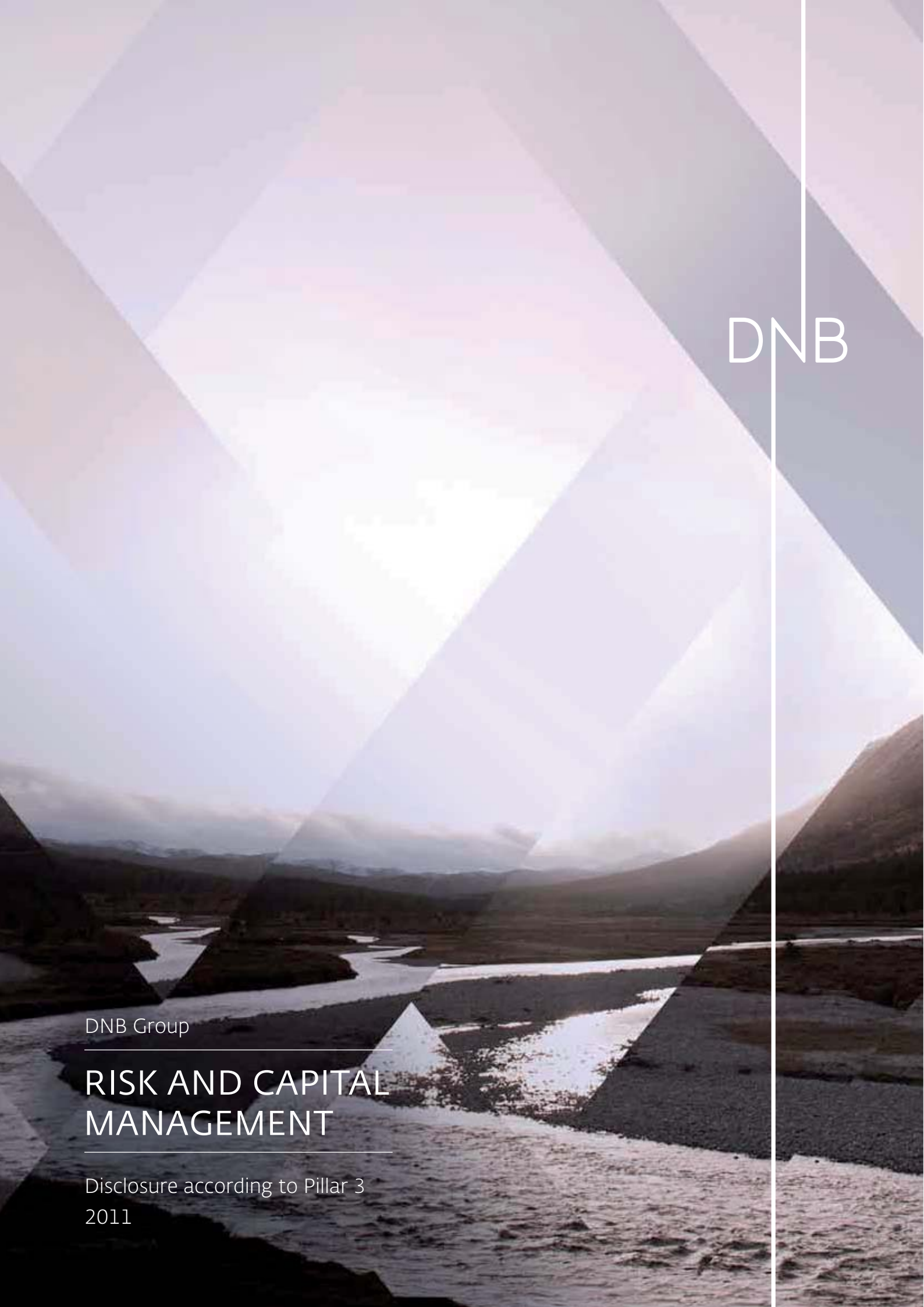


DNB

DNB Group

RISK AND CAPITAL MANAGEMENT

Disclosure according to Pillar 3

2011

INDEX

INTRODUCTION

New capital adequacy requirements for financial institutions, Basel II, entered into force on 1 January 2007. The capital adequacy requirements include specific requirements for the disclosure of financial information (Pillar 3), which will make it easier for various market players to assess the institutions' risk level, risk management, control and capitalisation.

