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Pursuant to Article 101, paragraph (2), item (3) of the Credit Institutions Act (Official Gazette159/2013, 19/2015, 102/2015 and 15/2018), Article 395, paragraph (1) and Article 493, paragraph (4) of Regulation (EU) No 575/2013 (OJ 176, 27.6.2013) as amended by Regulation (EU) 2017/2395 (OJ L 345, 27.12.2017) and Article 43, paragraph (2), item (9) of the Act on the Croatian National Bank (Official Gazette 75/2008 and 54/2013), the Governor of the Croatian National Bank hereby issues the

Decision on large exposures of credit institutions

I GENERAL PROVISIONS

Subject matter and terms and definitions
Article 1

(1) This Decision prescribes:

1) a lower limit for the purpose of Article 395, paragraph (1) of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176, 27.6.2013) as amended by Regulation (EU) 2017/2395 of the European Parliament and of the Council of 12 December 2017 amending Regulation No 575/2013 as regards transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds and for the large exposures treatment of certain public sector exposures denominated in the domestic currency of any Member State (Text with EEA relevance) (OJ L 345, 27.12.2017), hereinafter referred to as 'Regulation (EU) No 575/2013',

2) the application of Article 493, paragraph (4) of Regulation (EU) No 575/2013 and

3) indicators for the purpose of identifying a group of connected clients referred to in Article 3, item (18) of the Credit Institutions Act.

(2) The terms used in this Decision shall have the same meaning as in the Credit Institutions Act and Regulation (EU) No 575/2013.

(3) The examples of groups of connected clients provided for the purpose of easier understanding of this Decision shall be provided in Annex to this Decision which constitutes an integral part thereof.

II LIMIT FOR THE PURPOSE OF ARTICLE 395 OF REGULATION (EU) NO 575/2013

Limit threshold
Article 2

Credit institutions shall apply Article 395, paragraph (1), subparagraphs (1) and (2) of Regulation (EU) No 575/2013 so that the words 'EUR 150 million' are replaced by the words 'HRK 3 million'.

III TRANSITIONAL PERIOD FOR CERTAIN EXPOSURES TO PUBLIC SECTOR ENTITIES

Limits applicable during the transitional period
Article 3

(1) By way of derogation from Article 395, paragraph (1) of Regulation (EU) No 575/2013, credit institutions shall be allowed to incur exposures referred to in Article 493, paragraph (5) of Regulation (EU) No 575/2013 which meet the conditions laid down in paragraph (6) of that Article , up to the following limits:

1) 75% of the credit institution’s tier 1 capital until 31 December 2019 and

2) 50% of the credit institution’s tier 1 capital until 31 December 2020.

(2) The limits referred to in paragraph (1) of this Article shall apply to exposure values after taking into account the effect of the credit risk mitigation in accordance with Articles 399 to 403 of Regulation (EU) No 575/2013.

IV GROUP OF CONNECTED CLIENTS

Group of connected clients
Article 4

(1) Credit institutions shall apply the provisions of this Decisions relating to the group of connected clients in all cases in which Regulation (EU) No 575/2013 prescribes that two or more persons are to be connected in a group of connected clients because they constitute a single risk in accordance with Article 4, paragraph (1), item 39 of Regulation (EU) No 575/2013.

(2) When identifying the group of connected clients in the manner referred to in Article 4, paragraph (1), item (39) of Regulation (EU) No 575/2013, credit institutions shall identify whether there exists:

1) a control relationship in accordance with Article 4, paragraph (1), item (37) of Regulation (EU) No 575/2013 and

2) an economic and financial interconnectedness.

Procedure for identifying a group of connected clients
Article 5

(1) Credit institutions shall identify connections among their clients based on control as well as identify their economic and financial interconnectedness and document them. Credit Institutions shall take all reasonable steps and take into account all available information, including the data that another institution formed a group of connected clients for certain clients, as well as data on connected clients that a client is required to publish in accordance with the relevant standards of financial reporting. Identification of possible connections shall an integral part of the credit institution's exposure granting and monitoring process.

(2) Credit institutions shall regularly monitor changes to interconnections among clients in the context of the procedure of exposure monitoring and when a substantial increase to an exposure is planned.

(3) Credit institutions shall make the investigation of possible economic and financial interconnectedness among their clients proportionate to the size of the exposures.

(4) For the purposes of paragraph (3) of this Article, credit institutions shall carry out detailed investigations of interconnectedness in all cases where the sum of all exposures of a credit institution to one person exceeds 5% of tier 1 capital of the credit institution or of a group of credit institutions in the RC if the investigation is carried out on a subconsolidated or consolidated basis.

(5) When identifying a group of connected clients based on a combination of control and financial and economic interconnectedness indicators, credit institutions shall collect information on all entities forming a chain of financial contagion, taking into account the information on connections that stem from persons that are not clients of the credit institution, if the credit institution has such information available.

Duties of the management board and senior management
Article 6

(1) The management board of a credit institution shall adopt and implement the policy for the identification of connections among clients.

(2) The management board and senior management of a credit institution shall:

1) ensure the implementation of adequate processes for the identification of connections among clients,

2) ensure that the processes referred in item (1) of this paragraph are documented and

3) periodically review the processes referred to in item (1) of this paragraph.

Control relationship
Article 7

(1) For the purposes of Article 4, paragraph (1), item (39) of Regulation (EU) No 575/2013, credit institutions are required to identify that two or more persons constitute a single risk when there is a control relationship between them regardless whether the person has effective control.

(2) By way of derogation from paragraph (1) of this Article, where a credit institution considers that two or more persons do not constitute a single risk despite the existence of a control relationship, the credit institution shall justify this in a detailed and comprehensive manner (see Example C 1 in the Annex).

