

BEST PRACTICE GUIDELINE

From the Banking Regulation and Supervision Agency:

GUIDELINE FOR CREDIT MANAGEMENT OF BANKS

SECTION ONE

General Principles

Definition and Objective

1- The objective of this guideline is to declare the best practices expected from banks about credit risk management as part of the article 35 entitled "The objective of risk management and the establishment of risk management system" of Regulation on Internal Systems and Internal Capital Adequacy Assessment Process of Banks published in the Official Gazette dated July 11,2014 Nr:29057

2- The guideline is prepared on the basis of the Article 93 of Banking Law Nr:5411 dated October 19,2005 and the Article 7/A entitled "Best Practice Guides" of Regulation on Procedures and Principles For Supervision by the Banking Regulation and Supervision Agency published in the Official Gazette dated July 22,2006 Nr:26236.

3- Credit management include the activities on identifying the strategies, policies and procedures concerning credits which is one of the banks' main scopes, marketing and granting credits, measuring, controlling and reporting risks which are undertaken and will be undertaken because of credits and reserving adequate capital at a ratio of covering these risks. The following principles are implemented in the management of banks' all portfolios that cause credit risk to an extent that if bank's scale is in conformity with its portfolio and the structure of its products.

Establishing Credit Strategies

Principle 1- Banks determine their strategies concerning the credit activities and develop policy and procedures appropriate to these strategies.

4- The board of directors determines in writing and approves the credit strategies considering market conditions, financial condition, risk appetite, expected profitability level and equity level of bank. These strategies are updated at least annually.

5- The board of directors periodically reviews the financial and economic indicators used by bank in credit strategy establishment, and based on the results of this review, makes the necessary changes in its strategy and practices.

6- While establishing strategies, the cost of risk and risk return balance are considered. It is ensured that the determined strategies should not affect the stability and quality of profit negatively.

7- Credit strategy includes short/medium/long term plans.

8- Credit strategies are shaped with the help of adequate analysis that will be carried out on the basis of portfolio. In addition to that, Banks should have methodologies that enable them to assess the credit risk involved in exposures to individual borrowers or counterparties as well as at the portfolio level. For more sophisticated banks, the credit review assessment of capital adequacy, at a minimum, should cover four areas: risk rating systems, portfolio analysis/aggregation, securitisation/complex credit derivatives, and large exposures and risk concentrations.

9- While establishing strategies, the capital requirement is determined depending on the expected risk level. The analyses concerning prompt and future capital requirement because of credit risk are carried out. Capital requirement under different economic conditions is considered within the context of these analyses.

10- The credit strategies are established considering the bank's organizational structure and the technical information and capacity of staff and administration responsible for credit operations. The relevant staff is informed about credit strategy and it is ensured that the strategy is understood by the staff.

11- The credit strategies are established pursuant to reasonable economic indicator assumptions. These assumptions are stated in strategy documents. In its credit strategy, a bank should take into account the cyclical aspects of economy and the effects of them on the composition and quality of credit portfolio. The possible effects of forward-looking commitments, objectives and policies of regulatory and supervisory authorities on bank should also be considered.

12- The board of directors should ensure that the bank's remuneration and promotion policies do not contradict with its credit risk strategy.

Establishing Credit Policies

Principle 2- Banks establish marketing, credit-granting and monitoring policies in line with their credit volume and complexity of activities.

13- Credit policy is established depending on the principles of prudence, prompt applicability and creditworthiness of customer in conformity with the determined credit strategies. Policies are approved by the board of directors.

14- Credit policies establish the framework for credit-granting activities of bank. Credit policies address such topics as target markets, portfolio structure and concentration, large amount of credits, credit limitation practices, approval authorities, exceptional practices concerning general credit policies and procedures for reporting.

15- Credit policies are announced in the bank, implemented pursuant to appropriate procedures and reviewed at least annually. While reviewing the credit policies, economic outlook, the trend of bank's capital adequacy rate and the changes in the related legislation should be considered.

16- The policies concerning corporate and commercial credits are established depending on the topics such as credit type, size, customer quality, sector, country and region.

17- Policies concerning personal loans are established depending on the topics such as credit type, size, income status, craft knowledge and age of credit customers.

18- Credit policies establish an operational connection between the activities and risk capacity of bank. Policies include main activity fields in accordance with the target portfolio structure, the risks concerning expected and unexpected losses in accordance with the risk capacity, and limits concerning risk concentration. It is ensured that the limits are conformed with the related legislation and limitations that are determined by regulatory and supervisory authorities.

