

From the Banking Regulation and Supervision Agency:

**REGULATION ON PROCEDURES AND PRINCIPLES FOR CLASSIFICATION OF
LOANS AND PROVISIONS TO BE SET ASIDE**

(Published in Official Gazette dated June 22, 2016 Nr. 29750)

SECTION ONE

Objective and Scope, Basis and Definitions

Objective and Scope

ARTICLE 1- (1) The objective of this Regulation is to set down the procedures and principles for classification of loans of banks according to their qualifications and provisions to be set aside for them.

Basis

ARTICLE 2-(1) This Regulation has been prepared on the basis of Articles 37, 53, 57 and 93 of the Banking Law Nr. 5411 dated October 19, 2005.

Definitions

ARTICLE 3- (1) Following terms used by this Regulation shall have the express meanings designated to them below;

- a) Bank: Bank defined by Article 3 of the Banking Law,
- b) Performing loans: Loans classified under First and Second Groups pursuant to this Regulation,
- c) Financial guarantee: The contract requiring the bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument,
- ç) Law: Banking Law Nr. 5411,
- d) Provisions: Amount set aside by calculation and recognized as expense in financial statements to meet the loan loss,
- e) Loans: Transactions deemed as loans pursuant to Article 48 of the Law as well as other receivables presented on the financial statements,
- f) Board: Banking Regulation and Supervision Board,
- g) Agency: Banking Regulation and Supervision Agency,
- ğ) Net realizable value: The value found by deducting all predictive costs which can directly be associated by disposal of related collaterals and the amounts which are not in the possession of bank in the case that another party excluding bank has a right or possession over the collateral,

from fair value of collaterals calculated according to Turkish Accounting Standards published by Public Oversight Accounting and Auditing Standards Authority,

h) Risk Center: Risk Center stated in Article annex 1 of the Banking Law No. 5411,

i) TFRS 9: TFRS 9 Financial Instruments Standard published by Public Oversight Accounting and Auditing Standards Authority,

i) Consumer loans: Overdraft account loans extended in connection with savings deposits of real persons and loans that are recognized as consumer loans according to uniform accounts of banks, and loans granted to real persons via credit cards for purchase of goods and services, except for commercial purposes, or in cash,

j) Re-financing: Granting a new loan to a debtor who is in difficulty or likely to be in difficulty to pay the current loan, in order to ensure total or partial payment.

SECTION TWO

Classification and Restructuring of Loans

Classification of Loans

ARTICLE 4-(1) Banks, including their branches abroad, shall classify and monitor recognize their loans according to the principles indicated below.

a) First Group - Loans of a Standard Nature: In this group, the following loans are classified;

- 1) Granted to natural persons and legal entities having a creditable financing structure,
- 2) Principal and interest payments are determined according to the solvency and cash flow of its debtor,
- 3) Payments are made when due or past due up to thirty days and, repayment problems are not expected in the future and, totally collectable without realization of collateral,
- 4) No credit deterioration has been detected for the debtor,
- 5) Subject to 12-months expected credit loss provisioning according to TFRS 9.

b) Second Group - Loans Under Close Monitoring: In this group, the following loans are classified;

- 1) Extended to natural persons and legal entities with a creditable financing structure, but for which negative signs are observed or forecasted in debtor's solvency or cash flows due to unfavorable developments in macroeconomic conditions or in the sectors the debtor operates, or, independent from the above-mentioned ones, due to adverse developments peculiar to the debtor,
- 2) Requiring close monitoring due to reasons such as the debtor faces a substantial financial risk at the granting stage of loan, or,

3) Problems regarding timely payments of principal or interest in accordance with the contract are likely to arise and full repayment without realization of collateral is unlikely if problems are not solved, or,

4) Credit worthiness of the debtor has not weakened since the date the loan was granted but is likely to weaken due to an irregular and unmanageable cash flow structure, or,

5) Delinquency in principal and/or interest payments, which is between 30 days and 90 days, due to reasons that cannot be interpreted as credit deterioration, or,

6) Subject to expected credit loss provisioning required for financial assets with significant increase in credit risk according to TFRS 9, or,

7) Net realizable value of collateral is below the book value of receivables, in the case that repayment totally depends on collateral or,

