FINANCIAL MARKET SUPERVISION REPORT

2006

CZECH NATIONAL BANK

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On 1 April 2006, financial market supervision was integrated into the CNB. In this connection, a new legal obligation was imposed on the Czech National Bank to compile a Financial Market Supervision Report each year and submit it for information to the Chamber of Deputies, the Senate and the Government by 30 June of the following year.

Starting from 2007 this publication replaces the documents on regulation and supervision of the individual segments of the financial market previously issued by the Czech National Bank (*Banking Supervision*), the Czech Securities Commission (*Czech Capital Market Report*), the Finance Ministry's Office of the State Supervision in Insurance and Pension Funds (*Insurance Market Supervision and Development Report,* or *Annual Report*) and the Office for Supervision of Credit Unions (*Report on the Activities and Performance of the Office for Supervision of Credit Unions*). Besides fulfilling the legal obligation, this report is also intended to inform the public about financial market supervisory activities and financial market developments in the previous year.

The report is divided into two parts. Part A deals with financial market supervision in 2006, changes in legislation affecting the financial market, the introduction of new methods to enhance the stability and transparency of the financial market, and international cooperation in the supervisory area. Part B describes developments in the individual segments of the financial market (the banking sector, the credit unions sector, the capital market and the insurance sector) in 2006. Each part contains a brief summary of the principal conclusions.

In accordance with the Act on the Czech National Bank, the draft report was submitted to the Financial Market Committee, which exercised its right to append its opinion to the report. The report was discussed and approved by the CNB Bank Board on 14 June 2007.

FINANCIAL MARKET COMMITTEE

The Financial Market Committee (the Committee) was established on the basis of Act No. 57/2006 Coll., under which financial market supervision in the Czech Republic was integrated into the Czech National Bank,[1] as an advisory body for financial market supervision. The Committee debates matters of a conceptual nature relating to financial market regulation and supervision and also discusses significant financial sector trends having a regulatory aspect. Owing to its composition (with "market and state" representation), the Committee is an independent forum, providing the Czech National Bank with opinions or feedback on matters associated with its function as the authority supervising the entire domestic financial market. The staffing and remit of the Committee also allows it (in compliance with the law) to act in an advisory capacity in relation to the legislative powers of the Ministry of Finance in the financial market area. The Committee does not deal with matters concerning specific financial market entities.

The Committee members are:
- Jiří Rusnok, Chairman, Radek Urban, Vice-Chairman (both elected by the Budget Committee of the Chamber of Deputies on 6 June 2006) and Václav Tomek (elected by the Budget Committee of the Chamber of Deputies on 21 February 2007),
- Otakar Schlossberger, Financial Arbiter of the Czech Republic,
- Milan Šimáček, Deputy Finance Minister (who replaced his predecessor Tomáš Prouza after the second meeting of the Committee) and Klára Cetlová, Executive Director of the Financial Market Legislation Department at the Ministry of Finance,
- Miroslav Singer, Vice-Governor of the Czech National Bank (who replaced the then CNB Bank Board member Michaela Erbenová after the third meeting of the Committee).

The members of the Committee perform their duties in person and without remuneration.

Although the Committee is legally entitled – in its domain of competence – to submit opinions and recommendations to the Bank Board or the Ministry of Finance in a formal manner (i.e. in separate documents), it has not done so yet. Instead, detailed minutes of the meeting are prepared after each Committee meeting, containing a written record of the discussion, the opinions of the individual members and the conclusions approved by the Committee. After being approved by all Committee members, these minutes are passed on to the CNB Bank Board for information. To make the Committee's activities transparent, a record is also made of the main items on the agenda and the conclusions of the debate. After approval, this record is published on the CNB website (in Czech only: http://www.cnb.cz – *Dohled nad finančním trhem – Výbor pro finanční trh*). In the interests of enhancing its transparency and accountability to the public, the Committee decided at its most recent meeting also to post the agenda of its next meeting in advance on the website.

As the minutes of the Committee's meetings reveal, the Committee not only discusses and takes note of documents, but sometimes, if it considers it desirable, provides the Czech National Bank or the Ministry of Finance, or both, with recommendations or suggestions to carry out particular activities lying in their fields of competence. In addition to its advisory function, the Committee also has a control function. Twice a year, the CNB provides the Committee with a report on its main financial market supervisory activities in the previous period. The Ministry of Finance has also submitted a report on its recent and ongoing legislative activities and the Financial Arbiter has provided a report on his activities since his office was established. In addition, the Committee has a statutory duty to discuss the CNB's draft annual Financial Market Supervision Report before it is approved by the CNB Bank Board and submitted to the Chamber of Deputies, the Senate and the Government for information. The Committee is entitled to append its opinion to the report and has exercised this right below.

By law, the Committee should meet at least twice a year. However, it has already met five times during its less-than-one-year life (i.e. since the chairman and vice-chairman were elected) – on 27 June 2006, 26 September 2006, 28 November 2006, 20 March 2007 and (an extraordinary meeting) 26 April 2007. The first meeting was a founding and introductory meeting at which the Committee adopted its rules of procedure. The following ones were purely working meetings. Between its meetings, the Committee deals with less fundamental matters without face-to-face contacts, by electronic communication.

Besides the above reports on the activities of the Czech National Bank, the Ministry of Finance and the Financial Arbiter in the previous periods, the most important issue on the Committee's agenda was probably the future institutional arrangements for consumer protection on the domestic financial market. The Committee is dealing with this issue on

1 The position of the Financial Market Committee is governed by Articles 45a–45d of Act No. 6/1994 Coll., on the Czech National Bank, as amended by Act No. 57/2006 Coll.

an ongoing basis and in March this year invited the Ministry of Finance and the CNB, working in cooperation with professional associations of market participants and, where appropriate, with other central or local government organisations, to prepare a blueprint for the institutional arrangements for supervision (inspection) of consumer protection on the financial market and out-of-court settlement of disputes between client and financial institution.

The Committee also examined the future statutory objectives of the supervision work performed by the Czech National Bank. In this regard, it expressed its support for the Finance Ministry's plan to prepare, in the medium term, a new financial market supervision act to regulate competences and procedural aspects of financial market supervision as integrated in the central bank. In addition to incorporation of the objectives of supervision into the legislation, the Committee recommended that the Czech National Bank should initiate a debate about the national doctrine (vision) for financial market supervision, regulation and development. The defining of such a doctrine could help make the domestic financial market more attractive to both institutional and small investors.

The meetings also dealt with issues associated with the ongoing transposition of the European Markets in Financial Instruments Directive (MiFID) and the preparation of the new Insurance Act. The most debated issue in this respect was the future approach to the regulation of intermediaries of financial institutions' products, particularly insurance and investment intermediaries, about 57,000 of which currently operate on the Czech market. These intermediaries are not particularly important as regards financial system stability, but do make up quite a large proportion of financial institutions' distribution networks and are therefore risk bearers vis-à-vis clients. They also play a social role in terms of the financial security of the population, and they affect the level of financial literacy. The Committee would like to see greater application of self-regulatory mechanisms to the intermediaries segment directly by financial institutions and professional associations, and less interference from CNB supervision.

At its most recent meeting, the Committee discussed the potential impacts of the tax reform proposed by the Ministry of Finance on certain segments of the financial sector.

In its first year of life, the Financial Market Committee has already become a useful platform for discussing conceptual issues of Czech financial market regulation and development. Despite its statutory status and the varied interests of its members, it operates on a relatively informal but cooperative basis.

Opinion of the Financial Market Committee on the CNB's Financial Market Supervision Report for 2006

The Czech National Bank discussed the draft plan and schedule for the preparation of the Financial Market Supervision Report with the Committee back in the initial phase of its preparation. As agreed, the Committee members were supplied with the draft of Part A and subsequently the draft of Part B for comments. The members' comments, which related mostly to matters of style and formulation, were taken into account by the CNB. Comments directed at removing minor duplications found in the draft report and notes pointing out some inconsistencies in the description of the results of the individual sectors were also incorporated. The authors promised to take a few more conceptual suggestions into account in the report for 2007.

Having acquainted itself with last year's results and other data for the individual sectors of the financial market, the Committee affirms that the report indicates that compared to the other market segments, which are doing relatively well, the insurance sector is displaying worse dynamics as regards the insurance penetration criterion (i.e. the ratio of premiums written to GDP). In the Committee's opinion, this situation in the life insurance area is largely due to the relatively generous system of public health and pension insurance, which is not providing sufficient incentives for a large part of the population to seek market means of financial security for the event of loss of work productivity.

It can thus be said that the Financial Market Committee, being aware that the final version of the Financial Market Supervision Report for 2006 must also be approved by the CNB Bank Board, acknowledges this draft report and does not have any reservations about its content.

Prague, 7 June 2007
On behalf of the Financial Market Committee:

Jiří Rusnok
Chairman

A. FINANCIAL MARKET SUPERVISION IN 2006

SUMMARY

The most important event in financial market supervision in 2006 was the institutional integration of the financial market supervisory authorities into the Czech National Bank (CNB). As from 1 April 2006, the CNB is responsible not only for banking and foreign exchange supervision, but also for supervision of the financial market sectors that were previously the responsibility of the Securities Commission, the Ministry of Finance and the Office for Supervision of Credit Unions. The integration of supervision into the CNB has paved the way for better use of synergies in the supervision of individual financial market segments, greater harmonisation of regulatory rules and supervisory procedures, and lower supervision costs.

At the end of 2006, the CNB supervised a total of 24 banks and building societies, 20 credit unions, 33 insurance companies, 13 investment companies, 11 pension funds, 9 depositories, 77 open-end mutual funds, 33 non-bank investment firms and almost 3,000 non-bank foreign exchange licence holders. To a limited extent, the CNB also supervised 28 foreign branches of banks and insurance companies from EU/EEA countries and 1 new branch of an insurance company from outside the EU/EEA. Regulated markets (the Prague Stock Exchange and RM-Systém) are also subject to CNB supervision. In addition, the CNB approves documents relating to new issues of securities (bond issuance conditions, securities prospectuses), grants consents to takeover bid announcements and squeeze-outs, issues brokers' licences and keeps a register of investment and insurance intermediaries.

Except for the aforementioned integration of financial market supervision into the CNB under Act No. 57/2006 Coll., the changes made to the financial market legislation in 2006 were not fundamental in nature and mostly related to the transposition of European directives (e.g. amendments to the Payment System Act, the Capital Market Undertakings Act and the Act on Bonds). One major change was an amendment to the Collective Investment Act, which introduced new regulation of special funds (real estate funds and funds of qualified investors). More fundamental legislative changes are expected in 2007 in connection with the implementation of the new Basel II capital framework into Czech law, the transposition of the Markets in Financial Instruments Directive (MiFID), and the issuing of a new insurance act and a new anti-money laundering and terrorist financing act.

As in previous years, the exercise of supervision in 2006 was based on a combination of ongoing off-site surveillance of regulated entities and comprehensive or partial on-site inspections. Based on all available information, off-site surveillance helps the CNB to create a comprehensive picture of the financial condition of supervised entities and allows it to identify potential problems and risks, which provide an initial signal for the conducting of on-site inspections. During on-site inspections, the methods used by supervised entities to identify, measure and manage the risks they face are assessed, and the effectiveness of their internal control systems is verified. An important area addressed during on-site inspections in 2006 was the validation of advanced approaches to the calculation of capital requirements planned under the new Basel II framework.

The Czech Republic's accession to the EU in 2004 has led to a widening of the activities of CNB staff in the committees and working groups of the European Commission and the ECB. Following the integration of financial market supervision into the CNB, the supervisory departments together formulate and communicate to international institutions their collective opinions on common issues. Exchange of information and cooperation with foreign partner supervisors was another important aspect of supervisory work in 2006.

1. INTEGRATION OF FINANCIAL MARKET SUPERVISION

In February 2006, the Czech Parliament passed a financial market supervision integration act (Act No. 57/2006 Coll., on the Amendment of Acts in Connection with the Integration of Financial Market Supervision). On 1 April 2006, under this Act, the CNB took over all the activities of the Czech Securities Commission (CSC), the Finance Ministry's Office of the State Supervision in Insurance and Pension Funds (ÚDPP) and the Office for Supervision of Credit Unions (ÚDDZ), which all ceased to exist as of that date.

In the process of integration of all supervisory activities into the CNB, emphasis was laid on ensuring the continuity of all supervisory functions. Information systems remained fully operational, and staff and property were absorbed successfully. The integration of supervision in 2006 ran smoothly and had no negative effects on the exercise of supervision or the operation of the financial sector. Two new departments were added to the CNB's organisational structure. The Insurance Companies Regulation and Supervision Department is now responsible for the supervision performed up to the end of March 2006 by the ÚDPP, except for the area of pension funds. Pension fund supervision was transferred to the Capital Market Regulation and Supervision Department, which took over the activities of the CSC. Supervision of credit unions was incorporated into the CNB's existing Banking Regulation and Supervision Department.[2]

Under the financial market supervision integration act, a Financial Market Committee was established as an advisory body to the CNB Bank Board for financial market supervision. The Committee has seven members. Its chairman and vice-chairman and one other member are elected by the Budget Committee of the Chamber of Deputies (the lower house of the Czech Parliament) at the proposal of professional organisations or interest groups of financial market participants. The other Committee members are the Financial Arbiter, one CNB Bank Board member and two officials from the Ministry of Finance. The Committee monitors and discusses general frameworks, strategies and approaches to financial market supervision, significant new trends in the financial market and systemic national and international issues regarding the financial market and its supervision. Minutes of the Committee's meetings are published regularly on the CNB website.

The integration of all supervisory authorities into the CNB has paved the way for better use of synergies in the supervision of the individual financial market segments, greater harmonisation of regulatory rules and supervisory procedures, and lower supervision costs. Work started on unifying the reporting system, and joint on-site inspections were commenced. To realise further synergies and savings, however, optimal internal processes need to be set up to enable supervisors to communicate effectively and work efficiently. For this reason, the CNB has already opened discussions on the future organisational arrangements. The existing financial market legislation will also have to be revised in order to harmonise the rules for financial institutions' business. The decree on prudential rules for banks, credit unions and investment firms issued in connection with the Basel II implementation serves as an example.

2 The organisational chart of CNB Financial Market Supervision as of 31 December 2006 is given in Annex 2.

2. LEGISLATIVE CHANGES IN THE FINANCIAL MARKET SUPERVISION AREA IN 2006

Some acts were adopted in 2006 amending and regulating the business activities of financial institutions and other entities subject to regulation and supervision.

2.1 CHANGES TO LAWS

Responsibility for preparing primary legislation in the financial market area lies mainly with the Ministry of Finance. The CNB assists in this process.

Act on the Czech National Bank (No. 6/1993 Coll.)
The most significant change to this act is the transfer of responsibility for financial market supervision to the CNB as from 1 April 2006. The CNB supervises banks and foreign bank branches (from non-EEA countries) and sees to the sound operation of the financial system. Compared to the previous situation, the CNB's remit has been extended to include supervision of credit unions, electronic money institutions and branches of foreign electronic money institutions and other electronic money issuers, investment firms, securities issuers, the central depository, other entities maintaining a register of investment instruments, investment companies, investment funds, settlement system operators, organisers of investment instrument markets and other persons specified in special legal rules governing capital market undertakings, as well as insurance and reinsurance companies, pension funds and other entities active in the insurance and private pension industries under special legal rules. The CNB is thus the sole home supervisory authority for the Czech financial market. Besides financial market supervision, the CNB is responsible for foreign exchange regulation and supervision of non-bank foreign exchange entities and for supervision of payment systems.

Act on Banks (No. 21/1992 Coll.)
Licensing of banks or branches of banks (from countries outside the European Economic Area) and some matters connected with mergers, transfers of assets to partners and dissolutions of banks now fall fully within the responsibilities and powers of the CNB. Banks and foreign bank branches have new obligations connected with combating money laundering, maintaining international peace and security, protecting fundamental human rights and combating terrorism. In practice, these measures mean that banks are obliged to prudentially monitor the financial operations of their clients, to assess information obtained and, where necessary, to communicate that information to competent authorities in the Czech Republic and abroad.

Act on Credit Unions (No. 87/1995 Coll.)
Credit unions are now treated as banks in many respects, including as regards supervision by the CNB. The above laws therefore amend the conditions and tighten the requirements for the establishment, licensing, organisation and management of credit unions (including the competence requirements for senior officers) and the acquisition of qualifying holdings in such legal entities. Emphasis is also laid on ensuring that credit unions have adequate capitalisation and structures and on compliance with the liquidity and prudential rules. Full integration into the domestic payment system has also given rise to new obligations. With regard to combating money laundering, maintaining international peace and security, protecting fundamental human rights and combating terrorism, credit unions have to apply similar rules as banks and foreign bank branches.

Payment System Act (No. 124/2002 Coll.)
Following the finalisation of the transposition of Directive 2000/46/EC on the taking up, pursuit and prudential supervision of the business of electronic money institutions, changes were made to the rules governing the conditions for the issuing and use of electronic payment instruments. In particular, the act defines the set of entities authorised to issue electronic money, i.e. a monetary claim (deposit) on the issuer which is stored on an electronic money instrument and which can be used as a means of payment with persons other than the issuer. A completely new aspect is the introduction of another category of issuers – "electronic money institutions". This category consists of joint-stock companies or European companies which have their registered offices in the Czech Republic and which issue electronic money under a licence granted by the CNB, and foreign electronic money institutions which operate in the Czech Republic under the single licence pursuant to the Payment System Act. Besides issuing electronic money, electronic money institutions may only carry on related activities. They must not provide loans in any form.

Insolvency Act (No. 182/2006 Coll.)
The Insolvency Act is a completely new legal rule which will replace the existing inadequate Act on Bankruptcy and Composition. The Insolvency Act introduces a new bankruptcy framework and new bankruptcy resolution methods. In relation to the financial sector it contains special provisions on the bankruptcy of financial institutions, particularly banks, insurance companies, etc. The above provisions have been transposed from Directive 2001/24/EC on the reorganisation and winding up of credit institutions and Directive 2001/17/EC on the reorganisation and winding-up of insurance undertakings. The change consists in the fact that bankruptcy can be declared on a financial institution only after it has had its licence or permit revoked. Responsibility for resolving the financial difficulties of such legal entities lies with the supervisory authority until their licences or permits have been revoked. The CNB now also has the power to file a bankruptcy petition against a legal entity whose licence it has revoked, without being a creditor of that entity.

Capital Market Undertakings Act (No. 256/2004 Coll.)
The Capital Market Undertakings Act was amended six times during 2006. Act No. 56/2006 Coll. (known as the "technical amendment") incorporated the directive on prospectuses, completed the transposition of the directive concerning distance marketing of consumer financial services and made some changes relating to the central depository of securities. This Act also transposed the issue of distance securities contracts into the Civil Code (amendment of Act No. 591/1992 Coll., on Securities). The other changes arising from Act No. 159/2006 Coll., were limited in nature and linked directly with amendments of acts on conflicts of interests.

Collective Investment Act (No. 189/2004 Coll.)
The Collective Investment Act was amended three times in 2006. Some of the changes were connected with the integration of supervision into the CNB and with the Act on International Sanctions. Act No. 224/2006 Coll., which introduced new regulation of special funds, was a major change. It focused on defining funds intended for the public (among them substantially amended real estate funds) and funds intended for a limited group of entities (funds for qualified investors).

Act on Bonds (No. 190/2004 Coll.)
Act No. 56/2006 Coll. amended the Act on Bonds in connection with the transposition of the Prospectus Directive. The amendment was aimed, among other things, at eliminating duplications in the approval of bond issuance conditions and prospectuses. A further amendment was related to the integration of financial market supervision.

Act on International Sanctions (No. 69/2006 Coll.)
As from 1 April 2006, the CNB's supervisory responsibilities were extended to include supervision of compliance with Act No. 69/2006 Coll., on International Sanctions, and supervision of compliance with the directly applicable EC regulations implementing the common position or common action adopted pursuant to the provisions of the Treaty on European Union relating to the common foreign and security policy. The CNB checks compliance with the duties under this Act under its supervisory powers. If any shortcomings are detected, in particular a breach of duties under this Act, the CNB forwards documents for sanction proceedings to the Ministry of Industry and Trade in matters falling within its competence and to the Ministry of Finance in other matters, and continues to cooperate with these ministries in the proceedings.

2.2 DECREES AND PROVISIONS

Decree No. 90/2006 Coll., stipulating the essential elements of applications and notifications and the minimum amount of funds to be provided by a foreign bank to its branch. This Decree took effect on 1 April 2006 and replaced Decree No. 166/2002 Coll. The Decree contains the set of information normally required in order to ascertain whether capital is of transparent and unexceptionable origin, to identify a bank's shareholders and their competence to exercise shareholder rights, to assess the competence of proposed senior officers and to evaluate whether a bank's planned activities are realistic, etc. The scope of the information requirements is comparable with the requirements applied in advanced financial markets. The Decree reflects in particular changes in the relevant acts and past practical experience. It proposes a simpler procedure for submitting applications for banking licences and other consents under the Act on Banks. A new element is the specification of the minimum amount of funds to be provided by a foreign bank to its branch.

Decree No. 272/2006 Coll., stipulating the list of documents and the essential elements thereof for proving the competence and trustworthiness of persons elected to or nominated for some positions in savings and loans associations (credit unions) and for proving the competence of natural persons or legal entities having a qualifying holding in savings and loans associations and members having some other membership contribution to exercise membership rights. This Decree took effect on 7 June 2006 and implements the requirements laid down in the Act on Credit Unions. The Decree contains the normally required list of documents which banks and other entities are obliged to submit for the assessment of the competence and trustworthiness of senior officers of these entities and in the case of acquiring a qualifying holding in these companies. By issuing the Decree, the CNB is fulfilling its objective to harmonise as far as possible the regulation of identical areas across the relevant sectors, i.e. banks, credit unions, capital market entities etc., including alignment of the requirements applying to supervised entities.

Decree No. 347/2006 Coll., implementing certain provisions of the Act on Financial Conglomerates. . This Decree took effect on 30 September 2006 and regulates in more detail the methods for calculating the supplementary capital adequacy requirements for financial conglomerates, including the technical principles of the calculation, and the supplementary requirements for risk concentrations and intra-group transactions. It also specifies documents for assessing the trustworthiness and experience of senior officers of a financial holding entity (similar regulation as in Decree No. 14/2006 Coll., regulating the supporting documents proving the trustworthiness and experience of senior officers of a financial holding entity) and lays down the structure and time limits for supplying information for the purposes of supplementary supervision of a financial conglomerate. Additionally, it regulates the structure and manner of disclosure of information on the whole conglomerate which regulated entities within the conglomerate are required to publish on their websites.

In 2006, two decrees were issued to implement the Payment System Act:

Decree No. 91/2006 Coll., implementing the Payment System Act. This Decree stipulates the essential elements of an electronic money institution licence application and regulates related issues, e.g. the essential elements of an application for the CNB's consent to acquire or increase a qualifying holding in an electronic money institution.

Decree No. 92/2006 Coll., stipulating the essential elements of an application for a permit to issue electronic money. Under Article 18a of the Payment System Act, electronic money may be issued by entities other than banks, electronic money institutions and other listed entities, based on a permit from the CNB. These other entities mostly issue electronic money with some restrictions (see Article 19 of the Payment System Act) in addition to their core business.

To implement the Capital Market Undertakings Act, the Czech Securities Commission and (after 1 April 2006) the CNB issued the following decrees in 2006:

Decree No. 58/2006 Coll., on the method of keeping a separate register of investment instruments and a register linked to a separate register of investment instruments, which regulates in more detail the method of keeping a separate register of investment instruments and a register linked to a separate register of investment instruments pursuant to Article 93(4) of the Capital Market Undertakings Act.

Decree No. 105/2006 Coll., amending Decree No. 262/2004 Coll., on the rules for calculation of the capital adequacy of an investment firm that is not a bank on an individual basis, which completed the transposition of European laws regarding the capital requirements of investment services providers on a consolidated basis, based on an authorisation to issue a decree as stipulated in an amendment to Act No. 56/2006 Coll., on Capital Market Undertakings. However, the new capital framework (Basel II) will require further substantial changes to this regulation.

Decree No. 114/2006 Coll., on the fair presentation of investment recommendations, which transposed into the Czech legislation the relevant European directives, namely Directive 2003/125/EC implementing Directive 2003/6/EC on market abuse, in respect of the fair presentation of investment recommendations and disclosure of interests and conflicts of interests.

Decree No. 605/2006 Coll., on certain disclosure duties of an investment firm, which amends in particular the manner of reporting following the integration of financial market supervision.

The following decrees were adopted to implement the Collective Investment Act and in connection with an amendment thereto of May 2006 and with changes in regulatory reporting under the integrated supervision of the CNB:

Decree No. 431/2006 Coll., amending Decree No. 270/2004 Coll., on the manner of setting the fair value of assets and liabilities of collective investment funds and on the manner of setting the present value of shares/units of collective investment funds.

Decree No. 482/2006 Coll., on the minimum requisites of the statute and the statutory requisites of the simplified statute of a collective investment fund.

Decree No. 603/2006 Coll., on disclosure duties of collective investment fund and investment company.

Decree No. 604/2006 Coll., on the use of techniques and instruments for effective management of the assets of a standard fund and of a special fund which collects money from the public.

In the insurance area, the following decrees were issued in 2006:

Decree No. 96/2006 Coll., amending Decree No. 303/2004 Coll., implementing certain provisions of the Insurance Act, took effect on 1 April 2006. Provisions regarding the limits on the structure of financial placements were revised (mainly changes in formulation). In response to changes in the "life" and "non-life" directives ensuing from Directive 2002/87/EC on financial conglomerates, an amendment was also made to the calculation of the adjusted solvency margin as calculated by insurance companies having a participating interest in at least one insurance company, reinsurance company, bank, credit union, electronic money institution or investment firm. The calculation also newly includes the interests of a holding insurance company in financial institutions other than insurance or reinsurance companies.

Decree No. 458/2006 Coll., implementing certain provisions of the Insurance Act, which took effect on 1 October 2006, was a technical amendment of Decree No. 303/2004 Coll.

Decree No. 40/2006 Coll., implementing certain provisions of the Act on Insurance Intermediaries and Independent Loss Adjusters, amends Decree No. 582/2004 Coll. The amendment contains minor changes regarding competence examinations. New entities were entered in the list of training institutions (Annex 6 to the Decree).

Provisions published in the CNB Bulletin

- Provision No. 1 of 13 January 2006, amending Provision No. 1 of 17 May 2005, stipulating the manner of transmitting and accepting automated statement data submitted by banks and foreign bank branches to the CNB.
- Provision No. 2 of 18 April 2006, amending Provision No. 2 of 23 September 2003, stipulating the minimum liquidity level and the terms and conditions for creating minimum reserves, as amended by Provision No. 3 of 13 February 2004 and Provision No. 4 of 26 April 2004.
- Provision No. 3 of 25 May 2006, on the internal control system of an electronic money institution.
- Provision No. 4 of 25 May 2006, laying down requirements on capital of an electronic money institution.
- Provision No. 5 of 25 May 2006, laying down the mandatory investment assets of an electronic money institution and the conditions of investment in these assets.
- Provision No. 6 of 29 June 2006, stipulating the rules for capital adequacy, exposure and the internal control system of savings and loan associations.
- CNB Provision No. 7 of 5 December 2006, stipulating the submitting of statements by banks and foreign bank branches to the CNB.

2.3 OFFICIAL INFORMATION

Official information published in the CNB Bulletin

- Official information of 16 February 2006 regarding the opening of an informal dialogue with rating agencies in connection with the preparations for the implementation of the new regulatory framework – Basel II.
- Official information of 21 August 2006 regarding certain issues of Article 1(6)(b) and Article 8(2)(e) of the Act on Credit Unions.
- Official information of 2 November 2006 regarding CNB Provision No. 2/2003 of the CNB Bulletin, stipulating the minimum liquidity level and the terms and conditions for creating minimum reserves, as amended by CNB Provision No. 3/2004 of the CNB Bulletin, as amended by Provision No. 4 of the CNB Bulletin, and CNB Provision No. 2/2006 of the CNB Bulletin.
- Official information of 26 June 2006 regarding the submitting of documents on the activities of branches of insurance companies from other EU or EEA countries and other documents on the activities of domestic insurance companies and branches of insurance companies from third countries.
- Official information of 18 September 2006 regarding the manner of ensuring compliance with the legal obligation laid down in Article 23(3) of Act No. 363/1999 Coll., on Insurance, as amended.
- Official information of 16 October 2006 regarding the issue of the rules for examination of insurance agents and insurance brokers.
- Official information of 14 August 2006 regarding the completion of a special course on the identification of suspected counterfeited or altered banknotes and coins.

Official information documents are explanatory opinions or recommendations of the CNB; they do not constitute legal rules.

2.4 CHANGES TO THE REGULATIONS UNDER PREPARATION[3]

Preparation of a new act on certain measures against money laundering and terrorist financing

In connection with the transposition of Directive 2005/60/EC of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and financing terrorism, a new act on the prevention of money laundering and financing terrorism is currently under preparation. This will replace the existing Act No. 61/1996 Coll. The new act is expected to take effect on 15 December 2007. The new act is meant to increase the effectiveness of measures in the area of money laundering prevention and combating terrorist financing, and will represent a further step towards aligning the Czech legislation with FATF[4] recommendations. The new act amending the anti-money laundering act also contains substantial changes to the Foreign Exchange Act and the Payment System Act.

The CNB is actively assisting the Ministry of Finance in preparing the new act and is preparing a related implementing regulation.

Preparation of a new Insurance Act

In accordance with the agreement of 2 May 2006 on cooperation in the preparation of national legislation concerning the financial market and other regulations concerning the fields of competence of the Ministry of Finance and the CNB, the Ministry of Finance presented a working draft of a new Insurance Act at the end of 2006. This Act will implement Directive 2005/68/EC on reinsurance. In preparing the draft, the CNB is working with the Ministry of Finance and representatives of the Czech Insurance Association. Following the creation of the new act, the CNB will in 2007 start preparing regulations implementing this act under the authorising provisions of the act (e.g. on the calculation of available and required solvency margins, the investment of assets arising from technical provisions, finite reinsurance, etc.).

3 Changes in the regulations relating to Basel II, Solvency II and the MiFID are dealt with separately in section 3. *New approaches to the enhancement of financial market stability and transparency*.

4 The Financial Action Task Force, an intergovernmental organisation, is the main world authority in the area of combating money laundering and terrorist financing.

Preparation of changes in private pension legislation
At the end of 2006, a working group was established consisting of representatives of the CNB, the Ministry of Finance, the Pension Fund Association and the Ministry of Labour and Social Affairs. The changes in legislation should above all help to increase the transparency of pension funds' performance, contribute to their sound internal operation, standardise the conditions for the payment phase and ensure adequate supervision of the system.

In 2006, legislative work also started on other decrees or amendments thereto which should be completed in 2007:

- a draft decree on the details of compliance with the duties of a depository of a collective investment fund, including changes ensuing from an amendment to the Collective Investment Act (rules for "other custody of assets") and also providing for simplified inspection of funds' less important transactions;
- an amendment to the decree on protection against market abuse (minor changes, chiefly relating to changes in the terminology used in the act);
- a draft decree on broker examinations; the change consists in clarifying and relaxing the requirements in the case of taking instructions within distribution networks, which will reduce the administrative workload;
- a draft decree on the disclosure duties of pension funds for supervisory purposes, stipulating the content, form, manner and dates of submission of information by pension funds.
- a decree repealing Decree No. 121/1998 Coll., stipulating the specimen identity card for state supervision of the capital market (following the integration of supervision this decree is no longer required);
- an amendment to Decree No. 582/2004 Coll., implementing certain provisions of the Act on Insurance Intermediaries and Independent Loss Adjusters. This amendment is needed in order to revise the list of institutions given in Annex 6 to the Decree and to implement changes aimed at removing minor shortcomings found during practical application of the Decree (in particular elimination of the administrative workload in communications between registered intermediaries and the CNB).

A full and updated list of the CNB's decrees, provisions and official information relating to the financial market can be found on the CNB website (http://www.cnb.cz – *Legislation*).

3. NEW APPROACHES TO THE ENHANCEMENT OF FINANCIAL MARKET STABILITY AND TRANSPARENCY

3.1 THE NEW BASEL CAPITAL ACCORD (BASEL II)

In 2006, the CNB continued working to implement the new capital framework – usually referred to as Basel II. The first draft of the new framework was prepared by the Basel Committee on Banking Supervision (BCBS)[5] in 1999. The most recent revised version, entitled "International Convergence of Capital Measurement and Capital Standards", was published by the BCBS in November 2005.

The aim of Basel II is to support the stability of the financial system and the competitive environment on the financial services market and also to strengthen management responsibility. The new framework concentrates on more accurate risk measurement and on promoting enhanced risk management in banks. By applying more risk-sensitive approaches, banks can make better and more efficient use of capital to cover the risks they face. Basel II introduces a new capital requirement for operational risk, and the capital requirement for credit risk can be set more accurately. The new rules are more comprehensive, offer a wider range of options for measuring the risks faced and allow banks to align their internal risk measurement and management systems with the regulatory rules. They cover not only the risk of the bank alone (on a solo basis), but also the risk of the whole banking group (on a consolidated basis).

Basel II is based on three pillars. Pillar 1 contains methods for risk measurement and for setting capital requirements for credit, market and operational risk. Pillar 2 deals mainly with all major risks and with capital adequacy. The basic principle is that a bank should have in place appropriate internal processes to set, continuously assess and maintain its internal capital in relation to its risk profile. The supervisory authority assesses these processes and their outputs. It is entitled (in addition to other remedial measures) to insist on a higher capital requirement than that calculated by the bank under Pillar 1, i.e. above the threshold corresponding to the sum of the capital requirements for risk coverage. A capital ratio of 8% of the value of risk-weighted assets will still be considered the absolute minimum. Pillar 3 deals mainly with the issues of bolstering market discipline and attaining market transparency through reporting and comprehensive disclosure of relevant information by banks.

Transformation of Basel II into EC directives
In the form resulting from its transformation into Community law, i.e. into directives 2006/48/EC[6] and 2006/49/EC,[7] Basel II continues to be crucial for the Czech Republic. The core of the framework remains unchanged in the Directives. However, it differs in some minor respects from the BCBS source document, taking into account the specifics of the European market. The European Parliament and the EU Council approved the Directives after long negotiations, and the final texts were published in the EU's Official Journal on 30 June 2006. The final provisions of both Directives required Member States to adopt relevant national legislation implementing the Directives by 31 December 2006 and to apply this legislation from 1 January 2007. The final versions of the Directives are based on the previous versions, but also contain some relevant changes reflecting comments from the banking community in particular. One of the principal differences between the Directives and Basel II is their application to banks, credit institutions, investment firms and to a limited extent also to electronic money institutions, while the BCBS document is primarily intended for internationally active banks.

Implementation of the framework in the Czech financial sector
The preparations for the implementation of Basel II in the banking sector – in the form of a joint trilateral project of the CNB, the Czech Banking Association and the Chamber of Auditors of the Czech Republic – entered their final, legislative phase in 2006 and were finalised by the end of the year after an almost five-year period of

5 The Basel Committee on Banking Supervision (at the Bank for International Settlements) is an international committee that issues recommendations and standards for various areas of banking supervision.

6 Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions.

7 Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions.

cooperation. The CNB also worked closely with the Ministry of Finance on the preparation of other amendments to laws implementing Basel II, namely amendments to the Act on Banks, the Credit Unions Act, the Payment System Act and the Capital Market Undertakings Act. The CNB also drafted a related implementing decree and, following the integration of financial market supervision, held consultations on it – via the relevant associations – with the community of regulated entities (banks, credit unions and investment firms). The draft amendments to these acts were prepared in advance and entered the legislative process in the second half of 2006. Owing to general delays in legislative processes caused by the political discussions following the June elections, the new rules will take effect in the Czech Republic on 1 July 2007. Until that time, regulated entities will be subject to the current rules.

In 2006, CNB Banking Supervision worked more closely with the regulated entities that intend to switch in 2007 to one of the special, and hence more advanced, capital requirement calculation approaches. These approaches require validation and subsequent approval by the competent supervisory authority. In particular this concerns the internal ratings based approach for calculating the capital requirement for credit risk, which, if the relevant applications are approved, will be implemented in 2007 by a total of five banks.[8]

The CNB's progress with, and approach to, implementing Basel II is published and regularly updated on its website (in Czech only: http://www.cnb.cz – *Dohled nad finančním trhem – Bankovní dohled – Basel II*).

International cooperation on implementing Basel II

The Directives newly regulate relations between home and host supervisory authorities in the supervision of consolidated groups. Much closer international cooperation is expected of supervisory authorities, with the home supervisory authority of the parent bank or financial holding entity playing a coordinating role. CNB Banking Supervision held meetings or otherwise communicated with competent foreign supervisory authorities on the division of tasks in implementing Basel II with regard to individual multinational consolidated groups. In the case of selected groups headed by a European parent bank which have applied for approval of the internal ratings based approach, specific cooperation in 2006 was focused on verifying the relevant requirements regarding this approach and granting consent. The CNB, which under the new rules is in most cases the host authority, supports a uniform interpretation of the rules and coordination of procedures and a switch to the special (advanced) Basel II approaches.

These objectives can only be achieved through active involvement in international institutions. The CNB is represented in the International Liaison Group (ILG),[9] which operates within the Basel Committee on Banking Supervision and deals with the core principles of banking supervision. The CNB's membership of this group guarantees access to the latest information and enables it to voice its opinions on certain issues, including Basel II. The CNB is also involved in relevant committees and working groups operating within European structures,[10] where it acquires information and contributes to the implementation of Basel II in the EU.

3.2 SOLVENCY II

The insurance sector is lagging behind the banking sector somewhat in introducing a new capital framework at the European level. The legislation implementing Basel II was definitively adopted at EU level in 2006, whereas the analogous directive for the European insurance industry, known as Solvency II, is still only under preparation, on the basis of a European Commission call and a Solvency II consultancy framework[11] issued by the Commission and last amended in April 2006. An important step in the preparation of Solvency II is the codification of the current insurance directives (particularly the life directive, the non-life directive, the reinsurance directive, the directive on the supplementary supervision of insurance undertakings in a group, the directive on the reorganisation and winding-up of insurance companies, etc.) into a single concept laying the groundwork for a new framework directive.

8 For details, see section 4.5 *On-site examinations*.
9 The International Liaison Group is one of four committees operating within the Basel Committee on Banking Supervision.
10 For details, see section 5 *International cooperation*.
11 Amended Framework for Consultation – MARKT/2515/06, April 2006.

The starting points for the new rules and their supervision are configured in a similar way as for Basel II. The system will be based on three pillars, similar to those in the banking sector. It will contain quantitative requirements, qualitative requirements and reporting and information disclosure. The quantitative requirements in the first pillar will determine in particular the method of calculation of technical provisions and capital requirements, which will be calculated using either a standard formula or internal models approved by the supervisor. The second pillar will stipulate the supervisor's powers and responsibilities and specify rules for supervisory authorities for supervising individual entities and reviewing risk assessment and management systems, internal control systems, the competence of managers etc. On the strength of such findings, remedial measures will be adopted, including higher capital requirements. The third pillar will bolster market discipline and market transparency based on reporting and comprehensive disclosure of information by supervised entities.

The European Commission has stated several times that the draft framework directive will be ready for the legislative process by July 2007. This process will include the creation of measures implementing this framework directive, which the CNB will help to prepare within CEIOPS[12] and its working groups. Assuming that the legislative process is of the usual duration, the adoption of the final version of the Solvency II directive may become one of the items on the agenda during the Czech Presidency of the EU in the first half of 2009.

The CNB has so far been involved in the preparation of the new rules primarily in the Level 3 Committee, CEIOPS, which in 2006 prepared a large volume of technical advice for the European Commission either on request or at its own initiative, for example in the areas of capital requirements, supervision of insurance groups and information disclosure. The CNB works in partnership with the Ministry of Finance to prepare opinions for meetings of the European Commission's working group for solvency, or EIOPC[13] (a Level 2 Committee).

The Solvency II preparations include quantitative impact studies (QIS) conducted by the CEIOPS Committee at European level. The second round of QIS (QIS 2) – aimed primarily at testing capital requirement calculation methods – took place in mid-2006. Unlike in the first round, Czech insurance companies contributed to the study this time. Nevertheless, the fact that only two insurance companies – with a combined market share of less than 13% – took part might suggest that the Czech insurance sector is not yet preparing very intensively for the new Solvency II rules. The CNB therefore expects closer cooperation, primarily with the Czech Insurance Association, in the third round of QIS between April and June 2007. On the basis of the third round results, the CEIOPS Committee will prepare the final version of the standard formula for calculating capital requirements. This is planned to be adopted at the beginning of 2008. The standard formula will make up one of the implementing measures of the framework directive.

3.3 IMPLEMENTATION OF MIFID

Directive 2004/39/EC on Markets in Financial Instruments (MiFID) replaces Directive 93/22/EEC on Investment Services. It is a framework directive and is accompanied by implementing measures, specifically Commission Regulation No. 1287/2006 and Directive 2006/73/EC. EU Member States were obliged to transpose the relevant regulations by 31 January 2007, the implementation date being 1 November 2007.

MiFID lays down conditions for doing business on the capital market. Compared to the original regulation, it defines a new concept for financial instruments and investment services, newly regulates customer categorisation and deals at length with the rules for the best execution of customer orders. MiFID also defines alternative market platforms and expands the concept of measures to ensure market transparency. The implementation of MiFID necessitates a fundamental amendment of the Capital Market Undertakings Act and its implementing regulations, changes in domestic information systems and the establishment of pan-European ones, and close cooperation with partner supervisory authorities in other European countries.

As part of the MiFID implementation project and associated implementing regulations, the CNB subjected the new regulation to careful examination and prepared an analysis of the individual areas, paying particular regard to their

12 Committee of European Insurance and Occupational Pensions Supervisors.
13 European Insurance and Occupational Pensions Committee.

impact on Czech capital market participants. The above analyses were used both at international level at CESR[14] meetings and at national level in consultations on Ministry of Finance documents, at meetings with the representatives of capital market service providers, and in particular during the preparation of transposition decrees. At CESR level, the CNB is also involved in laying the technical and organisational groundwork for a common system for sharing reports on transactions in investment instruments admitted to trading on regulated markets.

More details are available on the CNB website (in Czech only: http://www.cnb.cz – *Legislativa – Kapitálový trh – Materiály k transpozici MiFID*).

3.4 CORPORATE GOVERNANCE

At meetings and in annual report compilation instructions, issuers of listed securities are invited by the CNB to sign up to a Corporate Governance Code based on OECD principles. However, the Code and the inclusion of a corresponding statement in annual reports is voluntary and cannot be enforced. The Code is in companies' own interest, as it increases the confidence of investors, banks and other stakeholders.

In 2006, eleven of the 88 issuers of listed securities who submitted an annual report for 2005 included in that report a statement of compliance with the Code.

3.5 INTERNATIONAL FINANCIAL REPORTING STANDARDS

2006 marked a turning point in the supervision of the disclosure duties of issuers of listed securities, with the duty to publish financial statements in accordance with the International Financial Reporting Standards (IFRS) being implemented for the first time. This did not, however, put a significant burden on issuers of listed securities, as they had been informed about the changeover to IFRS well in advance. The instructions for the preparation of annual reports alerted issuers to issues relating to consolidation in particular. Emphasis was also put on the description of their financial condition in order to ensure comparability with data for previous periods.