19- Banks develop policies to ensure that the credit portfolio is adequately diversified considering the target markets and credit strategies. In these policies, limits on credits that can be given to single counterparty or groups of connected counterparties and geographical regions, economic sectors and different products, are determined. Alternative action plans such as price differentiation, allocation of additional capital, are developed for possible increases in concentration risk.

20- The established limits on credits includes clear cut and simple methods such as the ratio of bank's risk exposure to bank's equity and overall credit portfolio.

21- If the risk return balance of portfolio determined by policies is affected negatively as a result of limitations that can be set by related institutions according to loan types, the quality of portfolio and credit policies are reviewed.

22- For credit-card operations, banks' credit policies include principles and procedures on the management of credit risk and non-performing credit-card receivables and request approvals in conformity with the credit strategy and the size of activities.

23- The guarantee policies are established on the basis of such criteria as the quality of credit customers, sector, country, region and credit types. While establishing guarantee policies, the capital adequacy projections of bank are considered.

24- Banks develop appropriate policy and procedures for identifying, measuring, monitoring and controlling country risk and transfer risk concerning their cross-border credit and investment activities.

Establishing Credit Procedures

Principle 3- Detailed credit procedures are established in conformity with the bank's strategy and policies.

25- Credit procedures are established in writing by senior management or the board of directors.

26- Credit process includes the steps of marketing, credit-granting, extending credit, monitoring and liquidation of credit. In the credit procedures, credit processes are organized in detail and the duties and responsibilities of relevant staff are determined clearly.

27- The principles concerning collateralization are determined clearly in procedures. If there is any collateralization apart from these principles, this matter is stated in the documents concerning credit customers together with its reasons.

28- The approval processes and work flows for credits which are provided for the bank risk group, are separately determined.

29- Before starting to activities and new products that include credit risk, banks verify the conformity of these with legislation. Before being introduced or undertaken, new products and services are approved by the control mechanisms in the bank.

Power and Organizational Structure

Principle 4- The organizational structure concerning credit activities are established in the manner that it should enable functional segregation of duties and it should not cause conflict of interest.

30- The board of directors establishes an environment which enables the units in credit assessment process to decide independently and away from the external factors.

31- Because the board of directors has the credit-granting power, it is expected that board members should have adequate information about assessing the creditworthiness of credit customer.

32- Credit-granting power is transferred by considering the type, size and collateral structure of credit. The board of directors and general management monitor if the transferred credit-granting powers are used within the determined limits, develop necessary controlling practices that will identify any limit violations, assess the risks arising from credit operations that includes limit violations, and enable to take necessary measures.

33- The transferred credit-granting powers are reviewed periodically by analyzing the trend of the relevant credit portfolio quality.

34- While establishing organizational structure, the matters, that may cause conflict of interest, such as reporting to the same vice general manager of units concerning credit monitoring and tracking together with the credit marketing and credit-granting, are considered. The board of

directors takes the necessary measures for preventing such conflict of interest.

35- While assessing the performance of credit repayment, the administrations in credit marketing process should be responsible together with the administrations in credit-granting and monitoring processes.

36- The relevant senior management units of bank is responsible for establishing the structure that the authorized staff in credit processes can carry out the transactions in conformity with the bank's policy and procedures.

37- The practices which enable in-bank accountability about the responsibilities of bank staff are established.

Principle 5- Banks measure the performance of units and staff that take part in credit processes pursuant to clear and predetermined criteria.

38- Performance criteria is established in the manner that they should not cause conflict of interest.

39- In assessment of performance and premium of staff that take part in credit activities and relevant marketing processes, the size of non-performing loans that the staff undertake their marketing activities, is considered.

40- It is ensured that additional benefits such as bonus payment and premium arising from credit activities that the staff get, should extend over a reasonable time which enable to monitor the performance of credit.

Documentation and Information Systems

Principle 6- Information and documents concerning credits are kept in the manner that the customers can access easily.

41- In order to use credit files effectively, the relevant information and documents are updated in the manner that they enable to have an opinion about customer.

42- Records concerning credit operations are filed in the manner that the customers can access easily.

43- Functions that will meet the information requests of in-bank or nonbank competent authorities concerning credit operations on the basis of borrower or counterparty, are established.

44- Credit file includes information and documents concerning the operations carried out in the credit granting process.

Principle 7- The quality of credit management is directly related to the effectiveness of information systems. The information generated from such systems enables the senior

management and the units carrying out the credit activities to fulfill their responsibilities effectively.

45- Banks should have information systems and analytical techniques that will enable effective credit management. Banks use measurement techniques which are suitable for the structure and levels of risks involved in their activities and based on robust data, and periodically review the validity of them.

46- The information systems of banks should be able to analyze credit risk at the product or portfolio level.