8) Subject to forbearance measures when being classified in Group 1 or Group 2 and do not meet the conditions to be classified as non-performing loans, or,

9) Subject to forbearance measures when classified as non-performing and classified as performing upon the realization of conditions stated in Article 7 of the Regulation.

c) Group Three - Loans with Limited Collectability: In this group, the following loans and other receivables are classified;

1) Debtor's credit worthiness has been deteriorated, or,

2) Full collection is unlikely without realizing collaterals since net realizable value of collaterals or debtor's own funds are inadequate to pay the debt on its maturity and loan loss is likely unless observed problems are removed, or,

3) Past due principal and/or interest payments between 91 days and 180 days,

4) Having the opinion that collection of principal and /or interest will be past due more than 90 days from its maturity or due date due to reasons such as having problems in the financing operating capital or creating additional liquidity due to unfavorable developments in macroeconomic conditions or in the sectors the debtor operates or, independent from all, due to adverse developments peculiar to the debtor, or,

5) Classified as performing loans following the application of forbearance measures but principal and/or interest payments are past due more than 30 days within the one-year probation period or being subject to forbearance measures within the one year probation period.

ç) Group four - Doubtful Loans: In this group, the following loans are classified;

1) Full collection of principal and/or interest in accordance with the contract is unlikely without realizing the collateral, or,

2) Debtor's creditworthiness has been deteriorated seriously but not considered completely loss due to the potential contribution of opportunities such as merger, new financing facilities or capital increase to the debtor and collectability of the loan, or,

3) Past due principal and/or interest payments between 181 days and one year from the due date, or,

4) Expected delinquency in the payments of principal and /or interest more than 180 days from its maturity or due date due to unfavorable developments in macroeconomic conditions or in the sectors the debtor operates, or, independent from the above-mentioned ones, due to adverse developments peculiar to the debtor.

d) Group Five - Loans classified as Loss: In this group, the following loans are classified;

1) Nil or negligible collection is expected since the creditworthiness of the debtor is totally deteriorated, or,

2) Despite having the qualifications for classifying in Group Three and Four, delinquency in payments more than one year is expected, or,

3) Past due principal and/or interest payments more than one year from the due date.

Non-performing Loans

ARTICLE 5-(1) In terms of implementation of this Regulation;

a) Loans classified in Groups 3, 4 and 5 within the scope of Article 4, or,

b) Loans whose debtor is considered in default pursuant to the Communiqué on Calculation of Amount Subject to Credit Risk by Internal Rating Based Approaches published in the Official Gazette dated October 23, 2015 No. 29511, or,

c) Loans which are subject to lifetime expected credit loss provisioning due to debtor's default, according to TFRS 9 are deemed as non-performing loans.

(2) Financial guarantees shall be classified as non-performing loans over their nominal amount where the financial guarantee is at risk of being called by the guaranteed party or where the underlying guaranteed exposure meets the criteria to be considered as non-performing.

(3) Cash loans granted as revolving credit lines without maturity condition in the contract shall be deemed as non-performing loans in case;

a) Accrued interests and fees are past due for more than 90 days from due date and added to the principal, or,

b) Payments are past due for more than 90 days as of the cutoff date, or,

c) Re-financing delinquent principal and/or interest by granting a new loan to the debtor, or,

ç) Continuously exceeding the credit line for more than 90 days.

(4) Loans considered as non-performing loans pursuant to first, second and third paragraphs of this article shall be classified in non-performing loan groups.

(5) In case its debtor has more than one loans granted by the same bank and any of the mentioned loans is deemed as non-performing loan, all loans of the mentioned debtor to the bank shall be classified as non-performing loans. Consumer loans can be classified as nonperforming on a transaction-by-transaction basis but in the case that a consumer loan is classified as non-performing, other consumer loans to the borrower shall not be classified in Group 1.

(6) In the case that loans of a debtor belong to a risk group is classified as nonperforming loans, credit worthiness of other debtors included in the debtor's risk group shall be assessed separately on the classification date and where conditions stated in Article 4 of this Regulation is met, their loans shall also be classified as non-performing loans.

(7) **(Addition - OG-27/3/2018-30373)**¹ The classification of the receivables amounting to 100 Turkish Lira or less as non-performing loan is in discretion of banks.

