight in accordance with Articles 21 to 33 of this Decision.

(5) When calculating total risk exposure amount referred to in paragraph (3) items 3) and 4) of this Article, capital requirements shall be multiplied by a weight of 10.

Exposure amount

Article 18

(1) The exposure value of an asset item shall be its accounting value reduced by value adjustments, required reserves, and other deductions from own funds arising based on that item.

(2) The exposure value of an off-balance-sheet item shall be the amount of its nominal value after the reduction for the amount of provisions for off-balance sheet items and the amount of required reserves, multiplied by the following conversion factor:

- 1) 0% for items carrying low risk;
- 2) 20% for items carrying medium to low risk;
- 3) 50% for items carrying medium risk;
- 4) 100% for items carrying high risk;

(3) Items carrying low risk:

- 1) undrawn credit facilities (agreements to lend, purchase securities, provision of guarantees), which may be cancelled unconditionally at any time without notice, or that do effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness.
- 2) unconditionally cancellable credit facilities the terms of which permit the Development Bank to cancel them to the full extent (unconditionally cancellable credit facilities).

(4) Items carrying medium to low risk shall be undrawn credit facilities which comprise agreements with an original maturity of up to and including one year which may not be cancelled unconditionally at any time without notice or that do not effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness.

(5) Items carrying medium risk:

- 1) sureties and guarantees (including performance bonds, completion guarantees, custom guarantees and tax guarantees) and guarantees not having the character of credit substitutes;
- 2) undrawn credit facilities (purchase of securities, provision of guarantees with an original maturity of more than one year);

(6) Items carrying high risk:

- 1) guarantees having the character of credit substitutes;
- 2) transactions with recourse;
- 3) assets purchased under outright forward purchase agreements;
- 4) the unpaid portion of partly-paid shares and securities;
- 5) asset sale and repurchase agreements;
- 6) other off-balance sheet items carrying risk.

(7) The exposure amount of derivatives shall be determined in accordance with Articles 46 and 47 of this Decision.

(8) Where an exposure is subject to funded credit protection, the exposure value applicable to that item may be amended in accordance with Article 44 of this Decision.

IV. RISK WEIGHTED EXPOSURES FOR CREDIT RISK

Exposure classes

Article 19

(1) The Development Bank shall assign each exposure to one of the following exposure classes:

- 1) exposures to central governments or central banks;
- 2) exposures to local self-government;
- 3) exposures to public sector entities;
- 4) exposures to multilateral development banks;
- 5) exposures to international organisations;
- 6) exposures to credit institutions;
- 7) exposures to business undertakings;
- 8) retail exposures;
- 9) exposures secured by immovable property;
- 10) exposures in default;
- 11) equity exposures; and
- 12) other items.

(2) Original exposure that has been classified before the application of conversion factor into one of the exposure classes referred to in paragraph (1) of this Article, after applying credit risk mitigation techniques having a substitution effect on that exposure (guarantees, credit derivatives) shall be reclassified into, i.e., shall be transferred to other exposure class which depends on the used credit risk mitigation technique.

(3) The Development Bank shall define the criteria for prioritising when assigning exposures into the corresponding risk categories, such as institutional categorisation, terms of exposure, default, and the like, thereby making sure that exposures with higher risk weights (default exposures, and the like) are classified first.

Calculation of risk-weighted exposure amounts

Article 20

(1) When calculating risk-weighted exposure amounts, risk weights shall be applied to all exposures, with the exception of items deducted from own funds.

(2) The application of risk weight shall be based on the exposure class to which the exposure is assigned and, its credit quality.

(3) Credit quality may be determined by reference to the credit assessments of the external credit assessment institutions (ECAIs) or the credit assessments of export credit agencies (ECA).

(4) For the purposes of applying a risk weight, as referred to in paragraph (1) of this Article, the exposure value shall be multiplied by the risk weight specified or determined in accordance with Articles 21 to 33 of this Decision.

- (5) Where an exposure is subject to credit protection, the risk weight applicable to that item may be applied.
- (6) Exposures for which no calculation is provided in Articles 21 to 33 of this Decision shall be assigned a risk-weight of 100%.

Exposures to central governments or central banks

Article 21

- (1) Exposures to central governments and central banks shall be assigned a 100% risk weight, except in the cases referred to in paragraphs (2) to (5) of this Article.
- (2) Exposures to central governments and central banks for which a credit assessment by a nominated external credit assessment institution (ECAI) is available shall be assigned a risk weight in accordance with Table 1 referred to in this paragraph.

Table 1

Credit quality step	1	2	3	4	5	6
Risk weight	0%	20%	50%	100%	100%	150%

- (3) Exposures to the European Central Bank (ECB) shall be assigned a 0% risk weight.
- (4) Exposures to Member States' central governments and central banks, denominated and funded in the domestic currency of those Member States, shall be assigned a risk weight of 0%.
- (5) Exposures to the Government of Montenegro and the Central Bank shall be assigned a risk weight of 0%.

Exposures to local self-government units

Article 22

- (1) Exposures to local self-government units shall be risk-weighted as exposures to credit institutions unless they are treated as exposures to central governments referred to in paragraph (2) of this Article or receive a risk weight as specified in paragraphs (4) and (5) of this Article.
- (2) Exposures to local self-government units shall be treated as exposures to the central government in whose jurisdiction they are established where there is no difference in risk between such exposures because of the specific revenue-raising powers of the local self-government units, and the existence of specific institutional arrangements the effect of which is to reduce their risk of default.
- (3) Exposures to churches or religious communities shall be treated as exposures to local self-government units in so far as they are constituted in the form of legal persons and raise taxes in accordance with the law.
- (4) Exposures to local self-government units of the EU Member States which are denominated and funded in the domestic currency of that Member State shall be assigned a risk weight of 20%.

(5) Exposures to local self-government units in Montenegro shall be assigned a risk weight of 20%.

Exposures to public sector entities

Article 23

(1) Exposures to public sector entities for which a credit assessment by a nominated ECAI is not available shall be assigned a risk weight in accordance with the credit quality step to which exposures to the central government of the jurisdiction in which the public sector entity is incorporated are assigned in accordance with the following table:

Table 2

Credit quality step assigned to the central government	1	2	3	4	5	6
Risk weight	20%	50%	100%	100%	100%	150%

(2) For exposures to public sector entities incorporated in countries where the central government is not rated by the ECAI, the risk weight shall be 100%.