Principle 8- Pursuant to credit monitoring activities, information systems suitable for the size and complexity of operations, are established.

47- Information systems should enable to monitor credits on the basis of customer, group, sub-portfolios and all portfolio and to measure the risks arising from all those. Information systems should consolidate information on monitoring matters including the concentrations of credit risk and enable to analyze them.

48- Information systems are designed in the manner that they can enable changes in the range automatically pursuant to determined criteria for possible/non-performing loans. The changes in the range which are made manually, are reduced to minimum level and the criteria concerning such operations is determined in writing.

49- The activities which are carried out within the context of processes, procedures and the system which is established with the aim of enabling to monitor the performance, quality and situation of credits regularly and continuously on the basis of credit and portfolio, are recorded. These records include the monitored matter, monitoring rates, monitoring results and operations concerning the identified matters within the context of monitoring activity.

50- The country, sector, borrower/counterparty, product, concentration, risk group and credit limits on individual basis determined in credit policies are recorded to information systems; in the case of approaching this limits, it is ensured that information systems should produce leading information and the limit exceeding including exceeding on exceptional operations should be reported in time. Information systems are structured resiliently to enable prompt and effective in-bank and legal reporting. Manual practices are avoided as far as possible.

51- Decision trees are established to enable systemic credit-granting in personal loans. Approval criteria are determined in assessing credit demands except for the automatic approval/dismissal mechanism.

52- Information systems are established in the manner that they should enable to monitor limits which are determined according to in-bank and legal legislations.

53- Information systems are structured in the manner that they should meet the information need of senior management about the guarantee/collateral structure of credit portfolio.

Activities under Internal Systems

Principle 9- Credit management activities are analyzed regularly by the units under internal systems.

54- Banks make internal controls and audits regularly for determining whether credit processes are maintained in conformity with credit policies and procedures of bank, credits are given within the principles and procedures determined by the board of directors and the amount, maturity and quality of credits are reported to the senior management correctly or not.

55- The activities carried out by units under internal systems are used in determining weaknesses of credit risk management process, policy and procedures and in identifying operations violating these limits, policy and procedures.

56- The matters identified as a result of analysis are shared regularly with senior management and audit committee regarding their importance.

57- The results of activities of units under internal systems are used by the administration effectively and the necessary measures are taken in order to avoid recurrence of weaknesses, contradictions and differences identified concerning the credit management.

58- The activities maintained by units under internal controls are carried out in the manner that they should enable to assess credit management processes, to carry out the process of credit approval effectively, to take measures for avoiding deterioration of credit portfolio quality and keeping credit risk within the legal and in-bank limits as soon as possible.

59- The units under internal systems, at a minimum,

- control the adequacy and accuracy of information in credit files periodically by sampling method
- reach an agreement between received collaterals and bank records by sampling method,
- assess the adequacy of collateral rate by sampling method,
- periodically assess the first 200 credits of bank which have the highest risks,
- assess the adequacy of practices which will identify the non-performing credits,
- assess separately and regularly the credit risk arising from exceptional operations.

SECTION TWO

The Management of Credit Marketing Processes

Informing Customers

Principle 10- It is ensured that the products which will be used in the period of credit marketing should be examined in all its parts and the customers should be informed truly.

60- Banks should have maximum sensitivity on informing the customers clearly about credit products and receiving their approval.

61- Pursuant to marketing activities the risks that the customers assumed and all the costs that the customers will bear for all credit products including derivative transactions, are clearly stated in writing.

Customer Selection

Principle 11- The selection of credit customers is made in conformity with the credit strategy and policies of bank.

62- In the pre-assessment that will be carried out for selecting credit customers, the reputation, financial condition, the performance of debt discharging, the morality of shareholders if available and the situation of these characteristics of customer before the bank policies are prioritized.

63- Banks provide the adequate information that will enable the assessment of real risk profile of borrower.

64- Pursuant to the principle of know your client, the necessary prior review about customers is carried out considering the relevant legislation.

Principle 12- The aim of credit-granting may be determined by customer or it may be identified by the bank according to the need of the customer.

65- The aim of credit-granting is determined clearly.

66- In personal loans, banks try to identify whether the loan applications have individual characteristics or not. In vehicle loan and mortgage applications, banks control if the transaction is prearranged or not.

67- Banks should be sensitive about granting credit to companies for their activity areas.

Other Marketing Principles

68- Pricing is done by considering the creditworthiness of customer and all components of provided credit.

69- The repayment performance of credits which is provided within the context of campaigns is monitored by banks.

70- The staff who is responsible for marketing credits is informed regularly about not only their objectives but also their powers, responsibilities and occupational risks.

