Content of question: **Capital instruments in the available-for-sale portfolio - their relationship to capital according to Decree No. 123/2007 Coll.** Answered by: **Jitka Svobodová** Approved by: **Pavel Vacek** Date: **11 June 2007**

Piece of law	**Decree No 123/2007 Coll.**
Explanation	Question: 1) Are the items of capital that relate to valuation differences (negative and positive) related to the overall valuation of the whole portfolio of capital instruments within the available-for-sale portfolio or the valuation of its individual instruments? Is it possible to include in capital the resulting amount arising from the revaluation of the whole portfolio (either positive or negative), or is the situation such that all the negative revaluations are included in Tier 1 and all the positive revaluations of those capital instruments for which there is an active market are included in Tier 2? Or is it possible that only the revaluation amount of those instruments which are simultaneously deducted within the capital investments category is included in capital? Answer: Valuation differences arising from changes in the fair values of capital instruments assigned to the available-for-sale portfolio for accounting purposes are assessed on the portfolio basis in determining capital; the compensation of negative and positive valuation differences arising from these instruments is not disallowed for the purpose of determining capital. The resulting valuation difference arising from the capital instruments assigned to the available-for-sale portfolio, if negative, is an item that reduces Tier 1. If this difference is positive, the part of this difference which is attributable to capital instruments traded on the active market (active in terms of IFRS) may be included in Tier 2. Question: 2) In case a positive market revaluation is included in Tier 2 (supplementary additional capital) in a significant amount, the possibility of receiving subordinated debt is reduced by this amount, because the limit in terms of 50% of Tier 1 applies to supplementary additional capital and not to the items constituting core additional capital. As Directive 2006/48/EC includes this item (a positive revaluation), as well as a negative revaluation, in Tier 1, does this not create a disadvantage? Answer: The issue of including valuation differences arising from financial

	instruments assigned to available-for-sale portfolio is dealt with by the Committee of European Banking Supervisors within its recommendations to the so-called prudential filters published on 21 December 2004. According to the information which is at the disposal of the Czech National Bank Member States have implemented these prudential filters to a large degree, particularly in the area of the available-for-sale portfolio. Therefore, our opinion is that this provision should not be regarded as creating a disadvantage. Question: 3) Positive valuation differences arising from capital instruments assigned to the available-for-sale portfolio for which there is not an active market are not included in capital in accordance with the Decree stipulating the prudential rules. Should the amount of this positive difference which is not included in capital appear elsewhere? Answer: If the resulting valuation difference for capital instruments assigned to the available-for-sale portfolio is positive, the part which is not assigned to capital instruments traded on an active market is not considered in determining capital in keeping with Decree No. 123/2007 Coll. Question: 4) Should a capital participation in an amount of more than 10% which is not to be consolidated and should thus be deducted from capital and for which there is not an active market be deducted from capital in an amount corresponding to the purchase price, i.e. without considering its positive market revaluation? An assumption is that this market revaluation is obtained as a result of expert judgement. Or, alternatively, should the item "capital investments" be stated in capital in its market value, i.e. the book value? Answer: If a capital investment is deducted it is deducted in its book value. A capital instrument assigned to the available-for-sale portfolio which is recognised at its fair value is deducted at its fair value. The strategy for assigning instruments to the individual portfolios for accounting purposes is determined by the accounting unit. In determining capital in accordance with the Decree No. 123/2007, the impact of profits from the revaluation of capital instruments for which there is not an active market may occur in case these instruments are assigned to the portfolio of instruments designated as at fair value through profit or loss, e.g. in profit brought forward or after-tax profit.