STANDARD SUMMARY PROJECT FICHE

1. Basic Information
   1.1 Désirée Number: CZ2003/004-338.02.04
   1.2 Title: Strengthening the Czech Banking Sector - Application of Basle II
   1.3 Sector: Internal Market and Economic Criteria
   1.4 Location: Czech Republic

2. Objectives
   2.1 Overall objective
   • Functioning market economy and the capacity to cope with competitive pressure and market force
   • The ability to take on obligations of membership including adherence of political, economic and monetary union.

   2.2 Project purpose
   • To increase the skills level within the commercial banking sector, in order to assess and manage credit risk in compliance with Basle II. Recommendation, thereby contributing to the reduction/prevention of bad loans;
   • To assist in implementation of scoring methods and methods for credit risk measurement.
   • To advise in the process of setting appropriate internal rules in the banks and matching these rules with measures of CNB.
   • To assist the CNB in the process of implementation of advanced methods of risk management including the New Basle Capital Accord (Pillar 1) within further development of the banking supervision area.
   • To advise the CNB in further development of the off-site and on-site execution of banking supervision in the field of consolidated banking supervision and financial analyses of banks and banking and financial holdings (twinning-light activity).

   2.3 Accession Partnership and NPAA priority

   The Accession Partnership highlights in the paragraph “Economic criteria” the following priorities:
   • improve the business environment by: (i) improving the operation of the commercial register, (ii) improving bankruptcy legislation and its implementation, and (iii) resolving the bad loan problem in a transparent and economically efficient way,
     and in the paragraph “Free movement of services”
   • reinforce supervision of financial services.

   The Action Plan for Financial Services based on the recommendations made by the Peer Review highlights the following priorities in the field of financial services/banking:
   • The CNB’s regulation on minimum prudential standards i.e. provisions on Management of Credit Risk, Market Risk and Internal Control System should be introduced as soon as possible.
   • Banks should be formally required to put in place a system to identify and monitor connected lending.

   2.4 Contribution to National Development Plan
   N/A.

   2.5 Cross Border Impact
   N/A.
3. Description

3.1 Background and justification

Since 1989, the banking sector structure has undergone very dynamic development. A large number of the newly established banks were unable to cope with the strong competition and risky conditions associated with the economic transformation and were forced to terminate their operations. The tightening of the conditions for setting up new banks has restricted the entry of new entities into the sector, particularly since 1996. Recently, the structure of the banking sector has been affected by mergers of individual banks, leading to a concentration of the sector. Between 1989 and the end of 1998, a total of 63 banking licenses were granted and 25 revoked. Of these, 17 were revoked because of the relevant bank's poor financial situation and failure to meet the prudential rules. 6 as a result of mergers, 1 because the bank failed to start its operations within the allotted legal period and 1 bank has been transformed by law into a specialized agency.

As of 31 December 2001, there were 38 banks and foreign bank branches operating in the banking sector, a fall of two from the same time a year earlier.

A total of 40,871 people were working in the banking sector as of 31 December 2001, i.e. 9 % less than a year earlier. The number of banking units dropped by 3.1% during 1998 to 1,751. The cuts in workforce and banking units were generated primarily by an effort to rationalise operations and increase efficiency. However, the reduction occurred only in large banks and foreign bank branches. The building societies, on the contrary, strengthened their workforces.

The decline in the number of banks and the ever-increasing level of total managed assets has brought about an increase in the average bank size. As of 31 December 1994, the average bank was managing total assets of CZK 27.7 billion, whereas by the end of 2001 the figure had more then doubled to CZK 73.2 billion.

The developments over the past three years demonstrate clearly that the near monopoly position (until recently) of the large banks as regards the two most interesting products from the point of view of clients - deposits and credits - is continuing to wane as the positions of the other bank groups strengthen.

The large banks group accounted for 58.2% of the overall total assets of the banking sector at the end of 2001. This is the smallest figure in the entire period under review, the decline being linked with the removal of Konsolidacnì banka from the banking sector. Virtually all the other bank groups meanwhile enjoyed rising shares of the total. As of 31 December 1994, the average bank was managing total assets of CZK 27.7 billion, whereas by the end of 2001 the figure had more then doubled to CZK 73.2 billion.