71- There should be adequate time and staff for customer analysis.

72- The marketing units of banks are informed about the developments in domestic and global economy.

73- The staff in marketing units takes into account that the interest/profit share and other costs of credit can be covered by the customer and the relation between risk and profit should be analyzed correctly.

74- The measures are taken for keeping the balance between the quality of credit portfolio and possible negative effects of aggressive marketing objectives.

SECTION THREE

The Management of Credit- Granting Processes

Assessment

Principle 13- Banks establish predetermined assessment and approval functions for an effective credit management. Credit approvals should be in conformity with the written procedures of bank.

75- Credit -granting process includes the assessment and analysis of customer demands, preparing credit offer, the allocation/revision of limits, maturity renewal, making changes in conditions of use, and reviewing of credit approvals.

76- Credit-granting processes are managed by specialists in this field.

77- Banks may carry out a sole signing approval, double signing approval or a committee approval process according to the size and nature of credit. The principle and procedures concerning approval process including the running of committees, are determined in writing. Banks should have adequate transparency on decisions taken in the credit approval process and the last resort which has the authority to approve credit should be appointed.

78- The board of directors establishes the structure and practices which will prevent the shareholders, administration or other relevant parties from intervening credit assessment process.

Principle 14- Banks should have adequate information in order to assess the risk profile of borrower or counterparty correctly. In the credit-granting process, prudence principle is essential. In the period of economic growth, banks avoid practices which may give harm to this principle.

79- Banks establish competent credit groups on the matter of analysis and approval of credit demands according to the factors such as credit amount, sector, region, product group or customer group or credit type.

80- Banks take into consideration the total profitability realized from the credit customer and they also assess risk/profit relation for each credit provided to customers.

81- Each credit offer is subjected to a careful analysis that will be made by the staff who has enough knowledge and experience in conformity with the size and complexity of the credit transaction. The minimum knowledge level and type which will be a basis to credit analysis are determined and the procedures include documents and information that the bank will need in the events of approval and renewal of credits and making changes in the conditions of agreement.

82- Banks, at a minimum, get information about the aim of credit usage and the repayment sources, the risk profile of borrower, the past payment performance and potential solvency of borrower, for commercial credits the expertise of borrower in the business line, the borrower's sector and condition in this sector and the adequacy of securities under various scenarios.

83- In credit assessment, the local conditions and requirements are taken into consideration.

Principle 15- The staff that assesses the credit and customer should reach the right information.

84- In the credit assessment, the bank needs the detailed analysis of the financial situation and solvency of counterparty based upon the right and up-to-date information. In the process of credit assessment, in order to reach right information, the customers are visited and information concerning customers is gathered if necessary.

85- In order to learn the creditworthiness of customers, the controlling shareholder/shareholders of the companies which apply for credit are determined and the morality analysis concerning counterparties and directors are made.

Principle 16- In the process of credit granting, banks, in conformity with their scale, employ staff who is expert in financial analysis with the aim of carrying out the financial analysis and intelligence studies of credits.

86- In banks, the analysis reports of credits are carried out by staff who is expert in financial analysis.

87- Especially for high amount of credits, these studies are carried out by staff who is expert in financial analysis beyond the effect of marketing unit.

88- The analysis reports of high amount credits that are provided above the amount determined by the bank, includes assessments of sectors in which the company operate in addition to the company analysis.

89- It is tried to get financial intelligence even in credits in which there are a large number of customers such as personal credit.

90- The financial intelligence studies are done regularly within the context of updating assigned credit limits and creditworthiness of customers. In the events that it is difficult to get extensive and reliable information, banks should be sensitive in information studies as far as possible.

91- The workings which will enable to update information studies in time are established in the event that banks get unfavorable information about the customer.

92- The company credit file includes information notes about visits made to the companies that the banks have credit relation with.

93- The financial analysis and information reports of credits which are classified as non-performing loans are examined retrospectively and the deficiencies in the process are assessed if available, and the efficiency of bank's financial analysis and intelligence activities are reviewed.

Principle 17- In determining the customers' limits, the indebtedness and solvency of customers are considered.

94- The main aim of credit assessment is to analyze the solvency of customer. In credit-granting activities, guaranty principle which is one of the basic credit facility elements, is taken into consideration.

95- In personal loans, banks benefit from the generally accepted ratios such as debt/income ratio, debt service ratio that show the solvency.

96- In credit applications, the limits and periodic payment amount are determined by considering the credits and limits of customers in other banks.

97- In determining the customer's credit limit, the sustainability of customer's income status is considered.