This document contains information about risk management, risk measurement and capital adequacy in accordance with the requirements in Pillar 3 of the capital adequacy regulations. The document is updated annually, except for information on capital adequacy and minimum primary capital requirements, which is updated quarterly in an appendix. Other relevant information can also be found in the appendix. Pillar 3 is not subject to audit.

The methods used to calculate capital requirements for credit risk, market risk and operational risk (Pillar 1) are described in the document. In addition, it includes information about the bank's internal risk measurement, reporting and management (Pillar 2). Methods for calculating economic capital and the use thereof in the management of the bank are also described. Calculations of economic capital include a quantification of risk categories other than those covered by the capital adequacy requirements.

IMPORTANT DEVELOPMENT TRENDS

2001 was characterised by market instability, and the financial market turmoil increased further towards the end of the year. The sovereign debt crisis in the Eurozone resulted in rising yields on a number of European government bonds and caused serious problems in the European banking system. Uncertainty regarding future economic developments gave a high level of volatility and rising risk premiums in the capital markets towards the end of 2011. Long-term government bond yields in the most creditworthy countries, such as Norway, fell to record-low levels.

Norwegian economic developments were subdued by the financial market turmoil and uncertain prospects for the global economy. A strong Norwegian krone rate and relatively high wage growth present increasing challenges for Norwegian companies exposed to international competition. Consumers and companies adopted a waiting attitude, though record-high oil investment compensated for much of the decline in demand. There was strong employment growth in Norway, coupled with low unemployment. Housing prices continued to climb during the year. DNB experienced brisk credit demand in 2011, and total lending increased by 9 per cent.

Risk-weighted assets rose by NOK 83 billion, to NOK 1 112 billion, in the course of 2011. The DNB Group's common equity Tier 1 capital ratio was 9.4 per cent. DNB thus met the 9 per cent common equity Tier 1 capital requirement introduced by the EBA to restore confidence in European banks. A year earlier, the corresponding figure for the DNB Group was 9.2 per cent. According to the transitional rules for capital adequacy, risk-weighted volume cannot be less than 80 per cent of the corresponding figure calculated according to the Basel I regulations. This transitional floor applied at year-end 2011. Based on measurement according to IRBA of all credit portfolios for which the Group has applied for approval to use such measurement (see plan on page x), and without the restrictions resulting from the transitional rules, the common equity Tier 1 capital ratio would have been 10.8 per cent.

The DNB Group measures risk by calculating economic capital, called risk-adjusted capital. Net risk-adjusted capital totalled NOK 63.3 billion at year-end 2011, up NOK 4.2 billion from year-end 2010.

RISK-ADJUSTED CAPITAL PER RISK CATEGORY

Million NOK	1112	1109	1106	1012
Credit risk	50.1	51.3	46.3	45.5
Market risk	5.2	6.1	6.2	6.0
Market risk in life insurance	10.6	13.2	14.1	12.5
Insurance risk	1.8	1.9	1.9	1.8
Operational risk	8.7	8.7	8.4	7.7
Business risk	4.7	4.7	4.7	4.5
Total risk-adjusted capital before diversification	81.2	85.9	81.6	78.0
Diversification	(17.9)	(16.8)	(20.0)	(18.8)
Total risk-adjusted capital after diversification	63.3	69.1	61.6	59.1
Diversification in per cent of gross risk-adjusted capital	22.0 %	19.6 %	24.5 %	24.2 %

Risk-adjusted capital for credit increased by NOK 4.6 billion through 2011 due to rising lending volumes. There was stable, sound credit quality in the healthy portfolio, though the volume of non-performing and doubtful commitments increased somewhat towards the end of the year as small parts of certain large commitments were classified as doubtful. Persistently low rates in the tanker, container and dry bulk segments in shipping put extensive pressure on shipping companies' earnings and liquidity. DNB is active in raising new equity and restructuring debt to find solutions to reduce the bank's risk and exposure over time. DNB's total shipping portfolio is still considered to be sound.