Re-classification

ARTICLE 6- (1) As to be quarterly balance sheet periods in maximum or without depending on that period, when a risk-bearing development is experienced in macroeconomic conditions or in sectors the debtor operate or independent from all, negative conditions appear in fulfillment of liabilities of the debtor to the bank, the banks shall examine the loans within the scope of Article 4, independent from credit and risk analysis they make in loan granting process and assess whether or not the loans shall be re-classified.

(2) Except for provisions stated in paragraph 3 of this Article regarding re-classification of non-performing loans as performing, in order for non-performing and performing loans to be re-classified in groups having a higher credit worthiness among sub-groups, they have to meet the conditions determined for the mentioned group in Article 4 of the Regulation.

(3) In order to classify non-performing loans as performing loans, whole of the following conditions should be met.

a) Whole of the past due payments causing the loan to be categorized as non-performing should be collected without realizing collaterals,

b) There must be no past due payments as of reclassification date and except for payments stated in (a), the latest two payments before that date should be made in due date and completely,

c) Conditions for classification in Group 1 or 2 stated in Article 4 should be met,

(4) Loans which are partially written-off or whose collateral is obtained by the bank against the loan or those paid in commodity cannot be classified as performing loans.

Forbearance

ARTICLE 7-(1) Forbearance which may be applied for performing and nonperforming loans refers to concessions granted to a debtor due to financial difficulty in payments and which would not be granted to a debtor with no difficulties in payments. Concessions granted in favor of the debtor who is unable or expected to be unable to meet his/her obligations are as follows;

a) Modification of the conditions of the contract, or

b) Fully or partially refinancing the existing loan.

(2) **(Repealed- OG- 15/8/2018-30510)**

¹ This amendment takes effect on the date of publication, effective from 1/1/2018.

(3) Implementation of provisions taking place in the loan agreement and providing privileges to debtor with financial difficulties is also considered as forbearance restructuring.

(4) **(Repealed- OG- 15/8/2018-30510)**

(5) In case all the following conditions are met, a forbore non-performing loan can be classified in the Group 2 as a forbore loan:

a) As a result of the assessment of the debtor's financial situation, it is detected that the conditions for non-performing classification have disappeared,

b) Recognizing as non-performing loans for at least one year following the restructuring,

c) There are not past due principal and/or interest payments as of the date of classification within the Group 2 after forbearance and there is no doubt regarding delinquency in the future payments,

ç) Past due or written-off principal and/or interest payments that are subject to forbearance measures have been collected.

(6) Loans which are classified as forbore in the Group 2 due to the realization of conditions set out in the fifth paragraph of this article and performing loans classified as forbore in Group 2 shall be exited from the status of forbore, where the following conditions are met:

a) Monitoring Recognizing as forbore loans in Group 2 for at least one year as of the date of classification,

b) Collecting minimum 10 % of interest and principal,

c) There is no delinquency in principal and/or interest payments more than thirty days for any loan to the debtor,

ç) Financial difficulty which caused forbearance has disappeared.

(7) Loans allocated to natural persons and legal entities in the risk group defined in the article 49(2) of the Law and to which the bank is included may be subject to forbearance measures within the principles stated in this article and on condition that there are no refinancing.

(8) **(Addition- OG- 15/8/2018-30510)** Banks can reclassify their performing-forbore loans that are in Group 2 under Group 1 by terminating the status of forbore at the end of at least three months monitoring period, on conditions that requirements stipulated in the subparagraphs (c) and (ç) of sixth paragraph are met, without the requirements stipulated in the subparagraphs (a) and (b) of sixth paragraph.

(9) **(Addition OG- 15/8/2018-30510)** The modification of the contract and/or partially or totally refinancing a Group 1-loan of a debtor who is not in financial difficulty is not considered forbearance and these loans can continue to be classified under Group 1.

Other Issues

ARTICLE 8- (1) It is essential that banks make the assessment concerning loan classification loan by loan basis. However, loans with small-balance and having common credit risk characteristics such as type, credit risk rating grade, collateral, allocation date, time remaining

to maturity, sector, geographic location of the debtor and credit collateral rate may be assessed together with regard to their classification, pursuant to the provisions of this Regulation.