98- The solvency is discreetly measured based upon the apparent and foreseeable cash flows of customer in the periods of capital and interest/profit share payments of credits. The credit repayment plan is determined by considering the solvency of customer.

99- As a part of the credit assessment, the payment status of customer in the products which he currently uses, is controlled.

100- The practices that enable to avoid providing credit to those who have not the adequate solvency, are established.

101- The cash flow of investment or credit activity is considered as primary repayment source. In assessing the solvency of customer, the guarantees/collaterals are not taken into account.

Principle 18- The creditworthiness of customer is assessed.

102- The risks of customers in bank and associations of bank which are subjected to consolidation are considered together.

103- The credit applications of customers, whose debt-income balance is over the determined threshold, are assessed more discreetly.

104- The risk assessment concerning credit applications of companies and the risk assessment concerning personal loan applications of company's shareholders are carried out together.

105- In personal loan applications, the real income status of customers are tried to be identified and are confirmed through reliable information and/or documents.

106- In determining the customer limits, banks take into consideration the risks arising from the customer positions such as commodity, liquidity, foreign exchange exposures.

107- While assessing the foreign exchange risk exposure of customers, banks consider the followings;

- Whether the cash flows of customer are based on a currency different from the currency of the demanded credit,
- Whether the customers have another debt in foreign currency or foreign currency indexed debt,
- The foreign currency position of customer and his ability to manage this position,
- If the customer is a resident in a foreign country, the possibility of failure to pay the credit in received currency because of the country risk,
- If the customer is engaged in foreign exchange or the customer is an institution which made a commitment of commercial activities with derivative financial instruments, the exchange risk that they may be exposed to.

As a result of these analysis and assessments, banks ensure that the customer has adequate cash flows in the same or indexed currency which he will pay the credit debt with, or the adequacy of customer's repayment capacity is approved by implementing stress testing.

Principle 19- Banks get information about the aim of credit usage and the reasons of credit requirement through the analysis.

108- Banks get information about the field that the customer will use the credit for, and assess the necessity of credit in terms of validity of credit usage aim that the customer stated.

109- In credit applications, if it is determined that the aim of credit usage is to get finance indirectly for the operations whose aims are speculative or for the high risk operations which is out of the main activity area, the real aim of credit usage is taken into account in credit assessments. Banks should be sensitive about providing credit to the companies for only their specialized activity area.

110- Banks take the necessary measures in order to avoid that companies may use short term credits as capital or in the financing of long-term assets.

111- Banks take measures in order to avoid providing credits to company shareholders from the limits of companies without assigning limits for these shareholders.

112- In the period of providing credit, it is ensured that the companies have the conditions for credit granting.

Principle 20- Project credits/directed loans are assessed by specific teams composed of experts.

113- According to bank's size, a specific team which is composed of experts is organized for project credits and directed loans. Banks assess the realism of expectation and projections concerning projects.

114- Banks determine a reasonable sub-limit concerning the part of the project which will be financed by the customer and ensure that it is not fallen below this limit during the investment period of the project. Banks verify that the part which is financed by customer is met by its equities.

Principle 21- Credit offers are prepared in writing and in detail.

115- In the period of preparing credit offers, the document includes the written and detailed opinions of those who take part in decision mechanism according to the size and type of credit. The opinions in credit offer are considered as a whole by decision making body of credit.

116- The practices are established that ensure the conformity of credit offers prepared for credit demands with the credit policies.

Determining Limits and Conformity with Limits

Principle 22- One of the most important elements of credit management is to establish credit limits at group level and at entity/company level. The controls of conformity with limits begin in credit management process and these controls are included in overall credit facility processes including the control process of conformity with in-bank regulations.

117- Credit offers include the conditions of providing credits in detail such as credit type, maturity, and collateral. Banks take the necessary measures for implementing the limits

determined in credit offers effectively and for changing them according to customer demands.

118- In establishing limits, banks benefit from the results of stress tests.

119- Banks take the necessary measures in order to ensure the conformity with the limits in relevant legislation and the limits determined in-bank including the information system infrastructure and establish the practices and processes that enable the administration who is entitled to determine the limits to monitor the conformity.

120- The reasons of approving credits exceeding the in-bank limits are explained by the approval authority and kept in relevant credit file. If the approvals exceeding limits become frequent, the effectiveness of current limitation system is reviewed.

Restructuring

Principle 23- In the process of extending credit, the current situation and credibility of customer is considered.

121- If there is a flaw in credit repayment because the borrower has a temporary liquidity shortage, banks may restructure this credit or make a new payment plan for this credit in order to enable the repayment of credits and make the borrower gain liquidity strength.

122- Apart from the reasons determined in clause 121, banks avoid the maturity extensions and renewal operations that decrease the liquidity of credit.