DNB's energy portfolio showed a particularly positive trend, with strong growth and very low risk. The annual growth rate was 42 per cent, and the portfolio totalled NOK 120 billion at end-December 2011. Large new oil findings in the Norwegian sector give reason for optimism for the offshore and oil supplier sectors.

The Norwegian commercial property market showed a positive trend in 2011, with increasing sales and a moderate rise in values. Large Nordic contractors experienced a healthy order inflow, and the positive trend is expected to continue in 2012.

2011 was a challenging year for DNB Livsforsikring, with volatile stock markets and falling long-term interest rates Long-term Norwegian swap rates declined by approximately 1 percentage point during 2011 and were on a level with policyholders' guaranteed rate of return at year-end. A prolonged low interest rate level will affect DNB Livsforsikring's ability to assume risk to ensure a healthy return for policyholders.

At year-end, equities represented approximately 8 per cent of total investments, compared with just over 20 per cent a year earlier. In consequence of this, market risk in life insurance declined in 2011. Risk-adjusted capital was NOK 1.8 billion lower than a year earlier.

Over the next few years, an increase in reserves will be required to meet the anticipated increase in life expectancy. The industry is in dialogue with the authorities regarding the implementation of such an increase.

Risk-adjusted capital for market risk in operations other than life insurance also declined in consequence of a lower equity exposure towards the end of the year. There were no significant changes in market risk limits during 2011.

Mark-to-market adjustments of swap contracts entered into in connection with the Group's financing of loans, basis swaps, are not included in the measurement of risk-adjusted capital for market risk. These contracts may have significant effects on the accounts from one quarter to the next. However, as the contracts are generally held to maturity, these effects will be balanced out over time.

There was a 43 per cent increase in registered events entailing operational risk from 2010, which may reflect adaptations to and

harmonisation of the Group's routines to external regulations. The level of losses was characterised by a few, large individual events. The majority of events and the largest losses are still in the category "processing and routine errors" relating to the Group's products and services. As from the autumn of 2011, it is possible to register which processes/products the events relate to. In the longer term, this will ensure useful information to be used in risk management.

Just like other international banks, DNB has to relate to increasingly detailed rules for its operations in various countries, including US sanction regulations and anti-money laundering rules. This implies higher compliance risk, which at worst could result in the Group losing its licence to operate in the US market. Administrative costs for avoiding such rule violations are increasing and could be high.

RISK MANAGEMENT AND LIMIT STRUCTURE IN DNB

RISK MANAGEMENT AND CONTROL

The Board of Directors of DNB ASA has a clearly stated goal to maintain a low overall risk profile, which is reflected in the DNB Bank Group's aim to maintain at least an AA level rating for ordinary long-term debt. The profitability of DNB will depend on the Group's ability to identify, manage and accurately price risk arising in connection with financial services. A general description of the organisation and distribution of responsibilities with respect to risk management and internal control in DNB is given in DNB's annual report in section 10 under chapter Corporate Governance.

Organisation and authorisation structure

- *Board of Directors*. The Board of Directors of DNB ASA sets long-term targets for the Group's risk profile. The risk profile is operationalised through the risk management framework, including the establishment of authorisations. Risk-taking should take place within established limits.
- *Authorisations*. Authorisations must be in place for the extension of credit and for position and trading limits in all critical financial areas. All authorisations are personal. Authorisations and group limits are determined by the Board of Directors and can be delegated in the organisation, though any further delegation requires approval by an immediate superior.
- *Annual review of limits*. Risk limits are reviewed at least annually in connection with budget and planning processes.
- *Independent risk management functions*. Risk management functions and the development of risk management tools are undertaken by units that are independent of operations in the individual business areas.

Monitoring and use

- *Accountability*. All executives are responsible for risk within their own area of responsibility and must consequently be fully updated on the risk situation at all times.
- *Risk reporting*. Risk reporting in the Group ensures that all executives have the necessary information about current risk levels and future developments. To ensure high-quality, independent risk reports, responsibility for reporting is assigned to units that are independent of the operative units.
- *Capital assessment*. A summary and analysis of the Group's capital and risk situation is presented in a special risk report to the Board of Directors in DNB ASA.
- *Use of risk information*. Risk is an integral part of the management and monitoring of business areas. Return on risk-adjusted capital is reflected in product pricing, profit calculations and in monitoring performance in the business areas.