(3) For exposures to public sector entities with an original maturity of three months or less, the risk weight shall be 20%.

(4) In exceptional circumstances, exposures to public-sector entities established in Montenegro may be treated as exposures to the Government of Montenegro, or an EU central government, only where there is guarantee of the Government of Montenegro or the guarantee of the EU central government that there is no difference in risk between such exposures.

Exposures to multilateral development banks

Article 24

(1) Exposures to multilateral development banks that are not multilateral development banks referred to in paragraph (2) of this Article shall be treated in the same manner as exposures to credit institutions.

(2) Exposures to the following multilateral development banks shall be assigned a 0% risk weight:

- 1) the International Bank for Reconstruction and Development;
- 2) the International Finance Corporation;
- 3) the Inter-American Development Bank;
- 4) the Asian Development Bank;
- 5) the African Development Bank;
- 6) the Council of Europe Development Bank;
- 7) the Nordic Investment Bank;
- 8) the Caribbean Development Bank;
- 9) the European Bank for Reconstruction and Development;
- 10) the European Investment Bank;
- 11) the European Investment Fund;
- 12) the Multilateral Investment Guarantee Agency;
- 13) the International Finance Facility for Immunisation;

- 14) the Islamic Development Bank;
- 15) the International Development Association;
- 16) the Asian Infrastructure Investment Bank.

(3) Multilateral development banks shall also be the following:

- 1) the Inter-American Investment Corporation;
- 2) the Black Sea Trade and Development Bank;
- 3) the Central American Bank for Economic Integration; and
- 4) the CAF-Development Bank of Latin America.

(4) A risk weight of 20% shall be assigned to the portion of unpaid capital subscribed to the European Investment Fund.

Exposures to international organisations

Article 25

Exposures to the following international organisations shall be assigned a 0% risk weight:

- 1) European Union and European Atomic Energy Community;
- 2) the International Monetary Fund;
- 3) the Bank for International Settlements;
- 4) the European Financial Stability Facility;
- 5) the European Stability Mechanism;
- 6) an international financial institution established by two or more EU Member States, which has the purpose to mobilise funding and provide financial assistance to the benefit of its members that are experiencing or threatened by severe financing problems.

Exposures to credit institutions for which a credit assessment by a nominated ECAI is not available

Article 26

(1) Exposures to credit institutions for which a credit assessment by a nominated ECAI is not available shall be assigned a risk weight in accordance with the credit quality step to which exposures to the central government of the jurisdiction in which the credit institution is incorporated are assigned in accordance with the following table:

Table 3:

Credit quality step assigned to the central government	1	2	3	4	5	6
Risk weight	20%	50%	100%	100%	100%	150%

(2) For exposures to credit institutions for which a credit assessment by a nominated ECAI is not available, which are incorporated in countries where the central government is also unrated, the risk weight shall be 100%.

(3) Notwithstanding paragraphs (1) and (2) of this Article, for exposures to credit institutions for which a credit assessment by a nominated ECAI is not available with an original effective maturity of three months or less, the risk weight shall be 20%.

(4) Exposures to credit institutions in Montenegro with residual maturity of three months or less shall be assigned a 20% risk-weight.

(5) Exposures to credit institutions in Montenegro with residual maturity over three months shall be assigned a 50% risk-weight.

(6) Exposures to financial institutions authorised and supervised by the Central Bank and subject to prudential requirements comparable to those applied to credit institutions in terms of robustness shall be treated as exposures to credit institutions.

Exposures to ECAI rated credit institutions

Article 27

(1) Exposures to a credit institution with a residual maturity of more than three months for which a credit assessment by a nominated ECAI is available shall be assigned a risk weight in accordance with Table 4 of this paragraph.

Table 4

credit quality step	1	2	3	4	5	6
risk weight	20%	50%	50%	100%	100%	150%

(2) Exposures to a credit institution of up to three months residual maturity for which a credit assessment by a nominated ECAI is available shall be assigned a risk-weight in accordance with Table 5 of this paragraph.

Table 5

credit quality step	1	2	3	4	5	6
risk weight	20%	20%	20%	50%	50%	150%

Exposures to business undertakings

Article 28

(1) Exposures for which a credit assessment by a nominated ECAI is available shall be assigned a risk weight in accordance with Table 6 of this paragraph.

Table 6

credit quality step	1	2	3	4	5	6
Risk weight	20%	50%	100%	100%	150%	150%

(2) Exposures for which a credit assessment is not available shall be assigned a 100% risk weight.

(3) Notwithstanding paragraphs (1) and (2) of this Article, the exposure to a business undertaking approved for financing a development or project of public importance may be assigned a risk weight of 80%, if the following conditions are met:

- 1) the exposure is to an entity that meets one of the following criteria:
 - it was created specifically to finance or operate physical structures or facilities, systems and networks;
 - it was created specifically to provide or support essential public services; or
 - it realises a project of local, regional and/or national importance approved with the consent of the Government of Montenegro
- 2) the debtor can meet its financial obligations even under stressed conditions that are relevant for the risk of the project;
- 3) the cash flows that the debtor generates including the cash flows arising from the project itself, cover all future loan repayments during the duration of the loan;
- 4) the contractual arrangements provide the Development Bank with a high degree of protection including the following:
 - adequate diversification of the sales market, so that the source of the revenues of the debtor are payments from a large number of users, or the contractual provisions are in place which effectively protect the Development Bank against losses resulting from the termination of the project by the party which agrees to purchase the goods or services provided by the debtor, or, in the event of a loss, customers can easily be replaced with new customers;
 - contractual provisions require the mandatory use of the loan in accordance with the planned project;
 - contractual provisions require the debtor to provide additional loan collateral instruments at the first request of the Development Bank in the event of the evident occurrence of unfavourable financial, commercial and other circumstances, as well as in the event of failure, impairment or unapproved encumbrances of the provided collateral;
 - the contractual provisions require the obligation of the debtor not to sell, assign, cede or lease the property in its entirety or a significant part of it without the prior written consent of the Development Bank, except in the regular course of business of which the Development Bank is aware;
 - the contractual provisions require the obligation of the debtor that, without the prior written consent of the Development Bank, it will not encumber or dispose of all or a significant part of its current or future income, which may jeopardize the orderly repayment of the loan obligations, except in the regular course of business of which the Development Bank is aware;
- 5) the obligation is superior or equal to other obligations of the debtor towards other creditors, except legal claims;
- 6) where the debtor is in the construction phase, the equity investor or a group of equity investors as a whole must have the following:
 - experience in project realisation, the financial strength and the relevant expertise;
 - a low risk of default, or there is a low risk of material losses for the debtor as a result of their default;
- 7) the debtor has adequate safeguards to ensure completion of the project according to the agreed specification, budget or completion date;
- 8) all necessary permits and authorisations have been obtained;
- 9) during the realisation of the project, the debtor complies with the regulations on environmental protection, including the obligation to prepare an environmental impact assessment with regard to the project.

