

OFFICIAL INFORMATION OF THE CZECH NATIONAL BANK

of 20 December 2013

regarding the conduct of business activities by banks, credit unions and investment firms

Application of overall discretions by the supervisory authority

1. The Czech National Bank occupies the position of a competent authority pursuant to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (hereinafter the "Regulation")¹.
2. Pursuant to the Regulation the competent authority is given the power to determine in stipulated areas within its remit and in a generally binding manner from when and in which extent credit institutions² and investment firms³ shall fulfil obligations arising from the Regulation, or in which cases a waiver to fulfil these obligations applies (hereinafter "overall discretions").
3. The general approach of the Czech National Bank to overall discretions is laid down in the Annex to this official information.
4. The Czech National Bank expects banks, credit unions and investment firms pursuant to Art. 8a(1), (2) and (3) of the Act on Business Activities on the Capital Market (hereinafter the "liable entity") to fulfil the obligations stemming from its approach to discretions as of the stipulated date and to continue to do so, until a provision determining the scope of application of these discretions in a generally binding manner enters into force.
5. This official information is applicable as of 1 January 2014.

Vice-Governor:

Ing. Mojmír Hampl, MSc., Ph.D., duly signed

Annex

The scope of application of overall discretions by the Czech National Bank

¹ Art. 4(1)(40) of the Regulation.

² Art. 4(1)(1) of the Regulation.

³ Art. 4(1)(2) of the Regulation.

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The scope of application of overall discretions by the Czech National Bank

I. The liquidity ratio, including the reporting of liquidity on an individual basis. (regarding Art. 6(4) of the Regulation)

1. Part Six of the Regulation is applied to banks and credit unions only.

II. Prudential consolidation (regarding Art. 18(3) and (5) of the Regulation)

2. A person or undertaking connected pursuant to Art. 12(1) of Directive 83/349/EEC⁴ is included in prudential consolidation using the full method.
3. Institutions⁵, financial institutions⁶ and persons pursuant to Art. 18(8) of the Regulation which are associated entities, persons or undertakings other than those pursuant to Art. 18(1) to (4) of the Regulation are not included in prudential consolidation.

III. Valuation (regarding Art. 24(2) of the Regulation)

4. Assets and off-balance sheet items are valued and own funds are determined in accordance with international accounting standards stipulated by the European Union law⁷.

IV. Deductions from own funds (regarding Art. 36(1)(g), Art. 56(b), Art. 66(b) and Art. 478 of the Regulation)

5. The exposure amount of a liable entity in the form of direct, indirect or synthetic capital investments in instruments included in the own funds of a financial sector entity⁸ is deducted from the liable entity's Common Equity Tier 1 capital, Additional Tier 1 capital and Tier 2 capital, if the financial sector entity has made similar investments in instruments included in the Common Equity Tier 1 capital, Additional Tier 1 capital and Tier 2 capital of the liable entity.

⁴ The seventh Directive of the Council 83/349/EC of 13 June 1983, based on Art. 54(3)(g) of the Treaty, on consolidated accounts, as amended.

⁵ Art. 4(1)(3) of the Regulation.

⁶ Art. 4(1)(26) of the Regulation.

⁷ Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards, as amended.

⁸ Art. 4(1)(27) of the Regulation.

6. As of the year 2014 the following deductions apply in full (i.e. in the amount of 100%):
 - a) the items pursuant to Art. 36(1)(a) to (h), excluding deferred tax assets that are dependent on future profitability and arise from temporary differences, are deducted from Common Equity Tier 1 capital,
 - b) the total amount of deferred tax assets that are dependent on future profitability and arise from temporary differences and significant direct, indirect or synthetic capital investments, after taking account of the exemptions from deduction pursuant to Art. 48 of the Regulation, are deducted from Common Equity Tier 1 capital,
 - c) the items pursuant to Art. 56(b) to (d) of the Regulation are deducted from Additional Tier 1 capital,
 - d) the items pursuant to Art. 66(b) to (d) of the Regulation are deducted from Tier 2 capital.

V. Qualifying holdings outside the financial sector

(regarding Art. 89 of the Regulation)

7. Qualified holdings outside the financial sector pursuant to Art. 89(1) and (2) of the Regulation are subject to the approach pursuant to Art. 89(3)(b) of the Regulation.