(2) Financial assets measured at fair value pursuant to the Turkish Accounting Standards shall be re-assessed and classified in the related non-performing group according to the article 4, depending on credit worthiness of their issuers as well as changes in their risk qualifications and classification of loans allocated by them as non-performing receivables.

(3) **(Addition- OG- 27/11/2019-30961)**² The portion of the loans classified under "Fifth Group-Loans in Loss" in accordance with the Regulation and for which lifetime expected loan loss provision or special provision has been set aside due to the default of the debtor and of which there exist no reasonable expectations regarding recovery may be writtendown within the scope of TFRS 9 from the first reporting period (interim or year-end reporting period) following their classification in this Group.

(4) **(Addition- OG- 27/11/2019-30961)**³ It is an accounting practice to writedown the loans that do not have the possibility to collect within the scope of the third paragraph of this Article and does not result in the right to waive.

(5) **(Addition- OG- 27/11/2019-30961)**⁴ Writedown policy including the indicators determined by the bank regarding the lack of reasonable expectations for the recovery of loans and policies regarding loans that are followed-up although they have been writtendown, the loan amounts writtendown during the period within the scope of TFRS 9 and its effect on NPL ratio are explained in the footnotes of the financial statements

SECTION THREE

General and Specific Provisions

Setting aside provisions within the scope of TFRS 9

ARTICLE 9– (1) It is essential that banks set aside provisions for their loans within the scope of TFRS 9.

(2) In the implementation of this Regulation, amongst provisions set aside within the scope of TFRS 9,

a) The amount of twelve months expected credit loss provisions and the amount of life time expected credit loss provisions set aside due to the significant increase in the credit risk of the borrower are considered as general provisions,

b) The amounts of life time expected credit loss provisions set aside due to the default of the borrower are considered as specific provisions.

² This amendment takes effect on the date of publication, effective from 19/7/2019.

³ This amendment takes effect on the date of publication, effective from 19/7/2019.

⁴ This amendment takes effect on the date of publication, effective from 19/7/2019.

(3) Banks which set aside provisions according to TFRS 9 are not obliged to set aside provisions also for loans defined as loans but not within the scope TFRS 9 pursuant to the Regulation hereby.

(4) Banks shall take into account country and transfer risks while calculating their provisions for expected credit loss pursuant to the first sub-clause.

(5) The Board may request banks to set aside provisions with higher amounts than the ones set aside pursuant to this article, considering the concentrations observed in time in loans size, type, currency unit, interest structure, sector and geographic distribution, collaterals, and similar issues, as well as credit risk level and management, on the basis of bank or loan.

(6) The Board may decide, upon the application of the bank including detailed reasons, based on an assessment which it will make by considering the bank's activities that provisions are set aside within the scope of the articles 10, 11, 12 and 13 of this Regulation instead of TFRS 9.

General provisions to be set aside by banks not implementing TFRS 9

ARTICLE 10- (1) Banks not implementing apply TFRS 9 shall set aside general provisions to cover their credit losses incurred but not reported on credit basis, in following amounts:

a) At least fifteen per mille (1.5%) of their total standard cash loans,

b) At least three percent (3%) of their total cash loans under closely monitoring.

(2) Banks shall also set aside general provisions for country and transfer risks in addition to the ones set aside pursuant to the first sub-clause.

(3) Non-cash loans, commitments, and derivative financial instruments shall be taken into account in the calculation of general provisions upon risk amount calculated pursuant to the Regulation on Measurement and Assessment of Capital Adequacy of Banks published in the Official Gazette number 29511 dated October 23, 2015, by applying general provision ratio for cash loans.

(4) Loans granted against cash, deposit, participation fund, gold depository accounts, and gold preserved by the bank on condition that a pledge or disposition agreement has been prepared, borrowing instruments issued by the Central Government of the Republic of Turkey, the Central Bank of the Republic of Turkey as well as sukuk certificates to which they are fund users and collaterals and sureties granted by them, and loans granted to the Central Government of the Republic of Turkey, the Central Bank of the Republic of Turkey are not considered in the calculation of general provisions.

(5) The Board may determine higher general provision rates than the ones determined in the first sub-clause, considering the concentrations observed in time in loans' size, type, maturity, currency unit, interest structure, sector and geographic distribution, collaterals and similar issues, as well as credit risk level and management, on the basis of bank or loan.