The CNB also cooperated with the Ministry of Finance on an opinion regarding the proposed way forward in the convergence of GAAP (Generally Accepted Accounting Principles) and IFRS, in order to ensure comparability of the national accounting standards of the USA, Japan and Canada with IFRS.

14 Committee of European Securities Regulators.

4. FINANCIAL MARKET SUPERVISION IN 2006

4.1 LICENSING, APPROVAL AND AUTHORISATION ACTIVITIES

Banks and credit unions

The CNB received a total of 33 petitions for the opening of administrative proceedings, 14 of them from banks and 19 from credit unions. No administrative proceedings were commenced in respect of electronic money institutions under Act No. 124/2002 Coll., on Payments, as amended. Nor were any penalty proceedings conducted with banks and credit unions in the period under review.

By the end of 2006, a total of 31 administrative decisions had been issued, 12 of which were prior consents to the acquisition of qualifying holdings in banks, 1 was a prior consent of the regulator to an agreement on the sale of a business to a bank, 15 involved certificates of competence for members of credit union bodies, and 1 concerned a change (extension) to a licence. One application for consent to invest another membership contribution in a credit union was refused (including a second instance decision of the CNB Bank Board). The remaining administrative proceedings were not concluded in the period under review. They concern a change in authorisation for some other activities of a credit union through its enlargement, and the acquisition of a qualifying holding in a bank.

One application for a banking licence (commenced back in 2005) was re-submitted to the CNB by an applicant based in a country outside the EU. The administrative proceedings were terminated by refusal of the application, including a second instance decision of the CNB Bank Board, after the applicant lodged an appeal under the act against the CNB's first instance decision.

Back in 2005, CNB Banking Supervision received notification of the establishment of a branch under the single banking licence principle from Japan's Bank of Tokyo-Mitsubishi UFJ (Holland) N.V., which started its operation in the Czech Republic in April 2006.

In the period under review, one domestic bank (J&T BANKA, a. s.) exercised the right of establishment under the European legislation on the basis of the single licence principle in another EU Member State, namely Slovakia. Four domestic credit unions (Družstevní záložna FIO, Spořitelní a úvěrní družstvo UNIBON, Spořitelní družstvo WPB Capital and Spořitelní družstvo Prague Credit Union) exercised the same right in Slovakia, Poland, Hungary and Cyprus.

A total of 24 banks and building societies and, to a limited extent, 13 foreign bank branches active on the domestic banking market were subject to banking supervision at the end of 2006. In addition, 20 credit unions came under the competence of banking sector supervision.

Capital market

In all, 221 administrative proceedings were opened in the area of collective investment and pension funds in 2006, 140 of which had been decided by the end of 2006. Of this total, 39 decisions concerned the approval of directors, 59 concerned the approval of changes to statutes, 6 involved licences to establish investment companies, 1 related to an extension of an investment company licence, 14 concerned licences to establish mutual funds, 6 concerned authorisations to acquire qualifying holdings and 15 dealt with other issues. The higher number of proceedings in progress was due mainly to a higher number of applications for changes to mutual fund statutes submitted at the end of 2006 following an amendment to the relevant decree.

Four new investment companies – AMISTA investiční společnost, a. s., AXA investiční společnost, a. s., REICO investiční společnost České spořitelny, a. s. and ORION CAPITAL MANAGEMENT investiční společnost, a. s. – were granted licences in 2006. In two cases, investment company licences were not granted. In the case of two investment company licence applications and one investment fund licence application, the proceedings were not concluded during the period under review. The entry of four new entities into the collective investment sector was linked chiefly with an amendment to the Collective Investment Act, which introduced, among other things, real estate funds for the public and funds for qualified investors with effect from the end of May 2006. The interest in establishing such funds (two mutual funds of qualified investors had been authorised by the end of 2006) generated demand for new investment companies that can manage such funds. In addition, a decision was issued permitting the merger of two pension funds – Hornický penzijní fond Ostrava, a. s. and ČSOB penzijní fond Progres, a. s., a member of the ČSOB group.

In the area of collective investment and pension funds, 13 investment companies (actively operating or newly authorised), 11 pension funds, 9 depositories and 77 open-end mutual funds, 26 of them standard funds, were subject to financial market supervision as of 31 December 2006.

In the area of investment services providers, a total of 51 entities holding investment firm licences, 13 of them banks, were registered under Article 5 of the Capital Market Undertakings Act at the beginning of 2006. During 2006, no new investment firm licences were granted, 2 such licences were withdrawn and 3 such licences expired under the legislation owing to changes in objects of business. The CNB registered 46 investment firms, 13 of them banks, as of the end of the period under review.

The CNB issued 193 first instance decisions in the area of investment services provision in 2006. Of these, 12 concerned the extension of current investment firm licences and in 3 cases the CNB refused applications for such extensions. The CNB withdrew investment firm licences in 2 cases – from Americas International Brokers, a. s. and AFIN BROKERS, a. s. – on the grounds of serious shortcomings in investment service provision. 25 decisions concerned prior consent to the discharge of office of director of an investment firm and in 2 cases the CNB refused to grant such consent. The CNB issued prior or subsequent consent to the acquisition of qualifying holdings in investment firms in 10 cases and refused to grant it in 2 cases. Other decisions in the investment services area mostly concerned the issuance, extension or withdrawal of broker's licences (95 issued/extended; 2 withdrawn), registration of investment intermediaries (29 withdrawn and two refused) and approval of investment firms' auction rules (4 approvals). Administrative proceedings were discontinued in 5 cases.

A total of 1,790 entities holding a broker's licence under Article 14(1) of the Capital Market Undertakings Act were registered at the beginning of 2006. In the period under review, the CNB issued 70 broker's licences and withdrew such a licence in 1 case. The CNB thus registered a total of 1,859 entities holding a broker's licence as of the end of 2006.

The CNB organised broker examinations in the period under review. Thirty rounds of broker examinations took place in 2006, with 270 participants.

Administrative proceedings in the regulated markets area in 2006 concerned in particular the Prague Stock Exchange (PSE), the OTC market operator RM-Systém (RM-S), and UNIVYC, a. s.[15] The PSE's licence was extended to include exchange trading in investment certificates, warrants and financial and commodity futures. UNIVYC's settlement system licence was extended in a similar way. A change in the OTC market trading rules introducing a new way of trading was approved during the period under review. At the end of 2006, RM-S applied to change the OTC trading rules and the SVYT[16] settlement system rules in connection with its plan to trade foreign securities. Consent to membership of a board of directors or to the discharge of office of director was granted in 4 cases, all of them related to the OTC market. The implications of a change in the owners of the OTC market operator for its sound and prudent management were also examined. Proceedings to grant a central securities depository licence were ongoing at the same time.

Two basic types of approval procedures are conducted in the area of securities issues. The first is the approval of documents connected with new securities issues, i.e. various combinations of bond issue conditions under Act No. 190/2004 Coll., on Bonds, and securities prospectuses and combinations thereof for the purpose of offers to the public and admission of securities to trading on the regulated market under Act No. 256/2004 Coll., on Capital Market Undertakings. In the case of bond issue conditions this involves a more or less formal check of the essential elements of such documents. In the case of approvals of securities prospectuses, compliance with the conditions laid down in Commission Regulation No. 809/2004, regulating the information contained in prospectuses, is checked; specifically, the adequacy of information stated in the prospectus is verified, particularly with regard to the issuer's management and activities and the description of the rights associated with the security. A total of 79 administrative proceedings were held in this area in 2006.

15 Universal Settlement Centre.
16 Transactions Settlement System.

The second type of approval procedure concerns the granting of consent to the publication of takeover bids and other public share-purchase contract offers relating to listed participating securities, and since September 2005 also the granting of prior consent to squeeze-out decisions made by general meetings. In both cases, the proceedings focus on examining company valuations and assessing the adequacy of prices offered or considerations provided. These proceedings are subject to time limits laid down in the Commercial Code. 21 administrative proceedings were held in the takeover bids area and 83 in the squeeze-out area in 2006.

In addition to these basic types of proceedings, 15 proceedings were held in 2006 in relation to the disclosure duties of issuers of listed securities, in particular proceedings concerning the narrowing of the scope of annual reports.

The insurance sector

Domestic insurance companies and reinsurance companies and insurance companies from third countries (non-EU/EEA countries) were subject to licensing and approvals. A total of 67 administrative proceedings were opened in 2006, 63 of which were closed by administrative decision.

The CNB granted authorisation to an insurance company from a third country to carry on insurance activities via a branch – to the Swiss insurance company Elvia Reiseversicherungs-Gesellschaft AG.[17] One administrative proceeding concerning an application for an insurance licence was not closed. Three insurance companies were granted licences to expand their activities.

Of the 48 administrative proceedings conducted concerning applications for prior consent to a change of member of a statutory or supervisory body or a proctor, consent was granted for 91 persons and not granted for 6 persons (an appeal was filed against one decision).

Prior consent to acquire or increase qualifying holdings was granted in 7 cases in 2006.

The CNB also approved a division of an insurance company (Česká pojišťovna, a. s.) through a split and establishment of a new successor company, the aim of which was to separate off activities relating to consumer lending. Two insurance companies were granted time limited consent to a different financial investment structure. A method for splitting common life and non-life insurance items was approved in the case of one insurance company. This consent is linked with parallel operation of life and non-life insurance and the condition of separate management of these activities under Article 40 of Act No. 363/1999 Coll., on Insurance.

In early 2006, in administrative proceedings opened in 2005, the former Office of the State Supervision in Insurance and Pension Funds identified the financial group PPF as a financial conglomerate within the meaning of Act No. 377/2005 Coll. Further administrative proceedings concerning the identification of a group as a financial conglomerate were opened in the second half of 2006. These proceedings were discontinued at the company's request.

A total of 33 domestic insurance companies and the Czech Insurers' Bureau were subject to supervision by the CNB as of the end of 2006. To a limited extent, the CNB also supervised 15 branches of insurance companies from EU/EEA countries and 1 new branch of an insurance company from a third country. These branches send documents regarding their activities to the CNB.

Other regulated entities

Under Act No. 219/1995 Coll., the Foreign Exchange Act, the CNB also supervises almost 3,000 non-bank foreign exchange entities. This group includes both entrepreneurs offering cash purchases and sales of foreign currency and entities engaged in non-cash foreign exchange transactions or money services.

Licensing certificates for bureau-de-change activities are issued locally by trade licensing offices. Such certificates only authorise entrepreneurs (natural persons or legal entities) to purchase foreign currencies in cash. Trade

17 Under the Agreement between the European Economic Area and the Swiss Confederation on direct insurance other than life assurance of 1991, the system for establishing branches of Swiss insurance companies in the EEA is similar to that for European insurance companies establishing branches in other Member States.

licensing offices request the CNB's opinion prior to granting licensing certificates. Entrepreneurs can carry on the purchase of foreign currencies only in premises and exchange machines that have been approved by the CNB in advance. In 2006, the CNB issued 126 opinions on the granting of licensing certificates and 235 opinions on the approval of premises (7 of them negative). The total number of foreign exchange entities with licensing certificates was 2,609 at the end of 2006. According to data available to CNB branches, roughly 60% of them were carrying on bureau-de-change activities. The number of foreign exchange entities has been flat since 2002. Compared to 2005 the number declined slightly, as did the number of foreign exchange premises, which totalled 2,460 at the end of the year.

Foreign exchange licences to sell foreign currencies in exchange for Czech currency in cash are issued by CNB branches, while other foreign exchange licences are issued by CNB headquarters. The number of entrepreneurs with foreign exchange licences is steadily increasing. The CNB received 27 foreign exchange licence applications in 2006. Most of these applications were granted by the CNB; applications were refused due to failure to meet the conditions for granting a foreign exchange licence.[18]

In 2006, the CNB issued 14 permits to issue electronic money under Article 19 of the Payment System Act. A total of 38 entities had such a permit as of 31 December 2006.[19] This figure puts the Czech Republic in a leading position among the EU Member States. The vast majority of these electronic money issuers are transport companies who issue chip cards that can be used to pay fares between regions to other transport companies. In 2006, one company issued electronic money for internet payments and one used electronic money to enable employees of various firms to withdraw money from a social fund. By contrast, no entity has so far shown any interest in obtaining an electronic money institution licence under Article 18b of the Payment System Act, or a payment system operator's licence.

4.2 NOTIFICATIONS

The Czech Republic's accession to the EU has also opened up the Czech financial market to other entities entitled to benefit from the free movement of services under the single licence (the European passport).[20]

During 2006, the CNB received 479 announcements by foreign regulators of notifications of cross-border provision of services, of which 32 from banks, 78 from insurance companies,[21] 281 from collective investment funds, 4 from investment companies, 83 from investment services providers and 1 from an electronic money institution.

The competent supervisory authorities from EU/EEA Member States were notified of the intention of three domestic insurance companies to carry on insurance business within their territory under the freedom to provide services.

The following table summarises the cross-border service provision notifications received as of 31 December 2006.

31 Dec. 2006	Banks	Insurance companies	Funds	Investment companies	Investment services providers	Electronic money institutions
Total	137	401[22]	1,271	29	293	2

18 A complete list of foreign exchange licences, updated quarterly, is available on the CNB website (http:\\www.cnb.cz – *Financial market supervision – Foreign exchange supervision – Complete list of foreign exchange entities from the register of foreign exchange entities*).

19 A list of entities which have been given a permit to issue electronic money by the CNB is available at http:\\www.cnb.cz (in Czech only: *Platební styk – Elektronické peníze*).

20 For more details on the single licence, see http:\\www.cnb.cz (in Czech only: *Dohled nad finančním trhem – Bankovní dohled – Výklad ČNB k jednotné bankovní licenci*).

21 In addition to insurance companies, insurance company branches operating in other EU/EEA countries are notified in this manner. In 2006, the CNB was notified by foreign regulators of the intention of nine branches to provide services in the Czech Republic (this figure is included in the total of 78 notifications).

22 Of which 79 are branches of such insurance companies in the EU/EEA.

In the area of prospectus notifications, the CNB received 52 notifications from foreign regulators, and in one case a prospectus was notified in another country (a ČEZ, a. s., share prospectus for the admittance of shares to trading on a regulated stock market in Warsaw).

During 2006, the CNB also received notification of the intention to carry on business in the Czech Republic from 2,060 insurance intermediaries having a home Member State other than the Czech Republic (1,900 of them from the Slovak Republic).

4.3 REGISTRATIONS

Under Article 39 of Act on the CNB, another four representations of foreign banks and financial institutions were registered in 2006. These were banks from Ukraine, Lithuania, Italy and Austria (Join Stock Commercial Bank "FORUM", AB Bankas SNORAS, Banca Monte dei Paschi di Siena SpA and Capital Bank – GRAWE Gruppe AG), which do not carry on banking business directly, but intermediate and offer the services of their banks in this territory. A total of 24 foreign bank representations were registered in the Czech Republic as of the end of 2006.

In all, 8,387 investment intermediaries were registered under Article 30 of the Capital Market Undertakings Act as of the beginning of 2006. During the period under review, 2,273 certificates of registration of an investment intermediary were issued and 32 were cancelled. The CNB thus registered 10,628 investment intermediaries as of the end of 2006.

In 2006, a total of 12,762 intermediaries were listed in the register of insurance intermediaries and independent loss adjusters, 121 of which were insurance agents and 58 insurance brokers. Decisions to cancel entries were made in 424 cases, at the request of the insurance intermediaries concerned. The register of insurance intermediaries is available on the CNB website (http://ispoz.cnb.cz). At the end of 2006 it contained 50,121 insurance intermediaries, 2,390 of them foreign.

In connection with the registration of insurance intermediaries, the CNB holds professional examinations of insurance agents and insurance brokers. The purpose of the examinations is to verify whether the applicants are competent to perform intermediary activities for which a medium or higher level of competence is required. In all, 1,732 candidates took these examinations and 1,713 passed.

During 2006, decisions were taken to register 4 entities in the register of responsible actuaries.

Central register of credits
The Central Register of Credits (CRC) administered by the CNB has been facilitating the sharing of information on credit commitments and payment discipline between banks since 2002. The following key data provide evidence of the growing use of the CRC over the past two years.

Key statistics on the CRC

	31 Dec. 2005	31 Dec. 2006
Number of users	1,927	2,284
Number of clients registered	302,799	356,247
of which: individual entrepreneurs	184,062	213,704
	(61%)	(60%)
legal entities	118,737	142,543
	(39%)	(40%)
Number of active claims	329,123	404,256
Number of enquiries on clients registered in CRC for year	256,425	305,919
Number of enquiries on total credit commitments of clients for year*	2,214,371	2,388,625
Number of extracts made for clients for year	133	195

* Including credit commitments of own clients obtained via batch reports made available to bank after each update.

Phase II of the CRC's development was completed in mid-2006, and new tools expanding and enhancing the use of the CRC going forward were made available to users. The innovations include an analytical module for work with aggregated data, a tool for creating groups of connected clients, simplified and more transparent outputs of client credit commitments and a new overview of client credit commitments – a credit monitor.

The CRC's analytical module enables use by a wider range of users of aggregations of the huge volume of data sent by banks to the CRC database. When defining statistical choices of key indicators, which include outstanding claim balances and past-due principal and interest, users can choose the following sorting criteria, for example: period, client type (legal entity, individual entrepreneur), resident vs. non-resident, legal form, economic sector, country, synthetic account, claim type, credit type, CZ-NACE (Industrial Classification of Economic Activities), claim status, number of days past due, currency and collateral type. Supplementary criteria include region, number of employees and turnover, taken from the RES (Register of Economic Entities) database administered by the Czech Statistical Office and used as a support database for the identification of CRC clients. Besides these key indicators, various calculation indicators can be used, for example average claim amount, average values calculated for a client, maximum, minimum, etc. The application enables time series to be constructed and selections to be made for the overall banking sector or for specified groups of banks (large banks, medium-sized banks, small banks, foreign bank branches and building societies) and, in the case of banks, also for the user's own bank.

This new functionality is directly available to analysts and statisticians from banks and the CNB. In the future, the general public will also have access to key banking sector characteristics obtained from the CRC through the analytical module on the website.

The credit monitor gives users a fast and accurate overview of all client credit commitments on a timeline of the CRC's entire history, including a graphical display of defaults on credit commitments. This functionality has been introduced primarily for bank users and provides a clear and concise picture of clients' payment discipline.

The CRC features a module for creating groups of connected clients (GCCs), offering users tools and functionalities for simple creation and administration of GCCs and their members. CRC users can set up groups, update, correct or delete them, or add a member to a group of a particular bank. Users from individual banks, for whom this new function is designed, are offered a clear output displaying all or selected GCCs of a bank and their members. The GCC creation module lets users generate selected output data for individual groups or individual group members within the credit commitment application, the credit monitor, the own claims application and the list of groups in which a client is registered by a bank. The data are only available to the bank that sets up the group.

The possibility of integrating the CRC into a project for the international exchange of information between EU Member States will be analysed in 2007. Within the WGCR (Working Group for Credit Registers) established by the ECB's Banking Supervision Committee[23] it was stated that the CRC administered by the CNB meets the formal requirements for integration into the data exchange project as regards both the information content of the register and its technical solution. The Czech Banking Association has expressed its support for the international data exchange project.

At present, Austria, Belgium, France, Germany, Italy, Portugal and Spain are involved in the data exchange project. Aggregate data on clients and their on- and off-balance-sheet claims are exchanged on a quarterly basis. In addition to this regular exchange of data, one-off enquiries can be made about individual clients.

Were the Czech Republic to join this project, the CRC would receive quarterly information on Czech clients contained in the national credit registers of the Member States participating in the international data sharing project, and would simultaneously enter into these national registers the latest information on clients from these countries stored in the CRC database. It would also be obliged to provide information on CRC clients in response to one-off enquiries from any of the member credit registers.

The CRC has served banks as a credit risk mitigation tool since its establishment. Through the analytical module, the CRC has provided a useful database for CNB and bank analysts and statisticians since mid-2006. As from 2007, the CRC will be one of the data sources for banking supervision activities.

23 For details, see section 5 *International cooperation*.

Information about the CRC is published for banks on the CRC website, which contains full methodological documentation, a user manual, operating information and contact details for CRC administrators. Information for the public is available on the CNB website. Besides basic information on the CRC, it contains information on providing extracts to clients and an application form for the provision of an extract from the CRC.[24] Extracts are only provided to legal entities and entrepreneurs, as the register pools data on these types of clients only. A fee is charged for CRC information services (use of the register by banks, provision of extracts from the register) in line with the CNB's price list. The CNB's overall income from these fees, amounting to around CZK 8.5 million a year, covers the direct expenses connected with the CRC's operation. System development costs and other indirect costs associated with the CRC's existence are covered by the CNB.

4.4 OFF-SITE SURVEILLANCE

Off-site surveillance consists in continuously monitoring the activity and financial performance of the individual entities operating on the market and assessing the evolution of the market as a whole and its key segments. Information is obtained mainly from the statements and reports regularly submitted by individual entities on a solo and consolidated basis. The required frequency and manner of sending data to the CNB still differs significantly across market segments. As the integration of financial market supervision progresses, however, efforts are being made to align them gradually in terms of both content and manner of reporting to the CNB.

The main change in the content of the reports prepared for 2007 concerned capital adequacy and the key financial statements and related statements of banks and investment firms. This change came in response to a requirement to harmonise disclosure duties with the standardised framework recommended by the CEBS[25] in connection with single European reporting under FINREP (Financial Reporting) and COREP (Common Reporting). The statements were adapted to the requirements of the new capital framework (Basel II) and International Financial Reporting Standards (IFRS).

Following the integration of financial market supervision into the CNB, the reporting duty statements were converted to the system used by the CNB for existing reporting entities. The changeover to the Non-bank Data Collection System (SDNS) as regards the reporting duty of collective investment funds, investment companies and insurance companies simplified and reduced the reporting requirements. Thanks to the SDNS system, which contains all the necessary data, the evolution of selected financial indicators for individual entities as well as the market as a whole can be summarised quickly and easily. Simplification of the structure of data reported on pension funds also proved useful. The effects of the rationalisation of data collection from pension funds and the convergence towards the structure of the reporting duty for collective investment funds were visible already in the reports drawn up in mid-2006.

Preparations were simultaneously made for fulfilment of the reporting duty of investment firms through the SDNS system for non-banks and through the EDIFACT[26] data channel for banks as from 1 January 2007. Training programmes on the new method of fulfilment of the reporting duty were held for investment firms in order to ensure a smooth transition to the new form of data reporting to the CNB.

In addition to the regular reports, all other available information from various sources is used for continuous monitoring of entities and the market. These sources include financial statements, annual reports, auditors' reports, information from on-site inspections and information-gathering visits, public presentations and press releases. Where additional information is needed, meetings with representatives of the supervised entities are organised on an ongoing basis.

Off-site surveillance helps the CNB to form a comprehensive picture of the financial condition of the supervised financial market entities and allows it to identify potential problems and risks, which provide a starting signal for conducting on-site examinations.

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24 CRC website: http://www.cnb.cz – *Financial market supervision – Banking supervision – Central Register of Credits*.
25 Committee of European Banking Supervisors.
26 Electronic Data Interchange for Administration, Commerce and Transport.

4.4.1 Supervision of banks, foreign bank branches and credit unions

The main analytical instrument employed in off-site surveillance is quarterly analysis of the financial condition of banks and the risks they undertake. The observance of prudential limits and rules (e.g. for credit exposure or capital adequacy) is monitored on a monthly basis. Early warning information is also assessed every month; this comes from an automatic system which helps supervisors to identify potential negative tendencies in individual banks. The assessment of foreign bank branches is slightly simpler, as the CNB's powers of supervision of these entities are limited.[27]

Staff involved in off-site surveillance use an automated Banking Supervision Information Centre. This internally created tool allows supervisors to view data from all the supervisory reports and statements and generates standard outputs. It also enables the creation of specific outputs for analytical assessments of individual banks and the banking sector as a whole. This informational support provides a quick overview of the main indicators of the financial condition of each bank and the banking sector and of compliance with the prudential rules.

In 2006, auditors' reports on banks' internal control systems and risk management systems continued to be evaluated. These reports are an important source of information on the internal systems in individual banks in periods when no on-site examination covering the given area is conducted. In 2006, CNB Banking Supervision obtained auditors' reports on a total of 7 control system areas in 7 banks, evaluating the situation in these banks as of 31 December 2005. Discussions with individual banks and auditing companies were subsequently held to assess the results of these examinations. The CNB's requests for audits as of 31 December 2006 were commissioned in the same way. These audits concerned 6 banks and were made available to the CNB in the first quarter of 2007.

In addition to regular assessment of banks' financial condition, off-site surveillance focuses on some other aspects of bank activities. In 2006, a total of 82 decisions were issued relating to the assessment of the competence and integrity of proposed senior officers in banks, the approval of external auditors, lists of shareholders prior to general meetings, the inclusion of subordinated debt in a bank's capital, etc.

On the strength of the findings from off-site supervision and on-site inspections, remedial measures were imposed on 11 banks. These required the banks concerned to eliminate shortcomings in their activities within a set timeframe. Banks' progress in eliminating shortcomings is constantly monitored. In 2006, CNB Banking Supervision opened no penalty proceedings to revoke licences or impose fines for violations of the Act on Banks. To eliminate shortcomings detected in banks during on-site inspections or off-site surveillance, the supervisor used alternative and equally effective instruments available to it under the law. These led to the required corrections as regards compliance with the prudential rules.

Cooperation with regulators from other countries supervising the parent banks of banks operating in the Czech Republic is an increasingly important component of supervisory activities. The CNB has concluded eight bilateral memoranda of understanding with foreign banking regulators. This number remained unchanged in 2006, reflecting the stable shareholder structure of domestic banks as regards the home country of their owners. In addition to the exchange of information on the financial condition of banks and other entities from financial groups operating in both countries, discussions with foreign regulators focused mainly on practical issues connected with the implementation of Basel II.

The development of the banking sector as a whole, and, where appropriate, individual segments of the sector, is also subject to analysis. A report on the development of the banking sector is prepared for the CNB Bank Board twice a year. This includes "internal ratings" dividing banks into five categories according to their financial condition and management quality. Basic information on the financial performance of the banking sector is published quarterly on the CNB website (http://www.cnb.cz – *Financial market supervision – Banking supervision – Banking sector – Basic indicators of the banking sector*). CNB Banking Supervision also communicates regularly with numerous entities interested in the development of the Czech banking and financial sector (e.g. international organisations, rating agencies, etc.). In cooperation with other supervisory units of the CNB, a publication on

27 Primary responsibility for supervision of foreign bank branches lies with home country supervisors. The CNB mainly monitors foreign bank branches' liquidity and compliance with the obligations in the Act on Banks.

financial market supervision, including sectoral information and analyses of the evolution of individual markets, is presented to the financial community every year.

On 1 April 2006, in connection with the integration of supervisory activities, the CNB also assumed responsibility for supervising the credit unions sector. At present, 20 credit unions with valid licences are operating on the market, with total assets amounting to around CZK 7 billion as of 31 December 2006. In 2006, CNB supervisors focused on reviewing the current situation in the sector and in selected credit unions, tackling major problems and aligning the procedures for the supervision of credit unions with those applied to banks. In this context, on-site examinations were commenced sequentially in 10 credit unions.

The CNB issued 22 prior consents regarding the assessment of compliance with the conditions for the performance of the position of member of a credit union body or a senior officer, approved auditors in 3 cases and imposed remedial measures to eliminate shortcomings in 3 cases. One request for prior consent to invest another membership contribution in a credit union was refused.

4.4.2 Supervision of capital market undertakings

Following the amendment of the Collective Investment Act, the methodology of supervision of collective investment funds and pension funds was updated. A new area of special real estate funds and funds of qualified investors was incorporated. A draft decree on the disclosure duties of pension funds was prepared.

Off-site surveillance in the collective investment and pension fund sectors is being considerably hampered by the need to deal with issues related to the liquidation or bankruptcy of around 60 entities. As many of the enquiries and complaints received from investors and pension planholders concern these entities, a methodology was prepared for the supervision of entities whose licences have been revoked.

Last but not least, off-site surveillance involved keeping lists of forced administrators and liquidators, final decisions, eligible markets and reports of depositories. It also included a number of analytical activities relating to the verification of data obtained under reporting duties pursuant to the relevant methodology.

As regards off-site surveillance of investment services providers, the CNB above all performed inspections of brokers, examined qualifying holdings in investment firms, analysed the structures of consolidated groups containing investment firms and checked compliance with other information duties of investment firms.

The inspections of brokers consisted in verifying the qualifications (examinations, specialisations and authorisations) of individual brokers for the performance of professional trading activities under Article 2 of Decree No. 259/2004 Coll. They also focused on compliance with the duty of investment firms to perform professional trading activities when providing investment services through brokers.

The inspections of qualifying holdings focused on reporting of direct and indirect qualifying holdings in investment firms, close links, acting in concert and control of investment firms.

The analyses of the structure of business groups containing investment firms were aimed at defining consolidated groups pursuant to Article 150 of Act No. 256/2004 Coll., on Capital Market Undertakings, as amended, and checking compliance with the new information duties under Decree No. 262/2004 Coll., on the rules for calculation of capital adequacy of an investment firm that is not a bank on an individual basis. The results of inspections of qualifying holdings in investment firms were also used to this end.

The inspections checking compliance with information duties consisted in analysing data sent under the information duty, especially data from the transactions and orders books of investment firms. The data were used chiefly for the purposes of regular qualitative and quantitative assessments of the level of risk associated with supervised entities and the potential impact of their default on the stability of the financial market and client assets. In addition to regular analyses, the data were used mainly in the context of on-site inspections and other activities, usually in the area of licensing.

Checking compliance with information duties also takes the form of verification of information in administrative proceedings, especially those in the area of licensing, which involve a comprehensive assessment of all prerequisites for the activity of an investment firm.

The duties of issuers of listed securities and their main shareholders and managers are also subject to off-site surveillance. Reports published by issuers of listed securities and sent to the CNB under the information duty were checked. These reports included regular half-yearly and annual reports and price-sensitive (internal) information published in the course of the year. Supervisors monitored information from various sources on a daily basis, assessing it and comparing it with information officially published by issuers of listed securities. Attention was given to the statutory requirements for annual and half-yearly reports (including auditors' reports, directors' reports on companies' activities and relationships reports), internal consistency and consistency with information published in the course of the year. The CNB was supervising 92 issuers of listed securities as at the end of 2006.

Supervisors also continuously monitored whether managers of issuers of listed securities were complying with their duties. Such managers are obliged to provide information on trades in securities of the issuers of whose bodies they are members. Information on these "management trades" was published on the CNB website (in Czech only: http://www.cnb.cz – *Dohled nad finančním trhem – Dohled nad kapitálovým trhem – www.sec.cz – Seznamy a přehledy – Manažerské obchody*). A total of 95 notifications were processed in 2006. Fulfilment of the disclosure duty regarding voting rights was also monitored. Under this duty, the shareholders of an issuer of listed securities are obliged to report increases/decreases of their shares in voting rights above/below the thresholds stipulated by law. There were 156 such notifications processed in 2006.

The activities of the exchange chamber, exchange committees and bodies of the Exchange Guarantee Fund were also monitored, especially with regard to the extension of exchange trading to investment certificates, warrants and futures and the admission of new issues. Information sent by the OTC market operator under its regular disclosure duty was evaluated.

Transactions on regulated markets were monitored continuously to detect irregular situations in capital market trading. In one case the CNB filed a report on the commission of a crime with the relevant prosecuting attorney's office and informed the Financial Analytical Unit at the Ministry of Finance. Compliance with Decree No. 114/2006 Coll., on the fair presentation of investment recommendations, was also checked. Work continued on further improving the information system for capital market monitoring.

As regards sanction procedures, 123 administrative proceedings were conducted in 2006. These concerned breaches of issuers' disclosure duty (26 cases), the disclosure duty for shares in voting rights (24 cases), duties in takeover bids (16 cases), the ban on market manipulation (1 case), the duty to report management trades (1 case), the ban on insider trading (1 case), the duties of collective investment undertakings (5 cases), the duties of investment firms (31 cases) and the duties of investment intermediaries (18 cases). A total of 97 decisions were issued in administrative or offence proceedings in 2006. These included 20 decisions imposing sanctions for breaches of issuers' disclosure duty (proceedings were terminated in 3 cases). As regards sanctions for breaching the disclosure duty on shares in voting rights, 11 sanctions were imposed and 9 proceedings were terminated. Four decisions on sanctions were adopted and four proceedings terminated regarding duties in takeover bids. One sanction was imposed for breaching the ban on market manipulation. Five proceedings on suspected breaches of the duties of collective investment undertakings were terminated. With regard to the duties of investment firms, 17 decisions on sanctions were adopted, the licence of the investment firm was revoked in one case and 4 proceedings were terminated. Six decisions imposing sanctions for breaching the duties of an investment intermediary were adopted and 12 proceedings in this area were terminated.

4.4.3 Supervision of insurance companies

The CNB's supervisory work involves checking insurance companies' compliance with the relevant legal rules as well as their solvency and financial management from the point of view of their ability to fulfil their obligations. It also includes verifying the methods of creation and application of technical provisions and the financial placement of assets arising from technical provisions, checking compliance with the CNB's decisions, inspecting the conformity of activities performed with licences granted, and checking accounting procedures and the effectiveness of control systems.

Off-site surveillance is based on regular assessments of the financial condition of insurance companies, including compliance with prudential rules, as well as imposing remedial measures where shortcomings are detected. Key economic indicators of insurance companies are assessed on the basis of mandatory reports. In insurance companies that belong to an insurance group, data obtained from supplementary supervision of insurance companies in groups are also evaluated.

In addition to the reports presented to the CNB on the dates stipulated by law, it was decided in administrative proceedings to impose a duty on some insurance undertakings to present their reports for supervisory purposes on dates other than those stipulated by law, e.g. monthly or quarterly. Five insurance companies were obliged to present their reports in this manner in 2006. This obligation was cancelled in four cases in the course of 2006.

Other important information is obtained from auditors' reports, which are a valuable source of information, especially in periods when no on-site inspection takes place in the insurance company. Cooperation with external auditors, which consisted in exchange of information and experience as regards the procedures and methods used by both sides in carrying out their activities, was further expanded in 2006. If the assessments of an insurance company by an external auditor and the CNB differ, meetings take place to clarify the different results.

In line with the new strategy for risk-based supervision, work was commenced on defining a set of indicators of an insurance company's financial soundness, including early warning criteria. This system should serve as one of the main analytical tools for monitoring trends in the financial condition of an insurance company based on data from its financial statements, also enabling the detection of weaknesses in an insurance company's financial performance.

In the context of monitoring insurance companies' financial condition, analytical procedures are gradually being implemented which not only cover past developments and reveal the most important factors underlying changes in financial condition, but also help to create a basis for estimating future developments.

Information-gathering visits in major Czech insurance undertakings became an integral part of supervision in 2007. These visits focus on strategy, exchange of information on risk management and internal control systems, and implementation of corporate governance principles.

4.4.4 Supplementary supervision of financial conglomerates

Financial conglomerates are groups in which insurance companies, banks and/or investment firms have a significant share in all the financial activities carried on by the members of the group. Off-site surveillance includes supplementary supervision of such groups (under Act No. 377/2005 Coll. and Decree No. 347/2006 Coll.).

Supplementary supervision of financial conglomerates focuses on capital adequacy, intra-group transactions, risk concentrations, internal control systems and risk management systems. Responsibility for supplementary supervision lies with a coordinator, who monitors the relevant indicators, including compliance with requirements for capital adequacy and risk management systems, and ensures cooperation with other supervisory bodies. In 2006, the CNB acted as supplementary supervision coordinator for one financial conglomerate.

4.4.5 Supervision of other regulated entities

In the area of foreign exchange supervision, the CNB may open administrative proceedings to impose sanctions if it detects a violation of the foreign exchange regulations.[28] If the suspicion of a violation of the foreign exchange regulations is proved, the participant's foreign exchange licence may be limited, suspended or revoked depending on the extent, manner and duration of the violation. A fine of up to CZK 50 million can also be imposed. Administrative proceedings are conducted *ex officio* by CNB headquarters. In 2006, the CNB concluded 13 administrative proceedings opened in 2005 and opened another 33 proceedings. Of the proceedings opened in 2006, 29 first instance decisions were issued and 21 decisions became final and conclusive as of 31 December 2006. In two cases decisions establishing guilt but not imposing a fine were adopted, while in the remaining ones a fine was imposed along with the guilty decision. Administrative proceedings were conducted with foreign exchange offices and with persons illegally offering, performing or mediating foreign exchange transactions.

The CNB also supervises foreign exchange licence holders' compliance with the obligations laid down in Act No. 61/1996 Coll., on Some Measures against Money Laundering and on the Amendment of Related Acts, Act No. 69/2006 Coll., on the Performance of International Sanctions, and selected directly applicable EC legal rules.

28 List of foreign exchange regulations: http://www.cnb.cz – *Financial market supervision – Foreign exchange supervision – Foreign exchange regulations in force*. For a complete list, see the Czech version of the CNB website.

The CNB's supervision of electronic money institutions consists in monitoring compliance with the conditions in Article 19 of the Payment System Act, under which licences are granted. Information is obtained from regular half-yearly reports and other sources. The CNB may revoke a licence in administrative proceedings for a violation of the conditions. Experience with individual institutions is positive and no licence has been revoked so far.

4.5 ON-SITE EXAMINATIONS

The CNB's on-site supervision work involves both comprehensive and partial examinations. Comprehensive examinations cover all the activities of the examined entity. On-site examinations focus on checking compliance with the prudential rules for banks and other financial institutions, their proper financial management and the manner of identification and measurement of the risks they undertake. Attention is given to the methods used to measure, evaluate and monitor risks, to whether the information used in risk management is complete, reliable and up-to-date, and also to clear definition and assignment of responsibilities to competent departments and staff members. On-site examinations evaluate compliance with the prudential rules specific to individual markets. Checking the effectiveness of internal control systems is another integral part of on-site supervision. Partial examinations focus on only a specific area of activity of the regulated entity.

The supervisory departments draw up annual inspection plans based on off-site surveillance findings. They also take into account the time that has elapsed since the last on-site examination and indicators from the risk assessment system, where this system is used in the market segment concerned. Other factors reflecting the present or expected situation of the regulated entity are also considered.

4.5.1 On-site examinations at banks and credit unions

In 2006, the CNB continued to conduct on-site examinations at banks in accordance with EC directives, the conclusions and recommendations of EU and BCBS working groups, and other recognised principles and standards. Individual examinations were planned according to the results of previous examinations and also reflected recent developments in the relevant segment of the financial market.

Cooperation with foreign banking supervisors in the exercise of on-site supervision was expanded further in 2006. Cooperation was particularly close in the preparation and approval of advanced methods for the calculation of capital requirements for credit risk (Internal Ratings Based Approach) and operational risk (Advanced Measurement Approaches) introduced by some banks and financial groups.

All these aspects are gradually being reflected in the procedures applied in on-site examinations. The procedures and assessment benchmarks used by the CNB were also presented at domestic and foreign professional forums in 2006.

In 2006, a total of 17 on-site examinations were carried out in 2 banks, 4 building societies and 10 credit unions. These examinations focused on the management of credit risk, market risks and operational risks, including information systems risks, as well as on the prevention of money laundering and an overall assessment of the internal control systems of banks and credit unions. All these areas or a selected set thereof were inspected. One specialised extraordinary on-site examination was conducted in 2006.

The level of risk undertaken is closely linked with the quality of the procedures used to identify, measure, evaluate and monitor risks. Another important aspect of prudential business on the financial market is the completeness, reliability and timeliness of the relevant information used in decision making. Last but not least, there must be clear definition and assignment of responsibilities to competent departments and staff members of the bank or credit union. Verifying these aspects is a standard part of on-site examinations.

As in previous years, assessment and verification of the systems used by regulated institutions to prepare reports and statements for CNB Banking Supervision was another important output from on-site examinations. This information indicates the condition of individual institutions, thereby serving as a key prerequisite for effective and efficient off-site supervision. Examinations in this area concentrate primarily on examining procedures associated with the aggregation of primary data and the maintenance of data integrity and correctness when the individual statements are compiled.

Examinations of credit risk management systems

In 2006, the on-site supervision work in the area of credit risk management focused chiefly on the inspection of credit risk management systems in credit unions and examinations of IRB credit risk management systems in banks.

After taking over supervision of credit unions, the CNB conducted on-site examinations in ten such institutions, focusing on the adequacy and reliability of credit risk management systems. During these examinations, the CNB took into consideration the nature, scale and complexity of their activities and systems. The findings from these examinations are used to refine the on-site supervision methodology. The credit risk management system in one building society was also examined in 2006.

The other area on which the on-site examinations were focused was the validation of IRB credit risk management systems in banks. In this context, the supervisory methodology was continuously updated. In the near future, banking supervisors will use this methodology to determine whether IRB systems are correctly configured and effective, and will also conduct examinations in banks that do not currently use these methods.

Examinations of management of market risks, liquidity risk and risks associated with trading on financial markets

The examinations in the area of market risks involved inspecting systems for the management of market risks, liquidity risk, credit risk associated with trading on financial markets and risks relating to the execution, processing and settlement of transactions on the money and capital markets.

The examinations were targeted at checking whether organisational arrangements, staffing and risk management methods conform to the regulatory requirements with regard to the degree of risk undertaken and the strategy of the bank or credit union (business strategy and risk management strategy). The examinations focused on verifying and evaluating the quality of risk measurement methods, the correctness of input data and parameters, the sufficiency of the system of limits, the preparedness for a substantial change in market parameters, the sufficiency of information made available to top management, the sufficiency and independence of control mechanisms, segregation of conflicting duties and the reliability of the system for creating reports for the CNB.

At the request of one bank, an evaluation of an internal model for the calculation of capital requirements for general interest rate risk and foreign exchange risk was commenced in 2006. The evaluation process will be concluded in 2007.

In addition, a survey was prepared by a working group comprising representatives of the CNB and the CBA in connection with the finalisation of the CEBS *Consultation Paper 12 on Stress Testing under the Supervisory Review Process*. This survey was aimed at obtaining up-to-date information on the current and planned approaches of banks to stress testing of selected banking risks. The results of this survey will be used by the CNB to improve the regulation and supervision of financial institutions, and also by the regulated entities themselves.

Examinations of operational risk management, including IS/IT risks

In 2006, the CNB continued to conduct examinations of operational risks, launched in 2005 owing to the implementation of Basel II and the growing role of operational risk in banking.

The on-site examinations focused mainly on compliance with the regulatory requirements in force. As regards operational risk management systems, emphasis was put on the way in which banks and credit unions identify the risks of loss due to shortcomings in internal processes, the human factor, systems, external events and non-compliance with legal regulations. In this context, it was evaluated whether the causes of the risks identified are assessed, whether alternatives applicable to the management thereof are considered and whether decisions on specific solutions are made. Taking into account the scale and nature of the activities of the examined entities, the appropriateness of the responsibilities and duties assigned with respect to these operational risk management activities was evaluated. Special attention was also given to issues relating to business continuity management and outsourcing.

The risks associated with information systems and information technology are traditionally a significant component of examinations of operational risk. This is linked with the rising influence of this area on the overall risk profile of regulated entities. CNB Banking Supervision again focused on assessing information security systems in 2006. In addition to the settings of control processes, their actual impact on specific procedures and measures in the areas of physical, logical and personal security was evaluated. Security aspects were also dominant in the evaluation of the development and operation of information systems. In 2006, the CNB devoted increased attention to electronic banking, pointing out risks connected with internet banking and supplementing its on-site examination procedures.

On-site supervision also involved preparations for the approval of advanced methods for determining the capital requirement for operational risk (AMA).