Exposures to portfolio of small loans with similar features (retail)

Article 29

(1) Receivables to legal persons, micro, small and medium-sized enterprises shall be assigned a 75% risk weight, provided that the following conditions are met:

- 1) the Development Bank's total gross receivables to a single person or a group of connected persons, including past due receivables do not exceed EUR 300,000 (retail loan);
- 2) the exposure represents one among a significant number of exposures with similar characteristics, therefore the risks associated with such exposure are substantially reduced;
- 3) retail loan portfolio is well diversified.

(2) Within the meaning of paragraph (1) item 3) of this Article, retail loan portfolio is sufficiently diversified if its diversification indicator does not exceed 0.2%.

(3) The diversification indicator of a retail loan portfolio represents a percentage share of an average receivable to one person or a group of connected persons in total retail loan portfolio.

Exposures secured by mortgages on immovable property

Article 30

(1) An exposure or any part of an exposure secured by a residential property up to 85% of its market value shall be assigned a risk weight of 40%, except for the part of the exposure which is assigned to another exposure class.

(2) An exposure or any part of an exposure that is fully secured by a commercial property up to 85% of its market value shall be assigned a risk weight of 60%, except for the part of the exposure which is assigned to another exposure class.

(3) The part of the exposure that exceeds 85% of market value of the immovable property shall be assigned the risk weight of 100%.

(4) The Development Bank shall clearly define in its internal acts the types of residential property and commercial immovable property it accepts as collateral and its lending policies on loans secured by mortgage on immovable property.

(5) The Development Bank shall regularly monitor the value of the immovable property and at a minimum once every year for commercial immovable property and once every three years for residential property, provided that the credit institution carries out more frequent monitoring where the market is subject to significant changes in conditions.

(6) The property valuation shall be reviewed when information available to the Development Bank indicates that the value of the property may have declined materially relative to general market prices, wherein for loans exceeding EUR 1,000,000 or 5%, whichever is less, of the own funds of the Development Bank, the property valuation shall be reviewed by such valuer at least every three years.

(7) The property valuation referred to in paragraph (6) of this Article shall be carried out by a valuer who possesses the necessary qualifications, ability and experience to execute a valuation of an immovable property and who is independent from the credit decision process.

(8) The Development Bank may monitor the value of the immovable property and identify the immovable property in need of revaluation, in accordance with paragraphs (6) and (7) of this Article, by means of advanced statistical or other mathematical methods, provided that those methods are developed independently from the credit decision process and that it sets out, in its policies and procedures, the criteria for using models to monitor the values of collateral and to identify the properties that should be revaluated, wherein those policies and procedures shall account for such models' proven track record, property-specific variables considered, the use of minimum available and accurate information, and the models' uncertainty.

(9) The immovable property taken as credit protection must be insured against the risk of damage.

(10) The Development Bank shall have in place procedures to monitor that the immovable property taken as credit protection is adequately insured against the risk of damage.

Past due exposures

Article 31

(1) The following risk weights shall be assigned to a receivable or unsecured part of a past due receivable:

- 1) a 150% risk weight if the sum of the value adjustment and the amount deducted from Common Equity Tier 1 capital does not exceed 20% of the unsecured part of total exposure before credit risk adjustments and deductions were applied;
- 2) 100%, where the sum of the value adjustment and the amount deducted from Common Equity Tier 1 capital exceeds 20 % of the unsecured part of the exposure value before credit risk adjustments and deductions were applied.

(2) Within the meaning of paragraph (1) of this Article, past due exposure shall be the Development Bank's receivable to a debtor that is past due by more than 90 days.

(3) Within the meaning of paragraph (1) of this Article, secured part of a receivable shall be a part of a receivable which is secured by:

- 1) cash collateral in euro and other convertible currencies;
- 2) unconditional guarantee of the state of Montenegro;
- 3) unconditional guarantee of multilateral development banks which are assigned a risk weight of 0%.

Equity exposures

Article 32

(1) The following exposures shall be considered equity exposures:

- 1) non-debt exposures conveying a subordinated, residual claim on the assets or income of the issuer; and
- 2) debt exposures and other securities, partnerships, derivatives, or other instruments, the economic substance of which is similar to the exposures specified in item 1) of this paragraph.

(2) Equity exposures shall be assigned a risk weight of 100%, unless they are deductions from Common Equity Tier 1 items referred to in Article 8 of this Decision;

Other items

Article 33

- (1) Tangible assets within the meaning of land and buildings occupied by the Development Bank for its own activities shall be assigned a risk weight of 100%.
- (2) Prepayments and accrued income for which the Development Bank is unable to determine the counterparty shall be assigned a risk weight of 100%.
- (3) Cash items in the process of collection shall be assigned a 20% risk weight.
- (4) Cash in hand and vault shall be assigned a 0% risk weight.
- (5) In the case of asset sale and repurchase agreements and outright forward purchases, the risk weight shall be that assigned to the assets in question and not to the counterparties to the transactions.

Use of the external credit assessment institution credit assessments for the determination of risk weights

Article 34

- (1) The Development Bank may nominate one or more ECAIs to be used for the determination of risk weights to be assigned to assets and off-balance sheet items.
- (2) The Development Bank shall not use the credit assessments selectively.
- (3) In using credit assessment, the Development Bank shall comply with the following requirements:
 - 1) when it decides to use the credit assessments produced by an ECAI for a certain class of items, it shall use those credit assessments consistently for all exposures belonging to that class;
 - 2) when it decides to use the credit assessments produced by an ECAI, it shall use them in a continuous and consistent way over time;
 - 3) where only one credit assessment is available from a nominated ECAI for a rated item, that credit assessment shall be used to determine the risk weight for that item;
 - 4) where two credit assessments are available from nominated ECAIs and the two correspond to different risk weights for a rated item, the higher risk weight shall be assigned;
 - 5) where more than two credit assessments are available from nominated ECAIs for a rated item, the assessments generating the two lowest risk weights shall be used, and if the two lowest risk weights are different, the higher risk weight shall be assigned, and if the two lowest risk weights are the same, that risk weight shall be assigned.