(3) Credit institutions shall apply the concept of control as defined in Article 4, paragraph (1), item (37) of Regulation (EU) No 575/2013 as follows:

1) in relation to a person that is a parent undertaking having its head office in the Republic of Croatia that prepares its consolidated financial statements in conformity with the Accounting Act (Official Gazette 78/2015, 134/2015 and 120/2016), in accordance with Article 23 of that Act, the credit institution shall form a group of connected clients to include undertakings included in the consolidated financial statements of that parent undertaking, regardless whether the parent undertaking is a client of the credit institution or not;

2) in relation to a person that is a parent undertaking having its head office in another Member State that prepares its consolidated financial statements in conformity with the regulation transposing Directive 2013/34/EU of the European Parliament and the Council of 26 June 2013 on the annual financial

statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (Text with EEA relevance) (OJ L 182, 29.6.2013) as last amended by Directive 2014/95/EU of the European Parliament and of the Council of 22 October 2014 amending Directive 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups (Text with EEA relevance) (OJ L 330, 15.11.2014), in accordance with Article 22, paragraphs (1) and (2) of this Directive as transposed into the regulations of this Member State, the credit institution shall form a group of connected clients to include undertakings included in the consolidated financial statements of that parent undertaking, regardless whether the parent undertaking is a client of the credit institution or not;

3) in relation to a person that prepares their consolidated financial statements in conformity with the international accounting standards applied in accordance with Regulation (EC) No 1606/2002, the credit institution shall form a group of connected person to include undertakings included in the consolidated financial statements of that parent undertaking, in accordance with these accounting standards, regardless whether the parent undertaking is a client of the credit institution or not; and

4) in relation to persons except the persons referred to in items (1) to (3) of this paragraph, it shall be deemed that a control relationship exists between a natural or a legal person and another undertaking if there is a similar relationship to the relationship between a parent undertaking and a subsidiary as referred to in items (1) to (3) of this paragraph, taking into account the provisions of paragraphs (4) and (5) of this Article.

(4) In the cases referred to in paragraph (3), item (4) of this Article it shall be deemed that a control relationship exists if any of the following criteria is met:

1) a person holds the majority of voting rights in another person;

2) a person has the right or ability to appoint or remove the majority of the members of the management board, the supervisory board, the administrative board or supervisory body of another person;

3) a person has the right or ability to exercise a dominant influence over another person pursuant to a contract or provisions in the articles of association.

(5) In the case referred to in paragraph (3), item (4) of this Article, when assessing whether a control relationship exists among two or more persons, credit institutions shall consider the following indicators of control:

1) whether the person has the power to decide on the strategy or direct the activities of another person;

2) whether the person has the power to decide on crucial transactions such as the transfer of profit or loss;

3) whether the person has the right or ability to coordinate the management of a legal person with that of another legal person in pursuit of a common objective (e.g. where the majority of the members of the board or other management bodies or supervisory boards of these undertakings are the same persons) and

4) a holding that exceeds 50% of the shares or 50% of the capital of another person.

(6) Credit institutions shall group two or more persons among whom there is a relationship of control into a group of connected clients even where they are, under the relevant accounting framework, exempt from the scope of the same consolidated financial statements.

(7) Credit institutions shall group two or more persons among whom there is a relationship of control into a group of connected clients regardless of whether or not the exposures to these clients are exempt from the application of the large exposures limit under Article 400, paragraphs (1) and (2) of Regulation (EU) No 575/2013.

Key indicators of economic and financial interconnectedness
Article 8

(1) When assessing the economic and financial interconnectedness among two or more persons in accordance with Article 4, paragraph (1), item (39) under (b) of Regulation (EU) No 575/2013, credit institutions shall take into account the specific circumstances of each case and identify a group of connected clients if their constitute a single risk because they are interconnected in such a way that financial problems experienced by one of these persons, in particular funding or repayment difficulties, would probably lead to funding or repayment difficulties for another or all other persons from the group (see Examples EF 1, EF 2, EF 3 and EF 4 in the Annex).

(2) By way of derogation from paragraph (1) of this Article, a credit institution may establish that despite identified indicators of economic and financial interconnectedness persons do not constitute a single risk where it demonstrates:

1) that financial difficulties or the failure of one person would not lead to funding or repayment difficulties for the other person or

2) that one person is economically or financially dependent on another person in a limited way, i.e. that the person can easily find a replacement for the other person.

(3) When assessing the economic and financial interconnectedness referred to in paragraph (1) of this Article, credit institutions shall asses the following indicators:

1) in the case when one person guarantees fully or partially for the exposure of another person and the exposure is so significant for the issuer that the issuer will be subject to serious financial difficulties if a claim occurs;

2) where a member of an entity, in accordance with the legal framework governing the operation of the entity, is liable for the exposure of such entity (e.g. a general partner in a limited partnership), and the amount of exposure is so significant that its collection might cause financial difficulties for the member of the entity;

3) where a significant part of a person's annual receipts or annual expenditures is derived from transactions with another person (e.g. the owner of a residential or commercial property derives the majority of rent income from one tenant) that cannot be easily replaced;

4) where a significant part of a producer’s production is for one single buyer which cannot be easily replaced;

5) where persons use or are expected to use the same source of funds to repay their obligations to the credit institution and none of the persons has an independent source of income from which these obligations to the credit institution may be serviced and fully repaid;

6) other situations where persons are legally or contractually jointly liable for obligations to the credit institution (e.g. bill debtors, debtor and co-borrower, or a debtor and his or her spouse/partner);

7) where the significant part of receivables or liabilities of a person is to one counterparty;

8) where persons have common owners, shareholders or managers, including undertakings linked by management on a unified basis referred to in Article 15, paragraph (1), items (1) and (3) of the Credit Institutions Act;

9) where legal persons have a small common client base and the potential for finding new clients is limited;

10) in a relationship between the debtor and collateral provider, where the amount of collateral is such that collection arising from collateral could cause serious financial difficulties for the collateral provider and

11) in other relationships that are in their substance similar to the indicators stated in items (1) to (10) of this paragraph.