Examinations of the operation and effectiveness of internal control systems
Examinations in this area are conducted as part of the comprehensive examinations of risk management systems. Components of internal control systems are assessed as integral parts of the management of individual risks, and the whole area of internal control systems is evaluated separately as internal governance. In the latter case, the following components of a bank's or credit union's internal control system are examined: corporate governance principles, the compliance function (based on international directives, standards and guidelines, in particular the BIS's April 2005 document *The Compliance Function in Banks* and the CEBS's January 2006 *Guidelines on the Application of the Supervisory Review Process under Pillar 2*) and the internal audit function.

Examinations in the area of corporate governance focus on evaluating the organisational structure of the bank as a whole, the functioning of the bank's bodies and their committees, and the links and information flows between such bodies and committees. The examinations also involve checks of the control environment, including the individual control mechanisms built into the bank's activities.

In the area of compliance, the examinations focus on verifying the compliance function system, which involves monitoring legislative changes, disseminating information about such changes within the bank and incorporating relevant changes into internal regulations. The parameters of the bank's internal regulations are also verified, in particular as regards whether they conform with the legislation in force, whether they are complete, intelligible and consistent, and whether staff abide by them.

In the area of internal auditing, the examinations focus on the organisation, methodology and staffing of the internal audit department. The prerequisites for ensuring the independence of the internal audit department within the bank, its links to each of the company's bodies and its links within the financial group are evaluated. Risk analysis and the related internal audit planning process, the audit activities themselves (including the quality of the outputs generated by each audit) and the quality of the auditor's file are also examined. The system for monitoring remedial measures is also subject to examination, in particular as regards whether the bank's management pays sufficient heed to the elimination of shortcomings identified by the internal audit department or other bodies.

Anti-money laundering
The examinations evaluate the operation and effectiveness of the AML[29] system. Supervisors focus on the compliance of the bank's system with Act No. 61/1996 Coll. and CNB decrees, the application of appropriate "know-your-customer" policies and the bank's ability to identify and analyse suspicious transactions and to notify the Ministry of Finance's Financial Analytical Unit (FAU) within the set time limit. The examinations also verify the strategy and internal control system in this area. The CNB works closely with the FAU in this respect.

Basel II implementation as regards advanced methods for determining capital requirements
Under the new capital adequacy framework (Basel II), in the wording of EU Directives 2006/48/EC and 2006/49/EC, banks are allowed to use advanced approaches based on mathematical models in order to calculate capital requirements for credit risk (IRB) as from 2007 and for operational risk (AMA) as from 2008.

In 2006, the two teams set up in order to examine the advanced methods continued consultations with banks that have shown an interest in using the IRB or AMA approach in 2007 or later. The activities of the teams included ongoing communication with foreign banking supervisory authorities in order to establish a common approach to validating these advanced approaches in multinational banking groups. Several meetings were held on this issue in 2006, with intensive meetings continuing into 2007.

29 Anti-money laundering.

Intensive pre-validation[30] meetings on the IRB approach were conducted in four banks, while the AMA approach was addressed by CNB staff in three banks. At the request of the foreign regulators of two parent banks of banks in the Czech Republic, pre-validation of the IRB approach in these cases progressed to the validation phase proper. These processes should result in the approval of the use of this model for calculating capital adequacy in two multinational groups. The banks concerned will be allowed to use the models for reporting capital adequacy only after the adoption of an amendment to the Act on Banks implementing Basel II and the issuance of a relevant implementing decree.

Foreign technical assistance
In 2006, as in previous years, the CNB provided foreign regulators with technical assistance. Two employees of the Banking Regulation and Supervision Department shared their experience in the operational risk field with banking supervisors from Morocco in a project coordinated by the Financial Services Volunteers Corp, a US non-profit organisation.

4.5.2 On-site examinations in capital market institutions

In the area of collective investment and pension funds, four inspections of the internal operations of investment companies were commenced in 2006 (inspection reports were issued by 31 December 2006 in three cases). These inspections focused on identifying potential shortcomings concerning compliance with the prudential rules and the rules of organisation of the internal operations of investment companies, particularly in terms of internal regulations, the investment process and the process of execution of transactions in investment instruments or other assets, the process of issuing, registering and repurchasing securities of a collective investment fund, the reconciliation rules, the process of valuation of assets in mutual funds, the operation of the internal control system, control and security measures for the processing and recording of data, and procedures designed to prevent conflicts of interests. No serious violations of the legal regulations were found within the scope of the inspection remit. Minor shortcomings were discussed with the inspected entities during the inspections and rectified either during the inspection proceedings or according to set time schedules.

In 2006, two inspections of depositories, commenced by the former Czech Securities Commission, were completed without serious findings. The inspections focused on risk assessment of the depositories' activities. Such assessment is a necessary condition for setting priorities and objectives for the inspection work, owing to depositories' vital and primary function in the supervision of investment companies and investment funds. By dint of its authorisations and duties, a depository is able to actively intervene *ex ante* in the event of potential breaches of duties associated with the management of assets in mutual funds. One inspection of a depository was commenced during the period under review, and a report on the inspection – with no serious inspection findings – was issued by the end of 2006.

In addition, five inspections were commenced focusing on risk assessment of pension funds and compliance with the rules for the management of assets entrusted to third parties and rules for the calculation of the fair value of assets. Shortcomings in pension fund asset management agreements were identified in two cases. A schedule for novation or the conclusion of new agreements was agreed with the inspected entities during the inspection proceedings, such that the agreements fully respected the legislation effective as of 1 April 2006.

Five on-site examinations were commenced in the area of investment service provision (four in investment firms and one in an investment intermediary). These were either comprehensive inspections or inspections focusing on compliance with rules for prudent provision of investment services (in particular, administrative and accounting principles, internal control systems, financial risk management systems and liquidity management systems) and rules of conduct towards clients. The inspections focused both on entities in respect of which shortcomings had been detected during a previous inspection and on entities in respect of which an inspection had not previously been conducted. The aim was to fully review the supervised entities on the financial market in the field of investment service provision.

30 A preliminary informal examination of advanced methods for the calculation of capital requirements before a bank or a financial group as a whole applies to use these methods for regulatory purposes.

Unlike in previous periods, the inspections in the capital market sector revealed no acute problems, although some quite serious violations of the legal regulations were detected. Many formal shortcomings were identified and in many cases the internal regulations of investment firms had not been complied with. There were also problems concerning records of client assets and the method of carrying out reconciliations between actual stocks of client assets and the stocks reported in investment firms' trading systems. One of the frequent shortcomings was ineffective internal control systems.

Actions following up on state inspections commenced in the previous period were completed. This included in particular the completion of five objection proceedings, including the subsequent enforcement of remedial measures and imposition of penalties. The investment firm licence of AFIN BROKERS, a. s., was revoked, owing to persisting serious shortcomings and clients' complaints relating to the provision of investment services.

An on-site inspection was conducted in the OTC market operator RM-Systém, a. s. This focused on the functioning of the system of measures to detect market manipulation and insider trading. The inspection led to requirements to modify and extend the system. These were gradually met.

On-site inspections also covered duties for issuers of listed securities or their shareholders arising from relevant provisions of the Commercial Code in the context of takeover bids and public share-purchase contract offers relating to listed securities. This primarily involved supervision of the proper publication and conduct of takeover bids with respect to the core principles laid down in the Commercial Code.

4.5.3 On-site examinations in insurance undertakings

In its on-site examinations in 2006, the CNB focused its attention on financial placement (investment) and the creation and application of technical provisions. As regards financial placement, the CNB monitors and verifies the sufficiency of financial placement of assets arising from technical provisions. Great emphasis is put on the quality of other financial placements (free assets) which supervised entities do not include in the lists of assets under technical provisions. The quality, volume and appropriate fair value measurement of such financial placements are significant factors indicating a sound and financially stable insurance company. As regards the inspection of technical provisions, the CNB examines the manner of creation and application of technical provisions created by inspected entities, and whether the amount of such technical provisions is sufficient. The quality of loss adjustment processes is assessed on a selected sample of insurance claims. Attention is also paid to the manner and quality of data transmission from the operating systems to the accounting systems of insurance companies.

At the start of 2006, the CNB completed two on-site inspections launched in 2005. It commenced 11 new inspections, of which inspection reports had been delivered to the representatives of nine inspected entities by the end of 2006. The remaining reports were completed and delivered in early 2007.

The examinations conducted in 2006 most frequently detected shortcomings arising from non-compliance with provisions of the Accounting Act (failure to measure financial placements at fair value, failure to record all facts subject to accounting, or recording them in a period other than that to which they relate, failure to make a stocklist of assets and liabilities under the Act) and the Insurance Act (imprudent behaviour by supervised entities in the performance of their activities, insufficient creation of technical provisions, failure to respect the principle of financial placement liquidity, no internal regulation governing the activities of the responsible actuary) and also shortcomings arising from non-compliance with internal guidelines (insufficient or erroneous regulations, non-compliance with legislation in force and failure to provide adequate internal control functions).

Of the total number of inspections completed, the CNB received objections to the wording of inspection reports from two supervised entities. The objections were decided on at the beginning of 2007. In the other cases, the supervised entities did not exercise their right to file objections and notified the CNB in writing of the measures adopted and the manner of elimination of shortcomings, including the setting of deadlines for eliminating them. Compliance with these measures was monitored throughout the year and continues into 2007.

In 2006, the CNB opened no administrative proceedings regarding the imposition of measures to eliminate shortcomings. This was partly because the inspection findings were not serious enough to pose a threat to financial stability and the enforceability of the inspected entities' liabilities, and also because the proceedings concerning the inspected entities' objections had not yet been completed in this period.

4.5.4 On-site examinations in other regulated entities

The CNB conducts on-site foreign exchange examinations through its branches. The aim of the inspections is to effectively verify all activities performed by a particular non-bank foreign exchange entity and its individual establishments. A total of 489 on-site foreign exchange examinations were conducted in 2006. Breaches of legal regulations were found in 393 cases.

The CNB is not authorised by law to conduct on-site examinations of entities that issue electronic money pursuant to Article 19 of the Payment System Act.

5. INTERNATIONAL COOPERATION

5.1 COOPERATION WITHIN THE STRUCTURES OF THE EUROPEAN COMMISSION

EBC

As in previous years, CNB Banking Supervision worked in partnership with the Ministry of Finance, through a technical expert, in preparing for and participating in the meetings of the Lamfalussy process Level 2 committee – the European Banking Committee (EBC).[31]

The EBC continued with its 2006 projects, which mainly concerned cross-border mergers and acquisitions, large exposures, own funds, deposit-guarantee schemes and regulation of electronic money institutions. Usually in cooperation with CEBS, current regulations and practices are being examined in order to propose potential changes in regulations to make them simpler, more transparent and convergent across financial sectors.

Specific results in 2006:
- draft amendments to sectoral directives regulating the conditions for the acquisition of holdings in regulated financial entities;
- discussion of the first report on the review of large exposures and a decision to continue the project into 2007, focusing on improving and simplifying the regulations, ensuring consistency of application across EU member states, and reporting;
- examination of the composition of own funds in EU member states and a decision to continue the project, focusing on hybrid forms of capital and the method of inclusion thereof in capital for regulatory purposes.

As regards the proposed review of the regulatory framework for electronic money institutions, the Czech Republic asked for resolution of the issue of hybrid issuers, e.g. telephone services providers. It disagreed with the plan to convert unlicensed institutions into licensed ones by applying exemptions laid down in the directive.

A new project in 2007 will examine liquidity management, following criticism from financial market participants of liquidity regulation, in particular the fact that regulators' inconsistent liquidity management requirements are hindering the application of suitable methods and giving rise to higher costs. It has been proposed that problems should be identified and existing regulatory practices analysed.

In 2006, CNB Banking Supervision nominated its representative for the EC's new Capital Requirements Transposition Group, which deals with the interpretation of the new capital adequacy directives.

CEBS

The aims of the Committee of European Banking Supervisors (CEBS), in which the CNB has a representative, are to achieve better regulation, to promote convergence in approaches to regulation and supervisory practices, and to enhance cooperation in the event of cross-border banking crises. In 2006, the Committee issued ten sets of guidelines on specific areas arising from the new directives introducing Basel II, prepared in three standing working groups (the Groupe de Contact, the Expert Group on the Capital Requirements and the Expert Group on Financial Information). The CNB is also represented in these working groups. The guidelines concern financial reporting and capital adequacy, stress testing, concentration risk, outsourcing, interest rate risk in the banking book, validation of advanced methods for the calculation of capital requirements, cross-border cooperation between supervisory institutions, banking supervision and recognition of rating agencies.

The guidelines were assessed internally on an ongoing basis in terms of their application, so that the existing regulatory framework could be refined or extended or new regulations developed. The implementation of CEBS banking supervision guidelines mostly takes the form of Official Information, through which the CNB specifies requirements concerning regulated entities and expresses its expectations.

31 The European Banking Committee is an advisory committee to the European Commission in the banking area

In 2006, CEBS, working in partnership with the BSC,[32] continued to prepare guidelines to help improve cooperation between individual European regulators and central banks for dealing with crises on financial markets, and to harmonise procedures for resolving such crises between individual countries. Findings from an international crisis simulation exercise held in April 2006 were also used in the preparation of the rules. The final text of the guidelines was approved by both committees in March 2007.

Surveys conducted in connection with calls for advice from the European Commission were another important aspect of CEBS's work. These primarily concerned a planned modification of the conditions for acquiring holdings in regulated entities, the practices of banks and supervisory institutions on large exposures, the prudential rules for commodities trading, the definition of own funds and the existing regulation of own funds.

The organisational foundations were laid in 2006 for a change in CEBS's orientation, from the issuing of guidelines to the delivery of a convergent supervisory framework. A project on operational networking was launched to identify and address practical issues emerging in the implementation of the Basel II directive and CEBS guidelines. The project comprises seminars and case studies, in which CNB representatives participate. As CEBS's orientation changes, the means it uses are also changing. In the future, attention will be paid to assessing the implementation of CEBS guidelines in the practices of banks and supervisory institutions. In this context, surveys will be used more frequently. Consideration is also being given to the creation of catalogues of practical supervisory responses in specific areas (e.g. on the validation of advanced approaches to risk management), FAQs and discussion forums. An expert discussion group, NOVI (Network on Validation Issues), in which the CNB has two representatives, was established in 2006.

CESR

The CNB worked closely with the Committee of European Securities Regulators (CESR), where it is represented in all key working groups. It is actively involved in the operational groups CESR-Fin (accounting and auditing) and CESR-Pol (market integrity) and in the sub-groups European Enforcers Coordination Sessions and Surveillance and Intelligence. The CNB also participates in the work of other CESR working groups, in particular the MiFID Level 3 expert group in relation to the implementation of the new Directive on Markets in Financial Instruments (MiFID). In the field of collective investment it is involved in the Investment Management expert group. As regards IT issues, CESR works in cooperation with the IT unit in the CESR-Tech group, which is implementing provisions of the European legislation that affect this area. The current activities are linked primarily with the introduction of a duty to exchange transaction reporting data between supervisory authorities (the TREM project). The CNB is also involved in the work of the Review Panel, which monitors compliance with CESR standards and guidelines.

The main areas of cooperation with CESR were concentrated in the following operational groups in 2006:

CESR-Fin coordinated the work of CESR members in the area of accounting and auditing. It supported cooperation in the implementation of international accounting standards. It also enhanced cooperation with third country supervisory authorities. The main full-year objective of the group was to support the application of international accounting standards in the EU through monthly European Enforcers Coordination Sessions.

CESR-Pol coordinated the work of CESR members in the monitoring of market integrity and the exchange of information between regulators. It established working groups to promote closer cooperation and to ensure consistent and effective application of key European directives. One of its sub-groups, the Surveillance and Intelligence Group, was set up to provide a forum for individual regulators to share their experience of cases of market abuse. In addition, Urgent Issues Groups were formed for joint investigations of specific cases of market abuse.

A new MiFID Level 3 Expert Group was established by CESR in connection with the implementation of key capital market legislation. The group undertook work to deliver supervisory convergence in the day-to-day application of the above legislation and set up two working sub-groups: MiFID Markets and MiFID Intermediaries. In the second half of 2006, the group prepared a consultation paper on the single European passport of

32 See section 5.2 *Cooperation within the structures of the European Central Bank*

investment services providers and was engaged in the preparation of other consultation papers related to the MiFID implementation.

The expert group on collective investment published rules for simplified notification by UCITS[33] funds. In the second half of the year, the group discussed reports by three expert groups established by the European Commission proposing recommendations to increase the efficiency of the UCITS market and addressing issues relating to hedge funds and private equity funds. The group sent its position on the issues to the Commission at the end of 2006.

The Prospectus Expert Group addressed specific problems regarding the implementation of the prospectus legal framework. In July 2006, the group published a guide for market participants which contains joint responses from supervisory authorities to questions on the preparation of prospectuses. The purpose of this guide is to provide market participants with greater certainty and quick answers to queries. The group started to analyse the practical functioning of the prospectus legal framework in the second half of 2006.

A new CESR-Tech Expert Group was established by CESR in May 2006 to deal with IT projects stemming from EU legislation (e.g. the transaction reporting exchange mechanism).

The CESR also established an ECONET group bringing together economic experts from member institutions. At the end of 2006, ECONET developed an impact analysis methodology in order to survey the impacts of CESR guidelines on market participants. This work supports the European Commission's policy of better financial market regulation.

In mid-2006, CESR presented a detailed report containing the specific steps it is taking to improve supervisory convergence in the EU to the Financial Services Committee (FSC).[34] The FSC is a political platform for discussions between representatives of EU ministries of finance. In 2006, CESR also discussed joint training programmes and staff exchange. Emphasis was put on regulatory harmonisation and the implementation of CESR guidelines and standards. Compliance with these guidelines and the mapping of supervisory authorities' powers in relation to specific European directives is dealt with by a Review Panel set up for this purpose.

CEIOPS

CEIOPS is in a rather different situation than the other two Level 3 committees. While the new EU banking and capital markets legislation (Basel II, MiFID) has already been passed and supervisory authorities' committees are already creating and implementing guidelines elaborating individual areas of these directives, the key insurance directive is still being prepared. CNB representatives are contributing to the preparation of the Solvency II directive in the Pillar 1 and Pillar 3 working groups and in the working group for insurance groups.

In 2006, CEIOPS delivered to the European Commission final answers to the third wave of Calls for Advice relating to eligible forms of capital, cooperation between supervisory authorities, provision of supervisory information and disclosure of information, procyclicality and small insurance companies. Based on further requests from the Commission and at CEIOPS's own initiative, further advice was drawn up in the area of requirements for internal risk and capital assessment, harmonised supervisory powers, group supervision, reporting and disclosure of information, etc. The second round of the QIS impact study was conducted in 2006, based on which the calculation of capital requirements using a standard formula was further elaborated.

In addition to drafting technical advice, CEIOPS is also gearing up for the adoption and application of the new rules. At the request of its members, it organised the first of a series of seminars for inspectors of insurance undertakings. This was attended by the CNB representatives who are going to inspect compliance with new regulations.

33 Undertakings for Collective Investment in Transferable Securities.

34 The Committee was established by EU Council decision in 2003. The activities of the FSC include strategic issues of the integration of the financial market in the EU, financial stability and crisis management, regulatory and supervisory structures, international cooperation and other issues relating to European financial markets.

CEIOPS regularly assesses conditions on the European insurance market and to this end collects data from its members. Twice a year it publishes a report on developments and financial stability in the insurance sector, which is sent to other European institutions and authorities (e.g. FSC, EFC).

Other issues addressed by CEIOPS included closer cooperation and exchange of information about insurance intermediaries providing services on the basis of the single licence, under the Luxembourg Protocol. A similar protocol regulating cooperation and the exchange of information was agreed for occupational pension funds (the Budapest Protocol).

Cooperation between CEBS, CESR and CEIOPS

Last year saw closer cooperation between CEBS, CESR and CEIOPS under a 2005 joint protocol on cooperation between these three Level 3 committees (sometimes referred to as 3L3). An Interim Working Committee on Financial Conglomerates (a Level 3 committee) was established at the joint initiative of CEBS and CEIOPS. It produced an extensive study comparing the conditions for the application of the different forms of capital stipulated by European sectoral regulations. The CNB is represented in this committee. In 2007, the group will deal with regulation and practical supervision of intra-group transactions and concentration risk within conglomerates in member countries. In the second half of 2006, the 3L3 committees also concentrated on comparing substitute products available on financial markets. Now that financial market supervision has been integrated into the CNB, its representatives in the above committees can communicate more effectively and thus better coordinate joint positions on cross-sectoral issues.

5.2 COOPERATION WITHIN THE STRUCTURES OF THE EUROPEAN CENTRAL BANK

The CNB has representatives in the Banking Supervision Committee and in the Working Group on Macro-Prudential Analyses and the Working Group on Developments in Banking.[35] CNB Banking Supervision has also had a representative in the Working Group on Credit Registers since 2006.

In 2006, the BSC's activities focused on liquidity management analyses, major risks to the largest banks, evaluation of financial stability, and the cyclical and structural development of the European banking system. Particular attention was paid to cooperation in resolving cross-border banking crises. In April 2006, three representatives of the CNB and the Ministry of Finance took part in the first large crisis exercise, the aim of which was to examine on a model case whether central banks, supervisory institutions and ministries of finance are able to cooperate. Similar exercises will take place again in the future.

The Working Group on Credit Registers organised a seminar for countries that plan to integrate into the existing registers in EU countries. The individual systems were presented at this event. The CNB will accept integration in the next two or three years, after all the necessary legislative and technical conditions have been met.

5.3 COOPERATION WITHIN THE BASEL COMMITTEE ON BANKING SUPERVISION (BCBS)

As in previous years, the CNB participated through its representatives in the Core Principles Liaison Group (CPLG) and the Working Group on Capital (WGC). An amendment to the Core Principles for Effective Banking Supervision, which should be in line with best international practices, was finalised in 2006. The amended rules were endorsed and officially published at an international conference of supervisors held in Mexico in October 2006. The amended Core Principles, the number of which remains the same (25), take into account the development of banking services, eliminate duplications and are aligned with other international standards.

The WGC focused on some key aspects of the new Basel II capital adequacy framework (e.g. national discretions and principles of cooperation between host and home supervisors).

35 Banking Supervision Committee (BSC), Working Group on Macroprudential Analysis (WGMA), Working Group on Developments in Banking (WGDB).

5.4 COOPERATION WITHIN THE GROUP OF BANKING SUPERVISORS FROM CENTRAL AND EASTERN EUROPE (BSCEE)

The CNB remains a member of the BSCEE and is involved in its activities. Two seminars and an annual conference in Montenegro were held in 2006. The group, established 16 years ago, has 19 members, 9 of which (including Bulgaria and Romania) were non-EU members at the end of 2006.

5.5 COOPERATION WITHIN THE INTERNATIONAL ORGANIZATION OF SECURITIES COMMISSIONS (IOSCO)

IOSCO was established in 1983. Its vision is to cooperate together to promote high standards of regulation in order to maintain just, efficient and sound capital markets. The CNB is represented by the Capital Market Regulation and Supervision Department, which is mainly involved in the European Regional Committee and the Emerging Markets Committee.

In 2006, discussions were held with IOSCO on the CNB's accession to the Multilateral Memorandum of Understanding. IOSCO's Verification Committee decided to recommend that the CNB be invited to sign the Multilateral Memorandum of Understanding, which will establish a framework for cooperation with the other signatories to the MoU – the 34 IOSCO members. The Memorandum will replace the existing bilateral MoUs.

5.6 COOPERATION WITHIN THE INTERNATIONAL ORGANISATION OF PENSION SUPERVISORS (IOPS)

At its meeting on 14 December 2006, the CNB Bank Board approved CNB membership of IOPS with effect from 1 January 2007. The expected benefits of membership include participation in its working groups dealing with issues relating to the supervision of pension funds, the opportunity to be involved in creating international standards for the regulation and supervision of pension funds, and exchange of information and experience in tackling issues common to pension fund supervisory authorities.

5.7 COOPERATION WITHIN THE INTERNATIONAL ASSOCIATION OF INSURANCE SUPERVISORS (IAIS)

Although the CNB partially scaled down its involvement in the meetings of IAIS working committees and subcommittees, it actively monitored work on individual standards and recommendations in 2006.

5.8 COOPERATION WITH PARTNER SUPERVISORY AUTHORITIES

Cooperation with partner banking supervisors focused on exchange of information on banks and other members of financial groups operating in both countries, on the division of tasks between host and guest banking supervisors in the examination of models for calculating capital requirements under Basel II, and on the sharing of information on the progress of such examinations. Four of the 11 meetings held were multilateral (meetings of interested supervisors of groups were organised by host supervisors).

Memoranda of understanding (MoUs) remain the formal basis for wider cooperation. Exchange of information is focusing increasingly on the sharing of experience between experts, especially in the context of Basel II implementation.

Capital market supervisors cooperated on an ongoing basis with foreign capital market supervisors and regulators, in particular those from EU Member States. Notification procedures were held, information on supervised entities was exchanged and experience was shared on a bilateral basis. Foreign entities and individuals were also provided with basic information about regulation, legislation and the structure of the Czech capital market.

The CNB signed an MoU with the Swiss insurance supervisor at the end of November 2006. This MoU, relating to exchange of information and cooperation in supplementary supervision of insurance groups, was created by CEIOPS and was signed by all its members. It thus took its place alongside the other MoUs that the former Czech Office of the State Supervision in Insurance and Pension Funds signed in the past with the German, Slovak, Polish and Austrian insurance supervisors.

As regards supplementary supervision of insurance groups, the CNB attended several coordination committee meetings organised by supervisors from countries whose insurance corporations have a significant share of the Czech market (Austria and the Netherlands). Common procedures for supplementary supervision are created in the CEIOPS Insurance Groups Supervision Committee, in which the CNB has a representative. Cooperation with partner supervisory authorities was also enhanced in supplementary supervision of financial conglomerates, with either the partner supervisor or the CNB acting as coordinator. This mainly involved the identification of financial conglomerates and consultations on methods for calculating supplementary capital requirements in such financial groups.

Statistical information on the performance of insurance corporations under the freedom to provide services (data on the amounts of premiums written, claim payments and commissions paid) continued to be exchanged with EU/EEA supervisory authorities in the second half of 2006. The 2005 data for 14 EU/EEA states were available at the end of 2006.

B. THE FINANCIAL MARKET IN 2006

SUMMARY

The developments on the Czech financial market in 2006 can be assessed as positive. No serious events endangered its stability and safe operation. Most financial market participants also enjoyed stability in 2006. The performance of the individual financial institutions was positively affected by the favourable macroeconomic situation.

As regards the number of banks and their ownership, the structure of **the Czech banking sector** has been stable for several years now. A total of 24 banks and 13 foreign bank branches were operating in the Czech banking sector at the end of 2006, i.e. only 1 branch more than in 2005. As of the end of 2006, a total of 137 banks from EU countries could also provide banking services in the Czech Republic after notifying the CNB of this activity under the freedom to provide services. The CNB received 33 such notifications during 2006. About 97% of the banking sector's assets are directly or indirectly controlled by foreign entities.

Dynamic growth in loans provided to households and non-financial corporations continued into 2006. Loans to non-financial corporations increased by 21.0% to CZK 635.3 billion and loans to households by 30.4% to CZK 494.9 billion. As regards households, growth was recorded particularly for mortgage and other housing loans, which rose by 32.5% to CZK 371.3 billion. At the end of 2006, housing loans accounted for three-quarters of all loans to households. Consumer credit grew by 22.8% to CZK 109.2 billion.

The banking sector saw no fundamental changes in 2006 with respect to risks undertaken. Credit risk remains the main risk, with its importance still growing due to the increasing volume of loans provided. Classified receivables from clients rose by 23.6% year on year, to CZK 154.4 billion. This, however, was due chiefly to an increase of 29.6% in the least risky category (i.e. watch loans), to CZK 100.9 billion. Non-performing loans (NPLs) rose by 13.7% to CZK 53.5 billion. As this relative increase was smaller than that of the total loan portfolio, the share of NPLs in total loans fell from 4.4% to 4.1% in 2006.

In principle, domestic banks still focus only on the domestic market, as reflected in a relatively low share of transactions with non-residents and a low proportion of foreign currency activities. Operations on foreign markets are usually executed by other entities from the financial group to which the domestic bank belongs. As regards securities, banks invest most in government and bank bonds and to a lesser extent in corporate bonds. The volumes of shares or units held by banks are negligible. Open positions from derivatives transactions tend to be minimal. More sophisticated transactions tend to be executed at the level of parent banks, as they have the necessary resources and better access to wider markets.

The capital ratio of the banking sector decreased by 0.45 percentage point to 11.41% in 2006, owing to a greater increase in capital requirements (mainly due to the growing loan portfolio) than in regulatory capital. Another reason is that the banking sector's capital was augmented to a lesser extent by retained earnings in 2006 than in previous years, owing to high dividend payments by some banks. Although some banks accepted subordinated debt or issued subordinated bonds, which are included in Tier 2, Tier 1 still has a dominant position in the sector's capital, accounting for roughly 85% of total regulatory capital.

The profit achieved by the Czech banking sector reflects the relatively good performance of the whole economy in 2006. The banking sector generated an unconsolidated net profit of CZK 37.9 billion. This represents a year-on-year decrease of CZK 1.2 billion (3.1%), due chiefly to higher income tax.[36] Pre-tax profit was practically the same as in 2005. Interest income has increased significantly in recent years owing to the growth in loans. On the other hand, this has been partly offset by rising administrative expenses and higher net creation of reserves and provisions. The effect of one-off extraordinary income was much lower in 2006 than in 2005.

36 The reason is higher deferred tax. By contrast, payable income tax decreased slightly year on year, owing to a lower tax rate.

At the end of 2006, **the sector of credit unions** consisted of 20 active credit unions, the same number as in 2005. The number of credit union members rose from 30,611 to 42,451 in 2006, i.e. by around 39%.

The credit unions sector has seen relatively rapid growth in recent years. In 2006 alone, the sector's assets grew by almost 70% to CZK 7.0 billion. The sector as a whole generated a profit of around CZK 84 billion in 2006, more than double that in 2005.

The situation on **the Czech capital market** in 2006 can also be assessed as positive overall. Most capital market participants experienced no major changes or dramatic events. This period saw intensive preparations by all parties involved for the changes to be made in 2007 linked with the implementation of Basel II and MiFID. The number of capital market undertakings from EU countries that notified their interest in operating in the Czech Republic, grew significantly during the year.

Trading volumes on both regulated markets – the Prague Stock Exchange (PSE) and the OTC market organised by RM-Systém (RM-S) – decreased compared to 2005. The PSE saw a decrease of about 8%, from CZK 1,574.4 billion to CZK 1,447.8 billion, while RM-S recorded a fall of almost 41%, from CZK 6.6 billion to CZK 3.9 billion. The main indices on both markets, however, recorded price increases. The PSE's PX index rose from 1,473.0 points at the end of 2005 to 1,588.9 points at the end of 2006, i.e. by 7.8%. RM-S's PK 30 index showed even stronger growth of 9.7%, from 2,364.9 points to 2,595.3 points. In July 2006, the CNB granted the PSE a permit for trading in new types of investment instruments, as a result of which investment certificates and warrants appeared on the market in 2006 Q4.

The number of investment firms licensed by the CNB fell further in 2006, to 46. During 2006, no new investment firm licences were granted, 2 such licences were withdrawn and 3 such licences expired owing to changes in objects of business. As of 31 December 2006, the CNB registered a total of 436 foreign entities (143 banks and 293 non-banks) authorised to provide investment firm services in the Czech Republic under the single European licence. Twelve of these were providing investment services via a branch. As of 31 December 2006, investment firms had concluded a total of 1,149 thousand contracts with clients, of which about 180 thousand were active. Client assets amounted to CZK 991 billion and the funds managed in individual portfolios totalled roughly CZK 325 billion.

At the end of 2006, a total of 13 investment companies licensed by the CNB, managing 77 open-end mutual funds, were active in the collective investment area. The number of foreign collective investment undertakings offering products in the Czech Republic increased further, to 58 companies with 1,282 funds and sub-funds. The undertakings licensed by the CNB managed CZK 156.2 billion in mutual funds at the end of 2006.

The number of pension funds remained unchanged in 2006, at 11. The total assets managed by pension funds amounted to CZK 145.9 billion at the end of 2006, up by around CZK 22.5 billion compared to the previous year. There were 3.6 million pension planholders at the end of 2006.

In the securities issuance area, the CNB supervised 92 issuers of listed securities, 8 of which were foreign. There were 51 bond issues in 2006, of which 17 were issues of listed bonds and 34 were issues of unlisted bonds. The CNB conducted 16 administrative proceedings relating to takeover bids or public share-purchase contract offers in the period under review. The CNB issued 79 decisions connected with squeeze-outs in 2006. It granted consent in 52 cases and denied consent in 22 cases, and 5 administrative proceedings were discontinued due to withdrawal of applications. A total of 29 foreign entities made use of the single passport during 2006 (securities of 3 issuers were admitted to trading on the regulated market based on notifications). A total of 63 prospectuses, base prospectuses and supplements to prospectuses were notified. The CNB gave notification of one prospectus abroad.

There were 33 domestic insurance undertakings active on **the Czech insurance market** in 2006, the same as in 2004. As regards the ownership structure of domestic insurance undertakings, foreign ownership predominates and the share of foreign capital in the total equity capital of domestic insurance undertakings is gradually increasing. The number of branches of foreign insurance undertakings increased from 12 to 16. The number of insurance undertakings from other EU or EEA countries intending to operate on the Czech insurance market under the freedom to provide services also rose, to 401, fostering growth in competition.

Gross premiums written amounted to CZK 122.1 billion in 2006, up by only 4.3%. This confirms the trend of 2005 and 2004, when growth rates were much lower than between 1996 and 2003. Growth was stronger in life insurance. Life premiums written grew by 5.1% in 2006, compared to only 1.7% the previous year. By contrast, non-life insurance showed lower growth than in 2005 (3.8%). The share of life insurance in total premiums written edged up to 38.7%. GDP has been rising faster than premiums written since 2004. Insurance penetration, as measured by the ratio of premiums written to GDP, has since then decreased by 0.1 percentage point each year, and stood at 3.8% in 2006.

This relatively low growth in life insurance premiums was probably due to households' preference for alternative financial products, such as building savings schemes, private pension plans, mutual fund units and mortgage-financed property investment. With respect to non-life insurance, the main probable reasons include strong competition among insurance undertakings themselves, augmented by the freedom to provide services in EU and EEA countries, which has led to a stagnation in premium rates.

The Czech insurance market is highly concentrated. The three largest insurance undertakings account for more than 62% of total premiums written. However, the concentration is gradually decreasing as a result of growing competition. Greater concentration is visible in non-life insurance.

Turning to the life insurance market, dynamic growth is being recorded by investment life insurance, whose share increased by 7.2 percentage points year on year to 24.0%, mainly at the expense of traditional assurance on death or survival, which recorded a share of 58.7% and still dominates the market. The most important segment of the non-life insurance market is motor third party liability insurance (30.0%), followed by insurance against damage to or loss of property (23.9%) and insurance against damage to or loss of land vehicles (20.7%). In 2006, the strongest growth was recorded for credit insurance.

Total claim settlement costs rose by 5.9% year on year, to CZK 56.7 billion. Claim settlement costs in non-life insurance rose by 12.0%, mostly due to several natural disasters in the first half of 2006. This, however, had no major negative effect on insurance undertakings' performance.

The total assets of insurance undertakings increased by 4.0% compared to 2005, to CZK 322.9 billion. The growth in assets was lower than in previous years, when it had been around 10%, chiefly thanks to transactions relating to sales of holdings in subsidiaries. Debt securities, which showed annual growth of 16.6% and accounted for almost 60% of total assets, are the most important asset item. The share of technical provisions on the liabilities side was 73%, an increase of 11.2%.

The favourable results of insurance undertakings are confirmed by their net profit, which was 82.1% higher than in 2005, reaching CZK 14.6 billion, the best result in the history of the Czech insurance market. Profits rose in both life and non-life insurance and were also greatly affected by one-off income from sales of ownership interests.

METHODOLOGICAL NOTE

The data in part B of the Financial Market Supervision Report are based mainly on statements submitted regularly to the CNB for supervisory purposes under the relevant legal rules. To better illustrate the situation, other information is sometimes also used, with the relevant source being cited. Many of the statements for the CNB are based on the accounting data of individual entities and thus reflect the accounting methods they apply. As from 1 January 2005, issuers of securities listed on regulated markets in EU member countries have used international accounting standards (IAS or IFRS) as laid down in European Community law to keep their accounts and compile their financial statements. Many regulated entities thus compile financial statements according to IAS/IFRS under this duty, while others continue to apply Czech accounting standards. However, the accounting procedures under the Czech accounting standards for banks and some other regulated financial institutions are almost the same as the IAS/IFRS procedures.[37]

The comparability of the 2005 and 2004 data on some selected items and indicators is affected by a revision of some international standards for financial reporting (particularly IAS 39) with effect from 1 January 2005. The effect of accounting changes on the comparability of the 2006 and 2005 data is less significant.

The end-2006 data partly take into account the results of external audits of individual entities. Additional partial changes to the data given in this publication cannot be ruled out, but these should not significantly affect the trends indicated.

In addition to data from the statements submitted to the CNB for supervisory purposes, section 2 (dealing with the banking sector) uses data from statements submitted for the purposes of the money statistics. These data mostly concern the sector structure of loans and deposits and the sectoral breakdown of the loan classification,[38] which are not included in the banking supervision statements. The methodology for compiling statements for the money statistics is different, however. For this reason, some figures, including ratios, are not fully comparable with those provided in the banking supervision statements. The most significant difference is that the banking supervision statements include data on foreign branches of domestic banks, i.e. they relate to banks as a whole.[39] All data in this Report are for commercial banks only, i.e. they do not include the CNB.

The data for the Czech insurance market in section 5 do not include figures relating to the activities of the Czech Insurers' Bureau. The data in this section are for domestic insurance undertakings as a whole, i.e. including their foreign branches.

37 The accounting procedures of insurance undertakings are an exception. Only one insurance undertaking (Česká pojišťovna) keeps accounts according to IAS/IFRS. For reasons of comparability, however, data for the whole insurance market are given in structure and content according to Czech accounting standards.

38 Specifically this applies to sections 2.3.1 and 2.3.2, the data on deposits broken down by sector in section 2.3.4 and the data on the classification of receivables from the point of view of the sectoral breakdown in section 2.4.1.

39 For more details, see http://www.cnb.cz – *Statistics – Money and banking statistics – FAQs*.

1. THE ECONOMIC ENVIRONMENT IN 2006[40]

2006 was a very good year from the macroeconomic point of view in the Czech Republic. This had a positive knock-on effect on the performance of institutions operating on the Czech financial market. For some time now, economic growth in the Czech Republic has been faster than that in the old EU Member States as well as that in Germany, which has long been the Czech Republic's biggest trading partner. Gross domestic product was CZK 3,204.1 billion at current prices. At 6.1%, annual GDP growth was the same as in 2005.

In 2006, GDP growth was driven chiefly by household consumption, fixed investment and inventories. The contribution of foreign trade to GDP growth decreased in 2006. Export activity was mostly related to export and investment activities in EU countries. Production facilities created by foreign direct investment had a positive effect.

Inflation was 2.5% on average in 2006, up by 0.6 percentage point on a year earlier. In Q1–Q3, inflation was close to the CNB's inflation target of 3%, but in Q4 it fell well below 2%. During the year, inflation was affected primarily by changes to regulated prices (prices of electricity, heat and gas for households).

The appreciation trend of the koruna's exchange rate against the euro and the dollar continued into 2006. The bulk of exports and imports are traded in these two currencies. The stronger koruna reduced the prices of most imported commodities, thereby contributing to the low inflation level. From an annual average of CZK 29.78 to the euro in 2005, the koruna firmed to CZK 28.34 to the euro in 2006. The koruna's average exchange rate against the dollar appreciated from CZK 23.95 to CZK 22.61 year on year.

The favourable macroeconomic developments did not avert a widening of the current account deficit as a percentage of GDP, which grew by 1.6 percentage points to 4.2%, or CZK 133.8 billion. This was due chiefly to a higher income deficit and also to a current transfers deficit. The financial account ended 2006 in a surplus of CZK 111.6 billion. This surplus did, however, narrow year on year. A direct investment surplus was still its largest component.

The labour market situation also improved gradually in 2006. Long-term unemployment decreased to 3.9% on average. The labour market was affected by seasonal factors in individual months. The registered unemployment rate declined under the existing methodology, averaging 8.1%. Average monthly nominal wages increased by 6.5% year on year, 1.3 percentage points more than in 2005. Average real wages increased by 3.9% year on year, up by 0.7 percentage point compared to 2005. Aggregate labour productivity grew faster than real wages.

Despite the robust economic growth, the state budget deficit amounted to CZK 97.6 billion, or 3.0% of GDP, in 2006. However, the public debt-to-GDP ratio was little changed in 2006, totalling 30.4% at the end of the year.

The Czech National Bank raised its key interest rates twice in 2006 (in July and September), each time by 0.25 percentage point. The monetary policy decisions were based on forecasts for the Czech economy and inflation and the external economic outlook. A gradual rise in interest rates was consistent with these predictions. The key domestic interest rates were raised as follows: the two-week repo rate from an initial level of 2.0% to 2.5%, the discount rate from 1.0% to 1.5%, and the Lombard rate from 3.0% to 3.5%.

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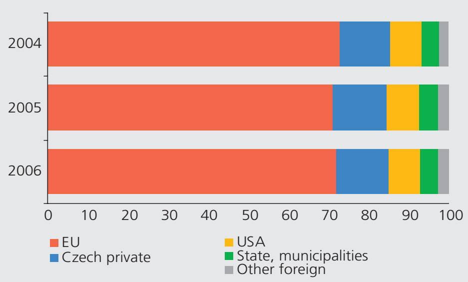
40 The data in this section are based on CZSO data available in May 2007.

TABLE II.1
Shares of bank groups in total assets
(in %; for banks with licences as of the given date)

	2004	2005	2006
BANKS, TOTAL	100.0	100.0	100.0
of which:			
large banks	59.8	61.2	59.8
medium-sized banks	15.9	15.1	16.2
small banks	2.3	2.0	2.3
foreign bank branches	10.0	9.5	9.2
building societies	12.0	12.2	12.5

CHART II.1
Bank ownership structure
(in %)



2. THE BANKING SECTOR

2.1 THE STRUCTURE OF THE BANKING SECTOR

As of 31 December 2006, the Czech banking sector consisted of 24 banks and 13 foreign bank branches. This means that the number of banks increased by one – a foreign bank branch operating under the single licence: Bank of Tokyo-Mitsubishi UFJ (Holland) N.V. Prague Branch, which opened in May 2006. On 1 January 2006, Českomoravská hypoteční banka changed its name to Hypoteční banka.

The breakdown of banking entities into five main groups remained virtually unchanged in 2006.[41] The group of four large banks is still the main component of the domestic banking market, although the share of their assets in total banking sector assets decreased slightly in 2006, to below 60%.

Bank groups are undergoing consolidation at the global and European level, and the banking sector in the Czech Republic is no exception. In 2006, an amalgamation of HVB Bank and Živnostenská banka was commenced following the merger of their parent banks. A change in the owner of eBanka resulted in a decision last year to merge it with the domestic Raiffeisenbank.