V. CREDIT RISK MITIGATION TECHNIQUES

Principles for recognising the effect of credit risk mitigation techniques

Article 35

- (1) No exposure after the application of credit risk mitigation techniques shall produce a higher risk-weighted exposure amount or expected loss amount than an otherwise identical exposure to which no credit risk mitigation techniques were applied.

(2) The Development Bank shall treat cash, securities or commodities purchased, borrowed or received under a repurchase transaction or securities or commodities lending or borrowing transaction as collateral.

(3) Where the Development Bank uses more than one credit risk mitigant covering a single exposure it shall:

- 1) subdivide the exposure into parts covered by each type of credit risk mitigant; and
- 2) calculate the risk-weighted exposure amount for each part obtained in item 1) of this paragraph separately, in accordance with Articles 21 to 33 of this Decision.

(4) When the Development Bank covers a single exposure with credit protection provided by a single protection provider and that protection has differing maturities, it shall:

- 1) subdivide the exposure into parts covered by each credit risk mitigant; and
- 2) calculate the risk-weighted exposure amount for each part obtained in item 1) of this paragraph separately, in accordance with Articles 21 to 33 of this Decision.

(5) The Development Bank may recognise funded credit protection in the calculation of the effect of credit risk mitigation only where the assets relied upon for protection meet the following conditions:

- 1) they are included in the list of eligible assets set out in Article 36 of this Decision, as applicable; and
- 2) they are sufficiently liquid and their value over time sufficiently stable to provide appropriate certainty as to the credit protection achieved.

(6) The Development Bank may recognise funded credit protection in the calculation of the effect of credit risk mitigation only where it has the right to liquidate or retain, in a timely manner, the assets from which the protection derives in the event of the default, insolvency or bankruptcy, or other credit event set out in the transaction documentation, of the debtor and, where applicable, of the custodian holding the collateral, wherein the degree of correlation between the value of the assets relied upon for protection and the credit quality of the debtor shall not be too high.

(7) In the case of unfunded credit protection, protection provider shall be recognised only if it is recognised protection provider under Article 38 paragraph (1) of this Decision.

(8) In the case of unfunded credit protection, a protection agreement (instrument of protection) shall qualify as an eligible protection agreement only where:

- 1) it is a protection agreement set out in Article 38 paragraphs (2) and (3) of this Decision;
- 2) it is legally effective and enforceable in the relevant jurisdictions, to provide appropriate certainty as to the credit protection achieved having regard to the approach used to calculate risk-weighted exposure amounts and to the degree of recognition allowed;
- 3) the protection provider is an eligible provider referred to in Article 38 paragraph (1) of this Decision.

(9) The Development Bank shall be able to demonstrate to the Central Bank that it has adequate risk management processes to control those risks to which it may be exposed as a result of carrying out credit risk mitigation practices.

(10) Notwithstanding the fact that credit risk mitigation has been taken into account for the purposes of calculating risk-weighted exposure amounts and, where applicable, expected loss amounts, the Development Bank shall continue to undertake a full credit risk assessment of the underlying exposure and be in a position to demonstrate the fulfilment of this requirement to the Central Bank.

(11) In the case of repurchase transactions and securities or commodities lending or borrowing transactions the underlying exposure shall, for the purposes of paragraph (10) of this Article, be deemed to be the net amount of the exposure.

Eligibility of financial collateral for funded credit protection

Article 36

(1) The Development Bank may use the following items as eligible collateral:

- 1) deposit held with a credit institution;
- 2) debt securities issued by central governments or central banks, which securities have a credit assessment by an ECAI or an export credit agency (ECA), associated with credit quality step 4 or above under the rules for the risk weighting of exposures to central governments and central banks under Article 23 of this Decision;
- 3) debt securities issued by the Government of Montenegro;
- 4) credit institutions' debt securities which have a credit assessment by an ECAI associated with credit quality step 3 or above under the rules for the risk weighting of exposures to credit institutions under Article 27 of this Decision;
- 5) other entities' debt securities which have a credit assessment by an ECAI associated with credit quality step 3 or above under the rules for the risk weighting of exposures to business undertakings under Article 28 of this Decision;
- 6) equities or convertible bonds that are included in a main index;
- 7) gold.

(2) The Development Bank may use debt securities that are issued by credit institutions and that do not have a credit assessment by an ECAI as eligible collateral where those debt securities fulfil the following criteria:

- 1) they are listed on a recognised exchange;
- 2) they qualify as a senior claim;
- 3) all other issues by the credit institution of the same seniority have a credit assessment by an ECAI associated with credit quality step 3 or above under the rules for the risk weighting of exposures to credit institutions under Article 27 of this Decision;
- 4) the liquidity of the instrument is sufficient for these purposes; and where
- 5) the Development Bank has no information to suggest that the issue would justify a credit assessment below that indicated in item 3) of this Article;

(3) With regard to paragraph (1) items 2) to 5), where a security has two credit assessments by ECAIs, the Development Bank shall apply the less favourable assessment, and where a security has more than two credit assessments by ECAIs, the Development Bank shall apply the two most favourable assessments, and where the two most favourable credit assessments are different, the Development Bank shall apply the less favourable of the two.

Requirements for financial collateral

Article 37

(1) Financial collateral and gold shall qualify as eligible collateral where all the requirements laid down in paragraphs (2) to (6) of this Article are met and if the residual maturity of the protection is at least as long as the residual maturity of the exposure.

(2) The credit quality of the debtor and the value of the collateral shall not have a material positive correlation, and where the value of the collateral is reduced significantly, this shall not alone imply a significant deterioration of the credit quality of the debtor, or, where the credit quality of the debtor becomes critical, this shall not alone imply a significant reduction in the value of the collateral.

(3) Securities issued by the debtor, or any person from the group related to the debtor, shall not qualify as eligible collateral.

(4) The Development Bank shall fulfil any contractual and statutory requirements in respect of, and take all steps necessary to ensure, the enforceability of the collateral arrangements in accordance with the law.