Relevant risk measures

- *A common risk measure for the Group*. The Group's risk is measured in the form of risk-adjusted capital, calculated for main risk categories and for all of the Group's business areas.
- *Supplementary risk measure*. In addition, risk is followed up through supplementary risk measures adapted to operations in the various business areas, for example monitoring of positions relative to limits, key figures and portfolio risk targets.

Risk categories

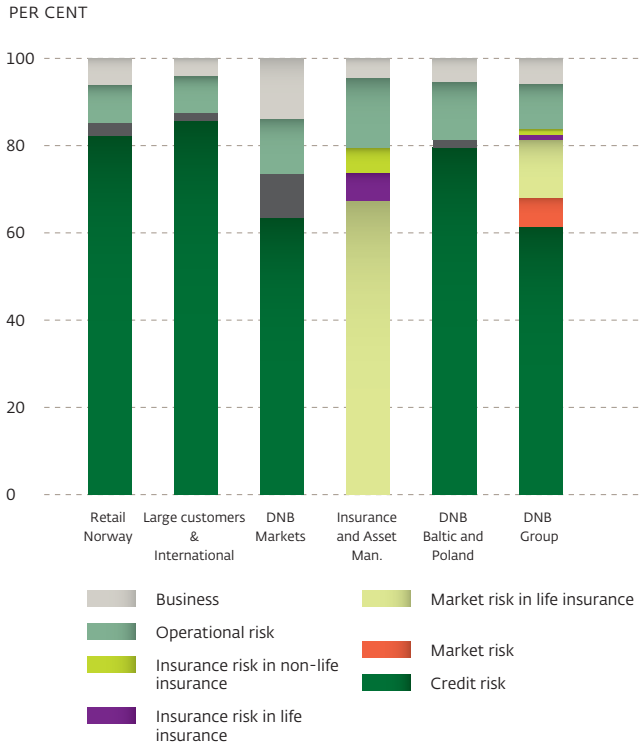
For risk management purposes, DNB distinguishes between the following risk categories:

- *Credit risk* is the risk of losses due to failure on the part of the Group's counterparties or customers to meet their payment obligations towards the DNB Group. Credit risk refers to all claims against counterparties or customers, including credit risk in trading operations, country risk and settlement risk.
- *Market risk* is the risk of losses or reduced future income due to fluctuations in market prices or exchange rates. The risk arises as a consequence of the bank's unhedged transactions and exposure in the foreign exchange, interest rate, commodity and equity markets.
- *Market risk* in life insurance is the risk that the return on financial assets will not be sufficient to meet the obligations specified in insurance policies.
- *Liquidity risk* is the risk that the Group will be unable to meet its obligations as they fall due, and risk that the Group will be unable to meet its liquidity obligations without a substantial rise in appurtenant costs. In a broader perspective, liquidity risk also includes the risk that the Group will be unable to finance increases in assets as its funding requirements rise.
- *Insurance risk* comprises risk in life insurance and risk in non-life insurance. Within life insurance, risk is related to changes in future insurance obligations due to changes in life expectancy and disability rates. Within non-life insurance, insurance risk comprises premium risk, reserve risk and natural disaster risk.
- *Operational risk* is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.
- *Business risk* is the risk of losses due to changes in external factors such as the market situation or government regulations. This risk category also includes reputational risk.
- *Basis risk* is the risk that the change in value of a hedge does not fully match the change in value of the underlying position it hedges. The reasons for the mismatch in value (basis risk) can be different start dates, maturity dates, delivery locations or quality, advantages/disadvantages of maintaining a holding of the underlying instrument, credit risk and supply and demand effects.

RISK MEASUREMENT AND RISK-ADJUSTED CAPITAL

The internal calculations of profitability and capital adequacy are based on the calculations of economic capital, which in DNB is

RISK-ADJUSTED CAPITAL PER BUSINESS AREA, 31 DECEMBER 2011



referred to as risk-adjusted capital. Risk-adjusted capital measures the risk of losses stemming from the different business activities, and allows for aggregation and comparison across risk categories. The quantification of risk-adjusted capital is based on statistical probability calculations for the various risk categories on the basis of historical data. In cases where the historical data is of limited quantity or quality, expert assessments has been applied. As it is impossible to guard against all potential losses, DNB has stipulated that risk-adjusted capital should cover 99.97 per cent of potential losses within a one-year horizon. This level is in accordance with an AA level rating target for ordinary long-term debt.