In addition, a total of 137 banks from EU countries were able to provide banking services in the Czech Republic as of the end of 2006 after notifying the CNB of this activity under the freedom to provide services (without establishing a branch) pursuant to Article 21 of Directive 2000/12/EC of the European Parliament and of the Council. However, the CNB has no information about the scale of the cross-border banking services they provide, since, as in numerous other countries, such activities are not subject to a reporting obligation and do not fall within the CNB's supervision. The number of banks that have provided notification of the provision of cross-border services in the Czech Republic increased by 33 in 2006. Two banks gave notification of the termination of such activities.

Banks registered in the Czech Republic may also provide banking services in other EU countries. In 2006, however, no Czech bank notified the CNB of such an intention. The only banks to provide notification of the provision of cross-border services in previous years were Komerční banka and GE Money Bank, both in respect of Slovakia. Two banks registered in the Czech Republic have foreign branches in EU countries (ČSOB and J&T BANKA).

2.1.1 Ownership structure

The banks operating in the Czech Republic recorded no major changes in ownership structure in 2006. Foreign capital dominates the sector's capital, with a direct share of 82.6% (this refers to cases where a legal entity registered abroad holds a direct share in a bank). This represents a year-on-year increase of 0.5 percentage point. From the legal perspective, foreign capital predominates in 16 banks, nine of them being wholly owned by foreign capital. Eight banks are majority owned by Czech shareholders. Five of them are wholly Czech-owned (Hypoteční banka, J&T BANKA and Modrá pyramida plus two state-controlled banks specialising in export and business promotion – Česká exportní banka and Českomoravská záruční a rozvojová banka).

41 For analytical purposes, bank groups are defined as follows: large banks (assets of more than CZK 100 billion), medium-sized banks (assets of CZK 20 billion to CZK 100 billion), small banks (assets of less than CZK 20 billion), building societies, and foreign bank branches. The group breakdown is provided in Annex 3. For more details, see http://www.cnb.cz – *Financial market supervision – Banking supervision – Banking sector – Basic indicators of the banking sector – Methodology*.

Foreign owners directly or indirectly control 97.0% of the total assets of the sector.[42] Owners from EU countries dominate. Their share in the foreign ownership of the sector stabilised at the end of 2006 at 87.2%. All the owners of the four large banks come from EU countries. Two US entities own two medium-sized banks (GE Money Bank and Citibank). As of 31 December 2006, only one small bank had owners from another region (IC Banka). The breakdown of ownership by EU country remains diverse. Austrian shareholders still have the largest share (39.5%) in the registered capital of Czech banks.

2.1.2 Employees and banking units

A total of 38,232 people were employed in the Czech banking sector as of 31 December 2006, a rise of 692 on the previous year (these figures include all full-time and part-time employees). The banking sector thus recorded a year-on-year rise in its workforce for the first time since 1998 (the number peaked at almost 51,000 people in 1996). The group of large banks as a whole continued to reduce its workforce during 2006, employing 145 less people at the end of 2006 than a year earlier. By contrast, medium-sized banks, small banks and foreign bank branches recorded increases of 605, 149 and 83 employees respectively. The total number of employees of building societies remained unchanged in 2006.

Unlike the number of employees, the number of banking units has been growing regularly since 2003. In 2006, the number of banking units in the Czech Republic rose by 52 to 1,877. All the bank groups except small banks recorded an increasing number of branches. The growth potential of banking business and banks' efforts to expand the range of services they offer is thus leading to a rising number of banking units. On the other hand, banks are trying to streamline their activities and establish banking units in locations where they can achieve maximum effectiveness of sales of products and services. This is reflected in the nature of the units and the ranges of services they offer.

At the end of 2006, there were roughly 5,500 citizens per banking unit in the Czech Republic, a slight decline in year-on-year terms. In addition to residents, however, retail bank networks provide services to clients temporarily resident in the Czech Republic and to other clients, particularly tourists and visitors. Productivity as measured by total assets administered per employee increased to CZK 82.4 million at the end of 2006, up by 4.6% year on year.

2.1.3 Electronic banking

As a rule, clients set up at least one form of electronic access to their bank accounts – via payment card, phone or PC. This trend is being supported, among other things, by a rising number of ATMs, high mobile phone penetration in the Czech Republic and increasing options for connecting to the internet as well as falling prices for such connections. At the end of 2006, only 14.6% of the more than 7 million household accounts lacked electronic services completely. Telephone and PC transactions could be executed on 37.3% and 33.5% of accounts respectively. Besides expanding the range of electronic banking products they offer, banks are currently focusing to a greater extent on improving security and client protection. Examples include wider use of chip cards and the introduction of new transaction authorisation features in internet banking.

42 This refers to the share of total bank assets controlled by foreign entities (i.e. foreign shareholders holding directly or indirectly at least 50% of the bank's shares) in the total assets of the banking sector.

CHART II.2
Capital origin
(in %; for banks with licences as of 31 December 2006)

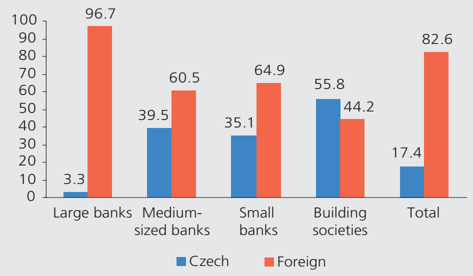


CHART II.3
Number of employees and number of branches

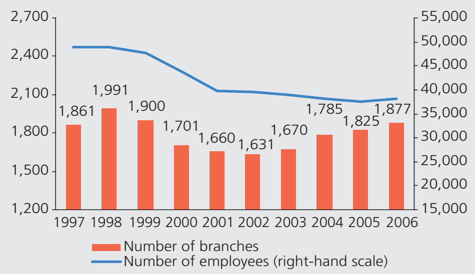


TABLE II.2
Number of employees and banking units in the banking sector in the Czech Republic
(for banks with licences as of the given date)

	2004	2005	2006
Number of employees	38,160	37,540	38,232
Number of banking units	1,785	1,825	1,877
Number of employees			
per bank	1,090	1,043	1,033
per banking unit	21.4	20.6	20.4
Number of citizens			
per bank (thous.)	292.0	284.8	278.0
per banking unit (thous.)	5.7	5.6	5.5
per employee	267.8	273.1	269.1

TABLE II.3
Electronic banking
(for banks with licences as of the given date)

	2004	2005	2006
Number of ATM networks	4	4	4
Number of ATMs	2,750	3,005	3,281
Number of cards issued (thous.)			
total	6,576	7,428	8,181
debit cards	6,174	6,556	6,824
credit cards	402	872	1,357
Current and deposit accounts (households; thous.)			
total	6,683	7,135	7,563
with cards issued	4,889	5,289	5,523
with PC access	1,736	2,400	2,537
with telephone access	2,291	2,713	2,824
without electronic service	1,302	1,142	1,106

The number of ATMs is rising by about 10% a year. Credit cards are becoming more prevalent, recording annual growth of more than 50% as of the end of 2006, partly due to base effects. The number of international payment cards issued by banks is constantly rising, reaching 7 million at the end of 2006.

2.2 BANKING SECTOR PERFORMANCE

2.2.1 Profit from financial activities and profit from other operating activities

The long-term financial stability of banks depends primarily on ongoing creation of profit from financial activities, i.e. profit from core banking activities. A bank's profit has to be high enough at least to cover its operating expenses and the costs arising from the banking risks it undertakes.

In 2006, profit from financial activities grew by a record CZK 7.9 billion (7.3%) to CZK 116.8 billion. Year-on-year increases were recorded in most of the banking institutions operating in the Czech Republic. The growth rates varied across the individual bank groups as follows: large banks 5.3% (CZK 4.1 billion), medium-sized banks 13.6% (CZK 2.6 billion), small banks 10.8% (CZK 0.3 billion), foreign bank branches 9.2% (CZK 0.4 billion) and building societies 8.9% (CZK 0.5 billion).

Interest profit was again the fastest growing category of profit from financial activities, rising by CZK 8.3 billion (13.0%) year on year to CZK 72.4 billion. Interest profit accounts for almost 62% of total profit from financial activities.

The rise in interest profit was chiefly due to continuing growth in interest income from "other clients" (i.e. excluding banks and general government). The annual growth of CZK 11.3 billion (21.0%), to CZK 65.1 billion, was a result of banks' continuing credit expansion. Interest received from other clients accounted for 52.1% of the banking sector's total interest income (compared to 45.3% in 2004). By contrast, interest income from general government was down by CZK 0.6 billion year on year, to CZK 3.2 billion, owing to a continuing decrease in the sector's exposure to this sector (and the CCA in particular). Its share in the banking sector's total interest income dropped below 3% at the end of 2006. Interest from debt securities in banks' assets amounted to CZK 25.5 billion, up by 8.3% on 2005. Interest expenses increased as well, reflecting growth in client deposits and a modest rise in interest rates in 2006. The interest rate spread remained virtually unchanged in year-on-year terms, at 2.31% at the end of the year. Net interest margin grew by 9 basis points to 2.51%.

In 2006, profit from fees and commissions grew by CZK 1.1 billion (3.5%) to CZK 32.9 billion. Although this is a slightly higher annual increase than in 2005, the rate of growth of profit from fees and commissions slowed significantly compared to previous years (12.0%–18.9% in 2001–2004, i.e. increases of CZK 2.7–4.9 billion). Some banks even recorded decreases compared to 2005.[43] This was due primarily to competition on the market and strong media and public interest in fees, which is preventing banks from raising the prices of their services. The rising fee income is thus being driven chiefly by a growing number of transactions. Almost half the income was attributable to payment system fees and

TABLE II.4
Banking sector performance
(in CZK millions)

	2004	2005	2006
PROFIT FROM FINANCIAL ACTIVITIES	103,486	108,957	116,836
of which:			
interest profit	59,760	64,044	72,370
income from shares and other equity instruments	1,369	2,189	1,676
profit from fees and commissions	31,326	31,834	32,944
profit from financial transactions	11,031	10,890	9,847
PROFIT/LOSS FROM OTHER OPERATING ACTIVITIES	932	4,935	2,242
ADMINISTRATIVE EXPENSES	48,819	51,630	55,665
WRITE-OFFS, CREATION AND USE OF RESERVES AND PROVISIONS	10,274	13,065	14,368
PROFIT/LOSS FROM CURRENT ACTIVITIES	45,366	49,272	49,158
PROFIT/LOSS FROM EXTRAORDINARY ACTIVITIES	-10	10	8
GROSS PROFIT	45,355	49,273	49,166
Income tax	12,503	9,847	11,241
Share in profit of subsidiaries and affiliates	41	76	114
NET PROFIT	32,852	39,426	37,925

CHART II.4
Structure of profit from financial activities by profit type
(in %)

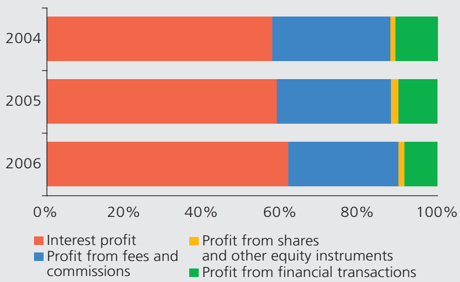
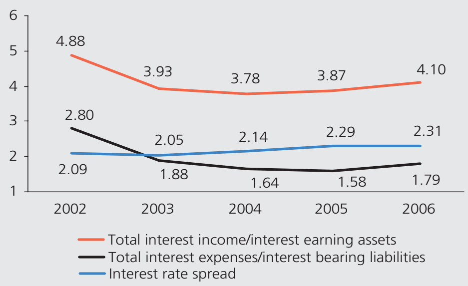


CHART II.5
Interest rate spread
(client operations; in %)



43 For example building societies, which are still experiencing the effects of the new rules for building savings schemes introduced on 1 January 2004. The number of building savings contracts in the saving phase is steadily falling (down by 276,000 to 5,298,000 in 2006).

commissions, although they fell slightly in 2006 compared to the previous period (by 0.9% to CZK 19.5 billion). The banking sector's buoyant lending is being reflected in growing income from lending-related fees, which rose by 14.1% to CZK 7.6 billion. Thanks to the increasing popularity of collective investment and private pensions, growth is also being recorded for fees from securities transactions and other financial operations (particularly fees related to the sale of products of non-banking financial institutions, such as mutual fund units, pension funds, insurance, etc.).

Income from shares and participations decreased by CZK 513.9 million (23.4%) year on year, to CZK 1.7 billion as of 31 December 2006. Of this amount, 96.7% is due to large banks and consists mainly of dividends received from subsidiaries and affiliates. The year-on-year decrease in this indicator in 2006 was mostly due to an extraordinary dividend received by one of the large banks in 2005.

At CZK 9.8 billion, profit from financial operations was CZK 1.0 billion (9.3%) lower than in 2005. Its largest component was again profit from foreign exchange transactions (CZK 9.3 billion), which consists mainly of profit from trading in foreign currencies (income on spreads in banks' exchange rates).

Profit from other operating activities decreased by more than half during 2006, to CZK 2.2 billion. This item includes income from specific one-off transactions, such as sales of ownership interests, sales of fixed assets, results of legal disputes and so on. In 2006, this extraordinary income was substantially lower than a year earlier. The most significant item on the expenses side is the contribution to the Deposit Insurance Fund, which was virtually unchanged in year-on-year terms at CZK 1.5 billion.

2.2.2 Administrative expenses, write-offs, creation and use of provisions

The administrative expenses of the banking sector totalled CZK 55.7 billion in 2006. This represents an annual rise of CZK 3.9 billion (7.5%). The share of administrative expenses in profit from financial activities was almost unchanged at 47.6% as of 31 December 2006. The strongest growth was recorded by total personnel expenses, which rose by CZK 2.8 billion (10.7%) to CZK 29.0 billion. These expenses account for 52.1% of the total administrative expenses of the banking sector. Average annual personnel expenses per employee increased by 10.5% to stand at CZK 773,000 at the end of 2006.[44]

Write-offs and creation of provisions and reserves increased by CZK 1.3 billion (9.9%) during 2006, reaching CZK 14.4 billion. Write-offs and creation of provisions for tangible and intangible assets stood at CZK 10.1 billion. This item has been relatively stable in the last three years.

Write-offs and creation of provisions and reserves for receivables and off-balance-sheet instruments amounted to CZK 5.4 billion at net value in 2006. This represented a significant rise of CZK 4.4 billion compared to 2005. Constant growth of the loan portfolio led to higher net creation of provisions for loans in the structure of the creation and release of provisions, reserves and write-offs of receivables. This was due to lower release of reserves compared to 2005 and

44 Calculated from the average converted stock of employees in 2006 (the average number of employees in the given year converted into full-time equivalents). Personnel expenses consist mainly of wages and social and health insurance, but also include employer contributions to health care, private pension schemes and food allowances, etc.

in particular to 2004 (owing to mandatory release of previously created reserves[45]) and higher creation of provisions for receivables in connection with growth in classified loans.[46]

2.2.3 Net profit

The pre-tax (gross) profit of the banking sector totalled CZK 49.2 billion in 2006, only slightly less than in 2005 (CZK 49.3 billion). However, the structure of this profit changed in 2006. Interest income increased significantly, but this was offset by rising administrative expenses and higher net creation of reserves and provisions. Compared to 2005, the 2006 profit was less affected by one-off income from specific transactions.

The net profit of the banking sector dropped by CZK 1.2 billion (3.1%) year on year, to CZK 37.9 billion as of 31 December 2006 (compared to CZK 39.1 billion at the end of 2005). The difference is due to higher reported income tax (CZK 11.2 billion in 2006, compared to CZK 10.1 billion in 2005). Payable income tax decreased year on year thanks to a lower tax rate, but reported deferred tax rose in 2006.[47]

The group of large banks recorded an annual decrease in net profit. Despite the overall decline, however, large banks generated 72.7% of the net profit of the entire banking sector (compared to 74.5% in 2005). Lower profits were recorded also by medium-sized and small banks, while foreign bank branches and building societies posted higher earnings. Two banks and three foreign bank branches reported losses in 2006.

2.2.4 Profitability, efficiency and productivity

Owing to the lower net profit and higher capital (see section 2.5) profitability measured in this way decreased in 2006. Return on Tier 1 (RoE) was 22.5% (2.7 percentage points less than in 2005). Declining profitability ratios were recorded in all the bank groups except building societies, which showed an annual rise of 3.3 percentage points to 25.8%. The RoE of large banks was 25.5%, down by 3.3 percentage points year on year. The respective figures for medium-sized banks and small banks were 13.4% and 6.9%.

Return on assets decreased by 0.14 percentage point to 1.23% in 2006. The highest value of 1.46% was again achieved by large banks. The figure for medium-sized banks was 1.21%. The RoA of other banks was below 1%.

At 47.6% as of the end of 2006, the ratio of administrative expenses to profit from financial activities was almost unchanged year on year. The lowest values were recorded by building societies (42.8%) and large banks (45.1%).

CHART II.6
RoE for bank groups
(in %)

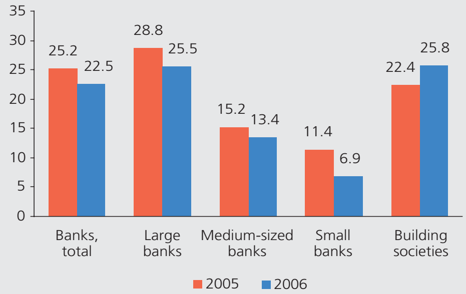
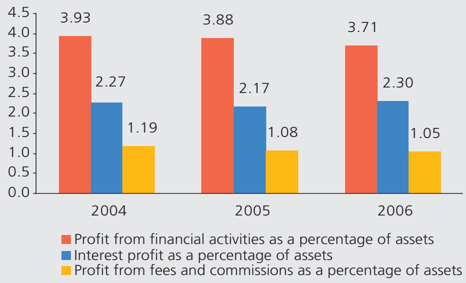


CHART II.7
Profit as a percentage of assets
(in %)



45 Under an amendment to the 2002 Act on Reserves for the Purposes of Determining the Income Tax Base, banks were obliged to use general reserves created before 2002 to cover losses from write-offs and transfers of receivables and to cover losses from guarantees provided. Banks were required to release the unused reserves in favour of income, reducing the balance for each taxation period starting from 2002 by at least 25% of the balance on 31 December 2001 in order to dissolve them entirely on 31 December 2005 at the latest. This legislative adjustment was related to the alignment of Czech accounting standards with international accounting standards.

46 See section 2.4.1 for more details on the quality of the loan portfolio.

47 In 2005, the banking sector as a whole had recorded income from deferred tax of CZK 480.3 million, whereas in 2006 it recorded an expense of CZK 481.9 million.

Net profit per employee fell by 4.9% to CZK 991,900. By contrast, profit from financial activities per employee increased by 5.3% to CZK 3.0 million, as a result of substantial growth in profit from financial activities. Total assets per employee rose by 4.6% to CZK 82.4 million.

2.3 ACTIVITIES OF THE BANKING SECTOR

The assets of the banking sector rose by CZK 197.4 billion (6.6%) to CZK 3,151.8 billion in 2006. The asset growth slowed significantly compared to 2005 (when annual growth of CZK 318.8 billion, or 12.1%, had been recorded). Lower growth was recorded in large banks, whose assets increased by 4.1% (CZK 75.3 billion), whereas small and medium-sized banks saw higher growth (23.7%, or CZK 13.8 billion, and 14.5%, or CZK 64.9 billion, respectively). Assets of building societies increased by 9.1% (CZK 32.8 billion) and those of foreign bank branches by 3.8% (CZK 10.6 billion). Owing to the lower asset growth in large banks, their share in banking sector assets decreased to just under 60% at the end of 2006. The Herfindahl index calculated from total banking sector assets declined to 0.110 (compared to 0.115 in 2005), indicating a modest increase in competition in the banking sector.[48] The share of the three largest banks in total banking sector assets decreased from 55.6% to 54.3% year on year.

A key factor with respect to the structure of the banking sector's assets was a 20.2% decline in exposure on the interbank market. At the end of 2006, the volume of transactions with the CNB (repo operations)[49] was lower than in 2005, as were exposures between commercial banks themselves. By contrast, receivables from clients continued to show strong growth. Receivables from other clients again showed an upward trend (+24.8%), while exposure to general government continued falling (-25.4%).

2.3.1 The loan portfolio (sectoral breakdown)[50]

Domestic banks' total receivables from clients rose by CZK 234.6 billion (19.9%) to CZK 1,413.2 billion in 2006. This represents a markedly higher increase than in previous years. In 2005 the volume of receivables had increased by CZK 168.2 billion and in 2004 it had gone up by CZK 59.5 billion.

All the bank groups lent more funds to clients. The loan volume increased by CZK 123.2 billion (18.2%) year on year in the case of large banks and by CZK 62.2 billion (22.1%) in the case of medium-sized banks. In 2005, large banks had been particularly affected by a decline in exposure to general government; this

TABLE II.5
Banking sector assets
(at net value; CZK billions)

	2004	2005	2006	Structure 2006 in %
TOTAL ASSETS	2,636	2,955	3,152	100.0
Cash and deposits with central banks	58	55	69	2.2
Securities accepted by CNB for refinancing	292	335	386	12.3
Receivables from banks	825	920	734	23.3
Receivables from clients	1,074	1,174	1,424	45.2
Debt securities	209	277	312	9.9
Shares and units	10	12	13	0.4
Interests	19	36	46	1.4
Tangible and intangible assets	52	49	47	1.5
Other balance-sheet assets	93	94	118	3.7
Deferred revenues and accrued expenses	3	4	3	0.1

CHART II.8
Concentration of banking sector
(as of 31 December 2006; in %)

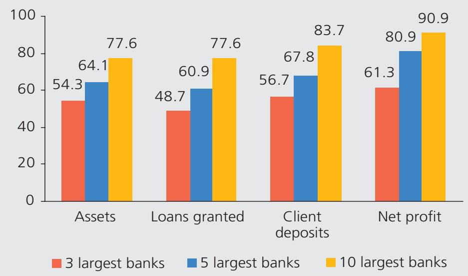


TABLE II.6
Liabilities by sector

	Volume in CZK bn 2004	2005	2006	Change in % from 2005
TOTAL	1,010	1,179	1,413	19.9
A. RESIDENTS	969	1,119	1,339	19.7
non-financial corporations	460	525	635	21.0
financial institutions	81	97	99	2.6
general government	115	81	68	-17.0
households	312	413	531	28.6
trades	29	33	36	7.7
individuals	283	380	495	30.4
non-profit institutions serving households	2	2	6	176.7
B. NON-RESIDENTS	41	60	74	24.0

48 The Herfindahl index (HI) is the sum of the squares of the market shares of all entities operating on the market. It takes values between 0 and 1; the closer it is to zero, the lower the concentration, or the stronger the competition, on the market.

49 In the case of repo operations with the CNB, this was, however, an extraordinary fluctuation, as in December some banks reported much lower amounts deposited with the CNB than in previous months. The average balance of funds deposited by the banking sector with the CNB at the end of individual months in the form of repo operations was slightly higher than in 2005 (up by CZK 10.7 billion to CZK 497.7 billion).

50 Data from the monetary statistics reporting statements submitted by banks were used to prepare this section. These statements use a different methodology than the banking supervision statements, so some of the resulting values (e.g. the total volume of loans provided) are not fully comparable with the data in other parts of the text. For more details, see http://www.cnb.cz – *Statistics – Monetary and banking statistics – FAQs*. The quality (degree of risk) of the loan portfolio is dealt with in section 2.4.1 *Credit risk*.

CHART II.9
Sector structure of loan porfolio
(in CZK billions)

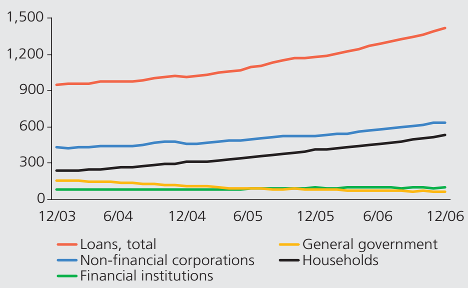


CHART II.10
Structure of loans by economic sector
(as of 31 December 2006; in %)

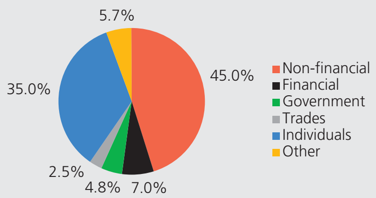


TABLE II.7
Loans to households by time and type

	Volume in CZK bn			Change in % from
	2004	2005	2006	2005
TOTAL LOANS AND RECEIVABLES	283	380	495	30.4
of which:				
short-term	17	21	24	16.6
medium-term	49	47	40	16.3
long-term	218	311	431	38.4
of which:				
housing loans	209	280	371	32.5
consumer credit, including current account overdrafts	68	89	109	22.8
other	6	10	14	37.5

effect was considerably smaller last year. Foreign bank branches provided CZK 28.5 billion (32.3%) more in client loans. Building societies also performed well, recording loan portfolio growth of CZK 28.1 billion (25.8%). Small banks likewise increased their lending by CZK 8.9 billion (28.2%).

Loans to households and loans to corporations both recorded dynamic growth in 2006. Receivables from households rose by CZK 117.9 billion (28.6%) to CZK 530.8 billion in 2006. Their share of total loans has risen from 30.9% to 37.6% over the last two years. Receivables from non-financial corporations increased by CZK 110.0 billion (21.0%) to CZK 635.3 billion last year, accounting for 45.0% of total receivables (a stable value over the last two years). Significant growth was recorded in 2006 in lending to private corporations with domestic owners. Lending to foreign-owned private corporations showed less growth. As for the individual loan types provided to non-financial corporations, the most significant were investment loans (with a 38.9% share). They also showed the highest absolute growth in 2006.

In contrast, general government showed a continuing decline in exposure. Receivables from general government fell by CZK 13.8 billion (17%) to CZK 67.6 billion, chiefly reflecting a decline in exposure to the Czech Consolidation Agency (CCA). Its liabilities to the banking sector fell from CZK 22.1 billion to CZK 5.4 billion last year (compared to CZK 49.3 billion as of 31 December 2004). Receivables from local government continued edging up in 2006 (by 13.6% to CZK 31.1 billion).

2.3.2 Loans to individuals[51]

Private individuals' debt with domestic banks rose by a further CZK 115.3 billion (30.4% year on year) in 2006. As usual, mortgage loans for housing, which increased by CZK 71.5 billion during the year to account for 48.2% of all the loans provided to individuals (compared to 44.0% at the end of 2005), showed the highest growth. The figures in Table II.7 also show a further upward trend in long-term loans, whose share rose from 76.9% in 2004 to 87.1% at the end of 2006.

Housing loans[52] accounted for 75.0% of all loans to individuals at the end of 2006. This share increased by 1.2 percentage points year on year. The principal reasons for this loan expansion remain persisting low interest rates, a preference for privately-owned or cooperative-owned flats and houses over rented dwellings, strong demand from the baby-boomers of the 1970s, and discussions fostering expectations of a possible rise in the VAT rate on construction work for housing purposes.

Total loans granted by building societies[53] increased by a record CZK 27.4 billion to CZK 135.5 billion. This growth was positively reflected in the loans-to-savings ratio, which rose from 32.8% to 37.6%. This ratio nonetheless remains low. The reasons include changes in state support for building savings schemes introduced on 1 January 2004. In 2003, building savings clients had signed a record high

51 This section describes loans to individuals who are residents of the Czech Republic. Individuals are a subcategory of the household sector. In addition to individuals, the household sector includes trades.

52 In addition to mortgage loans, housing loans include building society loans (standard and bridging) and consumer credit for real estate purchase or reconstruction.

53 Table II.8 also includes loans provided by building societies which are of a mortgage loan nature (i.e. secured with a lien on property).

number of building savings contracts under conditions that were more favourable for them. These contracts are now in the saving phase, and clients can be expected to show interest in obtaining loans in the future. The average new loan provided by a building society rose from CZK 210,000 to CZK 295,000 in 2006.

Consumer credit (including current account overdrafts) rose by CZK 20.3 billion to CZK 109.2 billion in 2006. Annual growth in consumer loans in absolute terms was only slightly lower in 2006 than in 2005 (CZK 21.0 billion). Due to a higher loan base, the annual rate of growth in relative terms fell from 30.8% to 22.8%.

2.3.3 Other asset items

Receivables from banks are still the second most important asset item in terms of volume, amounting to CZK 734.2 billion at the end of 2006. Receivables from the CNB account for CZK 330.1 billion of this amount. They chiefly include receivables arising from repo operations with the CNB. Receivables between commercial banks themselves totalled CZK 404.1 billion at the end of the year. Both components of receivables from banks are quite volatile from month to month.

The volume of securities excluding ownership interests increased by CZK 87.9 billion (14.1%), reaching CZK 710.9 billion. Securities issued by general government (government bonds, bonds of state institutions, municipalities etc.) account for 64.5% of this amount. Most of these securities are held by large banks (62.3%) and building societies (30.3%).

The value of bonds issued by other entities (bank and corporate bonds) rose by 18.0% to CZK 235.9 billion. The group of large banks, which held bonds worth CZK 188.9 billion at the end of 2006, dominated here as well. Building societies had bonds worth CZK 33.9 billion in their portfolios. The volume of asset-backed securities decreased to an insignificant CZK 910.2 million.

The value of the ownership interests of the banking sector increased by CZK 9.3 billion to CZK 45.6 billion. Most of this amount is attributable to the group of large banks.

2.3.4 Banking sector funds

Liabilities arising from client deposits increased by CZK 182.7 billion in 2006 and thus surpassed the CZK 2 trillion mark (CZK 2,102.2 billion). Total general government deposits in this period were almost unchanged, so all the growth in deposits was due to deposits of other clients. Owing to persisting low interest rates, clients continued to prefer current account deposits, which recorded almost double the growth of time deposits. Large banks received almost half of all new deposits (CZK 88.5 billion). Client deposits of medium-sized banks rose by CZK 35.3 billion and those of building societies by CZK 30.1 billion.

The sector structure of the total deposits of the domestic banking sector is based on monetary statistics data (Table II.10 and Chart II.11). The sectors' shares tend not to change much. Deposits of individuals account for just over half of total deposits, while non-financial corporations account for roughly one quarter (a slight year-on-year increase of one percentage point), general government for 8% and financial institutions for less than 5%.

Liabilities to banks fell by CZK 61.3 billion to CZK 348.3 billion. The decline on the interbank market affected all bank groups. Debt security liabilities rose by CZK 16.8 billion to CZK 278.7 billion. The largest increase was recorded by mortgage bonds, which rose by CZK 31.5 billion to CZK 153.3 billion in 2006,

TABLE II.8
Basic building society indicators
(in CZK billions)

	2004	2005	2006	Change in % from 2005
Amount saved	287	329	360	9.4
Total loans	84	108	135	25.3
of which:				
building society loans	29	32	35	10.5
bridging loans	55	76	100	31.5
Total loans/amount saved (%)	29.3	32.8	37.6	14.6

TABLE II.9
Banking sector liabilities

	Volume in CZK bn 2004	2005	2006	Structure 2006 in %
TOTAL LIABILITIES	2,636	2,955	3,151	100.0
Liabilities to banks	361	410	348	11.0
Liabilities to clients	1,732	1,919	2,102	66.7
Liabilities from debt securities	215	262	279	8.9
Other liabilities	108	114	146	4.6
Subordinated liabilities	8	12	26	0.8
Valuation differences	3	7	6	0.2
Own funds	209	231	245	7.8
of which:				
equity capital	70	70	71	2.3
retained profits	42	58	67	2.1
profit for accounting period	33	39	38	1.2

TABLE II.10
Client deposits by sector

	Volume in CZK bn 2004	2005	2006	Change in % from 2005
TOTAL	1,669	1,850	2,025	9.4
A. RESIDENTS	1,634	1,800	1,973	9.6
non-financial corporations	384	448	520	16.2
financial institutions	78	94	91	-3.1
general government	125	158	161	1.9
households	1,019	1,077	1,175	9.1
trades	67	70	91	30.4
individuals	953	1,007	1,084	7.6
non-profit institutions serving households	28	24	27	14.1
B. NON-RESIDENTS	35	51	52	3.3

CHART II.11

Structure of deposits by economic sector

(as of 31 December 2006; in %)

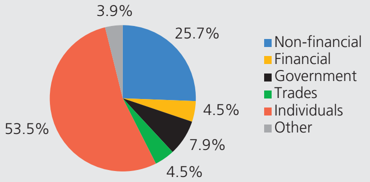


TABLE II.11

Banking sector off-balance sheet structure

	Volume in CZK bn		
	2004	2005	2006
SELECTED OFF-BALANCE SHEET ASSETS	4,642	5,000	6,663
of which:			
commitments and guarantees provided	486	583	686
collateral provided	8	2	3
receivables from spot transactions	59	55	64
receivables from fixed-term transactions	3,773	3,863	5,148
receivables from options transactions	197	374	628
receivables written off	42	40	40
assets provided into custody, administration and safekeeping	78	83	95
SELECTED OFF-BALANCE SHEET LIABILITIES	6,304	6,717	8,639
of which:			
commitments and guarantees received	299	311	341
collateral received	1,199	1,159	1,222
payables from spot transactions	60	55	63
payables from fixed-term transactions	3,745	3,843	5,119
payables from options transactions	195	373	628
assets received for management	26	30	36
assets received into custody, administration and safekeeping	780	945	1,231
NET POSITION FROM SPOT TRANSACTIONS	-0.6	-0.3	0.8
NET POSITION FROM FIXED-TERM TRANSACTIONS	27.8	20.0	29.1
NET POSITION FROM OPTIONS	1.7	0.3	-0.1

accounting for more than 50% of debt security liabilities. In contrast, short-term notes, which banks offer as deposit instruments for large clients, fell by CZK 12.4 billion.

The banking sector's own funds continue to rise thanks mainly to the retention of parts of profits on banks' balance sheets as retained earnings and reserve funds. However, owing to high dividend payments to shareholders by some large banks and building societies in 2006, the growth in retained earnings in 2006 (distribution of 2005 earnings) was less than half[54] that in 2005.

2.3.5 Off-balance sheet transactions

The off-balance sheet total continued to rise in 2006, chiefly due to a further rise in the volume of derivatives transactions. Derivatives transactions comprise transactions for clients, derivatives for banks' own trading purposes and hedging transactions to close banks' open positions vis-à-vis the risks they undertake. Transactions in interest rate instruments (interest rate swaps and forwards) make up the largest share, followed by transactions in currency instruments. Banks engage only minimally in commodity, equity and credit derivatives trading. Receivables/payables from fixed-term transactions, which both increased by more than 33%, are the largest volume items. However, the volume of options transactions also rose.

The net position from fixed-term transactions at nominal value[55] increased by CZK 9.2 billion to CZK 29.1 billion. However, its value fluctuates from month to month. At the end of June 2006, for example, it amounted to CZK 49.3 billion. The net fair value of derivatives (a balance sheet item that better expresses the potential level of risk of derivatives operations) remains very low.

2.4. RISKS IN BANKING

2.4.1 Credit risk

Credit risk has always been by far the most significant risk undertaken by the Czech banking sector. Past years have seen substantial clean-ups by domestic banks (often with the involvement of the state and its institutions) of their balance sheets of bad loans. This process was essentially completed in 2003, when banks recorded a record low volume of classified loans. Recently (since 2004), the volume of classified loans has started to creep up again, owing to the strong expansion of the loan portfolio. However, for the assessment of credit risk it is important that this absolute growth is not being accompanied by a rising share of classified loans in total loans and that the increasing volume of classified loans is manifesting itself primarily in the lowest-risk category (watch loans). The favourable evolution of the loan portfolio also reflects the relatively good economic situation in the Czech Republic.

54 For more details on own funds, subordinated debt and banking sector reserves, see section 2.5 *Capital adequacy.*

55 The difference between the nominal value of receivables and payables arising from fixed-term transactions.

As of 31 December of 2006, the Czech banking sector recorded classified receivables from clients (excluding classified receivables from banks) of CZK 154.4 billion, up by CZK 29.5 billion (23.6%) on the end of 2005. Since this relative increase was slightly larger than that of the total loan portfolio, the share of classified loans in total loans[56] grew from 11.6% to 11.9% in 2006.

Growth in the lowest-risk category, namely watch loans (an increase of 29.6%), accounted for the majority of the overall rise in classified loans. However, this was strongly affected by a change in internal loan classification methods which led to some receivables being moved between loan categories, most notably from standard to watch. By contrast, numerous banks recorded an absolute decline in the watch loan category.

The value of non-performing loans (NPLs)[57] rose by 13.7% to CZK 53.6 billion in 2006. The biggest increases were recorded in the substandard and loss categories (16.6% and 12.2% respectively). As this relative increase was smaller than that of the total loan portfolio, the share of NPLs in total loans fell from 4.4% to 4.1% in 2006.

The growth in NPLs varied across the individual groups of banks. The value of NPLs increased by CZK 3.5 billion (12.8%) in large banks, CZK 2.2 billion (15.3%) in medium-sized banks, CZK 87.9 million (8.2%) in small banks, CZK 256.0 million (11.4%) in building societies, and CZK 382.0 million (21%) in foreign bank branches. As of 31 December 2006, the ratio of NPLs to total loans was 4.6% in large banks, 5.0% in medium-sized banks, 2.9% in small banks, 1.8% in building societies and 1.9% in foreign bank branches.

As regards the resolution of classified loans in 2006, standard repayment of such loans and reclassification to standard loans still predominated, thanks to the improved economic situation of debtors (these methods accounted for almost 96% of all decreases in classified loans during 2006). Receivables of CZK 3.1 billion were written off, receivables of CZK 1.05 billion were sold to other entities, new loans were provided to repay classified receivables of CZK 643.7 million, and realisation of collateral was used to repay bank receivables of CZK 181.3 million.

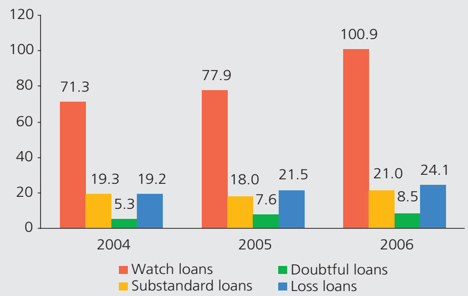
Since 2005, banks have been able to use the portfolio-based approach[58] to calculate provisions for certain loan types (particularly in the retail banking segment). Receivables assessed on portfolio basis amounted to CZK 149.7 billion in 2006, a year-on-year increase of almost 30%. The share of loans assessed on a portfolio basis in total client loans was 10.3% as of 31 December 2006. Provisions amounting to CZK 697.6 million, i.e. 0.05% of total receivables from clients, had been created for receivables assessed on a portfolio basis.

As of the end of 2006 banks had created provisions of CZK 32.1 billion for individually assessed receivables. This was less than the volume of weighted classified loans[59] (CZK 33.5 billion). However, in addition to provisions banks have

TABLE II.12
Classification of receivables from clients (excluding banks), gross
(in CZK billions)

	Volume 2004	2005	2006	Change in % from 2005
TOTAL RECEIVABLES FROM CLIENTS	1,100	1,198	1,448	20.9
A. RECEIVABLES ASSESSED INDIVIDUALLY	1,097	1,082	1,298	20.0
standard	981	957	1,144	19.6
classified	115	125	154	23.6
watch	71	78	101	29.6
non-performing	44	47	54	13.7
substandard	19	18	21	16.6
doubtful	5	8	8	10.9
loss	19	21	24	12.2
B. RECEIVABLES ASSESSED BY PORTFOLIO	3	116	150	29.0
Weighted classified receivables	26	30	34	13.0
Provisions for loans assessed individually	30	30	32	7.4
Provisions for loans assessed by portfolio	0.3	0.6	0.7	15.2
Share of classified loans in total loans (assessed individually; in %)	10.5	11.6	11.9	x
Share of non-performing loans in total loans (assessed individually; in %)	4.0	4.4	4.1	x

CHART II.12
Loan portfolio quality
(client loans assessed individually; in CZK billions)



56 The total volume of loans comprises only individually assessed receivables (i.e. loans assessed by portfolio are not included).

57 Non-performing loans are classified loans net of the lowest-risk category (watch loans). NPLs include (inter alia) all loans more than 90 days past due.

58 See CNB Provision No. 9/2002, stipulating rules for the assessment of financial receivables and the creation of provisions and reserves, and rules for the acquisition of certain types of assets, as amended.

59 Classified receivables weighted by the risk weight for the given category of receivables (watch 1%, substandard 20%, doubtful 50% and loss 100%).

Table II.13
Classified loans by sector as of 31 December 2006

	Volume in CZK bn			Change in % from 2005
	2004	2005	2006	
TOTAL CLASSIFIED LOANS	118.6	121.4	142.3	17.2
non-financial corporations	86.6	83.3	99.4	19.3
financial institutions	2.0	2.3	3.5	51.2
general government	1.1	1.4	1.4	-5.1
households	22.0	25.8	29.8	15.7
of which:				
trades	6.7	6.5	6.5	0.4
individuals	15.3	19.3	23.3	20.9
of which:				
housing loans	7.4	9.6	11.7	21.6
mortgage loans	3.7	5.1	6.6	30.3
consumer credits	7.5	9.1	10.3	14.2
other	0.5	0.6	1.2	111.7
non-profit institutions serving households	0.2	0.1	0.1	94.5
non-residents	6.7	8.5	8.1	-4.3

Chart II.13
Structure of classified loans to non-financial corporations as of 31 December 2006

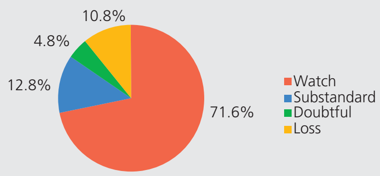
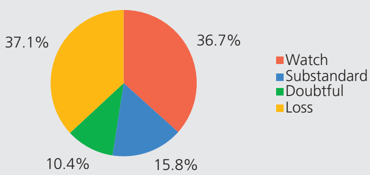


Chart II.14
Structure of classified loans to households as of 31 December 2006



access to high-quality collateral (pledges, sureties, etc.). Since January 2005, banks have been setting their provisions in line with the method they use to keep their accounts and compile their financial statements. Banks that use IFRS thus determine their provisions for receivables on the basis of an estimate of the expected future cash flows from these receivables (or related collateral). Those that use Czech accounting standards continue to set provisions using coefficients for the relevant classified loan category.

The classification of receivables by sector (see Table II.13) shows that non-financial corporations account for most of the increase in classified receivables (a rise of 19.3% to CZK 99.4 billion). However, due to a sharp rise in loans provided to non-financial corporations (of 21.0%) the ratio of classified receivables to the total volume of these receivables recorded a modest decline, from 15.9% to 15.6%. The lowest-risk category – watch loans – make up the majority of classified loans to non-financial corporations. NPLs to non-financial corporations totalled CZK 28.3 billion as of 31 December 2006.

Classified loans to individuals rose by 20.9% to CZK 23.3 billion in 2006. However, due to the significant growth of the overall credit portfolio, their share of total loans to individuals decreased from 5.1% to 4.7%. The increase in classified loans in the segment of individuals applied to all types of loans, but most of all to mortgages (a rise of CZK 1.5 billion, or 30.3%). NPLs to individuals totalled CZK 14.7 billion as of 31 December 2006.

Classified receivables from other banks amounted to CZK 2.0 billion (CZK 1.3 billion of which were watch loans) at the end of 2006, a fall of CZK 0.8 billion year on year.

Classified receivables from general government stayed at low levels (around 2% of total receivables from general government). The majority of them were recorded in the watch loan category. Most are receivables from municipalities.