Specific provisions to be set aside by banks not implementing TFRS 9

ARTICLE 11-(1) Amongst non-performing loans, following amounts of specific provisions shall be set aside to cover the credit loss realized;

a) At least twenty percent (20%) of the ones classified within Third Group,

b) At least fifty percent (50%) of the ones classified within Fourth Group,

c) One hundred percent (100%) of the ones classified within Fifth Group.

(2) Banks shall take into account also country and transfer risks while calculating specific provisions they will set aside for credit risk pursuant the first sub-clause.

(3) Impairment amounts set aside for assets specified in the article 8(2),

a) shall be transferred into accounts relating to specific provisions required to be set aside in case these assets are classified within Third, Fourth or Fifth Group of loans;

b) shall be set aside as additional specific provisions in case they are less than specific provision amounts required to be set aside; shall be maintained as specific provision in case they are more than specific provision amounts required to be set aside, as long as these assets are recognized in the related accounts,

(4) Pursuant to the article 5(5), in case a loan customer's any cash loan has become nonperforming and thus his/her non-cash loan or amounts relating to him/her monitored within the "Receivables from Derivative Financial Instruments" accounts have also been included within the scope of non-performing loans, specific provisions shall be set aside for their risk amount calculated according to the Regulation on Measurement and Assessment of Capital Adequacy of Banks. However, from the moment non-cash loans or receivables from derivative financial instruments have become cash; the whole of the amount turned into cash shall be taken into account as non-performing loan.

(5) The Board may determine higher amounts for specific provision than the ones specified in this article hereby, considering the concentrations observed in time in loans' size, type, maturity, currency unit, interest structure, sector and to geographical distribution and similar issues, as well as credit risk level and management, on the basis of bank or loan.

SECTION FOUR

Collaterals

General principles concerning collaterals

ARTICLE 12- (1) Banks shall take into account the principles regarding the management of collaterals and guarantees in the Guideline on Credit Management of Banks, published pursuant to the Regulation on Internal Systems and Internal Capital Adequacy Assessment Process of Banks published in the Official Gazette number 29057 dated July 11, 2014, in considering the collaterals they have taken in the enforcement of this Regulation.

(2) Collaterals taken based on agreements not having a legal validity or bindingness shall not be taken into account in the enforcement of this Regulation. Bindingness of agreements regarding collateral in the countries in which related parties reside shall also be analyzed from a legal point of view.

(3) Sureties and collaterals taken from natural persons or legal entities without credit worthiness as well as assets in the form of bill and cheque signed by them are not considered as collaterals in the enforcement of this Regulation.

Consideration of collaterals by banks not implementing TFRS 9

ARTICLE 13- (1) Banks which do not implement TFRS 9 are obliged to monitor collaterals concerning their loans by classifying them in respect of the following collateral groups.

a) First Group Collaterals;

1) Cash, deposit, participation fund and gold depositoryt accounts, member office receivables arising from credit cards and gold preserved by the bank, on condition that a pledge or disposition agreement has been prepared

2) Borrowing instruments issued by the Central Government of the Republic of Turkey, the Central Bank of the Republic of Turkey, Directorate of Privatization Administration and Housing Development Administration, as well as sukuk certificates to which they are fund users and collaterals and sureties granted by them,

3) Borrowing instruments issued by institutions subject to zero percent (0%) risk weight pursuant to the Annex-1 of the Regulation on Measurement and Assessment of Capital as well as sukuk certificates to which they are fund users and collaterals and sureties granted by them,

4) Borrowing instruments issued by European Central Bank or by its sureties as well as collaterals and sureties granted by this Bank,

5) Funds provided from repo transactions made based on securities specified in second and third sub-clauses as well as mutual fund certificates involving these securities,

b) Second Group Collaterals;

1) Precious metals except for gold,

2) Borrowing instruments issued by institutions subject to twenty percent (20%) risk weight pursuant to the Annex-1 of the Regulation on Measurement and Assessment of Capital Adequacy of Banks, as well as sukuk certificates to which they are fund users and collaterals and sureties granted by them,