DNB quantifies risk-adjusted capital for the following risk categories: credit risk, market risk, market risk in life insurance, insurance risk, operational risk and business risk. The calculations are carried out by a simulation tool, which is referred to as the Total risk model. A significant diversification or portfolio effect arises when the various risks are considered together, as it is unlikely that all losses will occur at the same time. An economic downturn will normally have a negative effect on most areas, but there will be a diversification effect, as not all areas will be hit equally hard. The diversification effect between risk categories and business areas implies that the Group's risk-adjusted capital will be much lower than if the business areas had been independent companies.

There are increasing similarities between the framework for risk-adjusted capital and the capital adequacy regulations for the portfolios that are reported according to the IRB approach (see table page 10). The main differences are due to the calculations of diversification effects between portfolios in the internal model, and the use of a higher confidence level.

Risk-adjusted capital and average losses over a normal business cycle are elements in calculations of risk-adjusted return, which is a key financial management parameter in the internal management of the DNB Group. The calculations are included in the financial planning for the business areas and are reported each quarter. Risk-adjusted return is a measurement parameter in the pricing model and is reported monthly in automated management systems.

RETURN ON CAPITAL, RARORAC AND RORAC

Return relative to tied-up capital is an important key figure at all levels of the Group, used in both profitability measurement and in ongoing monitoring and planning for the business areas and at group level.

In internal reporting and management, return on capital is based on DNB's model for calculating risk-adjusted capital. This enables comparisons between various units in the Group, as profits are measured relative to the assessed risk of operations.

Return on capital is measures relative to both recorded and normalised profits.

RORAC, **R**eturn **O**n **R**isk-**A**djusted **C**apital is defined as recorded profits after tax relative to risk-adjusted capital for operations and is used to measure historical profits and assessing plans in a short-term perspective.

RARORAC, **R**isk-**A**djusted **R**eturn **O**n **R**isk-**A**djusted **C**apital is defined as normalised, risk-adjusted profits after tax relative to risk-adjusted capital. When normalising profits, recorded write-downs are replaced by normalised losses calculated over a business cycle. RARORAC is adjusted for random fluctuations in write-downs and is used to assess profits achieved and plans in a longer-term perspective.

RORAC and RARORAC are used in parallel to measure a unit's return. By normalising profits for fluctuations in loan losses, RARORAC gives a better indication of the level of returns in a longer-term perspective, while RORAC shows the realised return at the moment and expected returns in the near future. Quantitative information can be found in "Supplementary information for investors and analysts".

STRESS TESTING IN DNB

Stress testing is an important management tool in DNB for assessing the risk of losses on credit exposures in connection with severe changes in macroeconomic conditions. Stress tests of DNB in its entirety may also illustrate corresponding changes in capital ratios. The total risk model measures risk-adjusted capital within DNB by calculating overall risk for all risk categories.

DNB's credit portfolios are stress tested annually in order to

identify factors that may affect developments in credit risk and capital adequacy. The DNB Group uses stress tests in the ICAAP and the capital planning process in order to determine how severe changes in the macroenvironment will affect the need for capital. The scope of the changes will depend on both the macroeconomic scenario and the quality of the portfolio. Stress testing of specific risk element in individual sub-portfolios is not mandatory, but may be performed in conjunction with industry analyses.

In 2011, DNB took part in stress tests initiated by the European Banking Authority (EBA) and the Norwegian supervisory authorities. The DNB Group had an adequate level of capital in these scenarios, although DNB Bank had to receive a capital injection from the holding company to reach the new capital requirements set by the EBA.

The EBA has issued recommendations (GL 32) which DNB uses as guidance for how the stress tests should be implemented in the organisation. DNB will start adapting to the requirements regarding reverse stress testing during 2012.