2.4.2 Foreign exchange risk

The exposure of the domestic banking sector to foreign exchange risk remains limited. The absolute amount of foreign exchange assets and liabilities of the banking sector remained almost unchanged in 2006, totalling CZK 660.3 billion (assets) and CZK 532.2 billion (liabilities) at the year-end. Their share of the banking sector's total assets fell slightly – by 1.5 percentage points to 20.4% (assets) and by 1.7 percentage points to 16.9% (liabilities). Foreign exchange assets and liabilities (balance-sheet and off-balance-sheet) are showing a similar pattern over time, with no significant opening of the net foreign exchange position.

The structure of foreign exchange assets saw a year-on-year fall in receivables from banks of CZK 105.8 billion (32.7%) to CZK 217.7 billion, whereas foreign currency receivables from clients recorded an increase of CZK 70.0 billion (34.3%) to CZK 238.8 billion. Foreign currency bonds held by the banking sector rose only slightly in 2006 – by CZK 4.5 billion to CZK 122.9 billion.

The structure of foreign exchange liabilities in the Czech banking sector showed similar changes as the asset side, i.e. liabilities to banks fell by CZK 51.2 billion to CZK 191.4 billion, whereas foreign currency client deposits rose slightly, by CZK 28.6 billion to CZK 270.6 billion.

The shares of off-balance-sheet foreign exchange assets and liabilities in the off-balance-sheet total increased by 3.1 percentage points to 32.8% and by 1.7 percentage points to 30.4% respectively in 2006. This was due mainly to foreign currency derivatives transactions. However, the open position is not growing in the off-balance sheet either.

The banking sector recorded its largest open foreign exchange position – CZK 1.6 billion – vis-à-vis the Slovak koruna (a short position). This represents 0.8% of total regulatory capital (i.e. bank capital adjusted in accordance with the capital adequacy rules – see section 2.5). The second-largest open position is vis-à-vis the euro (long, CZK 1.2 billion) and the third-largest vis-à-vis the dollar (short, CZK 954.5 billion). There were no major year-on-year movements in these values.

2.4.3 Territorial risk (country risk)

The local character of domestic banks is also reflected in a relatively low and stable share of transactions with non-residents. These transactions move in line with foreign currency items, since approximately 68% of non-resident assets are denominated in foreign currency. As of 31 December 2006, non-resident assets amounted to CZK 689.1 billion, representing 21.2% of the banking sector's total assets. This is a slight decline of CZK 35.9 billion compared to the end of 2005. Non-resident liabilities also showed a modest decrease of CZK 14.9 billion to CZK 404.3 billion in this period.

Receivables from banks – amounting to CZK 289.0 billion – dominate the structure of non-resident assets, despite falling by CZK 115.4 billion year on year. In contrast, receivables from non-resident clients rose by CZK 35.9 billion to CZK 121.5 billion. Non-resident bonds held by domestic banks totalled CZK 172.6 billion at the end of 2006 (up by CZK 12.3 billion on a year earlier). Deposits from non-resident clients amounted to CZK 103.5 billion (a rise of CZK 8.6 billion).

Table II.14 lists the ten countries to which the Czech banking sector has the largest exposures as measured by total assets. There were no changes in structure over the past three quarters except at the bottom of the table, where the USA replaced Luxembourg. Apart from the USA, all are EU countries. The exposure to these ten countries accounts for 78.9% of the total international exposure. The exposure to Slovakia declined by CZK 47.1 billion year on year, mainly because of lower receivables from banks; loans to Slovak clients conversely continued to grow in 2006. The list of countries to which domestic banks have the biggest liabilities[60] is almost identical. The banking sector recorded its largest open net positions (i.e. the difference between assets and liabilities transactions) vis-à-vis Slovakia (positive, CZK 72.6 billion), the Netherlands (positive, CZK 40 billion) and Germany (positive, CZK 29.7 billion) as of 31 December 2006.

2.4.4 Liquidity risk

The liquidity of the Czech banking sector remains very good, despite a slight worsening of some liquidity indicators. Quick assets[61] declined somewhat in year-on-year comparison – by CZK 14.7 billion (1.6%) to CZK 933.6 billion – and

CHART II.15
Share of foreign currencies in banking sector balance sheet and off-balance sheet
(in %)

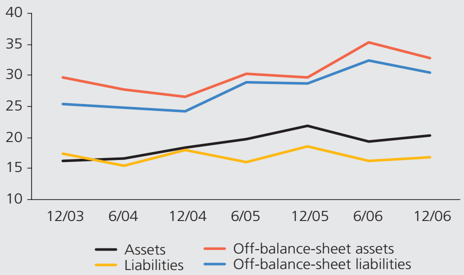


CHART II.16
Share of non-resident transactions in banking sector balance sheet and off-balance sheet
(in %)

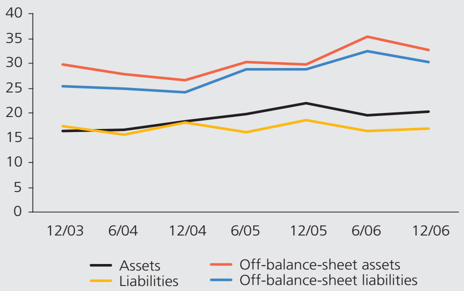


TABLE II.14
The ten countries with the largest exposures of the Czech banking sector as of 31 December 2006
(in CZK billions)

	Assets, total	Receivables from banks	Receivables from clients	Bonds
Slovakia	148.8	18.1	58.0	28.5
Germany	92.0	62.8	3.0	15.6
United Kingdom	66.5	30.3	2.3	13.0
Netherlands	59.3	32.7	5.6	17.9
Austria	39.0	23.4	1.9	2.8
France	33.8	17.6	5.0	4.2
Belgium	32.7	15.2	3.9	0.0
Italy	26.5	8.2	1.9	16.3
Greece	23.3	1.9	0.1	21.2
USA	21.8	7.5	1.1	10.5

60 In the case of liability transactions, only Italy is absent from the list of the ten largest countries. It is replaced by Ireland.

61 Quick assets comprise the following items: cash, deposits with central banks, T-bills and similar bonds issued by the state and central banks, current accounts with other banks and loans to other banks due within 24 hours.

TABLE II.15
Selected liquidity indicators

	2004	2005	2006
Total quick assets (in CZK billions)	864	948	934
Total quick assets/total assets (in %)	32.8	32.1	29.6
Total quick assets/total client deposits (in %)	49.9	49.4	44.4
Cumulative net balance sheet position to 3 months net of 80% of demand deposits (in %)	-1.8	-3.4	-7.6
Position on interbank market (in CZK billions)	40	78	56
receivables from banks	401	459	404
liabilities to banks	361	381	348
Loan coverage by primary funds (in %)	161.3	163.5	147.6
Share of demand deposits in total deposits, including banks (in %)	43.5	44.2	47.1
Share of value of time deposits > CZK 100 million in total deposits (in %)	18.8	21.1	18.8

CHART II.17
Quick assets
(in CZK billions; in %)

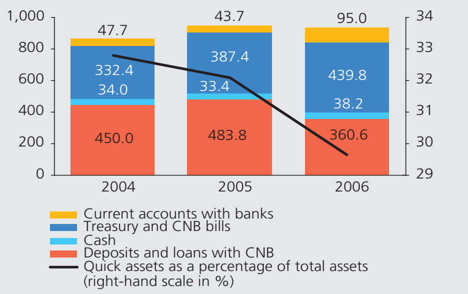


TABLE II.16
Banking sector capital structure
(in CZK billions)

	2004	2005	2006
A. TIER 1	141	160	172
Paid-up capital registered in Commercial Register	70	69	70
Paid-up share premium	11	13	14
Mandatory reserve funds	26	27	28
Other reserve funds (non-specific)	5	5	6
Retained earnings	41	57	66
Deductible items from Tier 1	12	12	12
Goodwill	3	3	3
Intangible assets other than goodwill	9	9	9
B. TIER 2	9	11	29
Deductible items	4	4	5
C. TIER 3	0	0	0
CAPITAL, TOTAL	147	167	196

their share in total assets fell, mainly because of the banking sector's growing total assets. The main factor underlying the decline in quick assets was a significant fall in funds deposited with the CNB and the NBS (a year-on-year decline of CZK 123.2 billion). The other quick assets items showed modest growth, in particular funds deposited on current accounts with other banks, which rose by CZK 51.3 billion. The volume of T-bills and government bonds increased by CZK 40.4 billion. The domestic banking sector as a whole continues to be a net creditor on the interbank market. Receivables from banks exceed liabilities to banks by CZK 55.8 billion.

2.5 CAPITAL ADEQUACY

Capital adequacy is of critical importance in banking regulation and supervision. Generally, capital adequacy means the ratio of capital to the risks to which a given entity is exposed. This ratio should be high enough so that the capital covers any losses arising from the entity's activities or, to put it differently, so that such losses are borne by the owners of the capital and not by the creditors of the entity. Capital adequacy can theoretically be calculated for any entity. However, it is of practical importance in the regulation of entities that use a large amount of external funds in their activities as compared to their own funds. The most difficult problem in calculating capital adequacy is identifying the extent of the risks to which an entity is exposed. It is easier to determine the size of its capital, although there are sometimes problems deciding whether or not certain items count as capital. Therefore, the concept of capital adequacy is subject to constant development and revision, with other types of banking risks being included in the calculation and so on. This was also the main reason for issuing the new capital adequacy framework, Basel II.[62] It is aimed at enabling more accurate measurement of credit risks (mainly using banks' own models) and at including operational risks in the capital adequacy calculation.

Total regulatory capital (i.e. capital adjusted for the purposes of the capital adequacy calculation) increased by CZK 28.6 billion (17.1%) to CZK 195.7 billion in 2006. The growth was due to the retention of part of the 2005 profit in banks' capital in the form of retained earnings or reserve funds (part of Tier 1) and the acceptance of subordinated debt or issuance of subordinated bonds in five banks (part of Tier 2).

Of the banking sector's overall 2005 profit of CZK 39.4 billion, banks paid CZK 23.6 billion in dividends and left CZK 13.9 billion in capital (CZK 12.0 billion as retained earnings and CZK 1.9 billion as mandatory additions to reserve funds).[63] However, some banks also paid dividends from previous years' retained earnings; these dividends totalled CZK 3.8 billion. Total retained earnings included in banks' capital thus rose by CZK 8.2 billion in 2006, compared to an increase of more than CZK 17 billion in the same period a year earlier.

Tier 2 increased by CZK 17.2 billion to CZK 28.5 billion in 2006, mainly due to accepted subordinated debt totalling CZK 14.7 billion. Higher growth was also recorded by the other capital funds item; this was linked with capital increases in

62 For more details, see part A, section 3.1.

63 The difference (CZK 1.9 billion) is made up of additions to social and other funds, which are not included in regulatory capital.

two banks.[64] In 2005, banks completed the mandatory cancellation of general reserves for standard loans, so this item no longer features in their capital. The ratio of Tier 2 to total regulatory capital increased by 7.8% to 14.6% in 2006.

Tier 3 capital is still not used in the domestic banking sector.[65]

In 2006, the total capital requirements of the banking sector rose by CZK 24.4 billion (21.6%) to CZK 137.2 billion. This increase was mainly due to continuing growth in the capital requirement for banking portfolio credit risk, which represents almost 93% of the total capital requirement. As in previous periods, this is because of banks' credit expansion, as reflected in a rise in assets with 100% and 50% risk weightings.[66] The total risk-weighted assets of the banking portfolio increased by CZK 367.8 billion (22.9%) to CZK 1,977.3 billion. However, the growth in their share of total assets slowed, staying below 55% throughout 2006.

The capital requirement for trading portfolio risks increased by CZK 1.3 billion to CZK 9.9 billion in 2006 (particularly in the second half of the year), mainly because of a rise in the capital requirement for general interest rate risk, which is the most significant item of the capital requirement for the trading portfolio. As of 31 December 2006, it represented 46.8% of the total capital requirement for the trading portfolio.

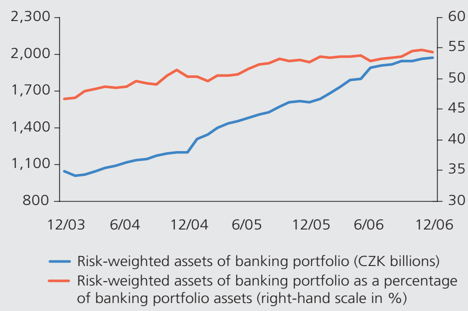
The capital ratio of the banking sector saw a year-on-year decline of 0.45 percentage point to an overall value of 11.41% as of the end of 2006, as a result of faster growth in capital requirements than in regulatory capital. Declines in capital adequacy were recorded by all bank groups, most of all the small banks.[67]

All banks complied with the required minimum capital ratio of 8% during 2006. Ten banks recorded a capital ratio of less than 10% at the end of the year, an annual increase of four banks.

TABLE II.17
Capital requirements and capital adequacy of the banking sector
(in CZK billions; in %)

	2004	2005	2006
TOTAL CAPITAL REQUIREMENTS	94	113	137
Capital requirement A			
- banking portfolio	86	105	127
Capital requirement B			
- trading portfolio	7	8	10
CAPITAL ADEQUACY (in %)	12.55	11.86	11.41

CHART II.18
Risk-weighted assets of banking portfolio



64 Under this item, both banks recorded an increase in registered capital, which was approved by their general meetings, and the funds were credited to the banks' accounts. These amounts will be transferred to the registered capital account when the capital increase is entered in the Commercial Register.

65 Tier 3 capital consists of subordinated debt with a minimum fixed maturity of two years.

66 A 50% risk weighting applies to mortgage loans granted to natural persons and secured by residential property.

67 All the banks in this group recorded falls in their capital ratios. This was due to only minimal growth in the capital of the small banks group in 2006 (a rise of 3.2%) as compared to the capital requirements, which increased by 34.8%.

3. THE CREDIT UNIONS SECTOR

3.1 BASIC CHARACTERISTICS

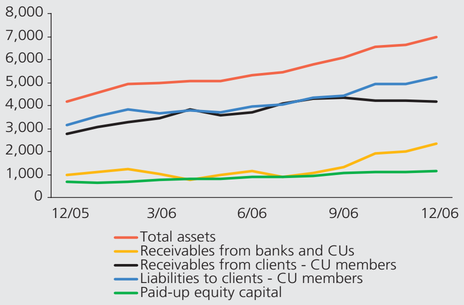
TABLE III.1
Number of CUs and their members

	2004	2005	2006
Number of active credit unions	33	20	20
Number of members	19,077	30,611	42,451

At the end of 2006, the sector of credit unions consisted of 20 active credit unions, the same number as in 2005. The assets of the credit unions sector amounted to almost CZK 7 billion as of 31 December 2006, representing around 0.1% of the assets of the entire financial sector. The number of credit union members rose from 30,611 to 42,451 in 2006, i.e. by around 39%.

Compared to banks, the credit union form of business predefines certain specific features of the sector. Credit unions carry on activities for their members.[68] These activities chiefly include accepting deposits and providing loans. The capital of a credit union is made up of membership contributions (both basic membership contributions and any other membership contributions).

CHART III.1
Basic CU sector indicators
(in CZK millions)



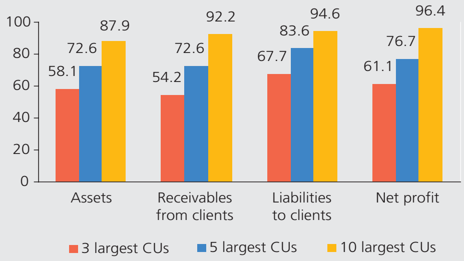
Like banks, credit unions must comply with regulatory limits and prudential rules. In addition to a minimum capital requirement (CZK 35 million), the main limits relate to capital adequacy (8%), exposures (20%, 25% and 800% of capital)[69] and liquidity. In connection with the ongoing implementation of Basel II and European directives in the Czech Republic, some qualitative regulatory requirements (for example in the area of internal control systems and risk management systems) apply to credit unions as credit institutions.

Under the Act on Credit Unions (ACU)[70] the CNB approves certain actions taken by credit unions. This includes for example the approval of persons appointed to credit union bodies (boards of directors, credit committees and control committees) and persons nominated as senior officers, and the approval of auditors, other membership contributions, qualifying holdings, subordinated debt, etc.

If a member's share of a credit union's capital were to exceed 5% as a result of making an additional membership contribution to the capital, this contribution is subject to the prior consent of the CNB. Acquiring a qualifying holding in a credit union (when reaching at least 10% of the capital or of the voting rights) or increasing a qualifying holding to at least 20%, 33% or 50%, is also subject to the prior consent of the CNB.

3.2 THE CREDIT UNIONS SECTOR IN 2006

CHART III.2
Concentration of CU sector
(as of 31 December 2006; in %)



The credit unions sector has seen relatively rapid growth in recent years. In 2006 alone, the sector's assets grew by almost 70% (from CZK 4.2 billion in 2005 to CZK 7.0 billion in 2006). Growth in assets is particularly visible in the four largest credit unions, whose total assets almost doubled in 2006 alone.

68 Credit unions are also authorised, inter alia, to deposit funds in credit unions and banks or to accept loans from credit unions and banks, solely for the purpose of performing activities for their members. Under Article 3(5) of the ACU, the performance of credit union activities for the state and its organisational units and other public institutions is not conditional on credit union membership. However, these activities are insignificant in terms of volume.

69 These capital adequacy and exposure limits were introduced on 1 August 2006 by a CNB Provision. Different limits, laid down in Ministry of Finance decrees, had previously been in effect.

70 Act No. 87/1995 Coll., on Savings and Loan Associations and Certain Related Measures and on the Amendment of Czech National Council Act No. 586/1992 Coll., on Income Tax, as amended.

The degree of concentration in the credit unions sector is higher than in the banking sector. At the end of 2006, the three largest credit unions accounted for 58.1% – and the five largest credit unions for 72.6% – of the sector's total assets. The Herfindahl index calculated from the total assets of the credit unions sector rose from 0.108 to 0.148 in 2006. This indicates a marked increase in the concentration of this sector.

Receivables from clients (credit union members) are the main item for the majority of credit unions. This item accounted for almost 60% of assets on average at the end of 2006 and is associated with one of the credit unions' main activities, i.e. providing loans. The volume of loans rose by 50.8% in 2006, from CZK 2.8 billion to CZK 4.2 billion. Receivables from banks and credit unions are the second most significant item (around 33% of the balance sheet). Other asset items are much less significant.

Liabilities to clients (credit union members), which accounted for almost 75% of liabilities on average at the end of 2006, are the dominant item of credit unions' liabilities. Their volume increased by 66.1% in 2006, from CZK 3.1 billion to CZK 5.2 billion. Equity capital (18.3% of the balance sheet), which consists of basic and other membership contributions, is the second most significant item on the liability side. In the case of some credit unions, part of the capital was not paid up. Other liability items are insignificant in terms of volume.

The credit unions sector as a whole posted a profit of CZK 84.1 million in 2006, more than double the 2005 figure. The bulk of credit unions' income is generated in the interest rate area, which is associated with lending. Similarly, the main part of costs relates to interest paid to clients, which is linked to the acceptance of deposits as the main financing source for credit unions' activities. Net income from fees and commissions is a complementary source of profit. Of the total of 20 credit unions, 17 were profit-making and 3 were loss-making at the end of 2006. In 2005, 18 credit unions had been profitable, while 2 recorded a loss.

A Ministry of Finance decree[71] stipulating the principles for classifying loan receivables and for provisioning for these receivables by credit unions has been in effect since 2005. As a result, the data given for this area are for 2005 and 2006 only. The data reported by individual credit unions suggest a relatively low level of classified receivables. Classified receivables amounted to CZK 112.2 billion at the end of 2006, i.e. roughly 1.7% of credit unions' total receivables.

The regulatory capital of credit unions and its structure differ from that of banks. Under Article 8 of the ACU, the capital of credit unions is composed of the sum of paid-up equity capital, the risk fund, the reserve fund and other reserve funds created from profit and retained earnings net of accumulated losses, the loss of the current accounting period and intangible assets. The settlement duty and subordinated debt can also be included in capital to the extent laid down in the Act and subject to fulfilment of the set criteria.

As in the case of banks, the amount of regulatory capital forms the basis for the regulatory limits derived from it. The capital requirement for credit unions was increased in previous years to the present CZK 35 million required by law. The capital of the entire credit unions sector totalled CZK 1,203.3 million at the end of 2006.

71 Decree of the Ministry of Finance No. 319 of 29 July 2005, stipulating the principles for classifying loan receivables and for provisioning for these receivables by credit unions.

Table III.2
CU asset structure
(in CZK millions)

	2004	2005	2006
Total assets	2,146	4,190	6,977
Cash and deposits with CNB	112	105	189
Receivables from banks and CUs	453	982	2,335
Receivables from clients – CU members	1,337	2,756	4,155
Debt securities	31	35	0
Intangible assets	6	4	3
Tangible assets	85	79	106
Receivables from paid-up capital	50	152	120

Table III.3
CU liabilities and own capital
(in CZK millions)

	2004	2005	2006
Total liabilities	2,146	4,190	6,977
Liabilities to banks	62	130	288
Liabilities to clients - CU members	1,525	3,146	5,224
Reserves	6	1	1
Equity capital	480	815	1,279
of which Paid-up equity capital	418	662	1,159
Reserve funds and other funds created from profit	11	25	40
Retained profits (accumulated losses)	-2	-6	8
Profit (loss) for accounting period	18	39	84

Table III. 4
CU sector performance
(in CZK millions)

	2004	2005	2006
Interest income and similar income	150	276	498
Interest expenses and similar expenses	94	164	267
Income from fees and commissions	55	51	56
Expenses on fees and commissions	36	30	40
Other operating income	25	30	126
Other operating expenses	14	20	131
Administrative expenses	59	91	118
Write-offs, creation and use of provisions and reserves for fixed assets	3	1	18
Release of provisions and reserves for receivables and guarantees, income from previously written-off receivables	2	17	1
Write-offs, creation and use of reserves and provisions for receivables and guarantees	4	26	11
Income tax	3	5	12
Profit (loss) for accounting period	18	39	84

Table III.5
Classification of CU receivables
(receivables from clients and banks; in CZK millions)

	12/2005	6/2006	12/2006
Total receivables	2,525	4,220	6,514
of which:			
standard receivables	2,436	4,130	6,402
watch receivables	48	21	31
substandard receivables	29	44	59
doubtful receivables	3	17	6
loss receivables	9	7	16
Sum of homogeneous standard portfolio receivables	214	501	0
Sum of receivables portfolios requiring attention	2	3	0
Sum of provisions	13	12	21
Ratio of classified receivables to total volume	3,32%	1,96%	1,72%

4. THE CAPITAL MARKET

4.1 INVESTMENT SERVICES PROVIDERS

4.1.1 Major events in investment service provision

The investment services providers sector was stable in 2006, recording no major changes except for a continuing rise in the number of entities registered as investment intermediaries and foreign entities authorised to provide investment services under the single European licence.

The major events in 2006 included thorough preparations for the key changes associated with the introduction of the regulatory framework for the application of new prudential rules to banks, credit unions and investment firms (Basel II) and the implementation of Directive 2004/39/EC on Markets in Financial Instruments (MiFID).

The CNB prepared a source document for a government bill to amend some laws in connection with the setting of capital requirements for banks, credit unions, investment firms and electronic money institutions, and a draft implementing measure to transpose amendments to European directives laying down prudential rules for banks, credit unions and investment firms[72] into the national legislation. CNB Decree No. 605/2006 Coll., on certain disclosure duties of an investment firm, took effect on 1 January 2007. This decree introduces a duty for investment firms to fulfil some disclosure duties using the internet interface of the CNB's Non-bank Data Collection System (SDNS) and, in the case of banks, using the EDIFACT data channel. In this regard, relevant statements were designed for the individual disclosure duties, accompanied by a methodological description of all data files, data areas, information elements and dimensional parameters.

CHART IV.1
Number of investment firms
(at end of period)

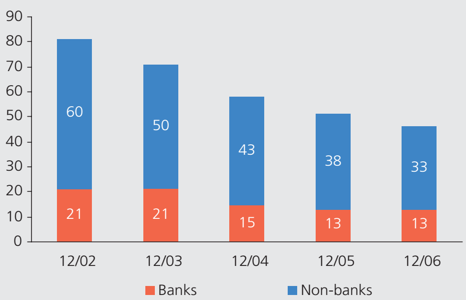
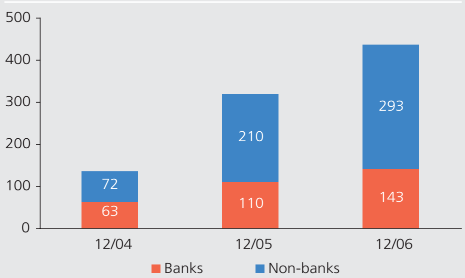


CHART IV.2
Number of foreign entities authorised to provide investment services in the Czech Republic under the single European licence
(at end of period)



4.1.2 Investment firms

At the start of 2006, a total of 51 investment firms had been granted investment firm licences by the CNB. Of this total, 38 were non-bank institutions and 13 were banks. By the end of the period under review, the total number of investment firms had decreased to 46 (33 non-banks and 13 banks).

During 2006, no new investment firm licences were granted, 2 such licences were withdrawn and 3 such licences expired owing to changes in objects of business.

A total of 210 entities using the possibility to provide investment services in the Czech Republic without establishing an organisational unit under the single European licence were registered at the start of 2006. In 2006, the CNB notified 81 foreign non-banks intending to provide investment services in the Czech Republic without an organisational unit, and further 2 entities intending to provide investment services through an organisational unit, of their disclosure duties and rules of conduct towards clients. As of 31 December 2006, the CNB registered a total of 436 foreign entities (143 banks and 293 non-banks) authorised to provide

72 The transposition of Directive 2006/48/EC of the European Parliament and of the Council relating to the taking-up and pursuit of the business of credit institutions and Directive 2006/49/EC of the European Parliament and of the Council on the capital adequacy of investment firms and credit institutions.

investment firm services in the Czech Republic under the single European licence. Twelve of these foreign entities were providing investment services via branches.

Investment firms[73] carried out trades for their clients totalling CZK 419,304 billion in 2006, of which share trades amounted to CZK 3,415 billion, bond trades to CZK 2,341 billion, derivatives trades[74] to CZK 411,776 billion, money market instrument trades to CZK 978 billion and unit trades to CZK 795 billion.

Chart IV.4 illustrates the concentration of trades for clients (excluding derivatives). The first three investment firms include just one non-bank, the first five include two non-banks and the first ten include four non-banks.

During the period under review, investment firms also carried out trades for their own account totalling CZK 55,499 billion, of which share trades accounted for CZK 2,247 billion, bond trades for CZK 2,505 billion, derivatives trades for CZK 39,955 billion and money market instrument trades for CZK 10,792 billion.

As of 31 December 2006, investment firms had concluded 1,149 thousand contracts, about 180 thousand of which were active. Client assets amounted to CZK 991 billion. The funds managed in individual portfolios totalled around CZK 325 billion as of the same date.

Non-bank investment firms' own capital totalled CZK 3,772 million as of 31 December 2006. Most investment firms had capital in the range of CZK 20–50 million or over CZK 100 million. A more detailed breakdown of investment firms by own capital is given in Chart IV.6.

4.1.3 Other supervised entities – investment intermediaries and brokers

The CNB had registered 8,387 investment intermediaries as of the start of 2006. A total of 2,273 investment intermediary registration certificates were issued and 32 were withdrawn or elapsed in the period under review. At the end of 2006, 10,628 entities (mostly natural persons) were thus registered as investment intermediaries.

In the period under review, the CNB also issued 70 broker's licences and withdrew one such licence. The CNB registered a total of 1,859 licensed brokers at the end of the period under review. Thirty rounds of broker examinations took place in 2006, with 270 participants.

CHART IV.3
Structure of procurement trades
(as of 31 December 2006)

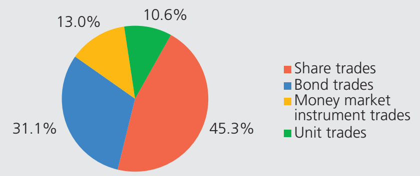


CHART IV.4
Shares in procurement trades
(in %; as of 31 December 2006)

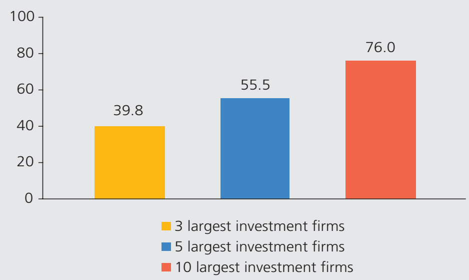


CHART IV.5
Trades of investment firms for own account
(as of 31 December 2006)

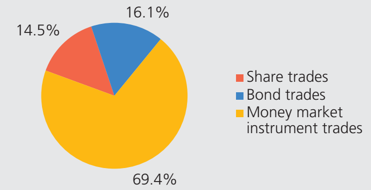
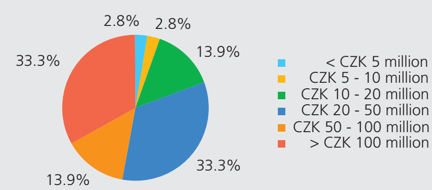


CHART IV.6
Investment firms by total own capital
(as of 31 December 2006)



73 Entities licensed by the CNB and branches of entities registered in another Member State of the European Union and authorised to provide investment services in the Czech Republic.

74 The volumes of derivatives transactions are recorded at nominal prices of underlying assets.

CHART IV.7

Market shares of investment companies by volume of funds managed in mutual funds

(in %; as of 31 December 2006)

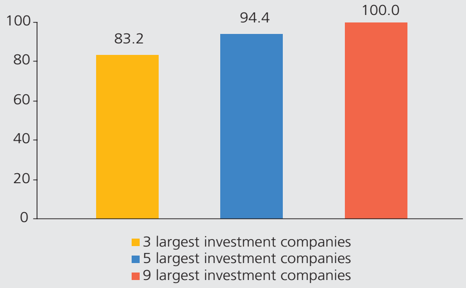


CHART IV.8

Structure of notified funds by country

(as of 31 December 2006)

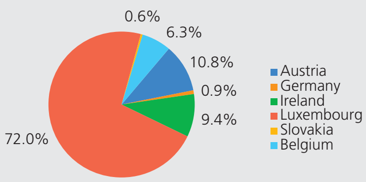


CHART IV.9

Structure of total investments in open-end mutual funds by fund type

(as of 31 December 2006)

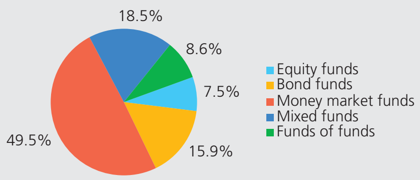


TABLE IV.1

Structure of total investments in open-end mutual funds by fund type

(as of 31 December; in CZK millions)

	2004	2005	2006
Equity OMFs	4,863	7,760	11,656
Bond OMFs	21,912	26,842	24,831
Money market OMFs	63,088	78,041	77,339
Mixed OMFs	22,488	23,767	28,949
Funds of funds OMFs	459	6,330	13,450
TOTAL OMFs	112,810	142,740	156,225

4.2 COLLECTIVE INVESTMENT

4.2.1. Major events relating to collective investment

An amendment to the Collective Investment Act, introducing real estate funds for the public and funds for qualified investors, took effect on 26 May 2006. As a result of this amendment, the CNB conducted more administrative proceedings on applications for investment company licences submitted by entities wishing to manage such funds. In 2006 Q4, the CNB received the first licence application for a real estate investment fund for qualified investors and the first licence application for a special real estate fund for the public.

4.2.2 Overview of collective investment undertakings

At the start of 2006, no investment funds were active on the Czech capital market under licences granted by the CNB (except investment funds in liquidation or bankruptcy). There were 9 active investment companies (i.e. excluding those in liquidation or bankruptcy or those whose licences have been revoked). They managed 65 open-end mutual funds. A total of 53 foreign collective investment undertakings were also active in this area, managing 1,038 foreign funds and sub-funds,[75] of which 1,025 were managed under the single European licence. The number of active investment funds remained zero at the end of the period under review. The number of active investment companies increased to 13 and the number of open-end mutual funds managed by them rose to 77. The number of foreign collective investment undertakings also increased, to 58 companies with 1,282 funds and sub-funds, with 1,271 funds and sub-funds operating in the Czech Republic under the single European licence and 11 as foreign special funds.

Four new investment companies – Amista investiční společnost, a.s., AXA investiční společnost, a.s., Reico investiční společnost České spořitelny, a.s. and Orion Capital Management investiční společnost, a.s. – were granted licences in the period under review. A licence for the management of client assets was granted to Investiční společnost České spořitelny, a.s. Investment company licences were denied in two cases.

Fourteen authorisations to establish open-end mutual funds[76] were issued in 2006. One authorisation to establish an open-end mutual fund was withdrawn at the company's own request and one decision authorising a merger of open-end mutual funds was issued.

In all, 281 new foreign funds and sub-funds made notifications under the European passport and 35 foreign funds and sub-funds operating under the European passport closed down in 2006. As of 31 December 2006, a total of 1,271 foreign funds and sub-funds were notified in the Czech Republic under the European passport, managed by or operating within 58 entities from 6 countries. However, the number of funds and sub-funds actually offering their securities to the public is lower. A total of 29 foreign investment companies had submitted notifications of service provision in the Czech Republic under the single licence as of 31 December 2006.

75 Part of a collective investment fund's assets with separate accounting.

76 This included 3 standard funds and 11 special funds, of which 2 were funds of qualified investors.

4.2.3 Volume of assets managed by domestic collective investment undertakings

Funds in open-end mutual funds increased by CZK 13.5 billion year on year in the period under review, to CZK 156.2 billion. Positive net sales of open-end mutual fund units totalled around CZK 9.1 billion in 2006. The average return on investment in collective investment funds was 3.1%.

4.3 PENSION FUNDS

4.3.1. Major events relating to pension funds

Pension funds were among those financial institutions whose administrative workload was reduced thanks to the integration of reporting. In mid-2006, pension funds started to send data using the internet interface of the CNB's Non-bank Data Collection System (SDNS) for both statistical and supervisory purposes. This eliminated some duplications that had been present in pension fund statements before the integration of supervision.

In connection with some proposed legislative changes in this area a working group was established at the Ministry of Finance at the end of 2006. Its task is to prepare an amendment to the Act on Private Pension Insurance, separating the assets of pension fund shareholders from funds credited to pension planholders. A change in planholders' status from creditors to owners should significantly enhance the transparency of pension funds. In particular, the issue of the costs of pension scheme contracts should be resolved.

A World Bank project concerning the quality of pension fund management in the Czech Republic continued in 2006.

4.3.2. Number of licensed entities

A total of 11 pension funds (excluding pension funds in liquidation or bankruptcy) were active on the private pension scheme market at the beginning of 2006. This number remained unchanged over the course of the year.

4.3.3 Licensing and authorisation activities – important decisions

In October 2006 the CNB authorised the merger of Hornický penzijní fond Ostrava, a.s., with ČSOB Penzijní fond Progres, a.s., a member of the ČSOB group.

4.3.4 Structure of pension fund assets and liabilities

The total assets managed by pension funds amounted to almost CZK 145.9 billion at the end of 2006, up by CZK 22.5 billion year on year. Profit fell by CZK 0.5 billion year on year, to CZK 4.1 billion. The annual increase in the book value of assets was 2.6%.

The growth in pension fund assets and profit over the past five years is shown in Chart IV.13. Concentration in the pension fund sector from the point of view of total assets is relatively high and has remained broadly unchanged in recent years. Its evolution over the past three years is shown in Chart IV.14. Chart IV.15 illustrates the allocation of pension fund investments by asset type.

CHART IV.10
Total investments in open-end mutual funds by fund type at end of period

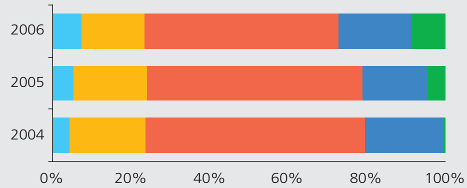


CHART IV.11
Assets of collective investment funds
(in CZK billions; at end of period; source: AFAM)

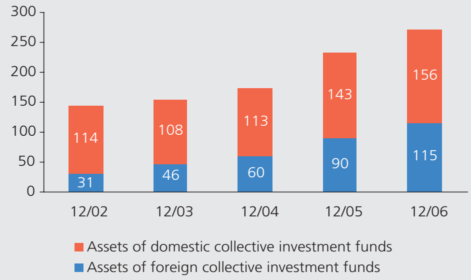


CHART IV.12
Domestic and foreign funds market segmentation
(as of 31 December 2006; source: AFAM)

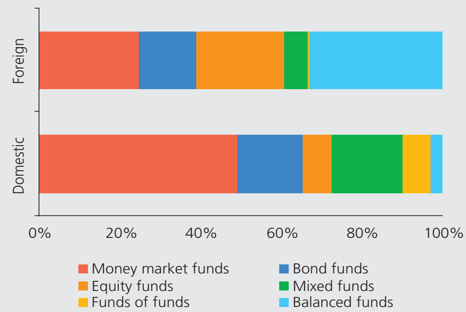


CHART IV.13
Total assets and profit of pension funds
(at end of period; in CZK billions)

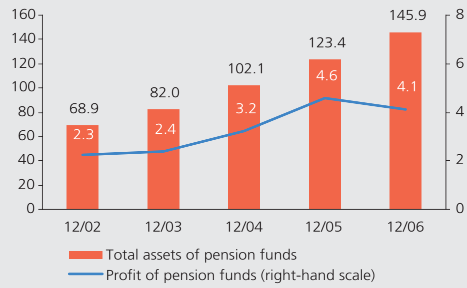


CHART IV.14
Concentration in pension fund sector by volume of assets
(in %; as of 31 December 2006)

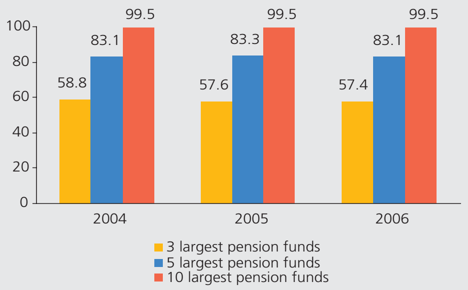


CHART IV.15
Structure of pension fund assets
(as of 31 December 2006)

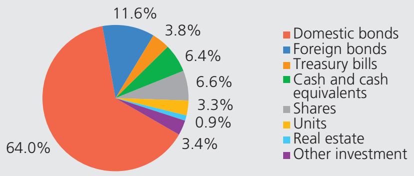


CHART IV.16
Planholders' funds
(in CZK billions; at end of period)

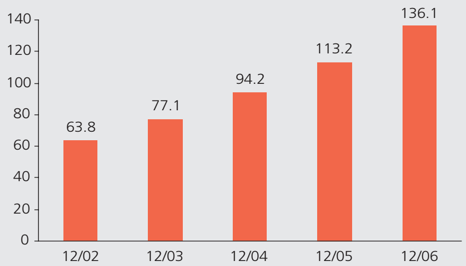
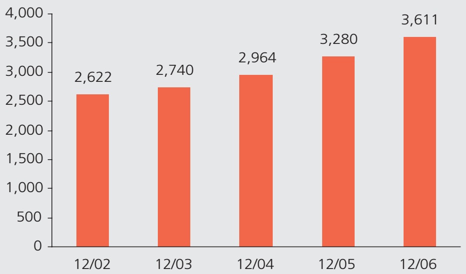


CHART IV.17
Number of planholders
(thousands; at end of period)



4.3.5 Volume of planholders' funds

The funds of pension planholders, i.e. planholders' deposits including state contributions, employers' contributions and related income, amounted to around CZK 136.1 billion at the end of 2006. This represented an increase of CZK 22.9 billion by comparison with 2005. The average volume of funds per planholder thus increased from CZK 34,500 to CZK 37,700. There were 3.6 million pension planholders at the end of 2006.

4.4 REGULATED MARKETS

4.4.1. Major events relating to trading on regulated markets

Calculation of the PX 50 and PX-D indices was terminated on 20 March 2006. These indices were replaced by the PX index, which continued seamlessly where the PX 50 had left off.

On 18 July 2006, the CNB granted the Prague Stock Exchange (PSE) a licence for trading in new types of investment instruments. The extended licence allows the PSE to organise trading in investment certificates, option warrants, other domestic securities to which similar rights can be attached, and foreign securities bearing similar rights (warrants). The new licence also extends the range of underlying assets for futures trading.

On 4 October 2006, trading in investment certificates was officially launched on the PSE's official free market. Initially, two investment certificates issued by Raiffeisen Centrobank AG were traded. Seven investment certificates were traded on the PSE at the end of 2006, of which six were index certificates and one was a turbo certificate. On 11 December 2006, the PSE launched trading in warrants on the official free market. The first traded warrant was issued by ECM Real Estate Investments A.G.

On 5 October, the PSE launched futures trading on the PX index. These financial instruments are traded on the PSE's regulated special market. The SPAD trading segment is used for futures trading.

On 7 December 2006, the PSE launched trading in a new issue of shares in ECM Real Estate Investments A.G. on the main exchange market. On 18 December 2006, trading in a new issue of Pegas Nonwovens shares started on the main exchange market.

4.4.2 Trading on regulated markets

The market capitalisation of securities traded on the regulated markets recorded annual growth on both the PSE and the OTC market operated by RM-Systém. The market capitalisation of stocks traded on the PSE was CZK 1,592 billion on 31 December 2006, up by 19.6% on the end of 2005. The number of share issues traded on this market fell from 39 to 32. Trading in shares also declined, from CZK 1,041.2 billion to CZK 848.9 billion.

The number of bond issues traded on the PSE rose by 14 compared to the previous year, to 110. The total volume of bond transactions grew by 12.3% compared to 2005, from CZK 533.2 billion to CZK 598.9 billion. The evolution of the number of issues traded on the exchange is shown in Chart IV.18.

The market capitalisation of shares traded on the RM-S market rose by 12.4% to CZK 1,621.9 billion. The number of share issues traded on the RM-S market in the period under review fell by 24.3%, from 70 to 53. The trading volume recorded a sharper decline, from CZK 5.4 billion to CZK 3.7 billion.

Trading in bonds in RM-S was negligible despite the fact that 54 issues were registered there. The volume of bond trades in RM-S fell from CZK 1.1 billion to CZK 0.2 billion.

The share of the RM-S market in the total trading volume on the regulated markets has been falling steadily. Having fallen below 1% in 2003, it decreased to 0.4% in 2005 and edged down further to 0.3% in 2006 amid an overall decline in trading volumes. The significance of the individual securities markets in terms of the trading volume on regulated markets is shown in Chart IV.19.

By comparison with the previous year, the total trading volume on the regulated markets fell by CZK 129.3 billion. Although the share of bond transactions in the total trading volume had been falling in previous years, this trend reversed in 2006. The share of bonds rose from 33.8% to 41.3% in relative terms and CZK 64.6 billion in absolute terms. Share transactions declined by CZK 192.3 billion, i.e. 7.5% in relative terms.

As for the bond market, the PSE accounted for almost all transactions on the regulated markets. This data is shown in Table IV.2, while the evolution of the volume of transactions by security type since 2000 is illustrated in Chart IV.20.

As the index bases for both markets are dominated by the same stocks, their overall evolution is similar and their fluctuations correspond. The PSE's PX index rose from 1,473.0 points at the end of 2005 to 1,588.9 points at the end of 2006, i.e. by 7.8%. The RM-System's PK 30 index showed even stronger growth of 9.7%, rising from 2,364.9 points to 2,595.3 points. The evolution of the PX exchange index, the PK 30 off-exchange index and the total volume of trading on regulated markets are shown in Chart IV.21.

