

**OFFICIAL INFORMATION
OF THE CZECH NATIONAL BANK**
of 18 July 2007

regarding the prudential rules for banks, credit unions and investment firms

Netting as a Credit Risk Mitigation Technique

The Czech National Bank hereby provides the following information with regard to Annexes 8, 15, 16 and 32 to Decree No. 123/2007 Coll., stipulating the prudential rules for banks, credit unions and investment firms (hereinafter the "Decree"):

1. When calculating the capital requirement for credit risk in the investment portfolio, netting in the form of a bilateral master netting agreement covering repurchase transactions or securities or commodities lending or borrowing transactions pursuant to Annexes 15, 16 and 32, or margin lending transactions pursuant to Annexes 15 and 16 to the Decree, may be taken into account. If the netting covers derivatives, Annex 8 of the Decree is used.
2. Netting pursuant to Annexes 8, 15, 16 and 32 of the Decree is understood to mean netting within the meaning of Articles 580 and 581 of Act No. 40/1964 Coll., Civil Code, as amended, Articles 358 to 364 of Act No. 513/1991 Coll., Commercial Code, as amended, close-out netting pursuant to Article 197 of Act No. 256/2004 Coll., on business activities on the capital market, as amended, and equivalent legal institutes under the law of foreign countries.
3. For the purposes of the application of provisions on netting pursuant to Annex 8, III, 3, a), Annex 15, A, I, 1, f) and g) and Annex 32, B, I, c), 9 of the Decree the following procedure shall be used:
 - a) the liable entity shall notify the Czech National Bank (hereinafter the "CNB") in writing of its intention to reflect a netting agreement in its calculation of the capital requirement, stating the expected type and volume of transactions it intends to effect within the agreement in question; it shall also notify the CNB of the counterparty's legal name (company name), legal form and registered office in the case of legal persons, and the name, surname, official residence and place of business, if different from residence, in the case of natural persons, and further the identification number if assigned. They must also confirm in writing that the conditions laid down by the Decree are satisfied. The notification must be signed by a competent person;
 - b) if the netting agreement does not take the form of any of the specimen agreements of the International Swaps and Derivatives Association, Inc. (hereinafter "ISDA") or the Master Agreement for Financial Transactions – Czech Banking Association Standard No. 20/2006(hereinafter the "CBA Standard"), besides notifying the CNB pursuant to para a) above, the liable entity shall send a copy of such agreement and a legal analysis drawn up by a person who has provided legal services in this field for a long period. This analysis must clearly show that the agreement satisfies the conditions laid down by the Decree. The analysis is updated as necessary;
 - c) if the netting agreement takes the form of one of the ISDA specimen agreements, the liable entity shall state this fact in the notification pursuant to para a) above and shall

send a copy of the legal analysis to the CNB. A copy of the netting agreement is not sent to the CNB;

- d) if the netting agreement takes the form of the CBA Standard, the liable entity shall state this fact in the notification pursuant to para a) above, also providing a reference to the relevant legal analyses registered with the Czech Banking Association that formed the basis for assessing that the conditions laid down by the Decree were satisfied. A copy of neither the netting agreement nor the legal analysis is sent to the CNB;
- e) The CNB does not provide comment on the substance of the netting agreement; it may, however, reject the agreement, e.g. on the grounds that the legal analysis does not show clearly that all the conditions laid down by the Decree are satisfied or on the grounds that the CNB has justified doubts about the relevant experience of the person that drew up the legal analysis.

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