123- The credits of companies whose operations completely stopped or there is a strong possibility about this, should not be restructured.

124- While restructuring credits, the processes of credit assessment and assignment are actuated again. The situation of borrower's having temporary liquidity shortage is shown in financial tables and relevant documents and the credit file of borrower includes all information and documents about restructuring in detail.

125- In restructuring credits, banks avoid all the collecting except cash or cash equivalents.

Rating

Principle 24- Banks establish internal rating systems in order to manage credit risk. Rating system is established proportional to bank's scale.

126- Internal risk ratings should be adequate to support the identification and measurement of risk from all credit exposures, and should be integrated into an institution's overall analysis of credit risk and capital adequacy. The ratings system should provide detailed ratings for all assets, not only for criticised or problem assets. Loan loss reserves should be included in the

credit risk assessment for capital adequacy. Banks ensure that the designed rating systems are used actively in credit processes. The ratings identified for the borrower in the process of providing credit are periodically reviewed afterwards.

127- It is important to inform the board of directors and senior management of bank regularly about the results of rating system and the structure of credit portfolio.

128- By periodically controlling the function and consistency of their rating systems, banks ensure that their rating system is in conformity with the credit portfolio and this system is able to measure the creditability within reason.

129- The rating system is established by considering the principles of scale economy when it is approved for the products that have credit risk. But, banks may establish rating systems without comparing the income and cost intentionally.

130- Rating systems are supported by intelligence information considering the market conditions.

131- The banks that have sophisticated activities are expected to use advanced calculation methods in measuring the capital requirement.

132- In rating models, the authorities that will approve the model, are determined, the minimum score level is identified and the validation tests are made. It is ensured that the users of the model and the approving authorities should be aware of the model.

133- Validation studies are done periodically for internal rating models that are used by banks

134- The credit repayment of retail customers are monitored through behavior models. In order to identify the changes in risk profiles in advance, rating system measures the potential and existing deteriorations in credit risk profiles.

135- In corporate credits, rating operation is carried out at least once a year and this enables company ratings to be up to date. In limit increases, the rating and credibility of companies are reevaluated.

136- The systemic infrastructure is established in order to use rating system in an active and effective way in the process of credit assignments.

137- The rating model used in retail credits, is considered as an important part of decision function. The manual approval criteria are determined clearly and discreetly. It is ensured that the rate of credits assigned by approving manually should be at the potential lowest level

The Management of Collateral and Guarantees

Principle 25- Banks can utilize the collateral and guarantees in order to mitigate their risk exposures, but operations is carried out by primarily assessing the repayment capacity of borrower. Collateral cannot be substitute for a comprehensive assessment of customer.

138- Banks determine in writing the policy and procedures concerning the collateral management. In collateralized credit operations, banks assess whether the possible devaluation in collateral or decreases in creditworthiness create the need for additional collateral by considering the reasons of collateral need. Banks determine in writing the principles and procedures for assessing the need for additional collateral on the basis of credit and collateral types and utilize the information systems in monitoring this need.

139- Banks analyze the form requirements and legality of collateral during collateralization. Banks also consider that,

- the market value of the asset subject to collateral may be determined easily or may be measured and proved through a reasonable method,
- the asset subject to collateral may be marketed and whether this asset has a secondary market to be disposed of easily,
- whether there is an impediment that avoid the asset to be converted into cash,
- there are systems suitable for the management of this asset.

140- The efficiency of collateral in terms of risk reduction function is ensured by having the minimum conditions in the relevant legislation. In addition, banks ensure that the collateral should be legal and the contracts concerning collateral should be legally-binding. Therefore, the bindingness of regulations concerning collateral in the countries in which the related parties are resident is analyzed legally.

141- Collateralizations carried out apart from the credit-granting conditions, take part in credit files with their reasons.

142- Collaterals are valued regularly by staff who have adequate information and expertise and banks take the necessary measures in order to keep the actuality and conformity with the market conditions of information.

143- Banks prefer the collaterals which can be easily converted into cash. In addition, banks consider the price volatility of asset and the conformity of credit with collateral in terms of currency.

144- Banks ensure that the units that take part in the credit process can monitor the collaterals

concerning credits through the system.

145- On condition that they will not exceed the legal limits, banks determine the credit collateral rate in credits that banks need to get security especially in credits that are provided under the collateral of an asset with the aim of financing this asset. Credit collateral rate is measured by rating the credit to the value of collateral. In determining this level, banks consider the risks concerning the asset which is used as collateral and the losses that may arise because of converting the collateral into cash.