(5) The Development Bank shall have conducted sufficient legal review confirming the enforceability of the collateral arrangements in a relevant jurisdiction, and it shall re-conduct such review as necessary to ensure continuing enforceability.

(6) The Development Bank shall:

- 1) properly document the collateral arrangements and have in place clear and robust procedures for the timely liquidation of collateral;
- 2) use robust procedures and processes to control risks arising from the use of collateral, including risks of failed collateral liquidation or reduced credit protection, valuation risks, risks associated with the termination of the credit protection, concentration risk arising from the use of collateral and the interaction with the Development Bank 's overall risk profile;
- 3) have in place documented policies and practices defining the types and amounts of collateral accepted;
- 4) calculate the market value of the collateral at least once every six months and whenever they have reason to believe that a significant decrease in the market value of the collateral has occurred;
- 5) where the collateral is held by a third party, take reasonable steps to ensure that such third party segregates the collateral from its own assets;
- 6) have in place collateral management policies to control, monitor and report the following:
 - the concentration risk to particular types of collateral assets;
 - the reuse of collateral including the potential liquidity shortfalls resulting from the reuse of collateral received from counterparties;
 - the surrender of rights on collateral posted to counterparties.

(7) The Development Bank may treat cash held by a credit institution as a guarantee provided by that credit institution, where the following conditions are met:

- 1) the debtor's receivable from the credit institution must be openly pledged or assigned to the Development Bank and such pledge or assignment must be legally effective and enforceable in a relevant jurisdiction and must be unconditional and irrevocable;
- 2) the credit institution with which the funds are deposited must be notified of the pledge or assignment to the Development Bank; and
- 3) as a result of the notification, the credit institution must be able to make payments solely to the Development Bank or to other parties only with the Development Bank's prior consent.

Eligible unfunded credit protection provider and instruments

Article 38

(1) The Development Bank may deem the following entities as eligible providers of unfunded credit protection:

- 1) central governments and central banks;

- 2) local self-government units;
- 3) multilateral development banks;
- 4) international organisations which are assigned a 0% risk weight under Article 25 of this Decision;
- 5) public sector entities, receivables to which are treated in accordance with Article 23 of this Decision;
- 6) credit institutions, and financial institutions the exposures to which are treated as exposures to credit institutions in accordance with Article 26 paragraph (5) of this Decision;
- 7) other business undertakings, including subsidiaries and affiliated business undertakings of the Development Bank, where those business undertakings have a credit assessment by an ECAI;

(2) The Development Bank may use guarantees and other sureties as eligible unfunded credit protection.

(3) The Development Bank may use, as eligible credit protection, the following types of credit derivatives and instruments composed of such credit derivatives or instruments that are economically effectively similar to credit derivatives:

- 1) credit default swaps (CDS);
- 2) total return swaps; (TRS); and
- 3) credit linked notes to the extent of their cash funding (CLN).

Requirements common to guarantees and credit derivatives

Article 39

(1) Subject to conditions referred to in Article 40 paragraph (1) of this Decision, credit protection deriving from a guarantee and other surety or a credit derivative may be used as unfunded credit protection, where all the following conditions are met:

- 1) the credit protection is direct;
- 2) the extent of the credit protection is clearly defined and incontrovertible;
- 3) the credit protection contract does not contain any clause, the fulfilment of which is outside the direct control of the Development Bank, that:
 - would allow the protection provider to cancel the contract unilaterally;
 - would increase the effective cost of protection as a result of a deterioration in the credit quality of the protected exposure;
 - could prevent the protection provider from paying out in a timely manner in the event that the debtor fails to make any payments due, or when the leasing contract has expired for the purposes of recognising guaranteed residual value of leased assets; or
 - could allow the maturity of the credit protection to be reduced by the protection provider; and
- 4) the credit protection contract is legally effective and enforceable in a relevant jurisdiction which is relevant at the time of the conclusion of the credit agreement.

(2) The Development Bank shall demonstrate to the Central Bank that it has in place systems to manage potential concentration of risk arising from its use of guarantees and other sureties and credit derivatives, as well as to demonstrate how its strategy in respect of its use of credit derivatives and guarantees and other sureties interacts with its management of its overall risk profile.

(3) The Development Bank shall fulfil any contractual and statutory requirements in respect of, and take all steps necessary to ensure, the enforceability of its unfunded credit protection under the regulations applicable to such contracts.

(4) The Development Bank shall have conducted legal review confirming the enforceability of the unfunded credit protection in a relevant jurisdiction, and it shall repeat such review as necessary to ensure continuing enforceability.

Requirements for sovereign and other public sector counter-guarantees

Article 40

(1) The Development Bank may treat the exposures protected by a guarantee which is counter-guaranteed as referred to in paragraph (2) of this Article as protected by a guarantee provided by the entities listed in that paragraph, provided that the following conditions are satisfied:

- 1) the counter-guarantee covers all credit risk elements of the receivable;
- 2) both the original guarantee and the counter-guarantee meet the requirements for guarantees set out in Articles 39 and 41 paragraph (1) of this Decision, except that the counter-guarantee need not be direct; and
- 3) the cover is robust and nothing in the historical evidence suggests that the coverage of the counter-guarantee is less than effectively equivalent to that of a direct guarantee by the entity in question.

(2) The treatment set out in paragraph (1) of this Article shall apply to exposures protected by a guarantee which is counter-guaranteed by any of the following entities:

- 1) central governments or central banks;
- 2) local self-government units;
- 3) public sector entities, receivables from which are treated as receivables from the central government in accordance with Article 23 paragraph (4) of this Decision;
- 4) a multilateral development bank or an international organisation, to which a 0% risk weight is assigned in accordance with Article 24 paragraph (2) and Article 25 of this Decision.

(3) The Development Bank shall apply the treatment set out in paragraph (1) of this Article also to an exposure which is not counter-guaranteed by any entity listed in paragraph (2) of this Article where such counter-guarantee is in turn directly guaranteed by one of those entities and the conditions listed in paragraph (1) of this Article are satisfied.