Chart IV.22 compares the changes in capital market share price indices since 2001. The PX index gained 360% over this period, a figure comparable to those recorded by other exchanges in Central and Eastern Europe.

4.4.3 Trading off the regulated markets

Securities transactions executed off the regulated markets[77] totalled CZK 3,182.5 billion in 2006. This represents a year-on-year increase of 23.2%. The volume of transactions at the Prague Securities Centre has been declining steadily and reached an all-time low of CZK 2.6 billion in 2006. By contrast, the volume of transactions settled through UNIVYC continued to grow gradually, from CZK 2,568.9 billion to CZK 3,179.9 billion. Trading volumes off the regulated markets in the past five years are shown in Chart IV.23.

The structure of transactions off the regulated markets by security type is in line with that on the regulated markets. Shares account for 58.7% of the total volume of transactions on the regulated markets and 59.4% of transactions off the

77 Transactions executed off the regulated markets are transactions where, in the case of securities transfers executed at the Prague Securities Centre, the counterparties state the price paid for the transfer. In the case of UNIVYC transactions, such transactions are commercial transfers and non-commercial transactions involving the transfer of money.

CHART IV.18
Number of issues on PSE
(as of 31 December)

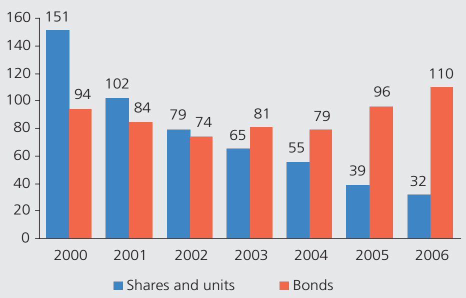


CHART IV.19
Trading volume on regulated markets
(in CZK billions)

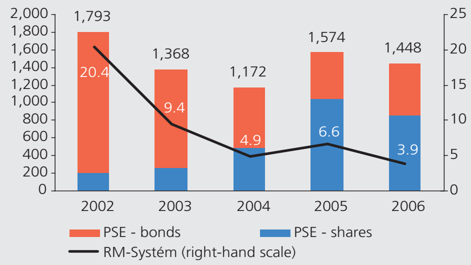


TABLE IV.2
Trading volume structure by instruments on PSE and RM-S in 2006

	Shares	Bonds	Total
		in CZK billions	
PSE	848.9	598.9	1,447.8
RM-S	3.7	0.2	3.9
Total	852.6	599.1	1,451.7
		in %	
PSE	99.6	100.0	99.7
RM-S	0.4	0.0	0.3
Total	100.0	100.0	100.0

CHART IV.20
Trading volume of shares, units and bonds on regulated markets
(in CZK billions)

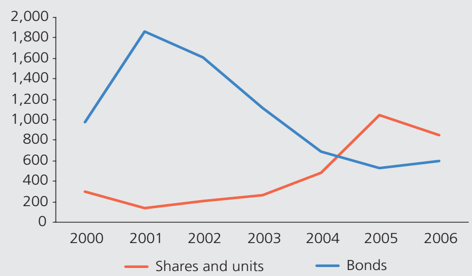


CHART IV.21
Trading volume on regulated markets; PX and PK 30 indices
(trading volume in CZK billions)

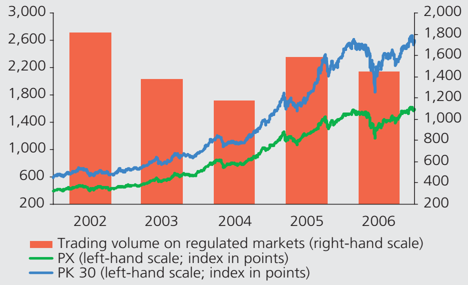


CHART IV.22
Share price indices
(2001 = 100%; source: Eurostat)

CHART IV.23
Trading volume off regulated markets
(in CZK billions)

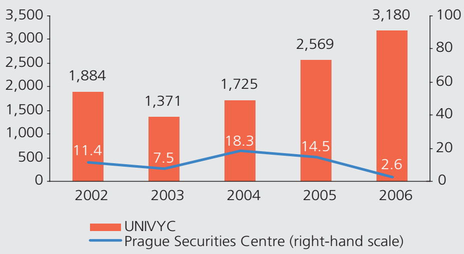


TABLE IV.3
Trading volume structure by investments on UNIVYC and SCP in 2006

	Shares	Bonds	Total
		in CZK billions	
UNIVYC	1,891.3	1,288.6	3,179.9
SCP	2.1	0.5	2.6
Total	1,893.4	1,289.1	3,182.5
		in %	
UNIVYC	99.9	100.0	99.9
SCP	0.1	0.0	0.1
Total	100.0	100.0	100.0

regulated markets. Just like the regulated markets are dominated by the PSE, so bilateral transactions settled through UNIVYC play the main role off the regulated markets. The share of the Prague Securities Centre is marginal. This information is shown in Table IV.3.

4.5 SECURITIES ISSUES

4.5.1 Major events relating to securities issues

A "technical amendment" of the Act on Capital Market Undertakings was adopted in 2006 in order to transpose Directive 2003/71/EC of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC. The main change was the introduction of a "single passport" for issuers.[78] The amendment also repealed the existing division into prospectus and abridged prospectus, changed the language requirements for prospectuses and introduced more variable prospectuses for different security types. The existing Decree No. 263/2004 Coll., setting out the minimum essential elements of a security prospectus and an abridged security prospectus, was replaced by direct application of Commission Regulation (EC) No 809/2004 of 29 April 2004 implementing Directive 2003/71/EC of the European Parliament and of the Council as regards information contained in prospectuses as well as the format, incorporation by reference and publication of such prospectuses and dissemination of advertisements.

In the period under review, 29 foreign entities used the single passport (securities of 3 issuers were accepted for trading on the regulated market based on notifications). A total of 63 prospectuses, base prospectuses and supplements to prospectuses were notified to the CNB. The CNB gave notification of one prospectus abroad.

4.5.2 New issues

There were 51 bond issues in 2006, of which 17 were issues of listed bonds (totalling CZK 36.3 billion) and 34 were issues of unlisted bonds.

4.5.3 Publicly offered unlisted securities

In 2006, the CNB approved prospectuses for offers to the public of five unlisted shares aimed at increasing equity. The CNB also approved 20 issue conditions for unlisted bonds that were not offered to the public. In 14 cases the offer of unlisted bonds and mortgage bonds took the form of an offer to the public. The breakdown of listed investment instruments as of the year-end is shown in Chart IV.25.

4.5.4 Issuers of listed securities

As of 31 December 2006, the CNB supervised 92 issuers of listed securities, 8 of which were foreign.

The annual and half-yearly reports of issuers of listed securities continued to be checked in 2006. Information from the 2005 annual reports of 89 issuers was verified. Although methodological instructions were issued at the start of 2006

78 A prospectus approved in one EU Member State is also valid in other EU Member States.

concerning the required content of annual reports, the most frequent shortcomings in the annual reports were inadequate descriptions of the principles of remuneration of senior officers and supervisory board members, erroneous structures of remuneration of auditors and insufficient reference to accounting under IFRS/IAS. Information from the half-yearly reports for 2006 H1 of 88 issuers was evaluated. The main shortcomings in the half-yearly reports were incorrect reference periods in the financial statements and insufficient descriptions of the issuer's activity over the past six months. The issuers were notified of the shortcomings in their annual and half-yearly reports and administrative proceedings were opened in one case.

After assessing the specific circumstances, the CNB allowed three issuers to fulfil their disclosure duty in the Czech Republic in English. All these issuers were registered abroad.

In 2006, the CNB conducted 12 administrative proceedings concerning requests of listed securities issuers – who are obliged to compile both financial statements and consolidated financial statements – for permission to publish only one of these in their annual reports. The CNB evaluates whether an annual report containing only financial statements (or only consolidated financial statements) would still provide investors with a true and fair picture of the issuer's financial condition, business activities and financial results. The CNB approved all but one of these requests.

4.5.5 Takeover bids and public share-purchase contract offers

The CNB conducted 16 administrative proceedings relating to takeover bids or public share-purchase contract offers in the period under review, of which:

- 13 concerned a mandatory takeover bid, of which:
    - 1 concerned a combined mandatory takeover bid and purchase offer – consent granted;
    - 12 concerned a takeover bid only – consent granted in 7 cases, bid prohibited in 3 cases and proceedings terminated due to withdrawal of applications in 2 cases.
- 1 concerned a public share-purchase contract offer relating to listed participating securities – consent granted;
- 1 concerned a voluntary takeover bid relating to listed securities – bid prohibited;
- 1 concerned an application for relief from the takeover bid duty – application found irrelevant and proceedings terminated.

In an effort to make as much information as possible available to shareholders entitled to accept takeover bids, a list thereof is published and updated daily at www.sec.cz under *List of Takeover Bids* (a temporary location used for the sake of continuity). It contains an overview of share issues where a takeover bid published with the CNB's consent is currently taking place or has already taken place. It enables investors to find out who is offering to buy participating securities and at what price, the dates from and until which the bid is binding, and the bidder's reason for making the bid. The daily updates enable investors to react to bids in time.

4.5.6 Squeeze-outs

The right to purchase participating securities ("squeeze-out") allows the General Meeting of a company to decide to transfer all other participating securities to the main shareholder. Such a resolution of the General Meeting is subject to prior approval by the CNB of the amount of the consideration proposed by the main shareholder. In the approval proceedings, the CNB carefully examines whether the

CHART IV.24
Domiciles of notified securities prospectuses
(as of 31 December 2006)

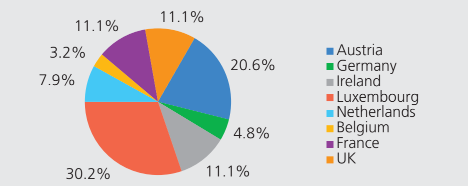
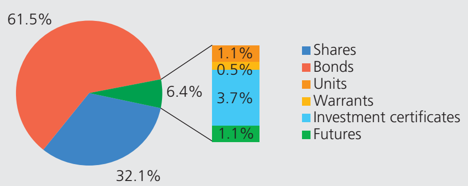


CHART IV.25
Listed investment instruments
(as of 31 December 2006)



expert opinion proves the adequacy of the consideration offered to minority shareholders. In this context, the CNB received 77 requests for prior consent in 2006 and issued 79 decisions (some of the proceedings opened in 2005 were concluded), of which:

- approval was granted in 52 cases (usually after a request for additional information);
- approval was refused in 22 cases (in 6 cases an appeal was filed against the decision, but all the decisions were confirmed in the second instance);
- the administrative proceedings were discontinued in 5 cases due to withdrawal of the application.

5. THE INSURANCE MARKET

5.1 NUMBER OF INSURANCE UNDERTAKINGS

The number of insurance undertakings registered in the Czech Republic (domestic insurance undertakings) remained unchanged compared to a year earlier. As of 31 December 2006, there were 33 domestic insurance undertakings active on the Czech insurance market. This figure does not include the Czech Insurers' Bureau.[79]

Domestic insurance undertakings continued to expand their activities abroad. In 2006, Winterthur pojišťovna, a.s.[80] carried on insurance business through branches in Slovakia and Norway, and 14 domestic insurance undertakings were authorised to carry on insurance business in other EU or EEA countries under the freedom to provide services.

Insurance undertakings from other EU or EEA countries remained interested in carrying on insurance business in the Czech Republic through branches or under the freedom to provide services in 2006.[81] The number of branches from other EU Member States increased by 3 compared to 2005. In 2006, the CNB received notifications from Österreichische Hagelversicherung – Versicherungsverein auf Gegenseitigkeit, organizační složka, Deutscher Ring Lebensversicherungs-AG, pobočka pro Českou republiku, AIG EUROPE, S.A., pobočka pro Českou republiku, and HDI Hannover Versicherung AG, organizační složka. On the other hand, Gothaer Allgemeine Versicherung Aktiengesellschaft, organizační složka pro Českou republiku, closed down. A licence to carry on insurance business through a branch was also granted to Swiss insurance undertaking Elvia Reiseversicherungs-Gesellschaft AG. Thus, a total of 15 branches of insurance undertakings from other EU Member States and 1 branch of an insurance undertaking from a third country were active on the Czech market as of 31 December 2006.

A total of 401 insurance undertakings and branches of insurance undertakings from other EU or EEA countries had announced their intention to carry on insurance business in the Czech Republic under the freedom to provide services as of 31 December 2006. Their number was up by 73 compared to the end of 2005. Insurance undertakings and branches of insurance undertakings from the UK and Ireland showed particular interest in providing insurance services on the Czech market. The number of insurance undertakings and branches of insurance undertakings broken down by Member State and specialisation is presented in Annex 5. An up-to-date list of insurance undertakings authorised to carry on insurance business under the freedom to provide services is available on the CNB website.

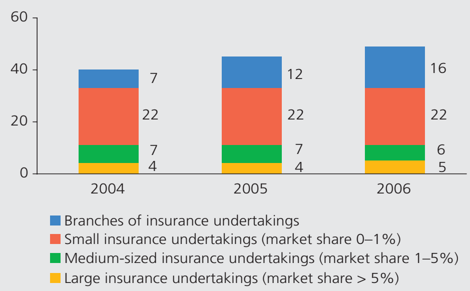
For analytical purposes, the insurance undertakings operating on the Czech insurance market were divided into domestic insurance undertakings and branches of insurance undertakings and subdivided according to their share in total premiums written into

TABLE V.1
Structure of the market by type of insurance undertaking

	2004	2005	2006
NUMBER OF DOMESTIC INSURANCE UNDERTAKINGS	33	33	33
of which:			
non-life	15	15	15
life	2	3	3
both life and non-life	16	15	15
NUMBER OF BRANCHES OF INSURANCE UNDERTAKINGS FROM EU AND THIRD COUNTRIES	7	12	16
of which:			
non-life	6	8	11
life	1	2	3
both life and non-life	0	2	2
TOTAL NUMBER OF INSURANCE UNDERTAKINGS a)	40	45	49
of which:			
non-life	21	23	26
life	3	5	6
both life and non-life	16	17	17

a) excluding insurance undertakings from Member States operating in the Czech Republic under the freedom to provide services

CHART V.1
Number of insurance undertakings by group



79 The Czech Insurers' Bureau (Česká kancelář pojistitelů, ČKP) is a professional organisation of insurers licensed to provide motor third party liability insurance. Its activity is governed by Act No. 168/1999 Coll., on Vehicle Liability Insurance, as amended. Its main tasks include providing frontier insurance, guaranteeing and providing compensation for personal injury or death caused by the operation of an unidentified vehicle for which an unidentified person is responsible, and providing compensation for damage caused by the operation of a vehicle without liability insurance and other types of compensation under the aforementioned Act. Detailed information on the activity and financial performance of the Czech Insurers' Bureau is available at www.ckp.cz.

80 AXA životní pojišťovna from 15 March 2007.

81 The carrying on of insurance business under the freedom to provide services only concerns insurance undertakings and branches thereof from other EU or EEA countries.

large insurance undertakings, medium-sized insurance undertakings, small insurance undertakings and branches of insurance undertakings. This classification is given in Annex 4.

The group of large insurance undertakings consists of the five largest domestic insurance undertakings, whose market share, as measured by total premiums written, exceeds 5% of the Czech insurance market. Except for Česká pojišťovna, which is a member of the largest Czech financial group PPF, the large insurance undertakings belong to major international insurance and financial groups. Large insurance undertakings offer a broad range of life insurance and non-life insurance products. As regards premiums written, non-life insurance is more important in all but one of the large insurance undertakings.

The group of medium-sized insurance undertakings is made up of six domestic entities having market shares of between 1% and 5%. Foreign ownership predominates in four medium-sized insurance undertakings, while domestic capital is more important in the other two. Four focus mainly on life insurance products, while non-life insurance accounts for the majority of premiums written in the other two.

The group of small insurance undertakings contains 22 domestic insurance undertakings with market shares of less than 1%. As regards ownership structure, foreign capital predominates in 11 undertakings and domestic capital is dominant in the same number. The range of products offered is narrower in small insurance undertakings, which focus on specialised insurance products such as credit insurance, travel insurance, legal protection insurance or investment life insurance.

Nationale-Nederlanden životní pojišťovna[82] has a specific position among branches of insurance undertakings. It specialises in life insurance products and ranks third on the Czech life insurance market from the point of view of premiums written. Most branches of insurance undertakings specialise in non-life insurance of industrial and business risks.

In 2006, Generali pojišťovna, a.s. moved from the group of medium-sized insurance undertakings to the group of large insurance undertakings, owing to a sizeable increase in its market share. The number of branches of insurance undertakings more than doubled compared to 2004. The indicators on the groups of insurance undertakings for 2004 and 2005 given in the sections below are based on the number of insurance undertakings in the individual groups in 2006.

CHART V.2
Ownership structure of domestic insurance undertakings

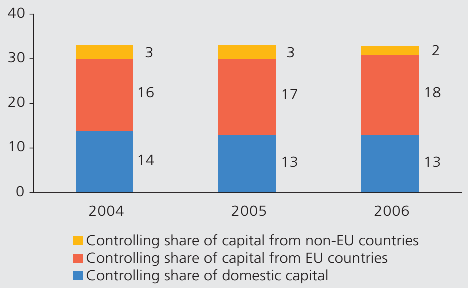
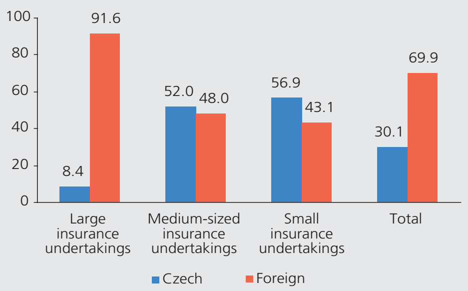


TABLE V.2
Ownership structure of domestic insurance undertakings by share in registered capital as of 31 December 2006

COUNTRY	AMOUNT OF PARTICIPATION (CZK thous.)	SHARE IN TOTAL REGISTERED CAPITAL (%)
Czech Republic	5,329,589	30.1
Austria	4,536,264	25.6
Netherlands[a)]	4,439,000	25.0
Belgium	1,174,300	6.6
France	789,512	4.4
United Kingdom	495,916	2.8
USA	370,000	2.1
Germany	350,100	2.0
Slovenia	189,000	1.1
Denmark	55,500	0.3
TOTAL CAPITAL	17,729,181	100.0

a) including direct shareholder of Česká pojišťovna, a.s.

CHART V.3
Domestic insurance undertakings by origin of capital as of 31 December 2006
(in %)



5.2 OWNERSHIP STRUCTURE OF DOMESTIC INSURANCE UNDERTAKINGS

Foreign ownership of domestic insurance undertakings predominates in the Czech insurance market. Of the total of 33 insurance undertakings, 16 were wholly owned by foreign investors and foreign capital predominated in 4 as of 31 December 2006. Insurance undertakings with a controlling share of foreign capital include Česká pojišťovna, a.s., whose capital is of Czech origin but whose direct shareholder is registered in the Netherlands. Compared to the previous year, the number of insurance undertakings with controlling shares from EU countries increased to 18 due to the acquisition of a holding in Winterthur pojišťovna, a.s by AXA S.A. In all, 12 insurance undertakings were wholly owned by Czech entities.

82 ING Životní pojišťovna N.V., pobočka pro Českou republiku, since 3 January 2007.

Compared to 2005, the total amount of registered capital increased by 6.3%. Domestic shareholders had the largest share in total registered capital (30.1%), followed by shareholders from Austria and the Netherlands. The state accounted for 24.3% of the share of domestic shareholders and 7.3% of total registered capital. The state has a holding in Exportní garanční a pojišťovací společnost, a.s., which specialises in the insurance of export risks. The share of foreign capital in total registered capital rose by 1.9 percentage points compared to 2005, to 69.9%.

With a share of 91.6% in registered capital, foreign capital significantly dominates the group of large insurance undertakings. By contrast, Czech capital has the edge in the groups of medium-sized and small insurance undertakings, accounting respectively for 52% and 56.9% of registered capital.

5.3 PREMIUMS WRITTEN

The growth rate of gross premiums written ("premiums written") is the basic indicator describing the development of the insurance market. Compared to 2005, total premiums written increased by 4.3% to CZK 122.1 billion, with the growth rate rising by 0.3 percentage point on a year earlier. Growth was stronger in life insurance, where premiums written rose by 5.1% to CZK 47.2 billion, compared to a 1.7% increase in 2005. This was due to a halt in the decline in single premium payments and a 6.7% increase in regular premium payments.

By contrast, premiums written in non-life insurance showed lower growth than in the previous year, rising by a mere 3.8%, compared to a 5.5% increase in 2005. Total premiums written in non-life insurance amounted to CZK 74.9 billion. The lower growth rate in non-life insurance is due to high competition on the Czech insurance market, which is pushing down premium rates, and also to insurance contracts – relating mainly to insurance of industry and entrepreneurs outside the Czech insurance market – concluded with insurance undertakings from other EU or EEA countries operating in the Czech Republic under the freedom to provide services. According to still incomplete data (lacking figures for 4 small countries), insurance undertakings operating in the Czech Republic under the freedom to provide services accounted for 1.0% of the total premiums written by domestic insurance undertakings in 2005. This equated to CZK 1.2 billion. Most of this amount is attributable to non-life insurance. Although figures for 2006 are not yet available, an increase in the scope and importance of this form of service provision can be expected.

The share of life insurance in total premiums written increased by 0.3 percentage point to 38.7%, but it is still below the record-high 2004 level (39.3%).

A large proportion of premiums written are ceded to reinsurers, especially in non-life insurance. Non-life insurance premiums ceded to reinsurers fell by 13.6% year on year to CZK 23.5 billion, which represented 31.4% of premiums written. Life insurance premiums ceded to reinsurers totalled CZK 1.3 billion, accounting for less than 3% of total premiums written in life insurance. Insurance undertakings use reinsurance to mitigate the risk arising from potential large losses which might threaten the financial stability of insurance undertakings.

The share of premiums written by large insurance undertakings in total premiums written was 74.2% in 2006, down by 2.4 percentage points from a year earlier. The share of large insurance undertakings is more significant on the non-life insurance market (83.5%), being just 59.3% on the life insurance market, where it declined by 4 percentage points. The share of medium-sized insurance undertakings in total premiums written increased by 1.6 percentage points to 14.8%; in life insurance it rose by 3.8 percentage points to 25.2%. Branches of insurance undertakings have

CHART V.4
Gross premiums written
(in CZK billions)

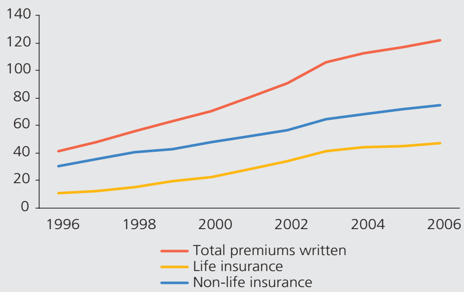


CHART V.5
Share of life insurance and non-life insurance in total premiums written

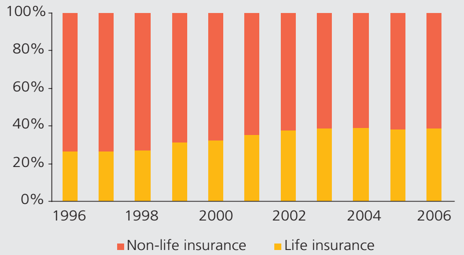


TABLE V.3
Premiums written by insurance group

	Amount (CZK millions)			Share (%)		
	2004	2005	2006	2004	2005	2006
TOTAL PREMIUMS WRITTEN	112,566	117,077	122,090	100.0	100.0	100.0
Large insurance undertakings	85,166	89,657	90,530	75.7	76.6	74.2
Medium-sized insurance undertakings	16,477	15,464	18,076	14.6	13.2	14.8
Small insurance undertakings	5,095	5,717	6,732	4.5	4.9	5.5
Branches of insurance undertakings	5,828	6,239	6,751	5.2	5.3	5.5
PREMIUMS WRITTEN – NON-LIFE INSURANCE	68,365	72,123	74,857	100.0	100.0	100.0
Large insurance undertakings	57,491	61,178	62,511	84.1	84.8	83.5
Medium-sized insurance undertakings	6,288	5,865	6,187	9.2	8.1	8.3
Small insurance undertakings	4,083	4,440	5,347	6.0	6.2	7.1
Branches of insurance undertakings	503	640	812	0.7	0.9	1.1
PREMIUMS WRITTEN – LIFE INSURANCE	44,201	44,954	47,233	100.0	100.0	100.0
Large insurance undertakings	27,675	28,479	28,019	62.6	63.3	59.3
Medium-sized insurance undertakings	10,189	9,599	11,890	23.1	21.4	25.2
Small insurance undertakings	1,012	1,277	1,385	2.3	2.8	2.9
Branches of insurance undertakings	5,325	5,599	5,939	12.0	12.5	12.6

CHART V.6
Share of classes of life insurance in premiums written

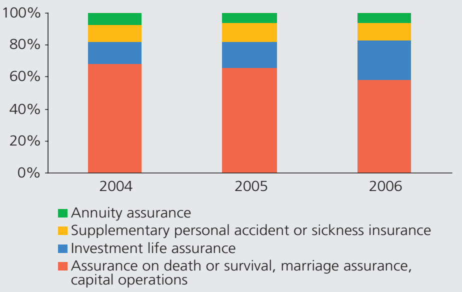


Table V.4
Premiums written by insurance class

Insurance classes	Amount (CZK millions) 2004	2005	2006	Change (%) 2006/2005
TOTAL LIFE INSURANCE	44,201	44,954	47,264	5.1
Assurance on death or survival, marriage assurance, capital operations	30,125	29,490	27,684	-6.1
Annuity assurance	3,247	2,779	2,799	0.7
Investment life assurance	6,052	7,550	11,357	50.4
Supplementary personal accident and sickness insurance	4,777	5,135	5,424	5.6
TOTAL NON-LIFE INSURANCE	68,365	72,123	74,857	3.8
Liability insurance for damage arising out of use of motor vehicle	21,155	21,994	22,454	2.1
Insurance against damage to or loss of property	16,931	17,626	17,864	1.4
Insurance against damage to or loss of land vehicles	14,370	15,322	15,507	1.2
General liability insurance for damage a)	8,402	9,291	9,723	4.7
Accident and sickness insurance	2,916	3,140	3,338	6.3
Other non-life insurance	4,591	4,750	5,971	25.7

a) including mandatory employer liability insurance for damage due to accidents at work or occupational disease.

Chart V.7
Share of classes of non-life insurance in premiums written

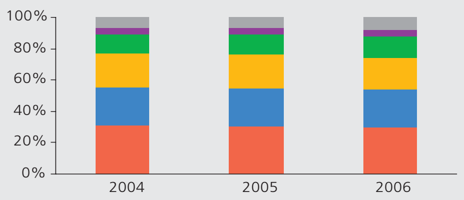
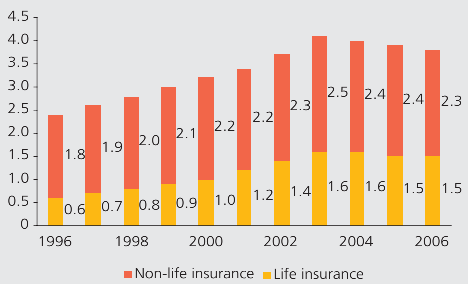


Table V.5
Total insurance penetration in the Czech Republic

	Amount (CZK billions) 2004	2005	2006	Change (%) 2006/2005
Premiums written	113	117	122	4.3
GDP (at current prices)	2,781	2,970	3,204	7.9
		%		
Premiums written/GDP	4.0	3.9	3.8	x

Chart V.8
Share of premiums written in GDP
(in %)



a significant share in life insurance premiums written. This share was 12.6% in 2006, primarily due to Nationale-Nederlanden životní pojišťovna.

Traditional products, such as assurance on death, assurance on survival or earlier death and insurance of benefits for child maintenance (marriage assurance), still predominate on the life insurance market, but their share in life insurance premiums written has been gradually declining. Dynamic growth is being recorded for assurance linked to investment funds (investment life insurance), which increased by 50.4% in 2006. The share of investment life insurance in life insurance premiums written has risen by more than 10 percentage points since 2004, to 24%, mainly at the expense of traditional life insurance products. In contrast to the latter, investment life insurance enables the client to choose where the savings part of the premium will be invested, under a preferred investment strategy. The investment risk is, however, borne by the policyholder, not the insurance undertaking.

As regards the non-life insurance market, the most important category is motor third party liability insurance (MTPL), which accounted for 30.0% of non-life insurance premiums written in 2006. MTPL premiums written increased by 2.1% on a year earlier. Other important categories of non-life insurance include insurance against damage to or loss of property and insurance against damage to or loss of land vehicles, which accounted respectively for 23.9% and 20.7% of total non-life insurance premiums. In 2006, the largest increase in premiums written was recorded in the other categories of non-life insurance (25.7%), mainly due to a sharp rise in credit insurance premiums (of more than 80%). Except for accident and sickness insurance and general liability insurance, growth in premiums in the other non-life categories was lower than that of the overall non-life market, and their share in non-life premiums written decreased somewhat.

Total insurance penetration, as measured by the ratio of premiums written to GDP, is an important insurance market indicator. The ratio of premiums written to GDP declined again in 2006, falling by 0.1 percentage point to 3.8%. Total insurance penetration has been declining continuously since 2004 and the gap between the Czech Republic and the old EU member states has thus been widening. Insurance penetration in the Czech Republic is around one half the EU average.

Although insurance market concentration, as measured by premiums written, is high, it is gradually decreasing as a result of growing competition. In 2006, the total market share of the three largest insurance undertakings declined by 3.4 percentage points year on year. The non-life market is more concentrated, but the market share of the three largest insurance undertakings recorded a larger annual fall in life insurance (5.5 percentage points) than in non-life insurance (2.1 percentage points). The market share of the ten largest insurance undertakings increased by 0.2 percentage point in 2006, declining by 0.7 percentage point on the non-life market and 0.8 percentage point on the life market.

5.4 CLAIM SETTLEMENT COSTS

Total claim settlement costs[83] amounted to CZK 56.7 billion in 2006, rising by 5.9% year on year. The increase in total claim settlement costs was due to a 12.0% rise in claim settlement costs in non-life insurance, as claim settlement costs in life insurance decreased by 4.5%. Claim settlement costs in non-life insurance were affected by natural disasters in 2006. Due to a long and severe winter, a large

83 Claim settlement costs are given on a gross basis, including reinsurers' share.

number of claims were caused by the weight of snow. The subsequent thaw caused floods in March, which were followed by flooding due to torrential rain in May and June. The number of claims relating to natural disasters exceeded 95,000, significantly outnumbering the usual figures in previous years. Total claim settlement costs due to natural disasters were estimated at CZK 3.3 billion.[84] This, however, had no major negative effect on insurance undertakings' performance. Reinsurers' share in the above losses was relatively low, since the damage caused by the weight of snow was largely unreinsured, and for the other natural disasters the aggregate loss threshold above which reinsurers are contractually obliged to contribute to individual risk coverage was not usually reached.

Reinsurers' share in non-life claim settlement costs totalled CZK 9.3 billion in 2006 (i.e. 24.7% of claim settlement costs), down by 6.9% from a year earlier. Reinsurers' share in life insurance claim settlement costs amounted to only CZK 325 million, falling by 30.0% compared to 2005, to 1.7% of claim settlement costs.

The share of the group of large insurance undertakings in total claim settlement costs decreased by 1.9 percentage points year on year, to 81.8%. The decline was more pronounced for costs in life insurance, where the share fell by 6.5 percentage points to 69.1%. The share of claim settlement costs in non-life insurance was 88.1%, down by just 0.2 percentage point. The share of large insurance undertakings in claim settlement costs is higher than that in premiums written, especially in life insurance, where the share of claim settlement costs exceeds the share of premiums written by almost 10 percentage points. In the other groups of insurance undertakings, the share of claim settlement costs is lower than or comparable to that in premiums written.

5.5 ASSETS OF INSURANCE UNDERTAKINGS

The total assets of insurance undertakings amounted to CZK 322.9 billion as of 31 December 2006, up by 4% on a year earlier. The rate of growth of assets of insurance undertakings decreased by 5.2 percentage points year on year. The total assets of insurance undertakings were affected mainly by developments in the group of large insurance undertakings, whose balance-sheet assets declined by 0.5% as a result of transactions relating to sales of holdings in subsidiaries. The share of the group of large insurance undertakings in total assets thus dropped by 2.9 percentage points to 65.5%. Growth in total assets was recorded by the other groups of insurance undertakings, most notably the medium-sized insurance undertakings (19.1%).

In terms of the type of insurance undertaking, the biggest contributors to total assets were undertakings carrying on both life and non-life insurance, whose share declined by 0.8 percentage point compared to 2005, to 82.7%. By contrast, non-life insurance undertakings and life insurance undertakings recorded an increased share in total assets (of 0.1 percentage point to 6.1% and of 0.7 percentage point to 11.2% respectively).

Financial placement (investment)[85] is the most important asset item in insurance undertakings' balance sheets. It accounted for 84.3% of total assets as of 31 December 2006, having decreased by 1.3 percentage point year on year as a

84 Source: Czech Insurance Association.

85 Financial placement (investment) is defined differently than financial placement of assets arising from technical provisions. Financial placement (investment) excludes reinsurance receivables.

CHART V.9
Concentration on insurance market by premiums written as of 31 December 2006
(in %)

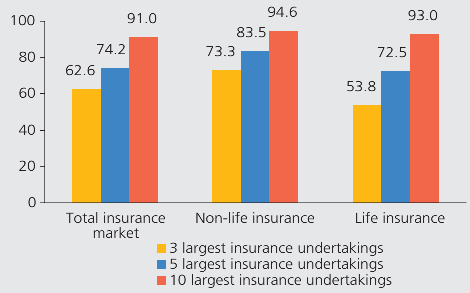


TABLE V.6
Claim settlement costs by insurance group

	Amount (CZK millions) 2004	2005	2006	Share (%) 2006
TOTAL CLAIM SETTLEMENT COSTS	58,357	53,560	56,736	100.0
Large insurance undertakings	49,766	44,811	46,415	81.8
Medium-sized insurance undertakings	4,934	4,744	5,856	10.3
Small insurance undertakings	1,829	1,837	1,936	3.4
Branches of insurance undertakings	1,828	2,168	2,529	4.5
CLAIM SETTLEMENT COSTS – NON-LIFE INSURANCE	34,914	33,830	37,899	100.0
Large insurance undertakings	30,908	29,887	33,392	88.1
Medium-sized insurance undertakings	2,276	2,271	2,724	7.2
Small insurance undertakings	1,661	1,626	1,664	4.4
Branches of insurance undertakings	69	46	118	0.3
CLAIM SETTLEMENT COSTS – LIFE INSURANCE	23,443	19,730	18,837	100.0
Large insurance undertakings	18,858	14,924	13,023	69.1
Medium-sized insurance undertakings	2,658	2,473	3,131	16.6
Small insurance undertakings	168	211	272	1.5
Branches of insurance undertakings	1,759	2,122	2,411	12.8

CHART V.10
Claim settlement costs
(in CZK billions)

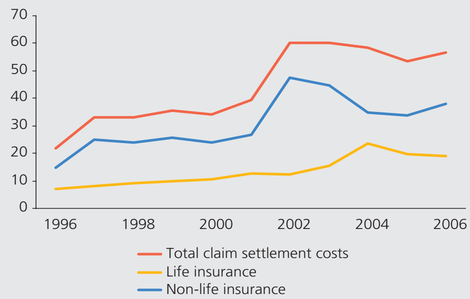


TABLE V.7
Share of individual insurance groups in total assets

	Amount (CZK millions) 2004	2005	2006	Share (%) 2006
TOTAL ASSETS	284,335	310,511	322,858	100.0
Large insurance undertakings	197,277	212,473	211,335	65.5
Medium-sized insurance undertakings	39,347	44,782	53,356	16.5
Small insurance undertakings	20,072	22,333	24,257	7.5
Branches of insurance undertakings	27,639	30,923	33,910	10.5

Chart V.11
Share of insurance undertakings in total assets by type

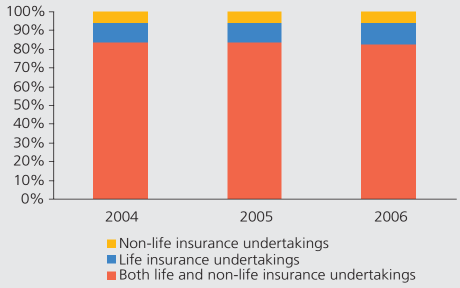


Table V.8
Assets of insurance undertakings

	Amount (CZK millions)			Share (%)
	2004	2005	2006	2006
TOTAL ASSETS	284,335	310,511	322,858	100.0
Financial placements (investment)	246,828	265,917	272,017	84.3
of which:				
real estate	10,533	9,315	8,766	2.7
participating interests	24,674	25,980	10,818	3.4
shares, variable-yield securities	26,694	33,102	30,434	9.4
bonds and other fixed-income securities	151,791	164,473	191,826	59.4
deposits at financial institutions	27,174	27,730	26,378	8.2
other financial placements	5,962	5,317	3,794	1.2
Financial placements of unit-linked life insurance	7,737	12,420	18,580	5.7
Debtors (receivables)	16,842	18,951	18,470	5.7
Other assets	12,928	13,223	13,792	4.3

Chart V.12
Financial placements of assets arising from technical provisions

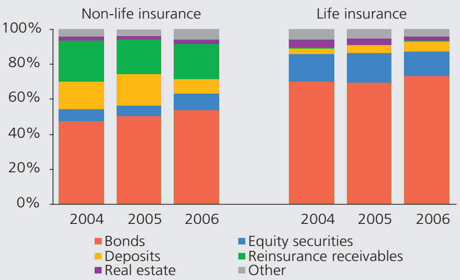


Table V.9
Liabilities of insurance undertakings

	Amount (CZK millions)			Share (%)
	2004	2005	2006	2006
TOTAL LIABILITIES	284,335	310,511	322,858	100.0
Shareholder's equity	53,308	57,466	58,147	18.0
Technical provisions [a)]	181,957	200,511	217,871	67.5
Provision for unit-linked life insurance	7,544	12,053	18,546	5.8
Creditors (liabilities)	26,539	26,874	18,833	5.8
Other liabilities	14,987	13,607	9,462	2.9

a) net amount

result of a significant decline in participating interests in subsidiaries. Debt securities are the largest item in insurance undertakings' assets in terms of financial placement. Their value increased by 16.6% compared to 2005 and their share in total assets rose by 6.4 percentage points to 59.4%. Shares and other variable-yield securities recorded a decline in volume of 8.1%, while their share in total assets decreased by 1.2 percentage point to 9.4%. Owing to the growing interest in investment life insurance, the volume of financial placements of life insurance where the investment risk is borne by the policy holder rose by 49.6% and its share in total assets increased by 1.7 percentage points to 5.7%.

To ensure that insurance undertakings can fulfil their obligations, Act No. 363/1999 Coll., on Insurance, as amended, stipulates the permissible structure of financial placement of assets arising from technical provisions. Insurance undertakings must also comply with limits for the individual financial placement items as laid down in Implementing Decree No. 303/2004 Coll., as amended. As technical provisions for life insurance are of a long-term nature, longer maturity bonds dominate financial placement of assets arising from technical provisions for life insurance, and there is also a larger proportion of shares and units. By contrast, financial placement of assets arising from technical provisions for non-life insurance is made up of more liquid financial placement items, such as deposits and treasury bills. Reinsurance receivables, including reinsurers' share in technical provisions, also have a significant share.

Bonds predominate in financial placement of assets arising from non-life insurance technical provisions. Their share increased by 3.5 percentage points to 53.9%. The share of deposits in financial placements declined by a sizeable 9.2 percentage points to 8.4%, whereas equity securities, real estate and other financial placements recorded increased shares. The share of reinsurance receivables decreased by 0.1 percentage point to 20.0%.

Bonds are also dominant in financial placement of assets arising from technical provisions for life insurance. This share increased by 3.6 percentage point to 73.5%. The shares of the other financial placement items moved in the opposite direction than in the case of financial placement of assets arising from technical provisions for non-life insurance – deposits recorded an increase while the other items showed a decline. Financial placement of assets arising from technical provisions for life insurance also includes financial placement items of life insurance where the investment risk is borne by the policy holder.

5.6 LIABILITIES OF INSURANCE UNDERTAKINGS

The most important item in insurance undertakings' liabilities structure is technical provisions, which represent the future obligations of insurance undertakings arising from insurance or reinsurance activities which are either likely to be incurred or certain to be incurred but uncertain as to amount or as to the date on which they will arise. The types of technical provisions and their creation and application are laid down in Act No. 363/1999 Coll., on Insurance, as amended, and in Implementing Decree No. 303/2004 Coll., as amended. Technical provisions are reported on a gross basis including the reinsurers' share in technical provisions and on a net basis less the reinsurers' share. In 2006, the share of net technical provisions (excluding provisions for life insurance where the investment risk is borne by the policy holder) in total liabilities increased by 2.9 percentage points year on year, to 67.5%. Commensurately with the rise in financial placement of life insurance where the investment risk is borne by the policy holder, the share in total liabilities of technical provisions for life insurance where the investment risk is borne by the policy holder increased by 1.9 percentage points to 5.8%.

Shareholders' equity accounted for 18% of total liabilities of insurance undertakings, down by 0.5 percentage point from a year earlier. The low growth in shareholders' equity (1.2%) was mainly due to an almost 50% decrease in retained earnings as a result of payments of dividends, particularly in the group of large insurance undertakings. Registered capital is the most important component of shareholders' equity. Its share has been gradually increasing and amounted to 30.5% at the end of 2006.

Compared to 2005, there was a 29.9% fall in the creditors (liabilities) item, which accounted for 5.8% of total liabilities. This fall was due to a marked decrease in obligations from reinsurance operations and other obligations. A decrease in the share of other liabilities in total liabilities, of 1.5 percentage point to 2.9%, was chiefly due to the payment of subordinated liabilities and also to a substantial decline in deposits in passive reinsurance.

On 31 December 2006, total gross technical provisions, including provisions for life insurance where the investment risk is borne by the policy holder, recorded an annual increase of 9% to CZK 259.7 billion. The rate of growth of provisions moderated compared to the previous period. Gross technical provisions for life insurance increased by 10.8%, while those for non-life insurance recorded a rise of 4.7%. Total net technical provisions grew faster than the gross amount for both life insurance and non-life insurance, owing to a decline in the reinsurers' share in technical provisions. Total net technical provisions increased by 11.2%, with growth rates of 12.2% and 7.9% recorded for life insurance and non-life insurance respectively.

As in the case of premiums written and claim settlement costs, the share of the group of large insurance undertakings in total net technical provisions has been gradually diminishing. At the end of 2006, it was down by 1.3 percentage point, to 67.4%. While the share of large insurance undertakings in net technical provisions for non-life insurance increased slightly, by 0.6 percentage point to 81.1%, that for life insurance decreased by 1.7 percentage points, to 63.4%. The share of the group of large insurance undertakings in total net technical provisions and in net technical provisions for non-life insurance was lower than the share in premiums written, whereas their share in net technical provisions for life insurance was higher. The shares of medium-sized insurance undertakings in net technical provisions for both life insurance and non-life insurance showed an increase.