VI. Financial information on a consolidated basis

(regarding Art. 99(3) and (6) of the Regulation)

8. Liable entities not covered by Art. 99(2) of the Regulation report financial information on a consolidated basis in accordance with the directly applicable piece of legislation of the European Union governing the reporting of financial information on a consolidated basis⁹.

VII. Exposures secured by immovable property

(regarding Art. 124(2) of the Regulation)

9. Exposures pursuant to Art. 125 and 126 of the Regulation secured by immovable property located in the Czech Republic are subject to a risk weight which is the higher of
 - a) the risk weight pursuant to Art. 125 and 126 of the Regulation, or
 - b) the risk weight determined by the Czech National Bank for the relevant period and published by the European Banking Authority pursuant to Art. 124(2) of the Regulation.

⁹ The implementing technical standard issued by the Commission pursuant to Art. 99(5) of the Regulation.

10. Exposures pursuant to Art. 125 and 126 of the Regulation secured by immovable property located in the Czech Republic are treated according to criteria which are the stricter of
- a) the criteria pursuant to Art. 125 and 126 of the Regulation, or
 - b) the criteria determined by the Czech National Bank for the relevant period and published by the European Banking Authority pursuant to Art. 124(2) of the Regulation.

VIII. Retail exposures secured by immovable property

(regarding Art. 164(5) of the Regulation)

11. Retail exposures secured by residential immovable property located in the Czech Republic and retail exposures secured by commercial immovable property located in the Czech Republic, as long as these exposures are not secured by a guarantee issued by a central government, are assigned an LGD value which is the higher of:
- a) the lower threshold LGD value pursuant to Art. 164(4) of the Regulation,
 - b) the lower threshold LGD value determined by the Czech National Bank for the relevant period and published by the European Banking Authority pursuant to Art. 164(5) of the Regulation.

IX. The materiality threshold of default

(regarding Art. 178(2)(d) of the Regulation)

12. A credit obligation pursuant to Art. 178(2)(d) of the Regulation is deemed material if it exceeds the amount which the liable entity does not collect when a receivable is written off, while this amount may not be higher than 100 EUR with regard to the retail exposure class and 1000 EUR with regard to other exposure classes. A single value of this threshold is determined for each exposure class and it is applied consistently over time.

X. Compensation of instruments

(regarding Art. 327(2) of the Regulation)

13. In case an instrument can be converted into its underlying instrument, the position in the underlying instrument determined by the delta equivalent can be offset with an opposite position in this underlying instrument.

XI. Exemption from large exposure limits

(regarding Art. 400 of the Regulation)

14. The range of exposures which are exempt from the scope of application of Art. 395(1) also includes:

- a) exposures in the form of covered bonds pursuant to Art. 129(1), (3) and (6) of the Regulation, capped at 75% of the exposure amount; this is without prejudice to point b) subpoints i. and ii.,
- b) exposures to:
 - i. an entity incorporated in the Czech Republic which is the parent undertaking of the liable entity and which is a bank or an investment firm pursuant to Art. 8a(1), (2) and (3) of the Act on Business Activities on the Capital Market,
 - ii. an entity which is a subsidiary of the liable entity and which is included in prudential consolidation by the liable entity,
 - iii. an entity which is an institution and which is subject together with the liable entity to the same supervision on a consolidated basis, in accordance with the Regulation, Directive 2002/87/EC or similar pieces of legislation valid in other than Member States, capped at 50% of the exposure amount; this is without prejudice to point b) subpoints i. and ii.,
- c) off-balance sheet letters of credit and undrawn credit commitments carrying medium risk pursuant to Annex I to the Regulation, capped at 50% of the exposure amount; this is without prejudice to point b) subpoints i. and ii.,
- d) exposures to recognised exchanges¹⁰.

XII. Capital ratios

(regarding Art. 465 of the Regulation)

15. In the year 2014 the Common Equity Tier 1 capital ratio shall be maintained at a level that does not fall below 4,5%.