(4) Where a credit institution's client is economically or financially dependent on more than one other person, which are not dependent on each other, the credit institution shall form several group of connected clients in order to include the client in them and separately each of the person on which the client is economically or financially dependent.

(5) Credit institutions shall include two or more persons that are economically or financially dependent on a third person in one group of connected clients, even if this third person is not a client of a credit institution.

(6) Credit institutions shall group two or more persons among whom there is a relationship of economic and financial interconnectedness into a group of connected clients regardless of whether or not the exposures to these persons are exempt from the application of the large exposures limit under Article 400, paragraphs (1) and (2) of Regulation (EU) No 575/2013.

Economic and financial interconnectedness through a main source of funding
Article 9

When assessing the economic and financial interconnectedness, the credit institution shall consider the following situations in addition to the indicators referred to in Article 8 of this Decision:

1) situations where the funding problems of one person are likely to spread to another on account of a one-way or two-way dependency on the same funding source; this does not include situations where persons are funded from the same market (e.g. the market for commercial papers) or where the persons' dependency on their existing source of funding is caused by their deteriorating creditworthiness, such that they cannot quickly replace the source of funding;

2) situations where the credit institution assessing the interconnectedness of its clients, its group of credit institutions in the RC or its group of connected clients make up a source of funding on which other persons are dependent, and the source of funding cannot be easily replaced (see Examples EF 5 and EF 6 in the Annex);

3) situations where there is one funding entity (e.g. the same credit institution or conduit that cannot be easily replaced);

4) situations where similar structures are used;

5) relying on commitments from one source (e.g. guarantees, credit support in structured transactions or non-committed liquidity facilities), taking into account its solvency, especially where there are maturity mismatches between the maturity of underling assets and the frequency of refinancing needs.

Approach for exposures to the central government
Article 10

(1) Credit institutions shall include in a single group of clients connected to the central government all persons connected to the central government by a control relationship referred to in Article 7 of this Decision or by the relationship referred to in Articles 8 or 9 of this Decision which reflect that they constitute a single risk with the central government.

(2) By way of derogation from paragraph (1) of this Article, credit institutions may in accordance with the definition of a group of connected clients under the last subparagraph of Article 4, paragraph (1), item 39 of Regulation (EU) No 575/2013 assess the existence of a group of connected clients:

1) separately for each group under the direct control of the central government or directly economically and financially connected to it ('Alternative approach – applied for all directly dependent persons', Example CG 2 in the Annex) or

2) separately for only a particular person under the direct control of the central government or directly economically and financially connected to it ('Alternative approach – partial use', Example CG 1 in the Annex).

(3) In the cases referred to in paragraph (2) of this Article, credit institutions shall:

1) include exposures to the central government in each group of connected clients that have been separately identified for each natural or legal person under the direct control of the central government or directly economically and financially connected to it (see Example CG 2 in the Annex) and

2) include in each group of connected clients the persons controlled by or economically and financially connected with the person under the direct control of the central government or directly economically and financially connected to it (see Example CG 3 in the Annex).

(4) In the cases referred to in paragraph (2) of this Article, where the persons under direct control of the central government or directly economically and financially connected to it are at the same time economically and financially dependent on each other, credit institutions shall form a separate group of connected clients for such persons, which excludes exposures to the central government (see Example CG 4 in the Annex).

(5) This Article applies to regional governments or local authorities subject to Article 115, paragraph (2) of Regulation (EU) No 575/2013 and natural and legal persons under the direct control of these regional governments or local authorities or connected to them.

Interconnectedness between the group identified through control relationship and the group identified through economic and financial interconnectedness

Article 11

(1) Credit institutions shall carry out the procedure of identifying a group of connected clients by first identifying the groups of persons connected by a control relationship in accordance with Article 4, paragraph (1), item (39), subitem (a) of Regulation (EU) No 575/2013 and the groups of persons economically and financially connected in accordance with Article 4, paragraph (1), item (39), subitem (b) of the same Regulation.

(2) After identifying groups in the manner referred to in paragraph (1) of this Article, credit institutions shall analyse whether there is a connection among groups identified in this way, i.e. it shall assess whether the groups identified based on a control relationship should be connected with the group of persons economically and financially connected. Credit institutions shall analyse each case separately in order to identify the possible chain of contagion based on individual circumstances (see Examples C/EF 1 and C/EF 2 in the Annex).

(3) Where persons that are a part of different groups based on a control relationship are economically and financially interconnected, credit institutions shall group all persons in the chain of contagion into one group of connected clients.

(4) In the case referred to in paragraph (3) of this Article, where the parent undertaking is a person that is economically and financially dependent on a person from another group, credit institutions shall include all persons under the control of that parent undertaking in one group of connected clients (see Example C/EF 3 in the Annex).

(5) Where the person that is economically and financially dependent on a person from another group is a subsidiary, credit institutions shall also include in a single group of connected clients the parent undertaking of that subsidiary only if the undertaking is economically and financially dependent on the subsidiary that constitutes the link between the two groups (see Example C/EF in the Annex).

V TRANSITIONAL AND FINAL PROVISIONS

Cessation of effect of the previous Decision
Article 12

On the date of entry into force of this Decision, the Decision on large exposures of credit institutions (Official Gazette 2/2010, 160/2013 and 12/2018) shall cease to have effect.