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Besides the large banks, the small banks were the only group to record a year-on-year decline on the client-deposit market. Client deposits in building societies continue to grow and are steadily strengthening their share in total deposits received from clients by the banking sector as a whole. By the end of 2001, they had reached almost one tenth of all deposits received.

Credit portfolio quality remains one of the fundamental problems of the Czech banking sector, despite the growing prudence of banks when providing new credits (which has led to falling volumes of newly granted credits in past years). Another positive change is a shift in the structure of the classified credits, with the lowest quality credits, i.e. loss credits, occupying an ever-decreasing position. To a large extent, however, the persisting high volume of classified credits is due to the low level of write-offs of these receivables against provisions. This is linked with difficulties in recovering written-off receivables through the courts and in deriving tax-deductible provisions from the volume of classified credits, and with the low recovery rate of collateral on classified credits. As of 31 December 2001, classified credits amounted to CZK 209.9 billion, a fall of 18.6% compared with end-2000 and of 27.9% compared with end-1999.

The share of classified credits in overall credits granted rose by 0.2 points during 1998 to 27.1%. This large volume of classified credits ensues primarily from banks’ inability to recover their claims by seizing collateral, particularly in the case of real estate.

Credit risk remains the greatest threat to the banks operating in the Czech Republic. The high ratio of classified credits to overall credits is evidence of the banks' experience with debtors, this having been the main cause of a reduction in the volume of new credits granted by banks. The more prudent approach of banks coincided with a period of overall economic slowdown, characterized, among other things, by a shortage of good-quality projects requiring credit.

Basle II aims to enhance the health and stability of the banking sector. One of the measures envisaged under Basle II is to accept a lower capital provision for loans granted by banks provided they can prove that they
operate a sophisticated risk management system. Which will, undeniably, give them a considerable competitive edge.

The existing Accord has made a major contribution to the stability and soundness of banking systems, but in an environment of rapidly developing financial markets it has become out of date and is no longer considered adequate. The newly proposed rules (Basle II) adopt a more sensitive approach to credit risk measurement and management. For the first time the rules address operational risks. On the other hand, they bring no major changes in the area of market risk. Other new features include the use of ratings from rating agencies in order to assign risk weights to receivables, an individualized approach by regulators to each bank, and increased demands regarding the disclosure of information by banks and regarding the setting of capital requirements on a consolidated basis. Overall, this is a comprehensive system of regulations that should improve the method for measuring banking risk.

The Basle Committee intends to finalize the New Capital Accord during 2003, allowing for implementation of the new framework in each country at year-end 2006. During this three-year period banks and supervisors are expected to adapt and develop necessary systems and processes in conformance with the standards of the new Accord. Banks adopting the Internal Rating Based and Advanced Measurement approaches will be required to conduct parallel calculations with the current Accord for one year prior to implementation.

BASEL II should be effective from Y2006. Nevertheless the banks, which would like to use Internal Rating Based (IRB) approach in credit area, have to start collect the data from Y2003. IRB approach saves the bank's capital in comparison with standardised approach. Therefore many banks worldwide work intensively on BASEL II project despite of the fact that final version is being work out. In addition there are not expected huge changes compared to current Consultative Package III instruction.

EU Backround of the implemetation of the New Capital Accord

The European Commission with the support of competent authorities in the Member States have adopted as a foundation for its efforts in the implementation of the New Capital Accord, the working principle that the EU capital adequacy framework should be revised in a manner that is consistent with the New Capital Accord taking account of specificities of the EU context.

According to the time frame of implementation of the New Capital Accord within the EU, adopted by the European Commission and set down in the Financial Services Action Plan, the Commission Services

- issued “Working Document of the Commission Services on Capital Requirements for Credit Institutions and Investment Firms” on 18 November 2002;
- shall issue the third Quantitative Impact Study early in 2003. The results will be analysed by the Basle Committee in order to finalize the proposed calibration of the New Capital Accord-
- shall issue a third and final consultative document in late Spring 2003;
- expect a proposal for the new framework to by adopted by the Commission in the first part of 2004.

3.2 Linked activities

This project is based on the cancelled Project CZ00.03.01 “Strengthening Credit Risk Management Methodology and Application in the Banking Sector” but the focus of the project is reshifted from the general issues of Credit Risk Management Methodology to latest techniques of Credit Risk Management which are incorporated in the New Basle Capital Accord.