146- Banks control if the collaterals are related to any commercial affair. Banks should be careful about the concentration on the borrower and drawer whose solvency is related to each other.

147- In the credits that are provided in return for guarantee, banks take the measures in order to avoid matters like that the borrowers and guarantors may stand security for each other in different credits or they may be cross guarantor for each other by having accommodation papers mutually.

148- Banks match the collateral and credits for the credits they provide. Banks establish the necessary algorithm concerning the mentioned matching in conformity with the relevant legislation and have controlling processes.

149- Banks delimitate and monitor the collaterals in order to avoid the risk concentration on collaterals. Risk concentration is monitored and delimited at the level of the asset which is, at a minimum, gotten as a security, the relevant market of the asset, the issuer of asset that is gotten as security and the guarantors.

150- Collaterals are periodically reported to relevant management units in order to be utilized in credit management within the principle and procedures determined by the bank.

Other Issues

151- Banks may use credit derivatives as well as collaterals and guarantees as a tool for risk reduction method. Banks determine in writing the policy and procedures on assessing and using credit derivatives. Credit derivatives are considered and used pursuant to the principles and procedures in "Communiqué on Credit Risk Reduction Techniques"

152- Credit risk reduction methods, may be inadequate in receiving the result expected from the method. Therefore, banks should take into account the residual risks (legal risk, covenant risk or liquidity risk etc) that they face with. If such risks arise, bank may encounter a credit risk amount which is above its expectations. The followings may be given as example for these risks:

- Banks may be enable to convert the collateral into money or to sequestrate (if the counterparty becomes overdue)

- The guarantor may reject or delay to make payment,
- Credit documents whose legality are not analyzed in detail may be ineffective in getting the expected legal result.

So, banks prepare the written policy and procedures with the aim of controlling these residual risks. Banks keep these policy and procedures available for sending to Agency if they are asked for during the supervision and periodically review the usage, effectiveness and conformity of them.

153- In the credit risk reduction policy and implementing procedures, banks take into consideration that whether it is appropriate to consider overall value of credit risk reduction tool and show that the protection provided by credit risk reduction tools are in conformity with capital level. The residual risks are assessed and controlled pursuant to written policies and methods.

154- Pursuant to credit management, banks can carry out securitization operations. The policy and procedures concerning securitization operations are established in writing. In order to assess and manage the credit risk exposure arising from these operations, banks utilize the necessary models and methodologies. The calculation of capital adequacy includes these operations pursuant to principles and procedures in "Communiqué on the Calculation of Risk Weighted Amounts concerning Securitization"

SECTION FOUR

The Management of Credit Monitoring Processes

Establishing Monitoring Process

Principle 26- Banks establish an effective monitoring process within the context of managing risks arising from credit portfolio.

155- Banks develop and implement detailed procedures for ongoing analyzing and monitoring the situations of borrowers and credits in their portfolio. In these procedures, banks identify the criteria concerning the determination and reporting of problematic loans which required to be monitored t closely, classified into a different group, made provision and/or took additional remedial measures.

156- Banks assign qualified staff for monitoring the credits. These monitoring activities include the situation of collaterals and guarantees concerning credits. In assigning this staff, banks establish a structure which will not cause any potential conflict of interests.

157- An effective monitoring process enables the following matters;

- Banks should have adequate information about the current financial situation of borrower,

- The credit should be in conformity with conditions of contract,
- Banks should monitor the usage of approved credit limits by the customers and the conformity of these limits with the policy and procedures of bank.
- There should be adequate collaterals concerning the current financial situation of the borrower,
- Banks should identify and classify the non-performing loans on time.

158- Internal rating is an important tool of monitoring and controlling systems. For the credit customers whose rating is getting worse, banks should develop additional monitoring methods such as more frequent customer visits and supervision by senior management.

159- The board of directors should have adequate information about portfolio quality and the risk that the bank takes, concerning the portfolios such as retail credits in which there are a great number of customers.

160- As part of credit monitoring process, banks establish early warning systems that reveal the effects of negative developments to the credit repayments, arising from the customer or that may arise in economic conjuncture or in sectors which the customer operate in or interact with. The results getting from early warning systems are used in monitoring the portfolio quality.

161- Monitoring frequency is determined by considering the size, payment plan, maturity, the risk level of credit/portfolio and other issues. However, the determined monitoring frequency is increased if there are weaknesses in credits or if the credits approaches the limits determined by the legislation or in-bank regulations.

162- In monitoring activities, banks in maximum utilize the platforms which include the overall information and analysis concerning the risk parameters of customers.

163- Banks monitor closely the developments concerning sectors and areas in which the credits or customers centered.