3) Collaterals, sureties, letter of credits, bills of guarantee, acceptances and endorsements granted by banks operating in Turkey,

4) Borrowing instruments, mortgage-backed securities and asset-backed securities and covered bonds issued by banks operating in Turkey, as well as sukuk certificates to which they are fund users,

5) Stocks traded in a stock market,

6) Excluding those issued by the borrower, borrowing instruments mortgage-backed securities and, covered asset-backed securitiesbonds issued by the private sector institutions established in Turkey and lease certificates for which those are fund users,

7) Credit derivative contracts providing protections for credit risk,

8) Pledge or disposition of claims of natural or legal persons from public institutions,

9) Sureties provided by Credit Guarantee Fund Inc. and which do not have the support of the Undersecretariat of Treasury,

c) Third group collaterals

- 1) Borrowing instruments issued by institutions subject to 50% risk weight pursuant to the Annex-1 of Regulation on Measurement and Assessment of Capital Adequacy of Banks, sukuk certificates for which those are fund users and guarantees and sureties provided by them,
- 2) Securities representing commodity and every kind of pledged commodity and movables
- 3) Real estate hypothecs,
- 4) Export document insured within the context of export credit insurance contract or based on bill of lading or transport bill,
- 5) Commercial receivable insurance policies,
- 6) Sureties provided by Credit Guarantee Fund Inc. and which do not have the support of the Undersecretariat of Treasury,
- 7) Stocks not traded in a stock market

ç) Fourth Group Guarantees cover

- 1) Borrowing instruments issued by institutions subject to 100% risk weight pursuant to the Annex-1 of Regulation on Measurement and Assessment of Capital Adequacy of Banks, sukuk certificates for which those are fund users and guarantees and sureties provided by them,
- 2) Commercial enterprise pledge,
- 3) Other export documents,
- 4) Pledge on vehicles, pledge on lines of commercial vehicles and pledge on license plates for commercial vehicles,
- 5) Pledges on airplanes or ships,
- 6) Sureties of natural persons and legal entities enjoying credibility higher than that of borrower,
- 7) Bills and cheques taken from natural persons and legal entities enjoying credibility higher than that of borrowers,

d) Fifth group collaterals; the types of guarantees not covered by the first four groups

- (2) Assets held in possession of banks as lessors as part of financial leasing transactions are treated on the basis of their groups of guarantees matching the respective qualifications in this article.
- (3) Mutual fund participation certificates are considered in the related collateral groups in proportion to the weights of money and capital market instrument that mutual fund includes.

Collateral Valuation

ARTICLE 14-(1) The following principles are taken into consideration by banks applying TFRS 9 or not, relating to the valuation of collaterals;

- a) Collaterals are considered on the basis of net realizable value in provision measurement.
- b) Pursuant to the Communiqué on Credit Risk Reduction Techniques published in the Official Gazette dated September 6, 2014 Nr:29111, banks subject their collaterals which may be

considered as credit risk reduction technique to valuation according to the principles and procedures in this Communiqué.

c) Pursuant to the Communiqué on Credit Risk Reduction Techniques, banks value their collaterals which may not be considered as credit risk reduction technique at reasonable intervals that they will determine according to collateral types and credit maturity. Banks document their policies relating to collateral valuation frequency with justifications.

ç) Banks assess their collaterals in order to determine whether they exposed to significant impairments or not when any kind of development which cause risk that will affect the value of collateral arises independently from the clauses (b) and (c).

d) The collaterals which have the characteristic of real estate hypothec of loans classified as non-performing loans are subjected to revaluation pursuant to the principles of this article until the end of the month following the date of classification.

e) In valuation of sureties taken from natural and legal persons which have creditworthiness, the solvency of these people is taken into consideration instead of surety or liability amounts. The determination of solvency is carried out by measuring the financial and economic potential of these warrantor or guarantors benefiting from the assessments of credit inquiry units and Risk Center records.

f) In valuation of collaterals which have the characteristic of enterprise pledge, the cost base to insurance is used for those subject to insurance or secondary market prices are used in measuring the fair value. In the event that the measured value is lower than the amount subject to pledge, the lower value is taken into account.