There is a twinning light project under Phare 2002 “Improvement of banking supervisory methods” of which the beneficiary is the Banking Regulation Department of the CNB. The project is focusing on implementation of recommendations of Pillar 2 of New Basel Capital Accord in banking supervision that is complementary to this project. No overlapping of activities foreseen.

3.3 Results

- Functioning of the banking sector in the CR strengthened; new methodology, including advanced scoring methods for credit risk measurements in accordance with Basle 2 introduced / applied;
- The CNB banking supervision function strengthened; advanced measures of the CNB introduced and matching with internal rules of banks;
(1) Technical Assistance:

a) Overall study defining appropriate criteria for internal rating systems in compliance with Basle II., all relevant documents issued by the EC and Proposals for Amendments of the EC Directives governing the Capital Framework for Banks and Investment Firms as well as other references for successful implementation of the New Basle Capital Accord (NBCA) drafted and issued. The Study shall be negotiated with participated banks and Czech National Bank and recommendations approved by participated banks implemented.

b) General scoring methodology, which could be adopted by individual banks, to be defined and issued.

c) Substantial number of Czech commercial banks top bank managers, specialists from respective departments (credit risk, liquidity management, financial department, corporate governance etc.), credit officers and trainers trained in new methodology based on the Basle II:

- Partly covered by open courses in the Banking Institute – College of Banking please see activities below – max. 200 trainees, the rest covered by the trained trainers in the banks;

- Approximately 350 specialists from respective departments (credit risk, liquidity management, financial department, corporate governance etc.) trained in new methodology;

- Approximately 100 credit officers trained in scoring methods.

- About 30 specialists from banks trained in modern methods of credit risk management and measurement. It has to include portfolio management techniques and tools as well.

- Approximately 50 top bank managers trained in new credit risk management methodology and systems, via workshop seminars (maximum 1 or 2 days workshops);

- Approximately 50 Czech trainers trained, under the selection of the Banking Association, including via fellowships/study visits to EU Member States please see means below to EU Member States.

d) Manuals covering following issues: performing banking supervision under new conditions stated by the New Basle Capital Accord and relevant EU directive, detailed review procedures to ensure that banks’ systems and controls are adequate for Internal Ratings Based Approach (including assessment of a bank’s internal rating system and standards for estimates of risk characteristics), assessment of credit risk management systems, assessing methods and models for operational risk quantification and incorporation of these methods into the overall operational risk management process, drafted, issued and used by banking supervisors.

(2) Twinning-light

a) In the light of further development of the off-site and on-site execution of banking supervision in the field of consolidated banking supervision and financial analyses of banks and banking and financial holdings an amended Manual drafted, issued and used by banking supervisors.

b) Czech National Bank’s Banking Supervisors trained in issues covered by twinning-light.

3.4 Activities

(1) Technical Assistance:

Services will be provided via Service Contract providing:

a) development of a Study analysing Czech market from the point of appropriate internal rating criteria and other impact of the Basle II. Rules including an Analysis of convenient rating or scoring tools and an Analysis of Czech SME’s market enabling delivery of useful training for scoring methods and Final recommendations focusing on Internal rating criteria and successful implementation of the Basle II (approx. 14 man-months of experts’ work)

b) development of General scoring methodology, which could be adopted by individual banks (approx. 14 man-months of experts’ work);

c) development / delivery of training programmes including seminars and workshops to be organized in the CR and the training-of-trainers programme including seminars to be organised in the CR and study visits/consultations in commercial banks from EU-Member states to be identified (the all personal costs associated with study visits/consultations developed under TA will financed by the benfiaciary commercial banks (see Article 5)o (approx. 50 man-months of experts’ work);
d) assistance to the CNB in the development of manuals covering following issues: performing banking supervision under new conditions stated by the New Basle Capital Accord and relevant EU directive, development of detailed review procedures to ensure that banks’ systems and controls are adequate for Internal Ratings Based Approach (including assessment of a bank’s internal rating system and standards for estimates of risk characteristics), assessment of credit risk management systems, assessing methods and models for operational risk quantification and incorporation of these methods into the overall operational risk management process (approx. 6 man-months of expert’s work);

e) development of training of CNB’s banking supervisors in the form of interships (in EU Member-state commercial banks applying internal rating system, assessment of credit risk management systems, assessing methods and models for operational risk quantification and incorporation of these methods into the overall operational risk management process (the all personal costs associated with internships developed under TA will financed by the CNB).