Entering into force
Article 13

This Decision shall be published in the Official Gazette and shall enter into force on 1 January 2019.

No.: 342-020/11-18/BV
Zagreb, 30 November 2018

Boris Vujčić

Governor

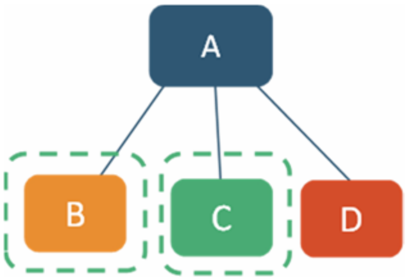
ANNEX

The examples of connecting persons in a group of connected clients

The examples in this Annex illustrate the application of this Decision to groups of connected clients falling under the definition referred to in Article 4, paragraph (1), item (39) of Regulation (EU) No 575/2013.

1 Group of connected clients based on a control relationship

<u>Example C 1:</u> Exceptional case (no single risk exists despite the existence of a control relationship)
The credit institution has exposures to all persons shown below (A, B, C and D). Person A has control over persons B, C and D. The subsidiaries B, C and D are special purpose entities.



To assess if there is no single risk, despite the existence of a control relationship, the credit institution shall assess at least all of the following elements in relation to each special purpose entity (entities B, C and D in this Example):

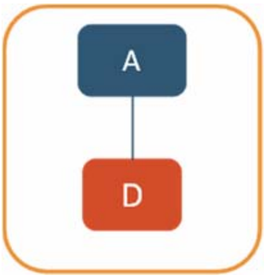
a) The absence of economic and financial interconnectedness or any other factors that could be indicative of a material positive correlation between the credit quality of the parent undertaking A and credit quality of the special purpose entity (B, C or D). Among other factors, the credit institution shall assess the following indicators as indicators of a material positive correlation: potential reliance on parent undertaking A for funding sources, some of the criteria preventing the deconsolidation of the special purpose entity or the derecognition of securitised assets under the applicable accounting rules.

b) The specific nature of the special purpose entity, especially its bankruptcy remoteness (in accordance with Article 300, paragraph (1) of Regulation (EU) No 575/2013) – in the sense that effective arrangements exist that ensure that the assets of the special purpose entity will not be available to the creditors of parent undertaking A in the event of its insolvency – and if the debt securities issued by the special purpose entity normally reference assets that are liabilities of third parties.

c) The structural enhancement in a securitisation and the delinkage of the obligations of the special purpose entity from those of parent undertaking A, such as the existence of provisions, in the transaction documentation, ensuring servicing and operational continuity.

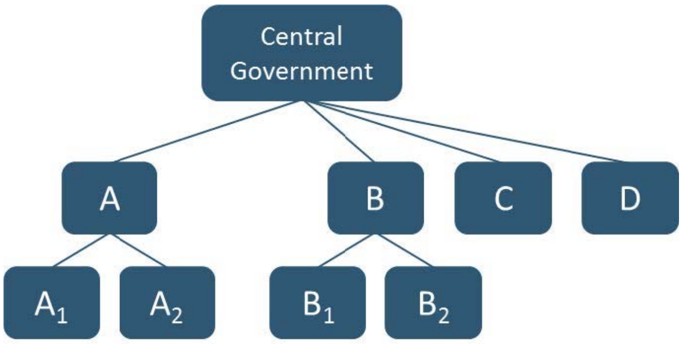
d) The compliance with the provisions of Article 248 of Regulation (EU) No 575/2013 regarding arm's length conditions.

Having assessed all of these elements, the credit institution could conclude that, for example, subsidiaries B and C do not constitute a single risk with parent undertaking A. Accordingly, it will be considered that the group of connected clients is composed only of persons A and D. The credit institution shall document these assessments and their findings in a comprehensive way.



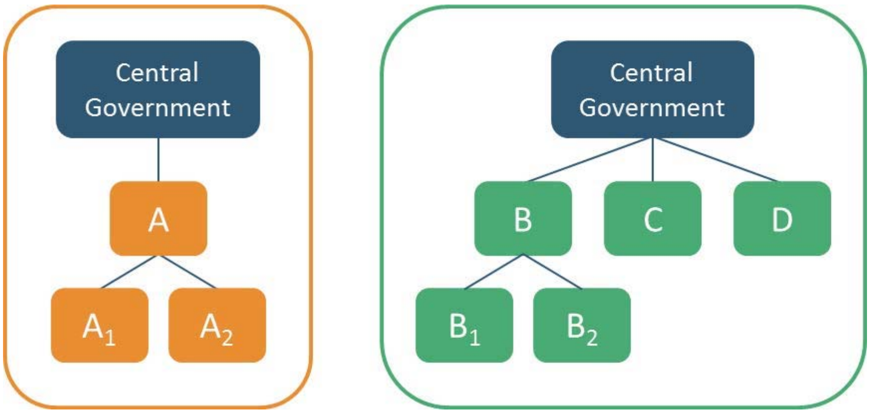
2 Alternative approach for exposures to central governments

To illustrate the possible examples, the following general assumption is used: the central government directly controls four legal persons (A, B, C and D). Persons A and B have direct control over two subsidiaries each (A_1/A_2, B_1/B_2). The credit institution has exposures to the central government and all of the persons shown.