Additional requirements for guarantees and other sureties

Article 41

(1) Guarantees and other sureties may be used as eligible unfunded credit protection where the conditions referred to in Article 39 of this Decision and the following conditions are met:

- 1) in the case of default of or non-payment by the counterparty, the Development Bank has the right to pursue, in a timely manner, the guarantor or provider of other surety for any monies due under the receivables in respect of which the protection is provided and the payment by the guarantor shall not be subject to the Development Bank first having to pursue the debtor;
- 2) the guarantee or other surety is an explicitly documented obligation assumed by the guarantor;
- 3) either of the following conditions is met:
 - the guarantee or other surety covers all types of payments the debtor is expected to make in respect of the exposure; or
 - where certain types of payment are excluded from the guarantee or other surety, the Development Bank has adjusted the value of the guarantee or other surety to reflect the limited coverage.

(2) In the case of unfunded credit protection covering residential mortgage loans, the requirements referred to in Article 39 paragraph (1) item 3) indent 3 of this Decision and in paragraph (1) item 1) of this Article have only to be satisfied within 24 months;

(3) In the case of guarantees or other sureties provided in the context of mutual guarantee schemes or provided by or counter-guaranteed by entities listed in Article 40 paragraph (2) of this Decision, the requirement referred to in paragraph (1) item 1) of this Article shall be considered to be satisfied where either of the following conditions is met:

- 1) the Development Bank has the right to obtain in a timely manner a provisional payment by the guarantor that meets the following conditions:
 - it represents an estimate of the amount of the loss, including losses resulting from the non-payment of interest and other types of payment which the debtor is obliged to make, that the Development Bank is likely to incur; or
 - it is proportional to the coverage of the guarantee or other surety; and
- 2) the Development Bank can demonstrate to the satisfaction of the Central Bank that the effects of the guarantee or other surety, which shall also cover losses resulting from the non-payment of interest and other types of payments which the debtor is obliged to make, justify such treatment.

Calculating the effects of funded credit protection

Article 42

(1) The Development Bank shall assign to eligible financial collateral a value equal to its market value as determined in accordance with Article 37 paragraph (6) item 4) of this Decision.

(2) The Development Bank shall assign to those portions of exposure values that are collateralised by the market value of eligible collateral the risk weight that it would assign under Articles 21 to 33 of this Decision where the Development Bank had a direct exposure to the collateral instrument, and for this purpose, the exposure value of an off-balance sheet item referred to in Article 18 paragraph (2) of this Decision shall be determined by applying the conversion factor of 100% rather than the conversion factor indicated in paragraph (2) of that Article.

(3) The risk weight of the collateralised portion shall be at least 20% except as specified in paragraphs (4) to (7) of this Article, and the Development Bank shall apply to the remainder of the exposure value the risk weight that it would assign to an unsecured exposure to the counterparty under Articles 21 to 33 of this Decision.

(4) The Development Bank shall assign a risk weight of 0% to the collateralised portion of the exposure arising from repurchase transaction and securities lending or borrowing transactions which fulfil the criteria referred to in paragraph (9) of this Article, and where the counterparty to the transaction is not a central counterparty, the Development Bank shall assign a risk weight of 10%.

(5) The Development Bank shall assign a risk weight of 0%, to the collateralised portion of exposure for the derivative instruments subject to daily marking-to-market, collateralised by cash where there is no currency mismatch.

(6) The Development Bank shall assign a risk weight of 10%, to the collateralised portion of exposure for transactions collateralised by debt securities issued by central governments or central banks which are assigned a 0% risk weight under Article 21 of this Decision.

(7) For transactions other than those referred to in paragraphs (4), (5), and (6) of this Article, the Development Bank may assign a 0% risk weight where the exposure and the collateral are denominated in the same currency, and where either of the following conditions is met:

- 1) the collateral is cash on deposit held with credit institution for that purpose; or
- 2) the collateral is in the form of debt securities issued by central governments or central banks eligible for a 0% risk weight under Article 21 of this Decision, and its market value has been discounted by 20%.

(8) For the purpose of paragraphs (5), (6), and (7) of this Article debt securities issued by central governments or central banks shall include:

- 1) debt securities issued by multilateral development banks to which a 0% risk weight is assigned under Article 24 paragraph (2) of this Decision;
- 2) debt securities issued by international organisations which are assigned a 0% risk weight under Article 25 of this Decision; and
- 3) debt securities issued by public sector entities which are treated as exposures to central governments in accordance with Article 23 of this Decision.

(9) For the purposes of paragraph (4) of this Article, the Development Bank may apply a 0% volatility adjustment where all the following conditions are met:

- 1) both the exposure and the collateral are cash or debt securities issued by central governments or central banks that are assigned a 0% risk weight under Article 21 of this Decision;
- 2) both the exposure and the collateral are denominated in the same currency;
- 3) either the maturity of the transaction is no more than one day or both the exposure and the collateral are subject to daily marking-to-market or daily re-margining;
- 4) the time between the last marking-to-market before a failure to re-margin by the counterparty and the liquidation of the collateral is no more than four business days;
- 5) the transaction is settled in a settlement system proven for that type of transaction;
- 6) the documentation covering the agreement or transaction is standard market documentation for repurchase transactions or securities lending or borrowing transactions in the securities concerned;
- 7) the transaction is governed by documentation specifying that where the counterparty fails to satisfy an obligation to deliver cash or securities or to deliver margin or otherwise defaults, then the transaction is immediately terminable.

Calculating the effects of unfunded credit protection

Article 43

(1) For the purpose of calculating the effects of unfunded credit protection, the value of unfunded credit protection (G) shall be the amount that the protection provider has undertaken to pay in the event of the non-payment of the debtor or on the occurrence of other specified credit events.

(2) In the case of credit derivatives which do not include as a credit event restructuring of the underlying obligation involving write-off or postponement of principal, interest or fees that result in a credit loss event, the following shall apply:

- 1) where the amount that the protection provider has undertaken to pay is not higher than the exposure value, the Development Bank shall reduce the value of the credit protection calculated under paragraph (1) of this Article by 40%;
- 2) where the amount that the protection provider has undertaken to pay is higher than the exposure value, the value of the credit protection shall be no higher than 60% of the exposure value.

(3) Where unfunded credit protection is denominated in a currency different from that in which the exposure is denominated, the Development Bank shall reduce the value of the credit protection by the application of a volatility adjustment as follows:

$$G^* = G \cdot (1 - H_{fx})$$

where:

- G^* = the amount of credit protection adjusted for foreign exchange risk;
- G = the nominal amount of the credit protection;
- H_{fx} = the volatility adjustment for any currency mismatch between the credit protection and the underlying obligation determined in accordance with paragraph (5) of this Article.

(4) Where there is no currency mismatch H_{fx} is equal to zero.