(2) The Board is entitled to determine different rates in order for considering collaterals through a lower amount from their net realizable values on the basis of bank or across the sector in special provision measurement by considering the developments in market conditions, concentrations in collateral types and the capacity of collaterals to recompense the loan losses for banks which do not apply TFRS 9.

Considering collaterals in special provision measurements

ARTICLE 15- (1) Banks which do not apply TFRS 9 consider collaterals according to the principles and procedures stated below in measuring the special provisions that they need to set aside pursuant to Article 11.

a) The amount of receivable to be subjected to special provision is measured by deducting the net realizable values of collaterals determined according to Article 14 from nonperforming loan amounts monitored recognized in Third, Fourth and Fifth Groups at the consideration rates stated below. The operation of determining the amount of receivable subject to special provision is carried out based on the individual claim of bank and net realizable values of their collaterals for each debtor.

First group collaterals: one hundred percent (100%) Second group collaterals: eighty percent (80%)

Third group collaterals: sixty percent (60%) Fourth group collaterals: forty percent (40%) Fifth group collaterals: twenty percent (20%)

b) The part of net realizable value of collateral which exceeds non-performing loan amount is not considered in special provision measurement.

c) In the event of having collateral types in different groups relating to non-performing loan;

1) In determining the claim amount subject to special provision, it is started from the collateral group which is considered the most liquid according to the group order stated in Article 13.

2) It is controlled that whether net realizable amount of each collateral type exceeds the remaining non-performing loan amount or not. 3) The part for which special provision is not applied for non-performing loan is determined by multiplying the part of net realizable value of collateral type taken into account firstly in measurement which is equal to highest non-performing loan amount by the consideration rate of this collateral. On condition that they are not from the same collateral type, the same operation is repeated separately and in order through the remaining non-performing loan balance for collateral types in the same group firstly and just after those in other groups.

4) At the end of these operations, if an amount for which special provision relating to non-performing loan will be applied remains, the special provision is set aside through this remaining amount.

Assets that banks obtained due to their receivables

ARTICLE 16- (1) Banks account the commodities and real estates which they obtained due to their receivables according to the related Turkish Accounting Standards. (2) Banks dispose the commodities and real estates which they obtained due to their receivables within three years as of the date of acquisition.

(3) Banks may assign the real estates they obtained due to their receivables for their own use on condition that they do not exceed the limit stated in Article 57(1) of the Law and the size and number that banks need for conducting banking activities and on condition that banks document their justifications available for audit. Banks may assign the commodity they obtained due to their receivables for their own use on condition that the quality and number of them are appropriate to those they need for conducting banking activities.

Income Recognition

ARTICLE 17- (1) The loans accepted as non-performing ones by banks which do not apply TFRS 9 according to this Regulation are not subjected to valuation and interest accrual are not performed for these loans. Interest accruals and valuation differences which were performed beforehand for receivables which turned into non-performing loans are cancelled on accounting records by debiting related income account at the same amount. The part of foreign currency loans extended by participation banks from foreign currency participation accounts whose risk belongs to participation accounts may be valued with current rates. Closing of interest accruals and valuation differences by cancelling is under the provisions of setting aside special provisions.

(2) Banks which apply TFRS 9 disclose interest accruals and valuation differences they calculate for their financial assets which were accepted as non-performing loans according to this Regulation in the notes to the financial statements.

SECTION FIVE

Documentation and System

Documentation and System

ARTICLE 18- (1) Banks must establish internal systems in conformity with the complexity of their operations and scales for determining the provision amounts in accordance with their own internal policies, Turkish Accounting Standards and regulations and guidelines published by the Agency. The senior management of the bank is responsible for establishing these systems and ensuring their operability.

(2). Banks must match the classifications relating to loans in this Regulation and the rating system which they established according to their own internal policies and must keep this matching available for audit.

(3) Banks must document and keep available for audit their assessment about reclassification of non-performing loan as performing and reclassification of non-performing or performing loans in the group which shows higher creditworthiness among the sub-groups and provision amounts set aside.

(4) Banks establish the necessary infrastructure for monitoring the loans in Second Group in three separate sub-groups as 0-30, 31-60 and 61-90 past due days.. The senior management of the bank is responsible for establishing policies and taking measures necessary for closely monitoring of these loans.

(5) In contract changes which do not give any concessions to its debtor, the justification for making these changes is documented by the bank.