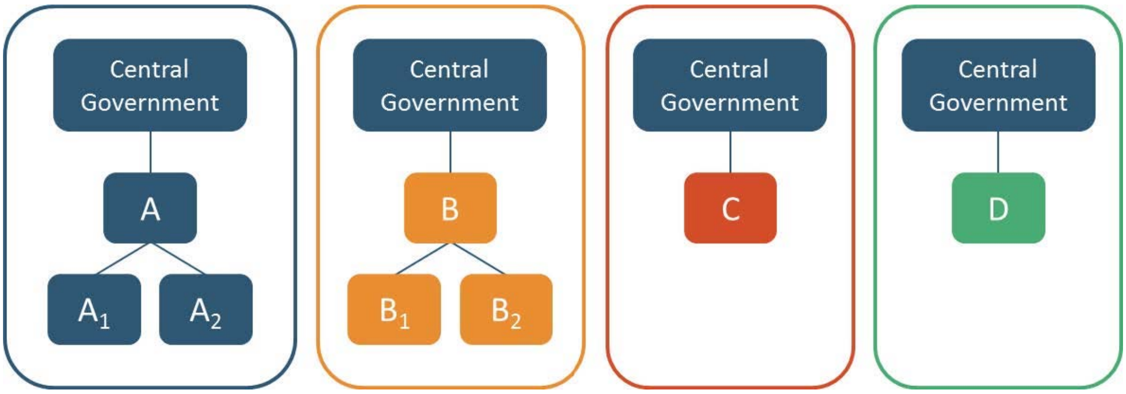


<u>**Example CG 1**</u>**: Alternative approach – partial use**

The credit institution could form only one group (central government/A/all controlled or dependent persons of A) and keep the general treatment for the rest (central government/B, C and D/all controlled or dependent persons of B):

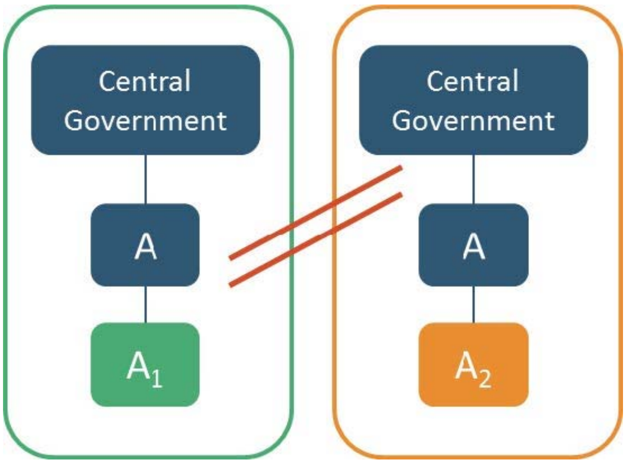


Example CG 2: Alternative approach – used for all directly dependent persons



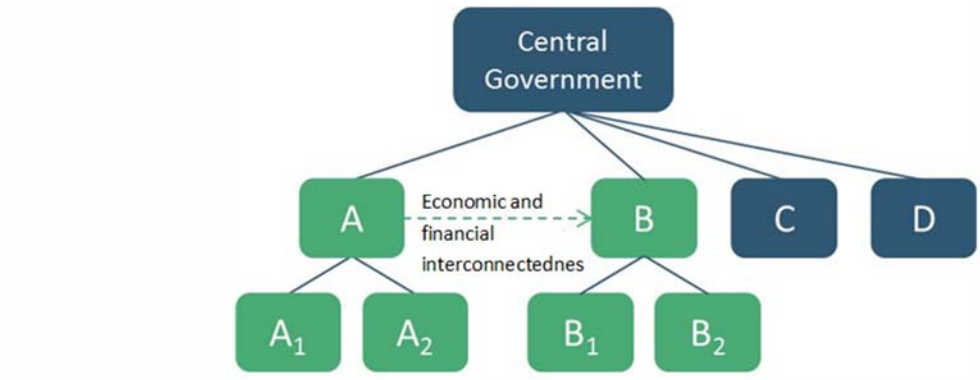
Example CG 3: Alternative approach – applicable on 'first/second level', not below

In the examples CG 1 and CG 2, persons A, B, C and D constitute the 'second level', i.e. the level directly below the central government ('first level'). Here, it is possible to form a subgroup of connected clients from the overall group of connected clients. However, entities A1, A_2, B_1 and B_2 are only indirectly connected to the central government. A carve-out on their level is not possible (e.g. both A1 and A_2 need to be included in the group 'central government/A'):

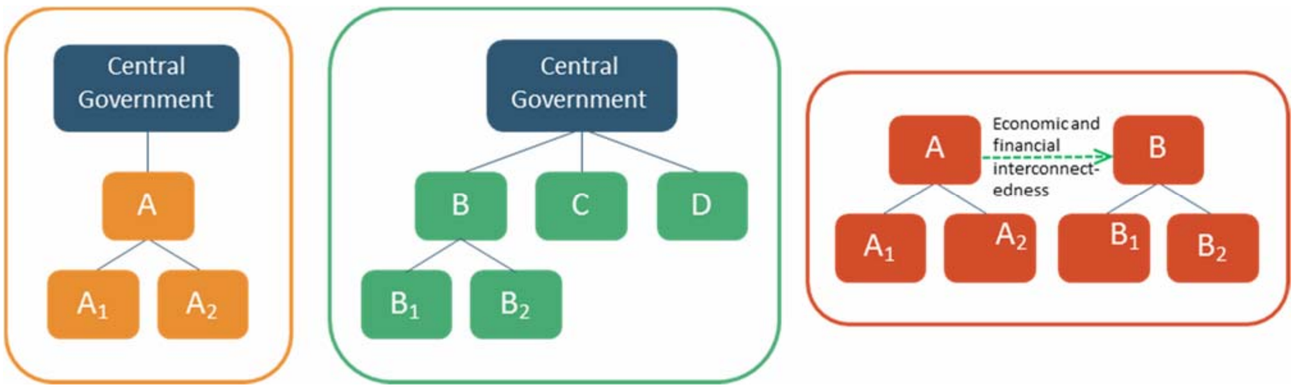


<u>Example CG 4:</u> Horizontal connections on the second level

In a variation from the general assumption above, persons A and B are economically connected (payment difficulties for B would be contagious to A):