As regards the type of insurance undertakings, non-life insurance undertakings accounted for 9.3% of total net technical provisions for non-life insurance in 2006. Their share declined by 1.5 percentage points year on year, at the expense of undertakings carrying on both life insurance and non-life insurance. Life insurance undertakings accounted for 15% of total net technical provisions for life insurance, their share declining by 0.1 percentage point compared to 2005.

5.7 ECONOMIC RESULTS

In 2006, domestic insurance undertakings and branches of insurance undertakings achieved an aggregate net profit of CZK 14.6 billion, the best result in the history of the Czech insurance market. Net profit rose by 82.1% year on year. The record total net profit was due to an increase in profit of 78.6% on the technical account[86]

86 The profit and loss account of insurance undertakings is divided by type of business into a technical account for non-life insurance, a technical account for life assurance and a non-technical account, which comprises income and expenses that cannot be assigned to life or non-life insurance.

TABLE V.10
Technical provisions

	Amount (CZK millions) 2004	2005	2006	Change (%) 2006/2005
TOTAL GROSS TECHNICAL PROVISIONS	211,979	238,373	259,765	9.0
of which:				
non-life insurance	65,897	72,448	75,855	4.7
life insurance	146,082	165,925	183,910	10.8
TOTAL NET TECHNICAL PROVISIONS	189,502	212,564	236,416	11.2
of which:				
non-life insurance	45,714	49,599	53,492	7.8
life insurance	143,788	162,965	182,924	12.2

CHART V.13
Net technical provisions
(in CZK millions)

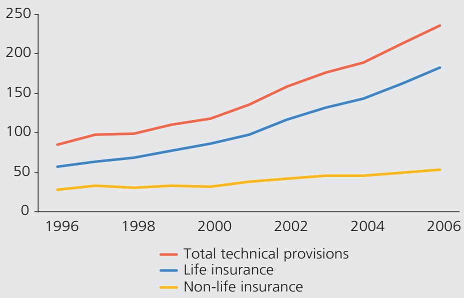


TABLE V.11
Net technical provisions by insurance group

	Amount (CZK millions) 2004	2005	2006	Share (%) 2006
TOTAL NET TECHNICAL PROVISIONS	189,502	212,564	236,416	100.0
Large insurance undertakings	134,132	146,004	159,307	67.4
Medium-sized insurance undertakings	28,389	35,899	43,774	18.5
Small insurance undertakings	6,929	7,878	8,233	3.5
Branches of insurance undertakings	20,052	22,783	25,103	10.6
NET TECHNICAL PROVISIONS – NON-LIFE INSURANCE	45,714	49,599	53,492	100.0
Large insurance undertakings	37,931	39,945	43,361	81.1
Medium-sized insurance undertakings	2,467	3,983	4,771	8.9
Small insurance undertakings	5,163	5,399	5,106	9.5
Branches of insurance undertakings	153	272	254	0.5
NET TECHNICAL PROVISIONS – LIFE INSURANCE	143,788	162,965	182,924	100.0
Large insurance undertakings	96,201	106,059	115,946	63.4
Medium-sized insurance undertakings	25,922	31,916	39,002	21.3
Small insurance undertakings	1,766	2,479	3,126	1.7
Branches of insurance undertakings	19,899	22,511	24,849	13.6

TABLE V.12
Net technical provisions by type of insurance undertaking

Type of insurance undertaking	Net TPs in non-life insurance (CZK millions) 2004	2005	2006
non-life insurance	5,069	5,378	4,970
both life and non-life	40,645	44,221	48,522
TOTAL	45,714	49,599	53,492
Type of insurance undertaking	**Net TPs in life insurance (CZK millions) 2004**	**2005**	**2006**
life insurance	21,325	24,574	27,479
both life and non-life	122,463	138,391	155,445
TOTAL	143,788	162,965	182,924

for life assurance to CZK 7.9 billion and also to an increase in profit of 38.8% on the technical account for non-life insurance business to CZK 5.3 billion. The results were strongly affected by one-off income from sales of ownership interests in the group of large insurance undertakings.[87]

Compared to 2005, net profit grew for all groups of insurance undertakings, but rose most markedly for small insurance undertakings, whose share in total profit increased by 6.9 percentage points year on year, to 8.4%. Although net profit rose by 76.2% in the group of large insurance undertakings, their share in total profit declined by 2.6 percentage points to 76.8%.

Profitability and efficiency indicators also showed year-on-year improvements thanks to the profits generated by insurance undertakings. The ratio of net profit to shareholder's equity increased by 11.1 percentage points year on year, to 25.1%, while the ratio of net profit to earned premiums[88] rose by 6 percentage points to 15.2%.

As regards non-life insurance, the ratio of profit on the technical account for non-life insurance to earned premiums was 10.7%, a year-on-year rise of 2.1 percentage points. The ratio of claims incurred, including change in technical provisions, to earned premiums fell by 2.4 percentage points, while the ratio of net operating expenses to earned premiums rose by 1.1 percentage point, mainly due to a decline in reinsurance commissions and profit participation.

Turning to life insurance, the ratio of profit on the technical account for life insurance to earned premiums increased by 6.7 percentage points compared to 2005, to 17%. The ratio of claims incurred, including change in technical provisions, to earned premiums dropped by 5.2 percentage points. And a slight decline of 0.3 percentage point was also recorded for the ratio of net operating expenses to earned premiums.

CHART V.14
Profits of insurance undertakings
(in CZK billions)

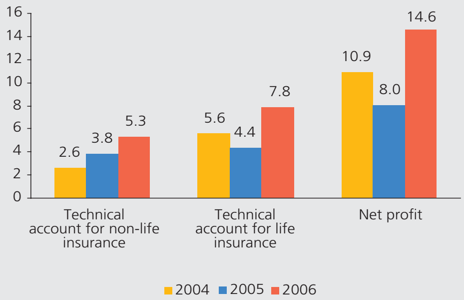


TABLE V.13
Profit by insurance group

	Amount (CZK millions) 2004	2005	2006	Share (%) 2006
TOTAL NET PROFIT	10,934	8,021	14,608	100.0
Large insurance undertakings	6,322	6,366	11,215	76.8
Medium-sized insurance undertakings	2,840	711	1,190	8.1
Small insurance undertakings	1,031	119	1,232	8.4
Branches of insurance undertakings	741	825	971	6.7

TABLE V.14
Selected profitability and efficiency indicators (%)

	2004	2005	2006
Net profit/assets (RoA)	3.8	2.6	4.5
Net profit/shareholder's equity (RoE)	20.5	14.0	25.1
Net profit/earned premiums	12.9	9.2	15.2
NON-LIFE INSURANCE			
Proft on technical account for non-life insurance/earned premiums	6.2	8.6	10.7
Claims incurred, including change in TPs/earned premiums	56.7	61.3	58.9
Net operating costs/earned premiums	30.8	25.2	26.3
Acquisition costs for insurance contracts/earned premiums	23.6	21.6	21.3
Administrative expenses/earned premiums	18.5	17.5	16.9
LIFE INSURANCE			
Proft on technical account for life insurance/earned premiums	13.4	10.3	17.0
Claims incurred, including change in TPs/earned premiums	55.5	45.3	40.1
Net operating costs/earned premiums	22.3	23.2	22.9
Acquisition costs for insurance contracts/earned premiums	13.6	14.6	14.3
Administrative expenses/earned premiums	9.6	10.3	10.5

5.8 SOLVENCY OF INSURANCE UNDERTAKINGS

Solvency means the ability of an insurance undertaking to meet all its liabilities from insurance activities on an ongoing basis. Insurance undertakings are therefore required to have available own funds equal to at least the required solvency margin over the entire duration of their activities. Specific procedures for the calculation of solvency are laid down in Decree No. 303/2004 Coll., implementing certain provisions of Act No. 363/1999 Coll., on Insurance, as amended. The Decree stipulates which items are eligible for inclusion in the own funds of an insurance undertaking, including any limitations relating to the calculation of solvency. It *de facto* defines the composition of the regulatory capital of an insurance undertaking, referred to as the available solvency margin (ASM). The Decree also stipulates the algorithm used to calculate the required solvency margin (RSM), which is, in essence, the capital requirement. In order to meet the statutory obligation, it is thus vital that the AMS is at least equal to the RSM. Another important regulatory requirement contained in the Decree is separate calculation of solvency for life insurance and non-life insurance. It is therefore necessary to perform two separate calculations for undertakings carrying on both life insurance and non-life insurance. The relevant calculation methods are also given in the Decree.

87 One-off income from the sale of eBanka and a holding in the Modrá pyramida building society strongly affected Česká pojišťovna, a.s.

88 Earned premiums and claims incurred, including change in technical provisions, are net of reinsurance.

Tables V.15 and V.16 show the aggregate ASM and RSM of all domestic insurance undertakings over the past three years, separately for life insurance and non-life insurance. The aggregate ASM is more than triple the aggregate RSM in all these years.

Tables V.17 and V.18 show the numbers of insurance undertakings according to percentage ASM/RSM ratios, divided into life insurance and non-life insurance. The solvency of undertakings carrying on both life and non-life insurance is incorporated into the respective tables for life and non-life insurance. All insurance undertakings recorded a higher ASM than RSM in the observed period of 2004–2006. However, taking into account the minimum amount of the guarantee fund[89] (insurance undertakings are obliged to keep their own funds above this level), one insurance undertaking failed to record adequate solvency in 2005.[90] However, it subsequently complied with the ASM by increasing its capital funds. It is worth noting that most of the ASM/RSM ratios in non-life insurance are concentrated in the band above 500%, whereas life insurance shows a more even distribution. The band above 500% mainly contains small non-life insurance undertakings. The group of small insurance undertakings has a small volume of premiums written and claim settlement costs relative to shareholders' equity compared to large and medium-sized insurance undertakings. In 2006, all domestic insurance undertakings recorded ASMs above the minimum guarantee fund level.

TABLE V.15
Aggregate solvency – non-life insurance (CZK millions)

	2004	2005	2006
ASM	25,113	29,760	30,936
RSM	7,546	7,696	8,400

ASM – available solvency margin RSM – required solvency margin

TABLE V.16
Aggregate solvency – life insurance (CZK millions)

	2004	2005	2006
ASM	21,137	23,970	24,785
RSM	6,424	7,004	7,883

ASM – available solvency margin RSM – required solvency margin

TABLE V.17
ASM/RSM ratio – non-life insurance

Number of insurance undertakings	2004	2005	2006
< 100%	0	1	0
100%–150%	4	1	2
150%–200%	2	2	2
200%–250%	3	3	2
250%–300%	1	1	2
300%–400%	3	2	2
400%–500%	2	3	2
> 500%	15	17	18
TOTAL	30	30	30

TABLE V.18
ASM/RSM ratio – life insurance

Number of insurance undertakings	2004	2005	2006
< 100%	0	0	0
100%–150%	4	4	3
150%–200%	1	1	1
200%–250%	4	2	2
250%–300%	1	2	3
300%–400%	2	2	3
400%–500%	1	3	2
> 500%	4	4	4
TOTAL	17	18	18

89 The guarantee fund is defined by Act No. 363/1999 Coll., on Insurance, as amended, as one-third of the RSM. However, it may not be lower than the limits stipulated by law for the type of business (scope of licensed insurance classes).

90 This undertaking failed to take advantage of the transitional provision of Article II(6) of Act 39/2004 Coll. and failed to apply to the supervisor for an extension of the time limit for the application of Article 22(2) of Act No. 363/1999 Coll., on Insurance, as amended. As of 2005, the Act stipulated a new, considerably higher guarantee fund amount, which affected the calculation of solvency. The insurance undertaking subsequently complied with the solvency requirement by increasing its capital funds.

ABS	asset backed securities
AFAM	Association of Funds and Asset Management of the Czech Republic
AMA	Advanced Measurement Approaches
AML	anti-money laundering
APF	Association of Pension Funds of the Czech Republic
BCBS	Basel Committee on Banking Supervision
BIS	Bank for International Settlements
bn	billion
BSC	Banking Supervision Committee
BSCEE	Group of Banking Supervisors from Central and Eastern Europe
CBA	Czech Banking Association
CCA	Czech Consolidation Agency
CEA	Comité Européen des Assurances (European Insurance and Reinsurance Federation)
CEBS	Committee of European Banking Supervisors
CEIOPS	Committee of European Insurance and Occupational Pensions Supervisors
CESR	Committee of European Securities Regulators
CESR-Fin	CESR operational group for accounting and auditing
CESR-Pol	CESR operational group for market integrity
CESR-Tech	CESR expert group for IT projects
ČKP	Czech Insurers' Bureau
CNB	Czech National Bank
Coll.	Collection of Laws of the Czech Republic
COREP	Common Reporting
CPLG	Core Principles Liaison Group
CRC	Central Register of Credits
CSC	Czech Securities Commission
ČSOB	Československá obchodní banka (a commercial bank)
CU	credit union
CUA	Act No. 87/1995 Coll., on Credit Unions
CZK	Czech koruna
CZ-NACE	Industrial Classification of Economic Activities
CZSO	Czech Statistical Office
EBC	European Banking Committee
EC	European Community
ECB	European Central Bank
ECONET	Financial Economists Network (a CESR expert group)
EDIFACT	Electronic Data Interchange for Administration, Commerce and Transport
EEA	European Economic Area
EEC	European Economic Community
EFC	Economic and Financial Committee
EIOPC	European Insurance and Occupational Pensions Committee
EMI	electronic money institution
EU	European Union
EUR	euro
FATF	Financial Action Task Force
FINREP	Financial Reporting
FSC	Financial Services Committee
FSI	Financial Stability Institute
GAAP	Generally Accepted Accounting Principles
GCC	group of connected clients
GDP	gross domestic product
HI	Herfindahl Index (measuring concentration)
IAIS	International Association of Insurance Supervisors
ICS	internal control system

IFRS/IAS	International Financial Reporting Standards/International Accounting Standards
ILG	International Liaison Group
IMF	International Monetary Fund
IOPS	International Organisation of Pension Supervisors
IOSCO	International Organization of Securities Commissions
IRB	Internal Ratings Based
MiFID	Markets in Financial Instruments Directive
MoF	Ministry of Finance of the Czech Republic
MoLSA	Ministry of Labour and Social Affairs of the Czech Republic
MoU	Memorandum of Understanding
MTPL	motor third party liability insurance
NBS	National Bank of Slovakia
NOVI	Network on Validation Issues (an expert discussion group)
NPL	non-performing loan
OECD	Organisation for Economic Cooperation and Development
OMF	open-end mutual fund
OTC	over-the-counter
PSE	Prague Stock Exchange (Burza cenných papírů Praha, a.s.)
PX	stock exchange indices: PX 50 (50 titles), PX-D (6–7 issues)
QIS	Quantitative Impact Study
REE	Register of Economic Entities
RM-S	RM-Systém, a. s. (an OTC market operator)
RoA	return on assets
RoE	return on equity
SDNS	Non-bank Data Collection System
SKK	Slovak koruna
SPAD	Share and Bond Market Support System
SVYT	Transaction Settlement System
TPs	technical provisions
TREM	Transaction Reporting Exchange Mechanism
UCITS	Undertakings for Collective Investment in Transferable Securities
UNIVYC	UNIVYC, a.s. (a universal settlement system)
USD	US dollar
VAT	value added tax
WB	World Bank
WGC	Working Group on Capital
WGCR	Working Group on Credit Registers
WGDB	Working Group on Developments in Banking
WGMA	Working Group on Macroprudential Analysis

Czech National Bank	www.cnb.cz

1. CZECH

Association of Credit Unions of the Czech Republic	www.asociacedz.cz
Association of Czech Insurance Brokers	www.acpm.cz
Association of Financial Intermediaries and Financial Advisers of the Czech Republic	www.afiz.cz
Association of Funds and Asset Management of the Czech Republic	www.afamcr.cz
Association of Pension Funds of the Czech Republic	www.apfcr.cz
Chamber of Auditors of the Czech Republic	www.kacr.cz
Chamber of Independent Loss Adjusters	www.kslpu.cz
Czech Association of Investment Firms	www.caocp.cz
Czech Banking Association	www.czech-ba.cz
Czech Capital Market Association	www.akatcr.cz
Czech Chamber of Independent Loss Adjusters	www.ckslpu.com
Czech Insurance Association	www.cap.cz
Czech Insurers' Bureau	www.ckp.cz
Czech Republic - official website	www.czech.cz
Czech Society of Actuaries	www.actuaria.cz
Czech Statistical Office	www.czso.cz
CzechInvest	www.czechinvest.cz
Deposit Insurance Fund of the Czech Republic	www.fpv.cz
Financial Arbiter of the Czech Republic	www.finarbitr.cz
Ministry of Finance of the Czech Republic	www.mfcr.cz
Prague Securities Centre	www.scp.cz
Prague Stock Exchange	www.pse.cz
RM-Systém, a.s.	www.rms.cz
Securities Brokers Guarantee Fund	www.gfo.cz
UNIVYC	www.univyc.cz

2. INTERNATIONAL

Bank for International Settlements	www.bis.org
Committee of European Banking Supervisors	www.c-ebs.org
Committee of European Insurance and Occupational Pensions Supervisors	www.ceiops.org
Committee of European Securities Regulators	www.cesr-eu.org
European Central Bank	www.ecb.int
European Commission	www.ec.europa.eu
European Commission, DG Internal Market and Services	ec.europa.eu/internal_market
European Fund and Asset Management Association	www.efama.org
European Insurance and Reinsurance Federation	www.cea.assur.org
Eurostat	ec.europa.eu/eurostat
Federation of European Securities Exchanges	www.fese.be
International Association of Insurance Supervisors	www.iaisweb.org
International Capital Market Association	www.icma-group.org
International Monetary Fund	www.imf.org
International Organization of Securities Commissions	www.iosco.org
Organisation for Economic Cooperation and Development	www.oecd.org
World Bank	www.worldbank.org
World Federation of Exchanges	www.world-exchanges.org

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27. Public contract offer following the decision of the bidder's General Meeting to delist shares

Annex 1

Main indicators of monetary and economic developments in the Czech Republic

		2002	2003	2004	2005	2006
Gross domestic product [1) 2)]	Volume (in CZK billions)	2,285.5	2,367.8	2,467.6	2,617.6	2,776.4
	Increase (in per cent)	1.9	3.6	4.2	6.1	6.1
Output – percentage increase [2)]	Industry	2.7	5.8	9.9	8.1	10.3
	Construction	-3.5	11.2	4.5	3.7	9.8
Prices [3)]	Inflation rate (in per cent)	1.8	0.1	2.8	1.9	2.5
Unemployment [4)]	Unemployment rate (in per cent)	9.15	9.9	9.19	8.97	8.13
Foreign trade	Exports (in CZK billions, current prices)	1,254.9	1,370.9	1,722.7	1,868.6	2,141.1
	Imports (in CZK billions, current prices)	1,325.7	1,440.7	1,749.1	1,830.0	2,093.8
	Balance (in CZK billions, current prices)	-70.8	-69.8	-26.4	38.6	47.3
Average wage [2)]	Nominal (in per cent)	7.3	6.6	6.6	5.2	6.5
	Real (in per cent)	5.4	6.5	3.7	3.2	3.9
Balance of payments	Current account (in CZK billions)	-136.4	-160.6	-167.3	-77.1	-133.8
	Financial account (in CZK billions)	347.8	157.1	183.7	154.8	111.6
Exchange rate [5)]	CZK/USD	32.74	28.23	25.7	23.95	22.61
	CZK/EUR	30.81	31.84	31.9	29.78	28.34
Average interbank	7-day	3.61	2.30	2.23	1.97	2.18
deposit rate (PRIBOR)	3-month	3.55	2.28	2.36	2.01	2.30
in per cent [5)]	6-month	3.56	2.28	2.48	2.05	2.42
Discount rate	(in per cent) [6)]	1.75	1.00	1.50	1.00	1.50
Lombard rate	(in per cent) [6)]	3.75	3.00	3.50	3,00	3.50
2W repo rate	(in per cent) [6)]	2.75	2.00	2.50	2.00	2.50
PX 50 capital market index [6)]		460.7	659.1	1,032.0	1,473.0	1,447.5

Source: CZSO (macroeconomic indicators), CNB
1) At constant 2000 prices
2) Percentage increase on a year earlier
3) Inflation rate, average
4) Average registered unemployment rate; based on existing methodology since 2004
5) Annual averages from monthly averages
6) End-of-period figures; on 20 March 2006, the Prague Stock Exchange's PX 50 and PX-D indices were replaced by a single index called the PX. Calculation of both the original indices was terminated on Friday, 17 March 2006. The new main PX index carries on from the PX 50 and takes over its history.

Annex 2

Organisational structure of CNB Financial Market Supervision
as of 31 December 2006

Bank Board

Zdeněk Tůma
Governor

Luděk Niedermayer
Vice-Governor

Miroslav Singer
Vice-Governor

Mojmír Hampl
Chief Executive Director

Robert Holman
Chief Executive Director

Pavel Řežábek
Chief Executive Director

Vladimír Tomšík
Chief Executive Director

- 530 **Banking Regulation and Supervision Department**
  - 531 **Regulation Division**
  - 532 **Off-Site Banking Supervision Division**
  - 533 **On-Site Banking Supervision Division**
  - 534 **Licensing and Enforcement Division**
  - 535 **Supervisory Support Division**
- 540 **Capital Market Regulation and Supervision Department**
  - 541 **Collective Investment and Pension Funds Division**
  - 542 **Investment Services Providers Division**
  - 543 **Markets and Settlement Division**
  - 544 **Securities Issues Division**
  - 545 **Sanction Procedures Division**
- 550 **Insurance Companies Regulation and Supervision Department**
  - 551 **Insurance Sector Regulation Division**
  - 552 **Supervision Division**
  - 553 **Licensing Division**

Annex 3

Breakdown of banks into groups

(as of 31 December 2006)

I.	**Large banks**	**IV.**	**Foreign bank branches**
1.	Česká spořitelna, a.s.	1.	ABN AMRO Bank N.V.
2.	Československá obchodní banka, a.s.	2.	Bank of Tokyo-Mitsubishi UFJ (Holland) N.V. Prague Branch, organizační složka
3.	HVB Bank Czech Republic a.s.	3.	CALYON S.A., organizační složka
4.	Komerční banka, a.s.	4.	COMMERZBANK Aktiegesellschaft, pobočka Praha
		5.	Deutsche Bank Aktiengesellschaft Filiale Prag, organizační složka
II.	**Medium-sized banks**	6.	Fortis Bank SA/NV, pobočka Česká republika
1.	BAWAG Bank CZ a.s.	7.	HSBC Bank plc – pobočka Praha
2.	Citibank a.s.	8.	ING Bank N.V.
3.	Česká exportní banka, a.s.	9.	Oberbank AG pobočka Česká republika
4.	Hypoteční banka, a.s.	10.	PRIVAT BANK AG der Raiffeisenlandesbank Oberösterreich, pobočka Česká republika
5.	Českomoravská záruční a rozvojová banka, a.s.		
6.	GE Money Bank, a.s.	11.	Raiffeisenbank im Stiftland eG pobočka Cheb, odštěpný závod
7.	Raiffeisenbank a.s.	12.	Všeobecná úverová banka a.s., pobočka Praha
8.	Volksbank CZ, a.s.	13.	Waldviertler Sparkasse von 1842 AG
9.	Živnostenská banka, a.s.		
		V.	**Building societies**
III.	**Small banks**	1.	Českomoravská stavební spořitelna, a.s.
1.	eBanka, a.s.	2.	HYPO stavební spořitelna a.s.
2.	IC Banka, a.s.	3.	Modrá pyramida stavební spořitelna, a.s.
3.	J&T BANKA, a.s.	4.	Raiffeisen stavební spořitelna a.s.
4.	PPF banka a.s.	5.	Stavební spořitelna České spořitelny, a.s.
5.	Wüstenrot hypoteční banka a.s.	6.	Wüstenrot – stavební spořitelna a.s.

Annex 4

Breakdown of insurance undertakings into groups

(as of 31 December 2006)

I. Large insurance undertakings

1. Allianz pojišťovna, a.s.
2. Česká pojišťovna a.s.
3. ČSOB Pojišťovna, a.s., člen holdingu ČSOB
4. Generali Pojišťovna a.s.
5. Kooperativa, pojišťovna, a.s.

II. Medium-sized insurance undertakings

1. Česká podnikatelská pojišťovna, a.s.
2. Komerční pojišťovna, a.s.
3. Pojišťovna České spořitelny, a.s.
4. PRVNÍ AMERICKO – ČESKÁ POJIŠŤOVNA, a.s., (FIRST AMERICAN CZECH INSURANCE COMPANY)
5. UNIQA pojišťovna, a.s.
6. Winterthur pojišťovna, a.s. [a]

III. Small insurance undertakings

1. AEGON Pojišťovna, a.s.
2. AIG CZECH REPUBLIC pojišťovna, a.s.
3. Aviva životní pojišťovna, a.s.
4. Cestovní pojišťovna ADRIA Way družstvo
5. Česká pojišťovna ZDRAVÍ a.s.
6. D.A.S. pojišťovna právní ochrany, a.s.
7. Euler Hermes Čescob, úvěrová pojišťovna, a.s.
8. Evropská Cestovní Pojišťovna, a.s.
9. Exportní garanční a pojišťovací společnost, a.s.
10. HALALI, všeobecná pojišťovna, a.s.
11. Hasičská vzájemná pojišťovna a.s.
12. Komerční úvěrová pojišťovna EGAP, a.s.
13. MAXIMA pojišťovna, a.s.
14. Nationale-Nederlanden pojišťovna, a.s. [b]
15. POJIŠŤOVNA CARDIF PRO VITA, a.s.
16. Pojišťovna Slavia a.s.
17. Pojišťovna VZP, a.s.
18. Servisní pojišťovna a.s.
19. Triglav pojišťovna, a.s.
20. VICTORIA VOLKSBANKEN pojišťovna, a.s.
21. Vitalitas pojišťovna, a.s.
22. Wüstenrot, životní pojišťovna, a.s.

IV. Branches of foreign insurance undertakings

1. AIG EUROPE, S.A., pobočka pro Českou republiku
2. Atradius Credit Insurance N. V., organizační složka
3. CG Car-Garantie Versicherungs-Aktiengesellschaft organizační složka pro Českou republiku
4. Coface Austria Kreditversicherung AG [c]
5. Deutscher Ring Lebensversicherungs-AG, pobočka pro Českou republiku
6. Elvia Reiseversicherungs – Gesellschaft AG – organizační složka
7. Erste n.oe. Brandschaden – Versicherungsaktiengesellschaft organizační složka pro ČR
8. GERLING – Konzern Všeobecná pojišťovací akciová společnost – organizační složka
9. HDI Hannover Versicherung AG, organizační složka
10. HDI Industrie Versicherung AG, organizační složka
11. ING Životná poisťovňa, a.s., pobočka pro Českou republiku
12. Nationale-Nederlanden životní pojišťovna [d]
13. Österreichische Hagelversicherung – Versicherungsverein auf Gegenseitigkeit, organizační složka
14. QBE poisťovňa, a.s., pobočka
15. Wüstenrot pojišťovna, pobočka pro Českou republiku
16. XL INSURANCE COMPANY LIMITED, organizační složka

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a) since 15 March 2007 AXA životní pojišťovna a.s.
b) since 3 January 2007 ING pojišťovna, a.s.
c) as at 29 March 2007 the undertaking was not entered in the Commercial Register
d) since 1 January 2007 ING Životní pojišťovna N.V., pobočka pro Českou republiku

Annex 5

Numbers of foreign financial undertakings providing financial services in the Czech Republic under the freedom to provide services (without establishing a branch) as of 31 December 2006

Home country of head office of financial institution	Total number				
	Banks	Insurance undertakings	Funds	Investment companies	Non-bank investment service providers
Belgium	1	10	80	1	-
Denmark	1	8	-	-	1
Estonia	-	2	-	-	-
Finland	3	6	-	-	1
France	13	29	-	1	6
Gibraltar	1	4	-	-	-
Ireland	7	67	119	-	6
Iceland	1	-	-	-	-
Italy	3	20	-	-	-
Cyprus	2	-	-	-	9
Liechtenstein	1	7	-	-	-
Lithuania	1	3	-	-	-
Latvia	-	1	-	-	-
Luxembourg	6	18	915	10	2
Hungary	4	6	-	1	-
Malta	1	2	-	-	1
Germany	25	27	12	5	6
Netherlands	6	24	-	-	16
Norway	1	-	-	-	2
Poland	1	11	-	-	-
Austria	32	24	138	8	16
Greece	-	-	-	-	1
Slovakia	2	9	7	2	5
Slovenia	-	3	-	-	1
Spain	1	2	-	-	-
Sweden	1	14	-	1	-
UK	27	104	-	-	220
Total	**141**	**401**	**1271**	**29**	**293**

Annex 6

Banking sector balance sheet

(including foreign bank branches; CZK thousands)

	31 December 2004	31 December 2005	31 December 2006		
	Data adjusted for provisions and reserves	Data adjusted for provisions and reserves	Data not adjusted for provisions and reserves	Provisions and reserves	Data adjusted for provisions and reserves
Total balance sheet assets	2,635,554,490	2,954,369,396	3,245,769,017	93,957,681	3,151,811,336
Cash and deposits with central banks	58,060,613	55,201,438	68,613,117		68,613,117
Treasury bills and other securities accepted by the central bank for refinancing	291,597,048	334,585,134	385,928,713		385,928,713
Securities issued by government institutions accepted by central banks for refinancing	272,625,299	330,780,643	369,918,625		369,918,625
Other securities accepted by central banks for refinancing	18,971,749	3,804,491	16,010,088		16,010,088
Receivables from banks	825,454,622	919,850,776	734,230,273	24,650	734,205,623
Receivables from banks payable on demand	50,728,537	46,503,438	99,635,471		99,635,471
Other receivables from banks	774,726,080	873,347,343	634,594,804	24,650	634,570,154
Other receivables from central banks	424,503,010	460,812,175	330,078,611	0	330,078,611
Other receivables from other banks	350,223,066	412,535,168	304,516,193	24,650	304,491,543
Receivables from clients	1,073,857,898	1,174,356,307	1,457,184,592	32,801,904	1,424,382,688
Receivables from clients payable on demand	10,712,950	13,113,529	18,682,025		18,682,025
Other receivables from clients	1,063,144,944	1,161,242,776	1,438,502,565	32,801,904	1,405,700,661
Debt securities	208,649,720	276,919,321	311,784,281	0	311,784,281
Debt securities issued by government institutions	60,424,919	72,453,590	73,180,978	0	73,180,978
Debt securities issued by other entities	148,224,800	204,465,730	238,603,302	0	238,603,302
Shares, units and other interests	10,391,740	11,503,372	13,159,448	0	13,159,448
Substantial interests	2,263,721	3,664,527	3,823,268	457,800	3,365,468
Controlling interests	16,338,797	32,623,062	42,639,097	426,516	42,212,581
Long-term intangible assets	11,822,231	11,940,831	30,755,364	18,452,765	12,302,599
Long-term tangible assets	40,570,735	37,000,164	75,358,456	41,068,295	34,290,161
Other balance sheet assets	93,140,071	93,360,177	119,280,630	725,749	118,554,881
Deferred revenues and accrued expenses	3,407,296	3,364,282	3,011,765		3,011,765
Total balance sheet liabilities	2,635,554,491	2,954,369,397			3,151,811,336
Liabilities to banks	361,134,450	409,690,637			348,351,979
Liabilities to banks payable on demand	65,186,762	65,812,694			72,821,586
Other liabilities to banks	295,947,685	343,877,943			275,530,395
Liabilities to clients	1,731,849,574	1,919,558,608			2,102,219,092
Liabilities to clients payable on demand	844,625,179	960,792,243			1,080,651,930
Other liabilities to clients	887,224,392	958,766,367			1,021,567,166
Liabilities from debt securities	214,619,119	262,046,499			278,719,585
Issued debt securities	201,466,318	247,935,040			267,743,673
Other liabilities from debt securities	13,152,801	14,111,459			10,975,912
Other balance sheet liabilities	107,876,189	113,818,285			146,401,131
Deferred revenues and accrued expenses	4,130,146	4,666,275			5,046,216
Reserves	16,519,843	12,764,018			11,023,215
Subordinated liabilities	8,158,411	11,995,624			26,294,794
Registered capital	70,415,961	69,820,010			70,582,596
Share premium account	11,296,451	12,929,645			13,588,498
Reserve funds and other funds created from profit	31,104,920	31,998,661			34,036,007
Capital funds	525,399	1,079,012			4,234,516
Valuation differences	2,886,473	6,815,182			6,109,041
Retained profits (accumulated losses) from previous periods	42,185,237	58,047,741			67,279,535
Profit (loss) for the accounting period	32,852,319	39,139,200			37,925,131

Annex 7

Banking sector profit and loss account

(including foreign bank branches; CZK thousands)

	31 December 2004	31 December 2005	31 December 2006
Interest income and similar income	102,644,223	107,143,638	124,921,782
Interest income from debt securities	23,645,131	23,533,133	25,496,911
Other interest income	72,925,513	77,898,780	92,837,342
Profit from hedging interest rate derivatives	6,073,579	5,711,721	6,587,526
Interest expenses and similar expenses	42,884,712	43,100,408	52,551,961
Interest expenses from debt securities issued	5,404,977	4,886,054	7,289,615
Interest expenses from debt securities issued	185,993	229,551	243,192
Other interest expenses	33,199,219	34,209,159	40,388,282
Loss from hedging interest rate derivatives	4,094,525	3,775,641	4,630,869
Net interest income	59,759,512	64,043,228	72,369,820
Income from shares and other equity instruments	1,369,107	2,189,410	1,675,508
Income from fees and commissions	38,085,392	38,899,100	41,252,027
Fees and commissions from credit activities	6,715,563	6,645,822	7,589,210
Fees and commissions from payments	19,234,838	19,681,798	19,507,477
Fees and commissions from securities transactions	323,068	483,679	679,899
Fees and commissions from foreign exchange transactions	254,536	1,165,476	1,487,011
Fees and commissions from securities and derivatives transactions for clients	999,162	1,374,803	1,626,772
Fees and commissions for consulting activities	39,160	139,100	88,883
Fees and commissions from other financial activities	10,519,064	9,408,416	10,272,780
Fee and commission expenses	6,759,608	7,068,140	8,308,075
Fees and commissions for credit activities	489,096	710,281	934,798
Fees and commissions for payments	2,042,731	1,306,956	1,701,871
Fees and commissions for securities transactions	202,274	268,020	322,579
Fees and commissions for foreign exchange transactions	44,533	51,106	47,538
Fees and commissions for securities and derivatives transactions for clients	286,022	143,948	141,211
Fees and commissions for other financial activities	3,694,952	4,587,828	5,160,077
Net income from fees and commissions	31,325,779	31,830,958	32,943,951
Net profit or loss from financial transactions	11,031,335	10,854,434	9,846,870
Profit (loss) from financial activities with trading financial instruments	9,354,601	10,245,147	9,442,518
Profit (loss) from financial activities with securities available for sale and held to maturity	1,676,733	609,288	404,351
Other operating income	5,148,692	7,610,223	6,124,512
Income from financial leasing	11,655	0	0
Profit from transfers of controlling interests	917,358	189,654	104,681
Profit from transfers of substantial interests	22,178	5,260	62,000
Income from transfers of tangible and intangible assets	1,273,918	2,191,628	3,157,215
Profit from transfers of non-trading debt securities acquired in primary issues	320,087	5,007	153,040
Profit from transfers of non-trading receivables	311,718	213,923	157,735
Other operating income	2,291,778	5,004,747	2,489,845

Banking sector profit and loss account (continued)

(including foreign bank branches; CZK thousands)

	31 December 2004	31 December 2005	31 December 2006
Other operating expenses	4,216,318	2,477,438	3,882,600
Contributions to Deposit Insurance Fund	2,759,690	1,483,667	1,531,941
Contributions to Investment Firm Guarantee Fund	23,102	18,297	40,155
Other operating expenses	1,433,528	975,472	2,310,504
Administrative expenses	48,819,031	51,785,559	55,665,153
Personnel expenses	24,544,499	26,223,481	29,036,458
Other administrative expenses	24,274,531	25,562,073	26,628,699
Release of provisions and reserves for tangible and intangible assets	207,174	684,024	214,333
Depreciation, creation and use of reserves and provisions for tangible and intangible assets	10,439,485	11,793,941	10,109,565
Release of provisions and reserves for liabilities and selected off-balance sheet instruments, income from written off receivables	16,187,071	16,427,596	14,544,524
Depreciation, creation and use of provisions and reserves for liabilities and selected off-balance sheet instruments	16,616,426	17,033,626	19,963,447
Release of provisions for controlling and substantial interests	1,383,642	764,463	2,398
Losses from transfers of controlling and substantial interests, creation and use of provisions	858,744	472,668	8,324
Release of other unnecessary reserves	845,224	982,093	789,380
Creation and use of other reserves	982,828	2,627,853	-162,281
Shares in profit (loss) of controlling or substantial interests	40,964	76,074	113,576
Pre-tax profit or loss from ordinary activities for the financial year	45,365,660	49,271,420	49,158,056
Extraordinary income	2,811	1,365	7,651
Extraordinary expenses	12,992	383	0
Pre-tax profit or loss from extraordinary activities for the financial year	-10,181	982	7,651
Income tax	12,503,162	10,133,202	11,240,578
After-tax profit or loss for the financial year	32,852,319	39,139,200	37,925,131

Annex 8

Insurance sector balance sheet

(total excluding the Czech Insurers' Bureau; CZK thousands)

	31 December 2004	31 December 2005	31 December 2006		
	Data adjusted for provisions and reserves	Data adjusted for provisions and reserves	Data not adjusted for provisions and reserves	Provisions and reserves	Data adjusted for provisions and reserves
Total assets	284,334,732	310,511,484	344,736,979	21,878,687	322,858,294
Receivables for subscribed share capital	40,000	300,000	0	0	0
Long-term intangible assets	4,192,874	4,294,501	9,416,148	5,816,331	3,599,817
Establishment expenses	1,524	6,600	32,254	27,348	4,906
Goodwill	2,506,967	2,289,222	3,589,288	2,002,725	1,586,563
Financial placement (investments)	246,828,463	265,917,108	272,087,231	70,559	272,016,672
Land and buildings (real estate),	10,533,258	9,314,767	8,782,691	16,359	8,766,332
Real estate used in operations	3,388,346	2,800,847	2,861,210	7,843	2,853,367
Financial placements in third-party companies	24,674,050	25,980,388	10,819,924	1,700	10,818,224
Participating interests in affiliates	18,674,180	22,056,890	9,627,084	1,700	9,625,384
Bonds and loans – affiliated companies	4,876,436	2,853,368	228,844	0	228,844
Participating interests with substantial influence	1,123,434	1,070,130	963,192	0	963,192
Bonds and loans – companies with substantial influence	0	0	804	0	804
Other financial placements	211,617,748	230,599,203	252,391,382	52,500	252,338,882
Shares, variable-yield securities, other participating interests	26,694,293	33,101,576	30,486,060	52,000	30,434,060
Bonds and other fixed-income securities	151,791,151	164,473,173	191,826,476	0	191,826,476
Financial placements in investment associations	361,473	273,847	459,082	0	459,082
Other loans	4,569,514	4,488,918	2,058,041	500	2,057,541
Deposits at financial institutions	27,174,419	27,730,481	26,377,835	0	26,377,835
Other financial placements	1,026,898	531,208	1,183,890	0	1,183,890
Deposits with ceding undertakings	3,407	22,750	93,235	0	93,235
Financial placement of unit-linked life assurance	7,737,291	12,419,621	18,579,751	0	18,579,751
Debtors	16,841,682	18,951,359	30,024,687	11,555,183	18,469,504
Receivables arising out of direct insurance operations	8,093,642	8,317,389	13,541,462	3,834,590	9,706,873
Policyholders	7,789,960	8,083,280	12,936,600	3,492,506	9,444,094
Intermediaries	303,682	234,108	604,861	342,083	262,778
Receivables arising out of reinsurance operations	5,239,189	6,897,050	4,438,907	120,923	4,317,984
Other receivables	3,508,851	3,736,921	12,044,317	7,599,670	4,444,648
Other assets	3,986,386	4,180,707	9,138,187	4,436,614	4,701,573
Long-term tangible assets other than land, buildings (real estate) and stocks	2,447,005	2,163,315	6,367,993	4,435,485	1,932,511
Cash at financial institutions, cash and other financial assets	1,490,325	2,015,936	2,763,951	1,130	2,762,821
Other assets	49,057	1,456	6,242	0	6,242
Temporary accounts of assets	4,708,034	4,448,188	5,490,973	0	5,490,973
Interest and annuities	92,882	116,185	82,400	0	82,400
Deferred acquisition costs for insurance contracts	3,138,599	3,107,604	3,797,076	0	3,797,076
- life assurance	1,505,518	2,025,623	2,091,801	0	2,091,801
- non-life insurance	1,633,082	1,081,981	1,705,277	0	1,705,277
Other temporary accounts of assets	1,476,553	1,224,398	1,611,498	0	1,611,498
Contingency items of assets	623,057	653,348	642,168	0	642,168

Insurance sector balance sheet (continued)

(total excluding the Czech Insurers' Bureau; CZK thousands)

	31 December 2004	31 December 2005	31 December 2006		
	Net	Net	Gross	Reinsurers' share in TPs	Net
Total liabilities	284,334,732	310,511,484			322,858,294
Shareholder's equity	53,307,776	57,466,192			58,146,936
Share capital	14,381,427	16,674,140			17,729,181
Movements in share capital	90,000	298,545			10,000
Own stocks or own interim certificates, own business shares	0	0			0
Share premium account	1,078,414	880,720			880,720
Revaluation reserve fund	0	0			-150
Other capital funds	13,973,808	13,544,700			12,213,550
Reserve fund and other profit funds	3,459,248	4,765,647			5,764,396
Profit or loss brought forward	9,480,785	13,579,823			6,951,024
Profit or loss for the current financial year	10,934,094	8,021,161			14,608,215
Subordinated debt	2,500,000	2,500,000			0
Technical provisions	181,957,697	200,511,113	241,219,905	23,349,186	217,870,718
Provision for unearned premiums	13,914,155	14,065,071	20,222,545	4,538,624	15,683,922
Provision for unearned premiums for life assurance	2,950,034	2,890,386	2,869,804	104,816	2,764,988
Provision for unearned premiums for non-life insurance	10,964,121	11,174,685	17,352,740	4,433,808	12,918,934
Life assurance provision	124,726,220	136,557,752	151,247,062	41,301	151,205,761
Outstanding claims provision	27,482,253	31,613,864	52,037,974	18,345,867	33,692,105
Outstanding claims for life assurance	2,878,122	3,115,743	4,412,681	839,868	3,572,813
Outstanding claims for non-life insurance	24,604,131	28,498,121	47,625,294	17,506,000	30,119,292
Provision for bonuses and rebates	1,139,265	1,165,093	1,287,320	60,229	1,227,092
Provision for bonuses and rebates in life assurance	389,698	473,032	483,545	130	483,415
Provision for bonuses and rebates in non-life insurance	749,567	692,061	803,776	60,099	743,677
Equalisation provision	4,529,406	4,404,943	4,576,488	0	4,576,488
Provision for the fulfilment of the commitments from the technical interest rate applied	5,294,923	7,589,392	6,039,689	0	6,039,689
Non-life insurance provision	170,862	164,535	216,500	144	216,356
Insurance provision for life assurance	5,006	3,730	29,853	0	29,853
Non-life insurance provision for non-life insurance	165,856	160,805	186,646	144	186,502
Provisions for the fulfilment of the commitments from the guarantee of the CIB		4,668,681	5,310,120	363,020	4,947,100
Other provisions	4,700,613	281,783	282,208	0	282,208
Other provisions for life assurance	0	281,783	282,208	0	282,208
Other provisions for non-life insurance	4,700,613	0	0	0	0
Technical provision for unit-linked life assurance	7,543,783	12,053,208	18,545,545	0	18,545,545
Provision for other risks and losses	2,673,562	1,406,899			2,023,434
Provision for pensions and similar liabilities	18,654	14,653			7,235
Tax provision	2,467,092	1,103,765			1,676,827
Other provisions	187,815	288,482			339,372
Passive reinsurance deposits	2,887,778	3,541,524			210,755
Creditors	26,538,827	26,874,363			18,833,419
Liabilities arising out of direct insurance	6,202,340	6,493,164			6,534,222
Liabilities arising out of reinsurance	7,420,030	10,462,490			6,971,309
Debenture loans	0	0			0
Convertible loans	0	0			0
Liabilities to financial institutions	1,524,388	1,025,364			528,248
Other liabilities	11,392,070	8,893,345			4,799,642
Tax liabilities and social security and public health insurance liabilities	3,418,815	2,530,311			2,098,192
Guarantee fund of the Czech Insurers' Bureau	0	0			0
Temporary accounts of liabilities	6,925,309	6,158,185			7,227,482
Accrued expenses and revenues	3,955,113	3,454,131			3,520,448
Other temporary accounts of liabilities	2,970,195	2,704,054			3,707,034
Contingency items of liabilities	2,885,366	2,695,673			3,679,218