164- In analysis that will carry out, banks consider the risks arising from mechanisms such as credit derivatives and securitization programmes used in credit risk management at the portfolio level. Further, the analysis of counterparty credit risk should include consideration of public evaluation of the supervisor's compliance with the Core Principles for Effective Banking Supervision.

165- Banks closely monitor of large amount credits with the aim of minimizing the losses that the bank will be exposed to as a result of sudden negative changes in the financial situation of credit customers. These risks are monitored through trends and assessments which are not only specific to the company but also on sectoral basis.

166- Banks periodically monitor on-premise the high-risk project credits as well as the activities of companies which have high credit risk.

167- If banks determine early warnings about becoming overdue or infraction, banks analyze the repayment capacity and creditworthiness of customer once again.

168- Banks monitor if there is a delay because of the customers in the credits including personal loans and report this to the relevant units on a daily basis.

169- Banks develop systems that will determine the overdue credit payments and report them to the relevant administration in time. This reporting duty should not be given to those who work in credit approval units.

170- If there is a disruption in the payment of capital or interest/profit share, banks should determine at which access level and how they take action.

171- The monitoring controls in information systems should include the following matters and if there become such matters they should give early warning signs;

- The negative indicators that take part in risk center records,
- The unexpected changes in the risk center data,
- The legal limitations concerning customer such as voluntarily measures, lien, suspension of bankruptcy
- Protested bills and overdraft cheques.

172- The information systems of banks are established to ensure monitoring credit conditions and the conformity between the collaterals that are taken from the customers and the conditions of providing credit.

Stress Testing and Scenario Analysis

Principle 27- As well as the developed models, banks benefit from stress testing and scenario analysis in monitoring and measuring risks arising from credit portfolio.

173- Banks make analysis on the prompt and future capital requirements because of credit risk. The capital requirement in negative economic conditions is considered within the context of this analysis.

174- In measuring the level of credit risk exposure, banks utilize the stress tests. The stress test measures the level of loss that the bank's credit portfolio will encounter before the negative developments that are less likely to happen.

175- In scenarios used in stress testing, banks take into consideration the issues such as the existence of negative developments in sectors that the banks are concentrated on, economic constriction, liquidity squeeze, the existence of unexpected developments in markets or the unexpected movements in interest rates.

176- The banks that provide credits in foreign exchange, add fluctuations in foreign exchanges rates to their scenarios in order to measure the losses arising from the weaknesses in customer's repayment capacity by considering the size of foreign exchanges in their portfolio and by paying the necessary attention.

177- Senior management analyzes the results of stress tests and scenarios and assesses the measures that can be taken for the losses the bank may encounter. Some of these measures are to change the limits or policy, to get hedging instruments, to implement methods that may reduce the risks.

178- In developing credit risk reduction methods, banks utilize the stress tests.

179- The results of stress tests and scenario analysis are also used in updating and determining the policy and limits of bank.

180- Banks that have complex nature of activity take into consideration that stress testing is a component of internal model approach in calculation of the capital required because of the risk exposure.

181- Stress test analysis is also carried out on consolidated basis. By considering the stress test analysis, banks establish a contingency plan including the actions that senior management may take in exceptional circumstances.

SECTION FIVE

The Management of Credit Tracking Processes

Principle 28- Banks have written policies concerning the management of non performing loans and receivables. The processes of credit tracking and liquidation are established to enable collection efficiency.

182-Banks establish the written policy and procedures concerning the management of non performing loans. Non performing loans express the loans and receivables determined in the first clause of Article 5 of the Provisions Regulation.

183- Banks establish a unit apart from the credit assignment and marketing units for the management of non performing loans.

184- Non performing loans are classified in accordance with the principles determined in the "Regulation on Procedures and Principles for Determination of Qualifications of Loans and Other Receivables and Provisions to be set aside". Banks may establish additional prudential criteria concerning the credits that will be monitored in each credit class. Banks make systemic developments to enable to monitor all the credits of a customer in the same class.

185- Banks establish the system that will enable the automatic classification for credits which become overdue according to the number of overdue days. Automatic dating is established based on the customer not the credit.

186- Banks clearly determine the principles and procedures for the management and liquidation of credits which are not still taken legal proceedings but take part in the period of collection.

187- Banks make the necessary developments in information systems in order to ensure the tracking of files in legal proceedings.

188- If the non performing loans are transferred, banks determine in writing the criteria for the receivables that can be transferred.

189- In the assessment of effectiveness and adequacy of bank's credit management, non performing loans and receivables are also considered.

190-This guideline shall enter into force in the publication date. The Guideline on Credit Management of Banks (Board Nr. 5945, dated July 17, 2014) is hereby abolished.