The experts will work in close co-operation with the Czech National Bank and the Czech Banking Association, although sizeable training needs analysis, delivery and expert consultations will actually be carried-out on-site in support of the commercial banking sector (in particular Credit Risk Management and In-house Training Departments).

As regards project beneficiaries commercial banks - members of the Czech Banking Association will participate in the Project. The only prerequisite for a bank to become a member of the Czech Banking Association is to be licensed as a banking business under the Act on Banks. There will be only one selection criterion for participation in the project – to be a member of Czech Banking Association.

In view of commercial realities of the main project beneficiaries, co-financing will be provided to support the Project’s goals, provided from the commercial banks themselves (this will represent a ‘head fee’ per trainee). The Co-financing Specification see Article 5.

In analyzing and proposing appropriate Internal Rating criteria experts should pay particular attention to the basic distinction between two types of credit risk management methodology:

- Credit risk management methodology used for retail banking;
- Credit risk management methodology used for wholesale banking.

Training materials shall content final version (if it is ready) New Basle Capital Accord including explanatory note and case studies.

Training will be provided at four levels of specialists in banks involved in applying new methodology:

- top management (approximately 50 people): training will primarily be delivered in the form of workshops, aimed at introducing key techniques and principles, with the aim to ensure support of the management to utilization of revised methodology;
- specialists from respective departments touching New Basle Capital Accord (approximately 350 people) including the Czech National Bank: training will primarily take the form of practical seminars, including microeconomics, qualitative and quantitative methods, wide use of case-work and the practical application of the revised methods to relevant cases.
- credit officers (approximately 100 people): training will primarily take the form of practical seminars on scoring methods.
- credit risk specialists from banks (approximately 30 people): training will primarily take the form of practical seminars on modern methods of credit risk management and measurement. It has to include portfolio management techniques and tools as well.
- the training of trainers will be included to ensure the continuation of systematic training in this field. Trainers will be selected (with a view to ensuring a regional coverage) by the Czech Banking Association for further training-of-trainers, allowing such trainers to continue the project’s roll-out. Training will also take the form of study visits/consultations in the EU-Member States with commercial banks applying similar methodology. It is assumed that approximately 50 trainers will be selected for additional training (these will be selected from the Credit Risk Methodology Specialists).

(2) **Twinning-light:**

Assistance will be provided via **one twinning-light contract** providing:

- short-term experts from a EU-Member State Banking Supervision Authority assisting in further development of the off-site and on-site execution of banking supervision in the field of consolidated banking
supervision and financial analyses of banks and banking and financial (approx. 6 man-months of expert’s work);

- short-term experts from an EU-Member State Banking Supervision Authority providing the training of banking supervisors in applying new rules set out in the elaborated manuals. Training will also take the form of study visits/consultations in the EU-Member States with banking supervisory authorities applying similar methodology.

3.5 Lessons learned
N/A.

4. Institutional Framework

The Project (except for twinning-light activities) shall be implemented under the authority of the Czech Banking Association and Working Group of the Steering Committee for the Implementation NBCA in the Czech Republic consisting of representatives of the CNB, Czech Banking Association and Chamber of Auditors (hereinafter referred to as “Working group”) and will be managed by the Steering Committee consisting of members the Working Group, representatives of European Commission, Czech National Bank (CNB) Phare Unit and the Banking Institute-College of Banking.

Twinning-light activity shall be implemented under the authority of the Czech National Bank and will be managed by the Steering Committees consisting of representatives of the CNB and experts of the EU-member Administrations delivering the assistance and CNB Phare Unit.

The Programme Officer at the CNB shall be responsible for the preparation, technical control and implementation of the project.

5. Detailed Budget (mil. €)

<table>
<thead>
<tr>
<th>Project Components</th>
<th>Phare Support</th>
<th>*National Cofinancing</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Investment</td>
<td>Institution Building</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Support</td>
<td>(=I+IB)</td>
<td></td>
</tr>
<tr>
<td>Technical Assistance</td>
<td>1.5</td>
<td>1.5</td>
<td>0.35</td>
</tr>
<tr>
<td>Twinning-light</td>
<td>0.15</td>
<td>0.15</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1.65</strong></td>
<td><strong>1.65</strong></td>
<td><strong>0.35</strong></td>
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</table>

*Beneficiary commercial banks will cover the following project costs in the total amount of 0.35M €:

- logistic expenses (simultaneous interpretation, translation of training documents, rooms, etc.) of about 3,000 training man-days (approx. 80 €/a training man-day) in amount of 0.25 M€;

- all personal costs of study visits (in the connection with TA activities of the project) to the selected commercial banks in the EU - the total amount of 0.1 M€.