Annex 9

Insurance sector profit and loss account

(total excluding the Czech Insurers' Bureau; CZK thousands)

Technical account for non-life insurance	31 December 2004	31 December 2005	31 December 2006
Result of technical account for non-life insurance	2,630,567	3,835,541	5,330,253
Earned premiums, net of reinsurance	42,584,617	44,774,469	49,897,872
Premiums written, net of reinsurance	41,390,489	44,882,067	51,329,003
Gross premium written	68,365,463	72,122,585	74,856,768
Gross premium written ceded to reinsurers	-26,974,974	-27,240,518	-23,527,765
Change in provision for unearned premiums, net of reinsurance	1,194,127	-107,597	-1,431,132
Change in gross provision for unearned premiums	248,815	-658,935	-1,516,778
Change in provision for unearned premiums – reinsurers' share	945,312	551,337	85,646
Allocated investment return transferred from the non-technical account	1,538,378	1,364,216	1,050,376
Other technical income, net of reinsurance	1,962,360	2,077,804	2,506,555
Claims incurred including change in provision, net of reinsurance	-24,142,849	-27,467,942	-29,406,966
Claims paid, net of reinsurance	-23,916,079	-23,790,032	-28,549,062
Gross claims paid	-34,913,935	-33,830,122	-37,898,648
Claims paid – reinsurers' share	10,997,856	10,040,090	9,349,587
Change in provision for claims, net of reinsurance	-226,771	-3,677,910	-857,905
Change in gross provision for claims,	-88,272	-5,852,559	-1,677,828
Change in provision for claims – reinsurers' share	-138,498	2,174,649	819,923
Change in other technical provisions, net of reinsurance	-374,370	71,609	-222,928
Bonuses and rebates, net of reinsurance	-644,212	-592,030	-761,691
Operating expenses, net amount	-13,118,863	-11,293,636	-13,147,616
Acquisition expenses for insurance contracts	-10,037,625	-9,668,616	-10,615,111
Change in deferred acquisition expenses	-14,284	-105,946	111,057
Administrative expenses	-7,868,627	-7,837,643	-8,419,589
Reinsurance commissions and profit participation	4,801,673	6,318,569	5,776,030
Other technical expenses, net of reinsurance	-4,731,245	-4,918,644	-4,412,241
Change of equalisation provision	-443,249	-180,306	-173,111

Technical account for life assurance	31 December 2004	31 December 2005	31 December 2006
Result of technical account for life assurance	5,638,223	4,394,911	7,849,365
Earned premiums, net of reinsurance	42,021,921	42,837,976	46,141,051
Premiums written, net of reinsurance	42,180,290	42,757,848	45,920,326
Gross premium written	44,201,009	44,954,269	47,233,338
Gross premium written ceded to reinsurers	-2,020,719	-2,196,421	-1,313,011
Change in provision for unearned premiums, net of reinsurance	-158,369	80,128	220,726
Change in gross provision for unearned premiums			226,810
Change in provision for unearned premiums – reinsurers' share			-6,084
Income from financial placements	41,159,101	29,741,508	19,552,852
Income from participating interests	102,549	139,816	206,741
Income from other financial placements	8,609,952	7,748,152	8,526,210
Income from land and buildings (real estate)	356,451	345,087	311,172
Income from other investments (except real estate)	8,253,501	7,403,065	8,215,038
Change in value of financial placements – income	28,382	87,759	1,518,301
Gains on the realisation of financial placements	32,418,218	21,765,781	9,301,599
Unrealised gains on financial placements	7,062,494	5,002,060	4,463,461
Other technical income, net of reinsurance	557,420	835,299	740,473
Claims incurred including change in provision, net of reinsurance	-23,329,268	-19,421,040	-18,948,320
Claims paid, net of reinsurance	-23,121,971	-19,298,066	-18,512,472
Gross claims paid	-23,442,780	-19,730,278	-18,836,987
Claims paid – reinsurers' share	320,809	432,213	324,515
Change in provision for claims, net of reinsurance	-207,297	-122,975	-435,849

Insurance sector profit and loss account (continued)

(total excluding the Czech Insurers' Bureau; CZK thousands)

Technical account for life assurance	31 December 2004	31 December 2005	31 December 2006
Change in gross provision for claims,	-684,878	-373,314	-486,922
Change in provision for claims – reinsurers' share	477,581	250,339	51,072
Change in other technical provisions, net of reinsurance	-13,855,550	-19,245,456	-17,778,418
Change in balance of life assurance provision, net of reinsurance	-9,607,663	-12,208,536	-13,663,988
Change in balance of gross life assurance provision	-10,033,045	-12,672,552	-13,586,516
Change in balance of life assurance provision – reinsurers' share	425,382	464,016	-77,472
Change in balance of other technical provisions (except life assurance provision), net of reinsurance	-4,247,888	-7,036,921	-4,114,430
Bonuses and rebates, net of reinsurance	-89,074	-46,971	-69,445
Operating expenses, net amount	-9,868,358	-9,917,687	-10,556,207
Acquisition expenses for insurance contracts	-6,013,315	-6,234,345	-6,592,951
Change in deferred acquisition expenses	-29,867	64,793	552,011
Administrative expenses	-4,239,579	-4,421,727	-4,855,531
Reinsurance commissions and profit participation	414,403	673,592	340,263
Expenses related to financial placements	-33,647,058	-21,804,409	-11,379,757
Administration expenses on financial placements, including interest	-1,819,906	-1,362,046	-1,378,446
Change in value of financial placements – expenses	-13,962	-2,777,316	-59,076
Realisation expenses on financial placements	-31,813,189	-17,665,046	-9,942,234
Unrealised losses on financial placements	-2,948,671	-2,156,248	-3,282,556
Other technical expenses, net of reinsurance	-896,843	-1,010,357	-640,599
Transfer of income from financial placement to the non-technical account	-527,890	-419,764	-393,171

Non-technical account	31 December 2004	31 December 2005	31 December 2006
Profit or loss for the accounting period	10,934,093	8,021,162	14,608,215
After-tax profit or loss on ordinary activities	9,133,438	7,782,606	14,595,948
Result of technical account for non-life insurance	2,630,567	3,835,541	5,330,253
Result of technical account for life assurance	5,638,223	4,394,911	7,849,365
Income from financial placements	8,073,480	7,288,969	10,379,901
Income from participating interests	126,061	1,860,245	2,180,132
Income from other financial placements	2,537,165	1,882,631	1,970,265
Income from land and buildings (real estate)	58,656	65,841	54,476
Income from other investments (except real estate)	2,478,509	1,816,790	1,915,790
Change in value of financial placements – income	777,774	1,261,340	1,131,612
Income from the realisation of financial placements	4,632,480	2,284,753	5,097,893
Transferred income from financial placements from technical account for life assurance	526,986	419,764	393,171
Expenses related to financial placements	-5,829,467	-4,737,742	-5,445,067
Administration expenses on financial placements, including interest	-747,261	-718,861	-603,810
Change in value of financial placements – expenses	-603,330	-1,360,031	-1,068,041
Realisation expenses on financial placements	-4,478,876	-2,658,851	-3,773,216
Transfer of income from financial placements to non-life technical account	-1,537,288	-1,364,133	-1,050,376
Other income	5,420,025	1,070,675	2,641,832
Other expenses	-2,265,765	-570,991	-1,976,377
Income tax on ordinary activities	-3,523,322	-2,554,388	-3,526,752
Extraordinary profit or loss	1,859,353	280,805	66,364
Extraordinary income	1,980,523	333,330	77,321
Extraordinary expenses	-121,170	-52,525	-10,957
Income tax on extraordinary activities	-8,161	4,701	-9,070
Other taxes	-50,537	-46,950	-45,029

Annex 10

Pension fund sector balance sheet

(CZK thousands)

	31 December 2004 Data adjusted for provisions and reserves	31 December 2005 Data adjusted for provisions and reserves	31 December 2006 Data adjusted for provisions and reserves
Total assets	102,104,186	123,416,677	145,939,162
Cash and deposits with central banks	812	604	932
Receivables from banks and credit unions	9,587,683	10,133,528	9,333,972
Receivables from banks and credit unions payable on demand	1,633,865	4,105,569	4,670,052
Other receivables from banks and credit unions	7,953,818	6,027,959	4,663,920
Receivables from non-banking institutions	5,318	5,467	11,341
Receivables from non-banking institutions payable on demand	0	0	0
Other receivables from non-banking institutions	5,318	5,467	11,341
Debt securities	82,796,618	99,106,151	115,791,688
Debt securities issued by government institutions	54,598,210	72,805,108	90,269,006
Debt securities issued by other entities	28,198,408	26,301,043	25,522,682
Shares, units and other interests	5,816,540	9,230,837	14,434,241
Shares	5,495,603	7,425,219	9,616,022
Units and other interests	320,937	1,805,618	4,818,219
Substantial interests	0	0	0
Substantial interests in banks	0	0	0
Substantial interests in other entities	0	0	0
Controlling interests	0	0	0
Controlling interests in banks	0	0	0
Controlling interests in other entities	0	0	0
Long-term intangible assets	175,917	144,098	122,828
Establishment expenses	0	0	0
Goodwill	11,001	5,663	328
Other long-term intangible assets	164,916	138,435	122,500
Long-term tangible assets	583,948	993,776	1,437,951
Land and buildings for operations	186,583	166,845	151,234
Other long-term tangible assets	397,365	826,931	1,286,717
Receivables from state budget – state contribution	726,863	811,059	919,219
Other assets	677,395	721,451	1,006,975
Receivables from subscribed registered capital	0	0	0
Deferred revenues and accrued expenses	1,733,092	2,269,706	2,880,015
Acquisition expenses for pension plans	1,720,512	2,217,241	2,870,269
Other deferred revenues and accrued expenses	12,580	52,465	9,746

Pension fund sector balance sheet (continued)

(CZK thousands)

	31 December 2004	31 December 2005	31 December 2006
Total liabilities	102,104,186	123,416,677	145,939,162
Liabilities to banks and credit unions	0	0	0
Liabilities to banks and credit unions payable on demand	0	0	0
Other liabilities to banks and credit unions	0	0	0
Liabilities to non-banking institutions	0	5,105	3,350
Liabilities to non-banking institutions payable on demand	0	0	0
Other liabilities to non-banking institutions payable on demand	0	5,105	3,350
Planholders' money	94,220,886	113,107,511	136,404,900
Planholders' contributions	71,287,522	86,068,910	104,543,054
Planholders' own contributions		75,541,445	90,589,522
Contributions paid by employer		10,400,306	13,749,580
Contributions paid by third parties for planholder		127,159	203,952
State contributions	14,312,153	16,503,900	18,990,951
Financial means for pension payments	117,151	148,207	187,710
Revenues on planholders' contributions	7,732,141	9,426,911	11,987,887
Unallocated planholders' contributions	512,481	575,888	517,258
Payables from eligible unpaid lump sums	258,001	383,695	178,040
Liabilities to state budget – state contribution	32,295	51,261	74,291
Liabilities to state budget – tax liabilities	47,257	79,847	70,280
Other liabilities	341,938	610,539	595,578
Deferred revenues and accrued expenses	5,049	13,857	13,374
Reserves	36,014	58,718	59,641
Reserves for pensions and similar payables	34,769	56,536	58,016
Reserves for taxes	0	0	0
Other reserves	1,245	2,182	1,625
Subordinated liabilities	0	0	0
Registered capital	1,063,438	1,063,438	1,063,438
Paid up capital	1,063,438	1,063,438	1,063,438
Own shares	0	0	0
Share premium account	148,771	148,771	148,771
Reserve funds and other funds created from profit	870,481	1,114,493	1,465,388
Statutory reserve funds and risk funds	652,609	851,317	1,117,164
Other reserve funds	12,445	0	0
Other funds created from profit	205,427	263,176	348,224
Pension reserves fund		114,059	173,325
Revaluation reserve fund	0	0	0
Capital funds	425,181	381,146	364,693
Valuation differences	1,534,252	2,059,445	1,207,103
Valuation differences from assets and liabilities	1,521,615	2,067,649	1,158,327
Valuation differences from hedging derivatives	12,637	-8,204	48,776
Valuation differences from recalculated shares	0	0	0
Other valuation differences	0	0	0
Retained profits (accumulated losses) from previous periods	171,782	154,868	343,833
Profit or loss for the accounting period	3,206,842	4,567,678	4,124,522

Annex 11

Pension fund sector profit and loss account

(CZK thousands)

	31 December 2004	31 December 2005	31 December 2006
Interest income and similar income	2,868,310	3,324,647	3,847,184
Interest on debt securities	2,706,934	3,133,429	3,618,374
Interest on other assets	161,376	191,218	228,810
Interest expenses and similar expenses	231	3,616	175
Interest expenses from debt securities	25	3,589	0
Costs of other liabilities	206	27	175
Income from shares and other equity instruments	181,571	144,505	365,256
Income from shares and other equity instruments representing substantial interests	0	0	0
Income from shares and other equity instruments representing controlling interests	0	0	0
Other income from shares and other equity instruments	181,571	144,505	365,256
Income from fees and commissions	1,566	1,422	2,257
Fee and commission expenses	715,644	942,891	1,094,950
Expenses associated with care for safety and administration of securities	243,912	360,878	340,021
Expenses associated with sale or other disposal of securities	3,644	8,774	14,356
Expenses for pension plans	433,820	550,324	716,775
Other fee and commission expenses	34,268	22,915	23,798
Profit or loss from financial operations	1,792,192	3,034,649	1,989,331
Other operating income	76,786	111,834	190,242
Other operating expenses	34,590	60,148	26,128
Administrative expenses	840,467	901,532	999,626
Personnel expenses	300,316	314,921	333,377
Social security and health insurance	128,717	78,804	78,954
Wages and remuneration – employees and statutory bodies	161,713	225,088	242,437
Other social expenses	9,886	11,029	11,986
Other administrative expenses	540,151	586,611	666,249
Release of provisions and reserves for tangible and intangible assets	700	0	0
Depreciation, creation and use of reserves and provisions for tangible and intangible assets	88,768	87,224	153,092
Depreciation of tangible assets	39,553	38,294	98,272
Creation and use of reserves and provisions for tangible assets	0	1,614	2,414
Depreciation of intangible assets	31,102	29,203	34,298
Creation and use of reserves and provisions for intangible assets	18,113	18,113	18,109
Release of provisions and reserves for receivables and guarantees, income from written-off receivables	2,382	0	7,875
Depreciation, creation and use of provisions and reserves for receivables and guarantees	2,420	3,574	2,456
Release of provisions for controlling and substantial interests	0	0	0
Losses from transfers of controlling and substantial interests, creation and use of provisions	0	15	23
Release of other reserves, including pension reserves	3,552	5,379	7,909
Creation and use of other reserves, including pension reserves	17,105	30,057	12,517
Shares in profit (loss) of controlling or substantial interests	0	0	0
Pre-tax profit or loss from ordinary activities for the financial year	3,227,834	4,499,389	4,062,299
Extraordinary income	1	0	4,693
Extraordinary expenses	0	0	0
Pre-tax profit or loss from extraordinary activities for the financial year	1	77,148	72,247
Income tax	20,993	25,703	3,634
After-tax profit or loss for the financial year	3,206,842	4,567,678	4,124,522

Annex 12

Investment company sector profit and loss account

(CZK thousands)

	31 December 2004	31 December 2005	31 December 2006
Interest income and similar income	26,814	20,944	37,271
Interest on debt securities	16,433	15,246	28,249
Interest on other assets	10,381	5,698	9,022
Interest expenses and similar expenses	1,976	1,244	111
Income from shares and other equity instruments	4,342	6,785	3,046
Income from shares and other equity instruments representing substantial and controlling interests	-20	0	0
Other income from shares and other equity instruments	4,362	6,785	3,046
Income from fees and commissions	1,568,013	1,532,722	1,850,518
Fee and commission expenses	511,068	759,613	809,793
Profit or loss from financial operations	58,959	17,839	5,235
Other operating income	181,720	92,335	122,653
Other operating expenses	264,769	66,243	74,740
Administrative expenses	504,337	427,319	466,147
Personnel expenses	191,691	201,972	225,827
Wages and salaries of employees	141,698	148,370	164,459
Social security and health insurance of employees	49,436	51,223	58,739
Other social expenses	557	2,379	2,629
Other administrative expenses	202,667	225,347	240,320
Release of provisions and reserves for tangible and intangible assets	0	4,273	1,153
Depreciation, creation and use of reserves and provisions for tangible and intangible assets	133,542	45,121	21,945
Depreciation of tangible assets		37,347	16,273
Release of provisions and reserves for receivables and guarantees, income from written-off receivables	658	15	62
Depreciation, creation and use of provisions and reserves for receivables and guarantees	857	15	56
Release of provisions for controlling and substantial interests	380	0	0
Losses from transfers of controlling and substantial interests, creation and use of provisions	376	0	0
Release of other reserves	1,889	0	1,268
Creation and use of other reserves	3,731	837	1,353
Shares in profit (loss) of controlling or substantial interests	5,218	-600	612
Pre-tax profit or loss from ordinary activities for the financial year	594,040	356,431	638,201
Extraordinary income	0	0	40
Extraordinary expenses	7,700	27	0
Pre-tax profit or loss from extraordinary activities for the financial year	-7,700	-27	40
Income tax	165,817	82,385	138,979
After-tax profit or loss for the financial year	420,523	274,019	499,262

Note: Owing to missing data, the above figures exclude data for two investment companies.

Annex 13

Investment company sector balance sheet
(CZK thousands)

	31 December 2004 Data adjusted for provisions and reserves	31 December 2005 Data adjusted for provisions and reserves	31 December 2006 Data adjusted for provisions and reserves
Total assets	2,389,085	2,152,605	2,520,385
Cash	509	279	588
Receivables from banks	409,467	417,357	730,097
Receivables from banks payable on demand	139,161	243,843	457,482
Receivables from banks other than those payable on demand	270,306	173,514	272,615
Receivables from non-banking institutions	0	7,500	17,000
Receivables from non-banking institutions payable on demand	0	7,500	17,000
Receivables from non-banking institutions other than those payable on demand	0	0	0
Debt securities	396,497	820,720	1,009,445
Debt securities issued by government institutions	0	0	0
Debt securities issued by other entities	396,497	820,720	1,009,445
Shares, units and other interests	1,205,754	499,779	292,850
Shares	182	0	0
Units	1,205,571	499,779	292,850
Other interests	0	0	0
Substantial interests and controlling interests	19,890	19,290	0
Long-term intangible assets	47,489	29,343	32,094
Establishment expenses	0	0	205
Goodwill	25,039	0	0
Other long-term intangible assets	22,450	29,343	31,889
Long-term tangible assets	118,169	116,203	114,573
Land and buildings for operations	99,334	96,911	94,872
Other long-term tangible assets	18,835	19,292	19,701
Other assets	172,939	216,654	258,045
Receivables from subscribed registered capital	0	865	503
Deferred revenues and accrued expenses	18,371	24,615	65,190

Investment company sector balance sheet (continued)

(CZK thousands)

	31 December 2004	31 December 2005	31 December 2006
Total liabilities	2,389,085	2,152,605	2,520,385
Liabilities to banks	31,894	5,000	0
Liabilities to banks payable on demand	4,994	0	0
Liabilities to banks other than those payable on demand	26,900	5,000	0
Liabilities to non-banking institutions	4,675	0	0
Liabilities to non-banking institutions payable on demand	4,675	0	0
Liabilities to non-banking institutions other than those payable on demand	0	0	0
Other liabilities	202,515	208,067	266,194
Deferred revenues and accrued expenses	41,614	47,500	24,984
Reserves	3,854	4,676	4,761
Reserves for pensions and similar liabilities	81	918	1,003
Tax reserves	15	0	0
Other reserves	3,758	3,758	3,758
Subordinated liabilities	0	0	0
Registered capital	650,000	616,960	646,960
Paid up capital	650,000	616,960	646,960
Own shares	0	0	0
Share premium account	388,110	388,110	388,110
Reserve funds and other funds created from profit	133,728	135,715	139,148
Statutory reserve funds and risk funds	122,538	123,264	125,711
Other reserve funds	0	0	0
Other funds created from profit	11,190	12,451	13,437
Revaluation reserve fund	0	0	0
Capital funds	27,845	43,645	45,640
Valuation differences	0	1,633	1,972
Valuation differences from assets and liabilities	0	1,633	1,972
Valuation differences from hedging derivatives	0	0	0
Valuation differences from recalculated shares	0	0	0
Other valuation differences	0	0	0
Retained profits (accumulated losses) from previous periods	484,327	427,280	503,354
Profit or loss for the accounting period	420,523	274,019	499,262

Note: Owing to missing data, the above figures exclude data for two investment companies.

Annex 14

List of insurance undertakings in the Czech Republic licensed to carry on insurance classes as of 31 December 2006

Name	Life insurance classes						Non-life insurance classes																						
	A 1	A 2	A 3	A 4	A 5	A 6	B 1	B 2	B 3	B 4	B 5	B 6	B 7	B 8	B 9	B 10	POPV	B 11	B 12	B 13	B 14	B 15	PCK	B 16	B 17	B 18
AEGON Pojišťovna, a.s.	x	x	x	x		x																				
AIG CZECH REPUBLIC pojišťovna, a.s.							x	x					x	x	x					x				x	x	x
Allianz pojišťovna, a.s.	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x		x	x	x		x
Aviva životní pojišťovna, a.s.	x			x		x																				
Cestovní pojišťovna ADRIA Way družstvo																										x
Česká podnikatelská pojišťovna, a.s.	x	x	x	x		x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x		x
Česká pojišťovna a.s.	x	x	x	x	x	x	x		x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x		x
Česká pojišťovna ZDRAVÍ a.s.							x	x																x		x
ČSOB Pojišťovna, a.s., člen holdingu ČSOB	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x		x
D.A.S. pojišťovna právní ochrany, a.s.																									x	
Euler Hermes Čescob, úvěrová pojišťovna, a.s.																					x	x				
Evropská Cestovní Pojišťovna, a.s.																										x
Exportní garanční a pojišťovací společnost, a.s.																					x	x		x		
Generali Pojišťovna a.s.	x	x	x	x		x	x	x	x				x	x	x	x	x			x	x	x	x	x	x	x
HALALI, všeobecná pojišťovna, a.s.							x							x	x					x				x		
Hasičská vzájemná pojišťovna, a.s.	x	x	x			x	x		x	x			x	x	x	x				x				x		x
Komerční pojišťovna, a.s.	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x		x	x	x	x	x	x	x		x
Komerční úvěrová pojišťovna EGAP, a.s.																					x					
Kooperativa, pojišťovna, a.s.	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x	x
MAXIMA pojišťovna, a.s.	x						x		x					x	x					x				x		
Nationale-Nederlanden pojišťovna, a.s. a)								x																		
POJIŠŤOVNA CARDIF PRO VITA, a.s.	x					x	x	x																x		
Pojišťovna České spořitelny, a.s.	x	x	x	x		x	x	x	x		x		x	x	x			x		x		x	x	x		x
Pojišťovna Slavia a.s.							x		x	x	x	x	x	x	x	x				x		x		x		x
Pojišťovna VZP, a.s.								x																		
PRVNÍ AMERICKO – ČESKÁ POJIŠŤOVNA, a.s.																										
(FIRST AMERICAN CZECH INSURANCE COMPANY)	x					x	x	x																		
Servisní pojišťovna a.s.									x																	
Triglav pojišťovna, a.s.							x		x				x	x	x	x	x			x				x		x
UNIQA pojišťovna, a.s.	x	x	x	x		x	x	x	x				x	x	x	x	x			x		x	x	x	x	x
VICTORIA VOLKSBANKEN pojišťovna, a.s.	x		x			x	x	x					x	x	x	x				x						x
Vitalitas pojišťovna, a.s.							x	x																		x
Winterthur pojišťovna, a.s. b)	x			x	x	x	x	x																		
Wüstenrot, životní pojišťovna, a.s.	x	x	x	x	x	x																				

a) since 3 January 2007 ING pojišťovna, a.s.
b) since 15 March 2007 AXA životní pojišťovna a.s.

Annex 15

List of branches of insurance undertakings from EU countries and third countries licensed to carry on insurance classes as of 31 December 2006

I. Branches of insurance undertakings from EU countries

Name	Life insurance classes						Non-life insurance classes																			
	A 1	A 2	A 3	A 4	A 5	A 6	B 1	B 2	B 3	B 4	B 5	B 6	B 7	B 8	B 9	B 10	POPV	B 11	B 12	B 13	B 14	B 15	PCK	B 16	B 17	B 18
AIG EUROPE, S.A., pobočka pro Českou republiku							x	x	x				x	x	x	x	x		x	x	x			x		x
Atradius Credit Insurance N.V., organizační složka																					x	x				
CG Car-Garantie Versicherungs-Aktiengesellschaft																										
organizační složka pro Českou republiku															x									x		
Coface Austria Kreditversicherung AG a)																					x					
Deutscher Ring Lebensversicherungs-AG, pobočka																										
pro Českou republiku	x		x	x		x																				
Erste n.oe. Brandschaden - Versicherungsaktiengesellschaft																										
organizační složka pro ČR	x	x	x			x	x		x					x	x	x				x				x	x	x
GERLING-Konzern Všeobecná pojišťovací akciová																										
společnost-organizační složka							x						x	x	x	x				x	x			x	x	
HDI Hannover Versicherung AG, organizační složka							x					x	x	x	x					x				x	x	
HDI Industrie Versicherung AG, organizační složka														x	x					x				x		
ING Životná poisťovňa, a.s., pobočka pro Českou republiku	x	x	x	x	x	x																				
Nationale - Nederlanden životní pojišťovna b)	x	x	x	x		x		x																		
Österreichische Hagelversicherung - Versicherungsverein																										
auf Gegenseitigkeit, organizační složka														x	x											
QBE poisťovňa, a.s., pobočka							x	x	x	x		x	x	x	x	x				x				x		x
Wüstenrot pojišťovna, pobočka pro Českou republiku	x			x		x								x	x		x			x						x
XL INSURANCE COMPANY LIMITED, organizační složka														x	x					x						

a) as at 29 March 2007 the undertaking was not entered in the Commercial Register
b) since 1 January 2007 ING Životní pojišťovna N.V., pobočka pro Českou republiku

II. Branches of insurance undertakings from third countries

Name	Life insurance classes						Non-life insurance classes																			
	A 1	A 2	A 3	A 4	A 5	A 6	B 1	B 2	B 3	B 4	B 5	B 6	B 7	B 8	B 9	B 10	POPV	B 11	B 12	B 13	B 14	B 15	PCK	B 16	B 17	B 18
Elvia Reiseversicherungs - Gesellschaft AG -																										
organizační složka							x	x	x		x		x		x			x	x	x		x		x		x

Annex 16

List of insurance classes and groups of insurance classes

PART A

CLASSES OF LIFE ASSURANCE

1. Assurance on death only, assurance on survival only, assurance on survival or earlier death, joint life assurance, money back term assurance.
2. Marriage assurance or insurance of benefits for child maintenance.
3. Annuity assurance.
4. Assurance referred to in 1 through 3 which is linked to an investment fund.
5. Capital operations
   a) capital redemption operations based on actuarial calculation whereby, in return for single or periodic payments agreed in advance, commitments of specified duration and amount are undertaken,
   b) management of group pension funds,
   c) operations accompanied by insurance covering either conservation of capital or payment of a minimum interest,
   d) operations relating to the length of human life, which are prescribed by or provided for in social insurance legislation, when the law provides that they can be effected or managed by insurance undertaking at its own risk.
6. Personal accident and sickness insurance if supplementary to classes of insurance 1 through 5.

PART B

CLASSES OF NON-LIFE INSURANCE

1. Accident insurance
   a) with lump sum settlement,
   b) with benefits in the nature of indemnity,
   c) combination of the two,
   d) injury to passengers.
2. Sickness insurance
   a) with lump sum settlement,
   b) with benefits in the nature of indemnity,
   c) combination of the two,
   d) contractual health insurance.
3. Insurance against damage to or loss of land vehicles other than railway rolling stock
   a) motor vehicles,
   b) other than motor vehicles.
4. Insurance against damage to or loss of railway rolling stock.
5. Insurance against damage to or loss of aircraft.
6. Insurance against damage to or loss of
   a) inland vessels,
   b) sea vessels.
7. Insurance of goods in transit including luggage and other property irrespective of means of transport used.
8. Insurance against damage to or loss of property other than referred to in 3 through 7 above caused by
   a) fire,
   b) explosion,
   c) windstorm,
   d) natural forces other than windstorm (e.g. lightning, flood, inundation),
   e) nuclear energy,
   f) landslide or land subsidence.
9. Insurance against damage to or loss of property other than referred to in 3 through 7 above due to hailstorm or frost, or any other event (such as robbery, theft or damage caused by forest animals) unless these are included in class 8, inclusive of insurance against damage to or loss of farm animals caused by infection or by other causes.
10. Liability insurance for damage arising out of
    a) use of land motor vehicle and its trailer,
    b) use of rail vehicle,
    c) the activity of the carrier.

List of insurance classes and groups of insurance classes (continued)

PART B

CLASSES OF NON-LIFE INSURANCE

11. Liability insurance for damage arising out of ownership or use of aircraft, including carrier's liability.
12. Liability insurance for damage arising out of ownership or use of inland or sea vessel, including carrier's liability.
13. General liability insurance for damage other than referred to in classes 10 through 12
    a) liability for damage to environment,
    b) liability for damage caused by nuclear installation,
    c) product liability
    d) other.
14. Credit insurance
    a) general insolvency,
    b) export credit,
    c) instalment credit,
    d) mortgage,
    e) agricultural credit.
15. Suretyship insurance
    a) direct suretyship,
    b) indirect suretyship.
16. Insurance of miscellaneous financial losses arising out of
    a) employment risks,
    b) insufficient income,
    c) bad weather,
    d) loss of profit,
    e) continuing expenses,
    f) unforeseen trading expenses,
    g) loss of market value,
    h) loss of regular source of income (loss of rent or revenue),
    i) other indirect trading financial loss,
    j) other financial losses.
17. Legal expenses insurance.
18. Assistance insurance to persons who get into difficulties while travelling or while away from their residence, including insurance of financial losses directly connected to the travelling (assistance services).

PART C

GROUPS OF NON-LIFE INSURANCE

a) Accident and Sickness Insurance for Classes 1 and 2,
b) Motor Vehicle Insurance for Classes 3, 7 and 10,
c) Insurance against Fire and other Damage to Property for Classes 8 and 9,
d) Aviation Insurance, Marine and Transport Insurance for Classes 4, 5, 6, 7, 11 and 12,
e) Liability Insurance for Damage ("Liability Insurance") for Classes 10, 11, 12 and 13,
f) Credit and Suretyship Insurance for Classes 14 and 15,
g) Insurance against Other Losses for Classes 16, 17 and 18.

Annex 17

Listed bonds issued in 2006 (in CZK)

Issue date	ISIN	Issuer	Maximum size
3 February 2006	CZ0000000195	Orco Property Group S.A.	1,500,000,000
26 January 2006	CZ0003501470	CAC Leasing, a.s.	3,000,000,000
26 April 2006	CZ0002000789	Hypoteční banka, a.s.	2,000,000,000
4 May 2006	CZ0002000797	Hypoteční banka, a.s.	2,500,000,000
24 May 2006	CZ0002000805	Raiffeisenbank, a.s.	500,000,000
21 June 2006	CZ0000000203	Home Credit B.V.	4,500,000,000
10 July 2006	CZ0002000839	Hypoteční banka, a.s.	1,000,000,000
10 July 2006	CZ0002000821	Hypoteční banka, a.s.	1,500,000,000
30 August 2006	CZ0002000862	Hypoteční banka, a.s.	1,500,000,000
27 September 2006	CZ0002000870	Hypoteční banka, a.s.	2,000,000,000
2 October 2006	CZ0003701187	Česká spořitelna, a.s.	3,000,000,000
6 October 2006	CZ0003501488	Home Credit, a.s.	4,000,000,000
4 October 2006	CZ0002000896	Česká spořitelna, a.s.	2,500,000,000
4 October 2006	CZ0002000888	Raiffeisenbank, a.s.	2,000,000,000
19 October 2006	CZ0002000912	Wüstenrot Hypoteční banka	1,250,000,000
19 October 2006	CZ0002000904	Česká spořitelna, a.s.	1,500,000,000
29 November 2006	CZ0002000938	Hypoteční banka, a.s.	2,000,000,000
TOTAL			**36,250,000,000**

Annex 18

Listed share issues/tranches admitted in 2006

Issuer	ISIN	Face value	Size
Central European Media Enterprises Ltd.	BMG200452024	0.08 USD	202,400 USD
ECM Real Estate Investments A.G.	LU0259919230	1.70 EUR	6,566,250 EUR
Pegas Nonwovens SA	LU0275164910	1.24 EUR	11,444,456 EUR
Hypoteční banka, a.s.	CZ0008030509	500 CZK	2,634,738,500 CZK

Annex 19

Listed investment certificate issues admitted as of 31 December 2006

Issuer	ISIN	Name
Raiffeisen Centrobank	AT0000454186	CTX
Raiffeisen Centrobank	AT0000A00M07	CECEXT
Raiffeisen Centrobank	AT0000489778	BRENT CRUDE OIL
Raiffeisen Centrobank	AT0000489398	GOLD
Raiffeisen Centrobank	AT0000340146	DJ EURO STOXX 50
Raiffeisen Centrobank	AT0000481221	RDX
Raiffeisen Centrobank	AT0000A029E3	CTX TURBO SHORT

Annex 20

Bond programmes and base prospectuses approved in 2006 (in CZK)

Issuer	Maximum size	Duration
HVB Bank Czech Rep.	CZK 20 bn	30 years
Česká spořitelna, a.s.	CZK 75 bn	10 years
Raiffeisenbank, a.s.	CZK 20 bn	15 years

Annex 21

Publicly offered unlisted shares (in CZK)

Issuer/Offeror	Face value	Size
STROJIMPORT, a.s.	1,000	481,573,000
VÚHŽ, a.s.	50	14,714,700
CIMEX Praha, a.s.	8	800,000,000
Metra Blansko, a.s.	20,625 and 51	34,770,435
Z, a.s.	10 and 40	29,218,750

Annex 22

Mandatory takeover bid after gaining control over the target company or acquiring a 2/3 or 3/4 share of the voting rights in the target company

Bidder	Target company	Decision
Via Chem Group, a.s.	Spolek pro chemickou a hutní výrobu, a.s.	Proceedings halted 2x
ČESKÝ OLEJ, a.s.	SETUZA, a.s.	Prohibited
RWE Gas International B.V.	Západočeská plynárenská, a.s.	Approved
Lesostavby Holding, a.s.	Lesostavby Šumperk, a.s. (OLZ, a.s.)	Prohibited
RWE Gas International B.V.	Severomoravská plynárenská, a.s.	Approved
AXIA Finance, a.s.	Jitka, a.s.	Approved
SYDERIT, a.s.	TRANZA, a.s.	Approved
E.ON Czech Holding AG	Jihočeská plynárenská, a.s.	2x (Prohibited, Approved)
RWE Gas International B.V.	Severočeská plynárenská, a.s.	Approved
RWE Gas International B.V.	Středočeská plynárenská, a.s.	Approved

Annex 23

Mandatory takeover bid combined with purchase offer

Bidder	Target company	Decision
Aqualia Gestion Integral Del Agua, S.A.	Severomoravské vodovody a kanalizace Ostrava a.s.	Approved

Annex 24

Squeeze-outs

Bidder (Main shareholder)	Target company	Decision
Agropol Group, a.s.	Agrona, a.s.	Approved
FITE-DV KONCERN, a.s.	ČKD PRAHA HOLDING, a.s.	Approved
Kooperativa, pojišťovna, a.s.	UNIGEO, a.s.	Approved
MADETA Group, a.s.	MADETA, a.s.	Approved
OSONA holding, a.s.	LARM a.s.	Not approved
Martin Pacner	KUKS, a.s.	Not approved
Českomoravský cement, a.s., nástupnická společnost	Českomoravské štěrkovny a.s.	Not approved
AGROFERT HOLDING, a.s.	Zemědělské zásobování a nákup Šumperk, a.s.	Approved
Ing. Petr Ptáček	PRAGA Hostivař a.s.	Approved
ČEZ, a.s.	Severočeské doly a.s.	Approved
Czech Energy Holding, a.s.	United Energy, a.s.	Approved
v. Wedel GmbH & Co. KG	PSP Technické služby a.s.	Approved
Ing. Josef Brettl, CSc.	PRAGA Strašnice a.s.	Not approved
SEEIF CR, a.s.	Moravské keramické závody, a.s.	Approved
AGROFERT HOLDING, a.s.	NAVOS, a.s.	Approved
OSONA holding, a.s.	LARM a.s.	Not approved
AGROFERT HOLDING, a.s.	ZENZA Znojmo, a.s.	Not approved
Správa majetkových účastí, a.s.	ART CENTRUM, a.s.	Not approved
Agropol Group, a.s.	Cerea, a.s.	Not approved
Jaroslav Přichystal	LCS Business Centre, a.s.	Approved
AGROFERT HOLDING, a.s.	ZZN Pardubice, a.s.	Approved
ZZN Polabí, a.s.	ZENA – zemědělský nákup a.s.	Approved
Agropol Group, a.s.	Doagra, a.s.	Halted
Dorsch Holding GmbH	HYDROPROJEKT CZ a.s.	Not approved
Dorsch Holding GmbH	HYDROREAL a.s.	Approved
ESET a.s.	H.J.Heinz CR/SR a.s.	Approved
Česká rybářská, spol. s r.o.	Rybářství Chlumec nad Cidlinou, a.s.	Approved
AGROFERT HOLDING, a.s.	ZENZA Znojmo, a.s.	Approved
BRITAL, s.r.o.	BRISK Tábor a.s.	Approved
Agropol Group, a.s.	Doagra, a.s.	Halted
Martin Burda	Lázně Luhačovice, a.s.	Not approved
ICOM transport a.s.	ČSAD Benešov a.s.	Not approved
GES ASSET MANAGEMENT, a.s.	KOH-I-NOOR Mladá Vožice a.s.	Approved
Věra Spěváčková	Zemská a.s.	Approved
AZYS Trading, a.s.	Prefa Pardubice a.s.	Not approved
MATADOR a.s.	Obnova Brno, a.s.	Approved
ČEZ, a.s.	Severočeská energetika, a.s.	Halted
Mittal Steel Ostrava a.s.	JÄKL Karviná, a.s.	Approved
Calabrone s.r.o.	DELTA CLIMATIZER a.s.	Not approved
Agropol Group, a.s.	Integral Vrchovina, a.s.	Approved

Squeeze-outs (continued)

Bidder (Main shareholder)	Target company	Decision
Agropol Group, a.s.	Doagra, a.s.	Approved
RWE Gas International B.V.	Severočeská plynárenská, a.s.	Approved
Martin Burda	Lázně Luhačovice, a.s.	Approved
LATROBE TRADING LIMITED	DKF, holding, a.s.	Approved
ČEZ, a.s.	Severočeská energetika, a.s.	Approved
SENAPOL, s.r.o.	KOVONA KARVINÁ, a.s.	Approved
SOUFFLET AGRICULTURE SAS	Selekta, a.s.	Not approved
ARCADA Capital, a.s.	Moravské železárny, a.s.	Approved
Ing. Miroslav Pešta	ROIF, a.s.	Approved
Agropol Group, a.s.	Obila, a.s.	Approved
LESTING s.r.o.	Lesostavby Frýdek-Místek a.s.	Not approved
Agropol Group, a.s.	ZZN Polepy a.s.	Approved
SOUFFLET AGRICULTURE SAS	Selekta, a.s.	Approved
Bohumil Vejvoda	ZPA Pečky, a.s.	Approved
Valentin Girstl	VUVL a.s.	Not approved
Agropol Group, a.s.	Tagrea, a.s.	Approved
ČSAD autobusy Plzeň, a.s.	Zlínská dopravní, a.s.	Approved
PROMABYT SLOVAKIA	ČSAD autobusy Plzeň, a.s.	Approved
ARNA, a.s.	LINEA NIVNICE, a.s.	Not approved
Expandia Ventures, a.s.	JITONA a.s.	Halted
Girstl Valentin	VUVL a.s.	Not approved
Agropol Group, a.s.	Cerea, a.s.	Approved
OSONA holding, a.s.	LARM a.s.	Not approved
Ing. Petr Vavro	Rybářství Telč., a.s.	Not approved
Agropol Group, a.s.	Belagra, a.s.	Halted
E.ON Czech Holding AG	Jihočeská plynárenská, a.s.	Approved
Zemědělské zásobování a nákup Louny, a.s.	ZZN Slaný a.s.	Approved
Siemens s.r.o.	VA TECH EZ a.s.	Not approved
Stoklásek Lubomír	UNIBETON, a.s.	Approved
AGT INVEST, a.s.	XAVERgen, a.s.	Approved
ARNA, a.s.	LINEA NIVNICE, a.s.	Approved
LUKROM, spol. s r.o.	LUKROM Valmez, a.s.	Approved
RWE Gas International B.V.	Středočeská plynárenská, a.s.	Approved
RWE Gas International B.V.	Západočeská plynárenská, a.s.	Approved
Agropol Group, a.s.	Belagra, a.s.	Approved
Siemens s.r.o.	VA TECH EZ a.s.	Not approved
Ing. Petr Vavro	Rybářství Telč., a.s.	Approved
MACH DRŮBEŽ a.s.	Vajax, a.s.	Approved
Jet Investments, a.s.	Lamet, a.s.	Approved

Annex 25

Application for relief from the takeover bid duty

Bidder	Target company	Decision
Paul Wohanka	MEDICAMENTA, a.s.	Halted

Annex 26

Voluntary takeover bid

Bidder	Target company	Decision
SYNEX PAPER HOLDING LIMITED	Jihočeské papírny, a.s., Větřní	Prohibited

Annex 27

Public contract offer following the decision of the bidder's General Meeting to delist shares

Bidder	Decision
Vodovody a kanalizace Hradec Králové, a.s.	Approved

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