(5) The Development Bank shall determine value adjustments on the basis of daily valuation.

(6) Where the Development Bank does not perform valuation on a daily basis, it shall apply larger volatility adjustments, and it shall calculate them by scaling up the daily valuation volatility adjustments, using the following square-root-of-time formula:

$$H = H_M \cdot \sqrt{\frac{N_R + (T_M - 1)}{T_M}}$$

where:

- H = the volatility adjustment to be applied;
- H_M = the volatility adjustment where there is daily valuation;
- N_R = the actual number of business days between valuations;
- T_M = the liquidation period for the type of transaction in question.

Calculating risk-weighted exposure amounts

Article 44

(1) For the purposes of Article 18 paragraph (8) of this Decision, the Development Bank shall calculate the risk-weighted exposure amounts in accordance with the following formula:

$$\max \{0, E - G_A\} \cdot r + G_A \cdot g$$

where:

- E = the exposure value in accordance with Article 18 of this Decision; for this purpose, the exposure value of an off-balance sheet item listed in paragraph (2) of that Article shall be 100% of its value rather than the exposure value indicated in paragraph (2) of that Article;
- G_A = the amount of credit protection as calculated under Article 43 paragraphs (3) and (4) of this Decision (G^*);

- r = the risk weight of exposures to the debtor as specified under Articles 21 to 33 of this Decision;
- g = the risk weight of exposures to the protection provider as specified under Articles 23 to 35 of this Decision;

(2) Where the protected amount (G_A) is less than the exposure (E), the Development Bank may apply the formula specified in paragraph (1) of this Article only where the protected and unprotected parts of the exposure are of equal seniority.

Maturity mismatch

Article 45

(1) For the purpose of calculating risk-weighted exposure amounts, a maturity mismatch occurs when the residual maturity of the credit protection is less than that of the protected exposure.

(2) For transactions subject to funded credit protection, where there is a mismatch between the maturity of the exposure and the maturity of the protection, the collateral shall not qualify as eligible funded credit protection.

VI. COUNTERPARTY CREDIT RISK

Determining the exposure value

Article 46

(1) The Development Bank shall determine the exposure value of derivative instruments in accordance with the original exposure method under Article 47 of this Decision.

(2) The Development Bank may determine the exposure value of repurchase transactions, securities or commodities lending or borrowing transactions, long settlement transactions and margin lending transactions in accordance with Article 47 of this Decision, instead of making use of Articles 35 to 45 of this Decision.

Calculation of the exposure value using the original exposure method

Article 47

(1) The exposure value of a netting set or a transaction shall be the product of 1.4 times the sum of the current replacement cost and the potential future exposure.

(2) The current replacement cost referred to in paragraph (1) of this Article shall be calculated as follows:

- 1) for netting sets of transactions that are traded on a recognised exchange and for transactions that are centrally cleared by a qualifying central counterparty referred to in Article (2) item 27) of this Decision, or for which collateral is exchanged bilaterally with the counterparty, the Development Bank shall use the following formula:

$$RC = TH + MTA$$

where:

RC = replacement cost;

TH = the margin threshold applicable to the netting set under the margin agreement below which the Development Bank cannot call for collateral; and

MTA = the minimum transfer amount applicable to the netting set under the margin agreement;

- 2) for all other netting sets or individual transactions, the Development Bank shall use the following formula:

$$RC = \max\{CMV, 0\}$$

where:

RC = replacement cost; and

CMV = the current market value.

(3) In order to calculate the current replacement cost, the Development Bank shall update current market values at least monthly.

(4) The Development Bank shall calculate the potential future exposure referred to in paragraph (2) of this Article as follows:

- 1) the potential future exposure of a netting set is the sum of the potential future exposure of all the transactions included in the netting set, calculated in accordance with item 2) of this paragraph;
- 2) the potential future exposure of a single transaction is its notional amount multiplied by:
 - the product of 0.5% and the residual maturity of the transaction expressed in years for interest-rate derivative contracts;
 - the product of 6% and the residual maturity of the transaction expressed in years for credit derivative contracts;
 - 4% for foreign-exchange derivatives;
 - 18% for gold and commodity derivatives other than electricity derivatives;
 - 40% for electricity derivatives;
 - 32% for equity derivatives;
- 3) the potential future exposure of netting sets referred to in paragraph (2) item 1) of this Article shall be multiplied by 0.42.

(5) For calculating the potential exposure of interest-rate derivatives and credit derivatives in accordance with paragraph (4) item 2) indents 1 and 2 of this Article, the Development Bank may use the original maturity instead of the residual maturity of the contracts.

VII. CAPITAL REQUIREMENT FOR OPERATIONAL RISK

Calculation of capital requirement for operational risk

Article 48

- (1) The Development Bank shall calculate capital requirements for operational risk by multiplying the base for calculating capital requirement for operational risk, determined in accordance with paragraphs (2) and (3) of this Article, by coefficient 0.12.
- (2) The base for calculating capital requirement for operational risk shall be the average of net interest bearing and net non-interest-bearing income of the Development Bank for the last three consecutive financial years.
- (3) Notwithstanding paragraph (2) of this Article, the year in which a sum of net interest bearing and net non-interest-bearing income of the Development Bank is negative, shall not be included in the calculation of capital requirement for operational risk.
- (4) Calculation of the capital requirement for operational risk shall be performed based on audited financial statements of the Development Bank, and if the audited financial statements are not available at the time of calculating the capital requirement, the calculation shall be performed based on unaudited reports, with the obligation to subsequently align the calculation according to the data base from the audited financial statements of the Development Bank.
- (5) When calculating annual net interest bearing and net non-interest-bearing income of the Development Bank, the following items shall be included:
 - 1) interest income;
 - 2) interest expense;
 - 3) income from dividends;
 - 4) commissions/fees receivable;
 - 5) commissions/fees payable;
 - 6) net gains or losses on financial operations;
 - 7) other operating income.
- (6) When determining capital requirements, annual income shall be calculated before any provisions are deducted.
- (7) When calculating capital requirement for operational risk the following positions shall not be used:
 - 1) gains and losses from sale of financial assets held to maturity;
 - 2) income not arising from regular operations of the Development Bank;
 - 3) income arising from insurance.
- (8) The operational risk exposure value shall be obtained by multiplying the capital requirement referred to in paragraph (1) of this Article by 10.