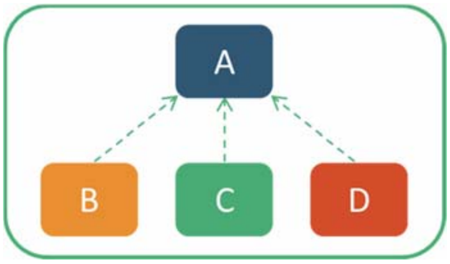
Assuming that the credit institution uses the alternative approach only in part, as described in example CG 1 above, the following groups of connected clients need to be formed:



3 Groups of connected clients based on economic and financial interconnectedness

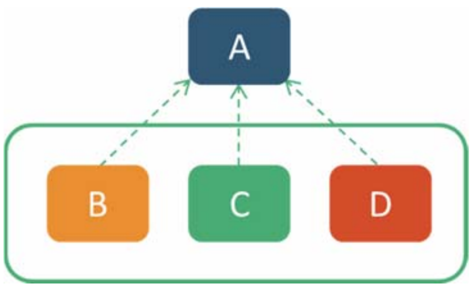
<u>Example EF 1:</u> Main case

The credit institution has exposures to all persons shown below (A, B, C and D). The persons B, C and D rely economically on A. Hence the person A is the underlying risk factor in all cases. The credit institution shall form one comprehensive group of connected clients, not three individual ones. It is irrelevant that there is no dependency among B, C and D.



<u>Example EF 2:</u> Variation on main case (no direct exposure to source of risk)

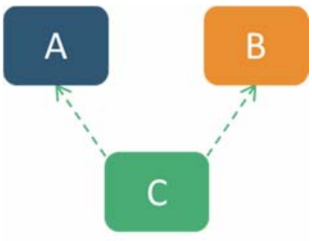
There is a grouping requirement even if the credit institution does not have a direct exposure to person A but is aware of the economic dependency of each person (B, C and D) on A. If possible payment difficulties for A are contagious to B, C and D, they will all experience payment difficulties if A gets into financial trouble. Therefore, they need to be treated as a single risk.



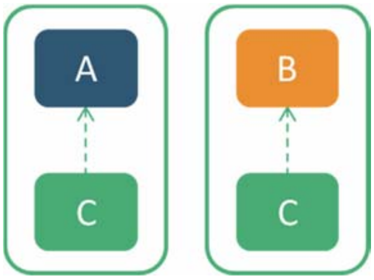
As in example EF 1, it does not matter that there is no dependency among B, C and D. The person A causes the grouping requirement, although it is not a client itself and this is not part of the group of connected clients.

<u>Example EF 3:</u> Overlapping groups of connected persons

If a person is economically dependent on two or more other persons (which means that payment difficulties of one of the other entities (A or B) might be sufficient to result in the person C being in difficulty);



it has to be included in the groups of connected clients of both (all such) persons:



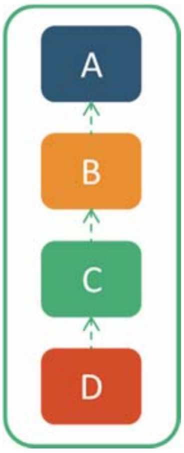
The argument that the exposure to C will be double-counted is not valid because the exposure to C is considered a single risk in two separate groups.

The large exposure limit applies separately, i.e. the limit applies once to exposures to group A/C and once to exposures to group B/C.

As there is no economic and financial interconnectedness between A and B, no comprehensive group (A + B + C) needs to be formed.

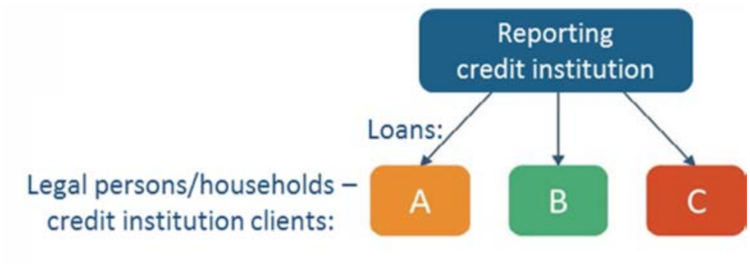
<u>Example EF 4:</u> Chain of dependency

In the case of a ‘chain of dependency’, all entities that are economically and financially dependent (even if the dependency is only one way) need to be treated as one single risk. It would not be appropriate to form three individual groups (A + B, B + C, C + D).



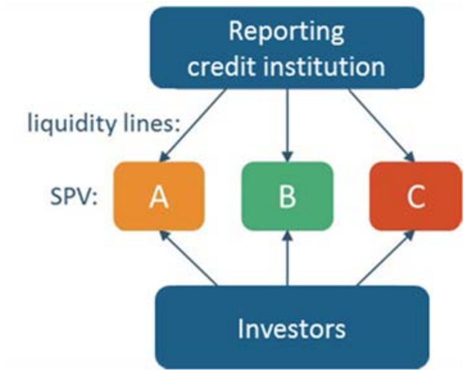
<u>Example EF 5:</u> Reporting credit institution as source of funding (no grouping requirement)

In the following example, the reporting credit institution is the sole funding source for three clients. It is not an ‘external source of funding’ that connects the three persons and it is a funding source that can normally be replaced.