There will be parallel co-financing

6. Implementation Arrangements

6.1 Implementing Agency

Responsibility for the administration related to the procedural aspects of procurement, contracting and accountancy will rest upon the CFCU.

Responsibility for the administration related to the preparation, technical control and implementation will rest with the Project Implementation Unit at the Czech National Bank.

The Contact Person is Mr. Jan Málek, Phare Senior Programme Officer, Czech National Bank, Na Prikope 28, 115 03 Prague 1, phone: +420 22441 4459, fax: +420 22441 3448, E-mail: jan.malek@cnb.cz.

6.2 Twinning-light

Responsibility for the administration related to the procedural aspects of procurement, contracting and accountancy will rest upon the CFCU.

Beneficiary institution will be the Czech National Bank, Banking Regulation Department. The contact person is Mrs. Vera Mašindová, Executive Director of Banking Regulation Department, Czech National Bank, Na Prikope 28, 115 03 Prague 1, phone: +420 22441 4417, fax: +420 22441 2686, E-mail: vera.masindova@cnb.cz.
Responsibility for the administration related to the preparation, technical control and implementation will rest with the Project Implementation Unit at the Czech National Bank. The Contact Person is Mr. Jan Málek, Phare Senior Programme Officer, Czech National Bank, Na Prikope 28, 115 03 Prague 1, phone: +420 22441 4459, fax: +420 22441 3448, E-mail: jan.malek@cnb.cz.

6.3 Non-standard aspects
N/A.

6.4 Contracts
(1) one service contract – 1,5 M €
(2) one twinning-light contract – 0,15 M €.

7. Implementation Schedule

7.1 Start of tendering/call for proposals
Technical Assistance Contract: 2Q/03
Twinning-light Contract 2Q/03

7.2 Start of project activity
Technical Assistance Contract: 1Q/04
Twinning-light Contract 3Q/03

7.3 Project Completion
Technical Assistance Contract: 1Q/05
Twinning-light Contract 1Q/04

8. Equal Opportunity

Equal opportunity principles and practices in ensuring equitable gender participation in the Project will be guaranteed.

9. Environment
N/A.

10. Rates of Return
N/A.

11. Investment Criteria
N/A.

12. Conditionality and Sequencing

No conditionality is foreseen, as the project is in line with the National Programme for Accession and the Action Plan for Financial Services.

ANNEXES TO PROJECT FICHE

1. Logical planning matrix
2. Detailed implementation chart
3. Contracting and disbursement schedule
### LOGFRAMME PLANNING MATRIX

<table>
<thead>
<tr>
<th>Overall Objective</th>
<th>Objectively verifiable indicators</th>
<th>Sources of Verification</th>
<th>Assumptions</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Functioning market economy and the capacity to cope with competitive pressure and market force</td>
<td>- Acknowledgement by the European Commission</td>
<td>- EC Monitoring Report</td>
<td>- World / EU economic growth remains positive for each of the five years following the completion of the project;</td>
</tr>
<tr>
<td>- The ability to take on obligations of membership including adherence of political, economic and monetary union.</td>
<td></td>
<td>- National &amp; CNB statistics</td>
<td></td>
</tr>
<tr>
<td>Project purpose</td>
<td>Objectively verifiable indicators</td>
<td>Sources of Verification</td>
<td>Assumptions</td>
</tr>
<tr>
<td>- To increase the skills level within the commercial banking sector, in order to assess and manage credit risk in compliance with Basle II. Recommendation, thereby contributing to the reduction/prevention of bad loans;</td>
<td>- Volume of lending by banks established in the Czech Republic is greater in real terms in each of the five years following the completion of the project than in 2003</td>
<td>- Analytic and comparative studies</td>
<td>- Implementati on of recommendations will depend on decisions to be taken by top management bodies of the individual banks;</td>
</tr>
<tr>
<td>- To assist in implementation of scoring methods and methods for credit risk measurement.</td>
<td>- Overall proportion of classified loans held by banks established in the Czech Republic shows a degressive tendency within five years after the completion of the project</td>
<td>- Reports from participating banks</td>
<td>- Measure of the objectivity of the reports</td>
</tr>
<tr>
<td>- To advise in the process of setting appropriate internal rules in the banks and matching these rules with measures of CNB.</td>
<td>- Appointing of proposed Internal Rating criteria by CNB</td>
<td>- Annual Reports of participating banks</td>
<td></td>
</tr>
<tr>
<td>- To advise the CNB in the process of implementation of advanced methods of risk management including the New Basle Capital Accord within further development of the banking supervision area.</td>
<td>- Implementation proposed Internal Rating criteria by the participating banks</td>
<td>- A&amp;E reports from implementing units</td>
<td></td>
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<tr>
<td>- To advise the CNB in further development of the off-site and on-site execution of banking supervision in the field of consolidated banking supervision and financial analyses of banks and banking and financial holdings (twinning-light activity).</td>
<td>- Implementation of scoring tools for SMEs.</td>
<td>- New Basle Capital Accord</td>
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### Results