VIII. CAPITAL REQUIREMENT FOR MARKET RISK

Calculation of capital requirement for market risk

Article 49

- (1) The Development Bank shall calculate the capital requirement for market risk as the sum of capital requirement for its trading book positions determined in accordance with paragraph (2) of this Article and the capital requirement for foreign exchange risk determined in accordance with paragraph (3) of this Article.
- (2) The Development Bank shall calculate the capital requirement for trading book positions in accordance with the provisions of this Decision governing the manner of calculating capital requirement for credit risk, or the manner of calculating risk weighted exposure value.
- (3) The Development Bank shall calculate a capital requirement for foreign exchange risk if the sum of 's overall net foreign-exchange position and its net gold position exceeds 2% of its total own funds.
- (2) The capital requirement for foreign exchange risk shall be the sum of the Development Bank's overall net foreign-exchange position and its net gold position, converted to EUR at valid spot exchange rate, multiplied by 10%.
- (5) For the purpose of calculating net foreign-exchange position referred to in paragraph (4) of this Article, the Development Bank shall sum all net short and all net long positions in each currency previously converted at valid spot rates into the EUR to form the total of the net short positions and the total of the net long positions respectively, and the higher of these two totals shall be the Development Bank's overall net foreign-exchange position.
- (6) The foreign exchange risk exposure value shall be obtained by multiplying the capital requirement referred to in paragraph (4) of this Article by 10.

Requirements for the trading book

Article 50

- (1) A trading book should include financial assets and financial liabilities that meet the following criteria:
 - 1) The Development Bank has acquired or obtained them with the intention to sell or repurchase them short-term;
 - 2) at initial recognition, they constitute a part of a portfolio of financial instruments that are managed jointly and for which there are evidences on recent actual form of income capacity in short-term;
 - 3) they represent derivatives.
- (2) Trading intent shall be evidenced on the basis of the strategies, policies and procedures set up by the Development Bank to manage the position or portfolio in accordance with Articles 51, 52, and 53 of this Decision.
- (3) The Development Bank shall establish and maintain systems and controls to manage their trading book in accordance with Article 51 of this Decision.

Management of the trading book

Article 51

(1) The Development Bank shall have in place clearly defined policies and procedures for the overall management of the trading book, which shall address in particular the following:

- 1) the activities which the Development Bank considers to be trading business and as constituting part of the trading book for own funds requirement purposes;
- 2) the extent to which a position can be marked-to-market daily by reference to an active, liquid two-way market;
- 3) for positions that are marked-to-model, the extent to which the Development Bank can:
 - identify all material risks of the position;
 - hedge all material risks of the position with instruments for which an active, liquid two-way market exists;
 - derive reliable estimates for the key assumptions and parameters used in the model;
- 4) the extent to which the Development Bank can, and is required to, generate valuations for the position that can be validated externally in a consistent manner;
- 5) the extent to which legal restrictions or other operational requirements would impede the Development Bank's ability to effect a liquidation or hedge of the position in the short term;
- 6) the extent to which the Development Bank can, and is required to, actively manage the risks of positions within its trading operation;
- 7) the extent to which the Development Bank may reclassify risk or positions between the non-trading and trading books and the requirements for such reclassifications as referred to in Article 53 of this Decision.

(2) In managing its positions or portfolios of positions in the trading book, the Development Bank shall comply with all the following requirements:

- 1) it shall have in place a clearly documented trading strategy for the position or portfolios in the trading book, which shall be approved by senior management and include the expected holding period;
- 2) it shall have in place clearly defined policies and procedures for the active management of positions or portfolios in the trading book, which include the following:
 - positions or portfolios of positions which may be entered into by each trading desk or, as the case may be, by designated dealers;
 - the setting of position limits and monitoring them for appropriateness;
 - ensuring that dealers have the autonomy to enter into and manage the position within agreed limits and according to the approved strategy;
 - ensuring that positions are reported to senior management as an integral part of the Development Bank's risk management process;
 - ensuring that positions are actively monitored with reference to market information sources and an assessment is made of the marketability or hedgeability of the position or its component risks, including the assessment, the quality and availability of market inputs to the valuation process, level of market turnover, sizes of positions traded in the market;
 - active anti-fraud procedures and controls;
- 3) it shall have in place clearly defined policies and procedures to monitor the positions against its trading strategy, including the monitoring of turnover and positions for which the originally intended holding period has been exceeded.

Inclusion in the trading book

Article 52

For the purposes of calculating its capital requirements for trading book positions, the Development Bank shall, taking into account its risk management capabilities and practices, have in place clearly defined policies and procedures for determining which position to include in the trading book in accordance with the trading book requirements set out in Article 50 of this Decision.

Reclassification of a position

Article 53

(1) The Development Bank shall have in place clearly defined policies for identifying the exceptional circumstances which justify the reclassification of a trading book position as a non-trading book position or, conversely, the reclassification of a non-trading book position as a trading book position, for the purpose of determining their own funds requirements to the satisfaction of the Central Bank.

(2) The Development Bank shall review the policies referred to in paragraph (1) of this Article at least annually.

(3) The management board of the Development Bank shall approve the decision on reclassification referred to in paragraph (1) of this Article.

(4) The Development Bank shall:

- 1) publicly disclose, without delay:
 - information that its position has been reclassified; and
 - where the effect of that reclassification is a reduction in the Development Bank's capital requirements, the size of that reduction; and
- 2) where the effect of that reclassification is a reduction in the Development Bank's capital requirements, not recognise that effect until the position matures.

(5) The Development Bank shall calculate the net change in the amount of its capital requirements arising from the reclassification of the position as the difference between the capital requirements immediately after the reclassification and the capital requirements immediately before the reclassification.

(6) The calculation referred to in paragraph (5) of this Article shall not take into account the effects of any factors other than the reclassification.

(7) The reclassification of a position in accordance with this Article shall be irrevocable.

IX. TRANSITIONAL AND FINAL PROVISIONS

Application of the provision on determining exposure class

Article 54

The provision of Article 19 of this Decision shall apply as of 1 January 2026.

Repealed regulation

Article 55

As of the commencement date of the application of this Decision, the Decision on the Method of Calculating Capital Adequacy Ratio of Investment and Development Fund of Montenegro (OGM 79/18).

Entry into force

Article 56

This Decision shall enter into force on the eighth day following that of its publication in the “Official Gazette of Montenegro”.