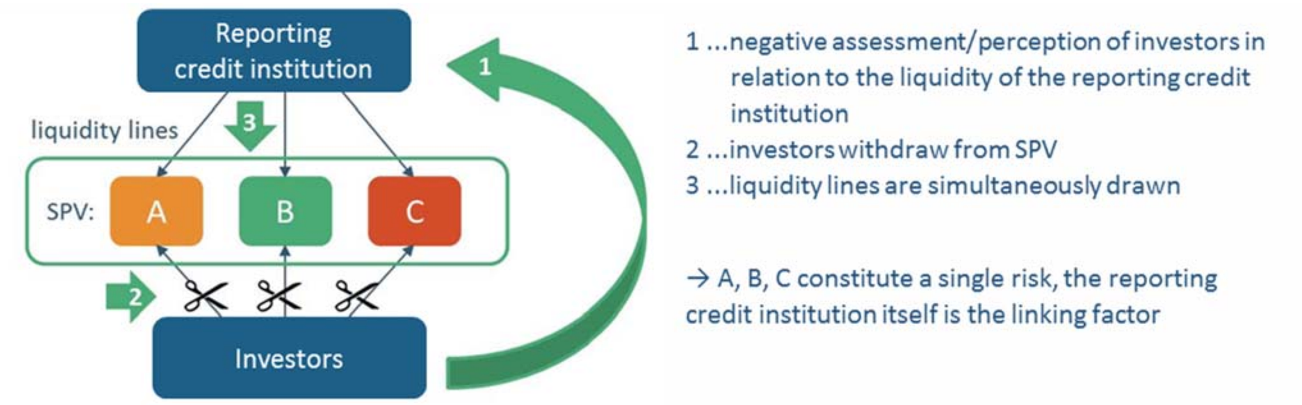


<u>Example EF 6:</u> Reporting credit institution as source of funding (grouping requirement)

In the following example, the reporting credit institution is the liquidity provider of three special purpose entities or conduits (similar structures):



In such a case, the reporting institution itself can constitute the source of risk as recognised in recital 54 to Regulation (EU) No 575/2013:

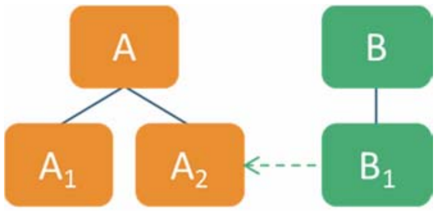


In the example above, it does not make a difference whether the liquidity lines are directly to the special purpose entity or to underlying assets within the special purpose entity. What matters is the fact that liquidity lines are likely to be drawn on simultaneously. Diversification and quality of the assets are also not considerations in this example, nor is the reliance on investors in the same sector (e.g. investors in the asset backed commercial papers market), as the single risk is created by the use of similar structure and the reliance on commitments from one source (i.e. the reporting institution as the originator and sponsor of the special purpose entity).

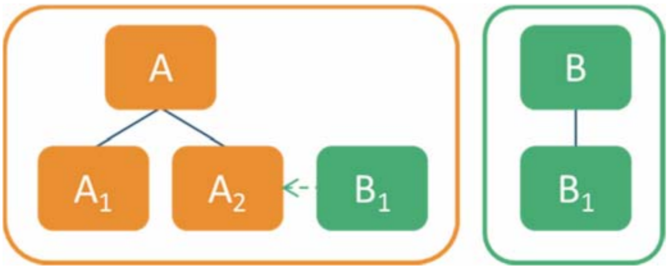
4 Interconnectedness between the group identified through control relationship and the group identified through economic and financial interconnectedness

<u>Example C/EF 1</u>: Combined interconnectedness based on control and based on economic and financial dependency (one-way dependency)

In the following example, the credit institution has exposures to all entities shown in the diagram below. Person A controls A_1 and A_2, person B controls B_1. In addition, B_1 is economically dependent on A_2 (one-way dependency):



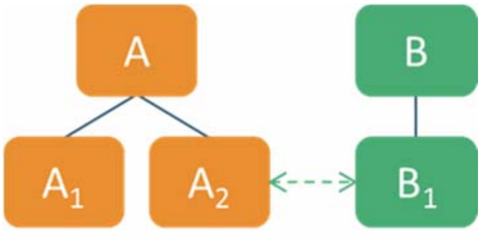
<u>Grouping requirement:</u> In this example the credit institution shall come to the conclusion that B_1 is in any case to be included in the group of connected clients of A (the group thus consisting of A, A1, A_2 and B_1) as well as of B (the group thus consisting of B and B_1):



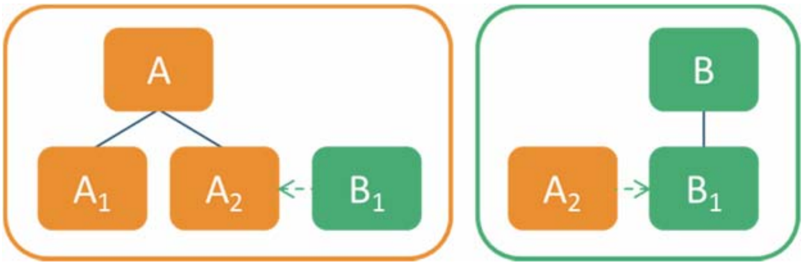
In case of financial difficulties for A, A and ultimately B_1 will also experience financial difficulties on account of their legal (A_2) and economic (B_1) dependency respectively. The forming of three different groups (A + A1 + A_2, A_2 + B_1, B + B_1) would not be sufficient to capture the risk stemming from A, because B_1, although dependent on A_2 and thus on A itself, would be carved out of the single risk of group A.