<table>
<thead>
<tr>
<th>Technical Assistance:</th>
<th>Objectively verifiable indicators</th>
<th>Sources of Verification</th>
<th>Assumptions</th>
</tr>
</thead>
<tbody>
<tr>
<td>- Overall study (document defining / recommending appropriate criteria for internal rating systems in compliance with Basle II) to be drafted, issued and implemented by the participating banks (after negotiated / recommendations approved).</td>
<td>- Trainees trained (approx. 530 people divided into four levels as indicated hereabove)</td>
<td>- Monthly progress reports from the Czech National Bank Senior Programme Officer;</td>
<td>- Implementati on of recommendations will depend on decisions to be taken by top management bodies of the individual banks;</td>
</tr>
<tr>
<td>- General scoring methodology, which could be adopted by individual banks, to be defined and issued.</td>
<td>- Trainers (approx. 50 people) trained and Czech Banking Association develops systems to reutilize</td>
<td>- Reports from consultants;</td>
<td></td>
</tr>
<tr>
<td>- Substantial number of Czech commercial banks' experts, specialists, managers and trainers fully trained in areas of implementation of the New Basle Capital Accord (NBCA) and scoring methods and portfolio management tools.</td>
<td>- Acceptance of the proposals and recommendations and their implementation, analytic and comparative studies, trained personnel (approx. 530 people)</td>
<td>- Reports issued by commercial banks</td>
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<tr>
<td>- Training of trainers organized including study visits/consultations.</td>
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</tbody>
</table>

Project title: Strengthening the Czech Banking Sector - Application of Basle II

- Project Number: CZ 2003/004-338.02.04
- Contracting Period Expires: 31/10/2005
- Disbursement Period Expires: 31/10/2006
- Total Budget: 2.00 M€
- Phare Budget: 1.65 M€
− Training programme including workshops and seminars designed and delivered in the CR.
− Manuals covering the following issues to be drafted and issued and used by banking supervisors:
  
  performing banking supervision under new conditions stated by the New Basle Capital Accord and relevant EU directive, detailed review procedures to ensure that banks’ systems and controls are adequate for Internal Ratings Based Approach, including assessment of a bank’s internal rating system and standards for estimates of risk characteristics, assessment of credit risk management systems, assessing methods and models for operational risk quantification and incorporation of these methods into the overall operational risk management process;

Twinning-light:
− Amended manual on the performance of banking supervision on consolidated basis, drafted, issued and used by the banking supervisors.
− The CNB banking supervisors trained in specific issues covered by TWL.

Activities:

<table>
<thead>
<tr>
<th>Technical Assistance activities:</th>
<th>Means:</th>
</tr>
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<tbody>
<tr>
<td>Elaboration of Overall Study and the document recommending appropriate criteria for internal rating systems in compliance with Basle II, as well as other references for successful implementation of the New Basle Capital Accord,</td>
<td>1. Service contract at the amount of 1,5 MEUR:</td>
</tr>
<tr>
<td>Development of General scoring methodology, which could be adopted by individual banks</td>
<td>Services to be provided by specialist firm(s) in the field of credit risk management via a single advisory team:</td>
</tr>
<tr>
<td>Training of bank staff in the new methodology based on the Basle II (as indicated under results);</td>
<td>- developing an overall study/ analysing document and general scoring methodology (28 man-months),</td>
</tr>
<tr>
<td>Training of trainers as indicated under results through Specialized Training Programme for Trainers,</td>
<td>- developing and delivering a training programme -seminars in the CR, consultations and training of trainers (50 man-months),</td>
</tr>
<tr>
<td>Open seminars organized in the Banking institute -College of Banking,</td>
<td>- assisting the CNB in developing an amended manuals ( 6 man.months),</td>
</tr>
<tr>
<td>In-house seminars for experts as indicated above organized in participating banks by a contractor,</td>
<td>In total of 84 man-months..man.months</td>
</tr>
<tr>
<td>Identification of suitable commercial banks from EU Member-states applying the methodologies as indicated under results for study visits/consultations and defining the programme of the study visits (issues and timing) with the chosen EU banks (all personal costs associated with study visits/consultations to the EU partner institutions/banks will be financed /covered by beneficiary commercial banks themselves),</td>
<td>2. One twinning light contract at the amount of 0.15 MEUR:</td>
</tr>
<tr>
<td>assistance to the CNB in the development of manuals covering following issues: performing banking supervision under new conditions stated by the New Basle Capital Accord and relevant EU directive, development of detailed review procedures to ensure that banks’ systems and controls are adequate for Internal Ratings Based Approach (including assessment of a bank’s internal rating system and standards for estimates of risk characteristics), assessment of credit risk management systems, assessing methods and models for operational risk quantification and incorporation of these methods into the overall operational risk management process (approx. 6</td>
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</table>

Assumptions:

produced by those involved in the implementation of the project

Appendix 1: Means:

1. Service contract at the amount of 1.5 MEUR:
Services to be provided by specialist firm(s) in the field of credit risk management via a single advisory team:
- developing an overall study/ analysing document and general scoring methodology (28 man-months),
- developing and delivering a training programme -seminars in the CR, consultations and training of trainers (50 man-months),
- assisting the CNB in developing an amended manuals ( 6 man.months),

In total of 84 man-months...man.months

2. One twinning light contract at the amount of 0.15 MEUR:
Assistance to be provided by STEs from EU-Member State Banking Supervision Authority in the form of:
- manual,
- training seminars,
man-months of expert’s work).

- Development of training of CNB’s banking supervisors in the form of interships in EU Member-state commercial banks applying internal rating system, assessment of credit risk management systems, assessing methods and models for operational risk quantification and incorporation of these methods into the overall operational risk management process.

### Twinning-light activities:

- Production of manual covering the performance of banking supervision on consolidated basis to be used by banking supervisors.
- Training of banking supervisors as indicated under results.

### Preconditions

- Beneficiaries of this project are to be the Czech National Bank and private banks.
- All major banks agree to participate, provide necessary co-financing and nominate trainers to be trained and this will be confirmed in writing.
- The Banking Institute-College of Banking shall provide the contractor with premises, organizational and logistic support for Open seminars. The costs associated with realization of those duties will be covered in the form of “head-fee” per trainee paid by beneficiary commercial banks. This will be confirmed in writing.
### Detailed Implementation Chart

**Strengthening the Czech Banking Sector - Application of Basle II**

<table>
<thead>
<tr>
<th>Action</th>
<th>Year</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
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<tr>
<td><strong>Technical Assistance</strong></td>
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<tr>
<td>- Tender Launch (May 2003)</td>
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<td>- Contract Signature</td>
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<td>- Project activities</td>
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<td>commences</td>
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<tr>
<td>• Development of the overall study on implementation of Basle II. recommendations</td>
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<tr>
<td>• Development of training programmes</td>
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<tr>
<td>• Delivery of training</td>
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<tr>
<td>• Staff training/fellowships</td>
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<tr>
<td><strong>Twinning-light Activity</strong></td>
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<td>- Selection of a Member State</td>
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<tr>
<td>- Implementation of Activity</td>
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# CONTRACTING AND DISBURSEMENT SCHEDULE

## Cumulative Quarterly Contracting Schedule (mil. €)

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<th>Project</th>
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<th>3Q/02</th>
<th>4Q/02</th>
<th>1Q/03</th>
<th>2Q/03</th>
<th>3Q/03</th>
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## Cumulative Quarterly Disbursement Schedule (mil. €)

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