(6) Banks establish the necessary system for monitoring and reporting of forborne loans classified under the performing or non-performing loans.

(7) Banks establish the necessary system for monitoring the collection amounts obtained from loan collaterals of non-performing loans on the basis of collateral type.

(8) In the event that the guarantees and sureties taken from natural and legal persons and bills drawn by them are considered as collateral, banks make the assessments relating to the creditworthiness of these persons available for audit.

(9) Pursuant to Article 6(1), banks must document the assessment results relating to loans which exceed the amount of (**Amentment-OG- 27/3/2018-30373**)⁵ one million³ Turkish Liras and the highest first two hundred loans in terms of amount with their justifications and make them available for audit.

(10) (**Amentment-OG- 27/3/2018-30373**)⁶ Banks must monitor recognize the loans classified pursuant to this Regulation according to their reference in the accounts which are determined in the Communiqué on Uniform Chart of Accounts and Prospectus or the Communiqué on Uniform Chart of Accounts and Prospectus to be applied by Participation Banks.

⁵ This amendment takes effect on the date of publication, effective from 1/1/2018.

⁶ This amendment takes effect on the date of publication, effective from 1/1/2018.

SECTION SIX

Miscellaneous and Final Provisions

Funds extended by participation banks

ARTICLE 19-(1) Special and general provisions set aside for financings extended by the participation banks from participation accounts in accordance to the provisions of this Regulation are reflected in accounts of expenses and accounts of participation according to the rates of participation in losses laid down by the relevant provision of the Regulation on the Procedures and Principles for Acceptance and Withdrawal of Deposits and Participation Funds, Custody and Receivables Undergoing Lapse of Time.

(2) Participation banks may reflect in their accounts of expenses the portion of provisions set aside which correspond to the participation accounts, without prejudice to the provisions of Turkish Commercial Code Nr. 6102 dated January 13, 2011 and provided that this is approved by their general assemblies.

(3) **(Abolished- OG-18/10/2018-30569)**

(4) Interest terms mentioned in this Regulation refer to a share of profit in respect of the funds provided by the participation banks stated in Article 48 (2) of the Law.

Guidelines

ARTICLE 20-(1) The Board is entitled to issue guidelines relating to the application of this Regulation.

Exceptions

ARTICLE 21-(1) Rates of specific and general provisions are deemed zero as for any loans allocated from the funds established pursuant to the relevant laws, decrees and communiqués in line with instructions of competent authorities and risks of which do not belong to intermediary banks, banks' sums of receivables to be monitored recognized under "Receivables from Public Agencies and Establishments" accounts, receivables transferred to another bank by way of liquidation according to the relevant articles of the abolished Decree Law Nr. 70, and abolished Banking Law Nr. 4389 and Nr. 3182 and for the transactions made in accordance with the abolished Banking Law transactions made upon the Law Nr. 3332 dated March 25, 1987.

Abolished Regulation

ARTICLE 22- (1) Regulation on the Procedures and Principles for Determination of Qualifications of Loans and Other Receivables by Banks and Provisions to be Set Aside published in Official Gazette dated November 1,2006 Nr. 26333 is abolished.

Banks that are not able to adapt to TFRS 9 as of 1/1/2018

PROVISIONAL ARTICLE 1- (Amended with the title: OG-14/12/2016-29918)⁷ (1) The Board may decide to extend to the adaptation of TFRS 9 implementation on the condition that

⁷ This amendment takes effect on 1/1/2017.

a bank applies to the Agency with the detailed justifications and based on the Board's assessment of the application.

Application regarding general provision

PROVISIONAL ARTICLE 2- (1) The general reserve ratios in the first paragraph of Article 10 are applied until 1/1/2018 as follows:

- a) At least one percent (1%) of the sum of standard qualified cash loans.
- b) At least two percent (2%) of the total cash loans in close monitoring.

Entry into Force (Amended-OG-14/12/2016-29918)⁸

ARTICLE 23 – (1) This Regulation enters into force as of January 1, 2018

Enforcement

ARTICLE 24 – (1) The provisions of this Regulation are enforced by the Chairman of the Banking Regulation and Supervision Agency.

⁸ This amendment takes effect on 1/1/2017.