Example C/EF 2: Combined interconnectedness based on control and based on economic dependency (two-way dependency)

In this example, the economic dependency of A_2 and $B_1$is not only one way but mutual:

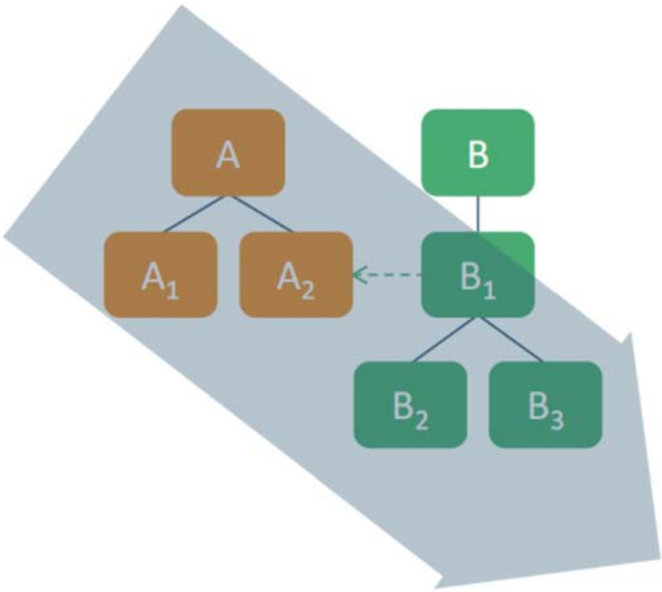


Grouping requirement: Person A_2 needs to be included additionally in group B, and B_1 needs to be included additionally in group A:

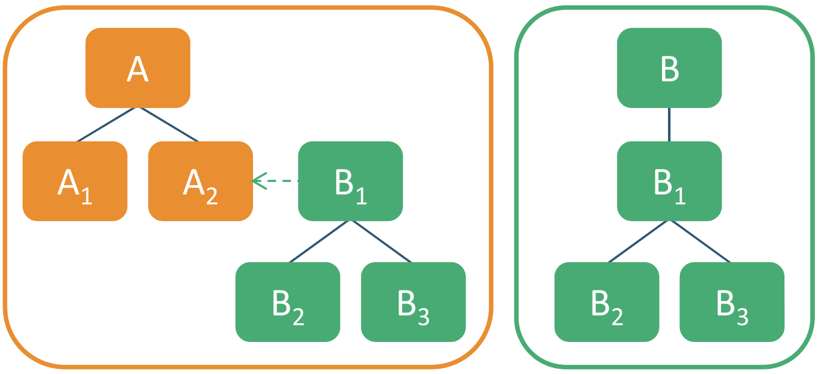


<u>Example C/EF 3</u>: Downstream contagion

In a variation on example C/EF 1 above, B_1 also controls two persons (B_2 and B_3). In this case, the financial difficulties of A will pass through A_2 and B_1 down to the two subsidiaries controlled by B_1 ('downstream contagion').

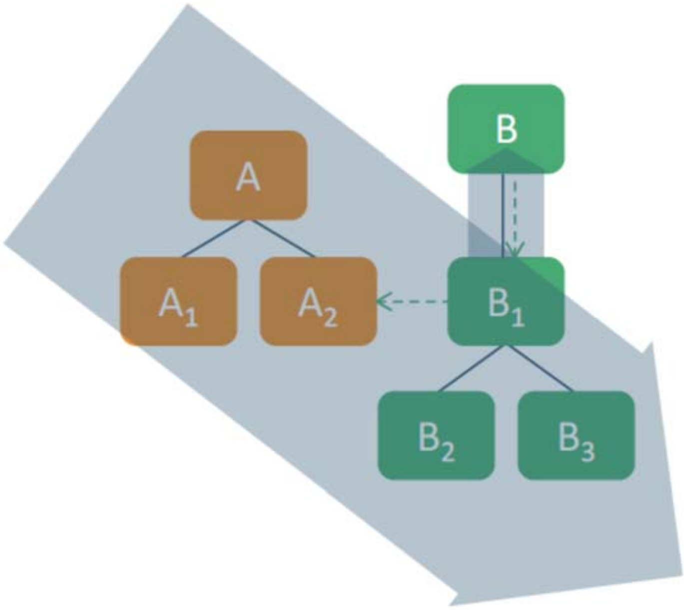


<u>Grouping requirement:</u>

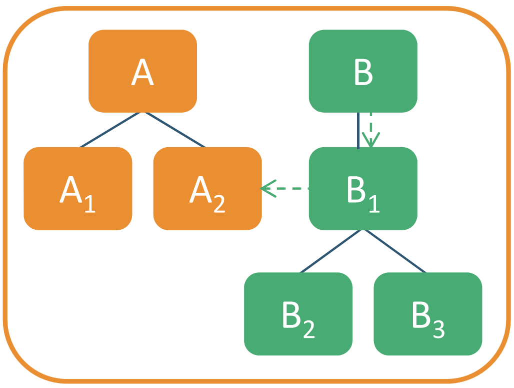


<u>Example C/EF 4</u>: Upstream contagion

The control relationship between B and B_1 does not automatically lead to including B in the group of connected clients of A, as financial problems for A are not likely to result in financial difficulties for B. However, the parent undertaking B needs to be included in the group of A if B_1 forms such an important part of group B that B is economically dependent on B_1. In this case, the financial difficulties of A will proceed not only downwards but also upwards to B, causing payment difficulties for B (i.e. all persons now form a single risk).



<u>Grouping requirement:</u>



5 Procedure for identifying a group of connected clients

<u>Example Mm 1:</u> Limits to the identification of a chain of contagion

Further in connection to the example C/EF 4, the credit institution has exposures only to persons A and B_3. In such a case, it should be taken into account that the credit institution might not be able to become aware of the chain of contagion and the group of connected clients might not be correctly formed.