16. In the year 2014 the Tier 1 capital ratio shall be maintained at a level that does not fall below 6%.

XIII. Valuation

(regarding Art. 466 of the Regulation)

17. A liable entity that is required to effect the valuation of assets and off-balance sheet items and the determination of own funds in accordance with International Accounting Standards as applicable under the law of the European Union for the first time from the date of application of the Regulation shall adjust its internal processes and requirements so that it will become compliant with these International Accounting Standards in no more than 2 years from the date of application of the Regulation.

¹⁰ Art. 4(1)(72) of the Regulation.

XIV. Unrealised loss

(regarding Art. 467 of the Regulation)

18. From the year 2014 the total unrealised loss related to assets and liabilities measured at fair value and reported on the balance sheet, excluding unrealised losses related to the items referred to in Art. 33 and unrealised losses reported as part of the profit and loss account, shall be fully deducted from Common Equity Tier 1 capital, i.e. in the amount of 100%.

XV. Unrealised gain

(regarding Art. 468 of the Regulation)

19. From the year 2015 the total unrealised gain related to assets and liabilities measured at fair value and reported on the balance sheet and the total gain related to investment properties reported as part of the profit and loss account can be fully included in Common Equity Tier 1 capital, i.e. in the amount of 100%.

XVI. Minority interests, qualifying Additional Tier 1 and Tier 2 capital

(regarding Art. 479 and 480 of the Regulation)

20. From the year 2014 the instruments and items which cannot qualify as minority interests pursuant to Part Two Title III of the Regulation shall not be included in consolidated Common Equity Tier 1 capital; the applicable percentage for the purposes of Art. 479(2) of the Regulation shall be 0%.

21. From the year 2014 the percentage for the purposes of Art. 84(1)(b), Art. 85(1)(b) and Art. 87(1)(b) of the Regulation shall be multiplied by a coefficient of 1.

XVII. Additional filters and deductions

(regarding Art. 481 of the Regulation)

22. From the year 2014 the applicable percentage for the purposes of Art. 481(1) and (2) of the Regulation shall be 0%.

XVIII. Items of own funds

(regarding Art. 486 of the Regulation)

23. The items which can be included in Common Equity Tier 1 capital pursuant to Art. 484(1) and (2) of the Regulation are treated pursuant to Art. 484(3) of the Regulation and pursuant to paragraph 26.

24. The items which can be included in Additional Tier 1 capital pursuant to Art. 484(1) and (2) of the Regulation are treated pursuant to Art. 484(4) of the Regulation and pursuant to paragraph 26.
25. The items which can be included in Tier 2 capital pursuant to Art. 484(1) and (2) of the Regulation are treated pursuant to Art. 484(5) of the Regulation and pursuant to paragraph 26.
26. The applicable percentage pursuant to Art. 486(5) of the Regulation is equal to:
 - a) 60% in the year 2014,
 - b) 40% in the year 2015,
 - c) 20% in the year 2016 and
 - d) 0% from the year 2017.

XIX. Equity exposures

(regarding Art. 495 of the Regulation)

27. From the year 2014 a liable entity which is eligible to use the Internal Ratings Based Approach may determine, while using this approach, capital requirements for its equity exposures or equity exposures of entities incorporated in Member States included in prudential consolidation according to the Standardised Approach pursuant to Part Three Title II Chapter 2 of the Regulation or, where applicable, pursuant to Part Three of the Regulation. A precondition for this treatment is that this equity exposure class is immaterial and its extent is no larger than that of the corresponding equity exposure class held by the liable entity as at 31 December 2007. The liable entity may increase this extent by adding those equity exposures, the acquisition of which arises directly as a result of owning these equity exposures, provided they do not increase the proportional share in the equity of the entity which issued them. If these acquired equity exposures increase the proportional share in the equity of the entity towards which the equity exposure arises, or if these are equity exposures which originally fell within the scope of this exception but they were later sold and then reacquired, the application of the provision in question is not permitted.
28. The equity exposure class of the liable entity is deemed material if its aggregate amount exceeds 10% of the liable entity's own funds. In case the number of these equity exposures is lower than 10 individual participations, this limit is equal to 5% of the liable entity's own funds. Equity exposures included in the legislative programmes referred to in Art. 150(1)(h) of the Regulation are excluded for the purposes of the summation of equity exposures in the equity exposure class.