Internal stress test scenarios

The bank's main stress scenario is presented in the financial plan each year, which is approved by the Board of Directors. The scenario consists of a set of macroeconomic variables that are projected for the next three years. These variables are translated into model-specific variables in order to conduct stress tests on the different credit portfolios. In these models the probability of default (PD) for each customer is stressed, and accordingly the bank will suffer higher loan losses and have a greater need for capital than in the baseline scenario. Furthermore, the loss given default (LGD) and exposure at default (EAD) models are subject to the same macroeconomic shocks.

On the basis of the results from the stress testing of the models, the DNB Group calculates its capital requirement under this specific scenario. The PD models are not fully cyclical, which means that the PD values will not be fully consistent with the observed default frequency over a business cycle. In addition, risk-weighted volume will be less cyclical than the PD value included in the calculation. Therefore, the transition from IRB figures to projections of actual levels of new defaults and losses must take into consideration the IRB system's calibration level and cyclicality, in addition to the current position in the economic cycle.

DNB also uses custom-made scenarios when stress testing different subsidiaries and portfolios. These might consist of fewer macroeconomic variables and/or more direct changes in the different risk parameters in the model, thus reflecting the needs of the different business areas.

Requirements for stress testing by the authorities

The regulatory stress tests build on specific macroeconomic scenarios applied by the banks on their portfolio models. The EBA conducted a stress test of European banks during the spring/summer of 2011. The test covered 91 banks representing more than 65 per cent of banks' assets within the EEA. The test aimed to assess the robustness of the European banking system in the event of a severe shock in the economy, including the financial strength of the individual bank in such a scenario.

Originally, the assumptions of the test and the methodology used were established to assess banks' capital adequacy against a requirement of a 5 per cent common equity Tier 1 (CET1) capital ratio. The stress test was based on an assumption of a static balance as of December 2010 and covered a projection period of two years (2011 to 2012). The test did not take into account future adjustments in business strategies in such a crisis situation. Therefore, the stress test is not a forecast of how the profits of DNB Bank will develop in such a scenario.

The stress test showed that DNB Bank will achieve significant profits even under the adverse scenario, and combined with the assumption of static balance this will contribute to an increase in the CET1 capital ratio. The ratio increased to 9.0 per cent at the end of 2012 under the adverse scenario, compared with 8.3 per cent at the end of 2010.

In the autumn of 2011, there was an update of the stress test, where sovereign debt exposures in the trading and balance books were adjusted to the current market prices. DNB Bank had no exposure to government bonds whose values had to be written down. The CET1 capital ratio requirement was also increased to a minimum of 9 per cent. By the third quarter of 2011, DNB Bank had a CET1 capital ratio of 7.8 per cent. In line with the DNB Group's capitalisation policy, a substantial liquidity reserve is retained in DNB ASA (the holding company) for the capitalisation of DNB Bank and other subsidiaries. The DNB Group was able to meet the 9 per cent requirement with immediate effect by redistributing the available internal capital resources in the fourth quarter of 2011.

DNB Bank passed the EU-wide stress test with a good margin. The solid performance is due to a robust Norwegian economy, a strong capital position, a low risk profile and no exposure to debt-ridden sovereigns in the Eurozone.

Other stress tests of market and insurance risk

Two stress scenarios have been developed for testing market and insurance risk (sudden changes in share prices, interest rates and property prices). A mild scenario describes a possible negative market performance for the year. A strict scenario describes a low probability, although not improbable, outcome. The stress test of market risk uses the stress parameters in the Norwegian FSA's stress test 2 and is performed quarterly.

CAPITAL

CAPITAL MANAGEMENT

Group policy for risk management
DNB's group policy for risk management should serve as a guide for DNB's overall risk management and describes the ambitions for, attitudes to and work on risk in the DNB Group.

According to the group policy for risk management, DNB aims to maintain a low risk profile and will only assume risk which is comprehensible and possible to follow up, and which will not harm its reputation. The Group's corporate culture shall be characterised by transparent methods and processes which promote sound risk management. All managers are responsible for risk within their own area of responsibility. Responsibility for entering into agreements which entail risk for the Group will be delegated to the organisation through personal authorisations and limits. Risk management functions and the development of risk management tools shall be organised in units which are independent of the units which engage in business operations.

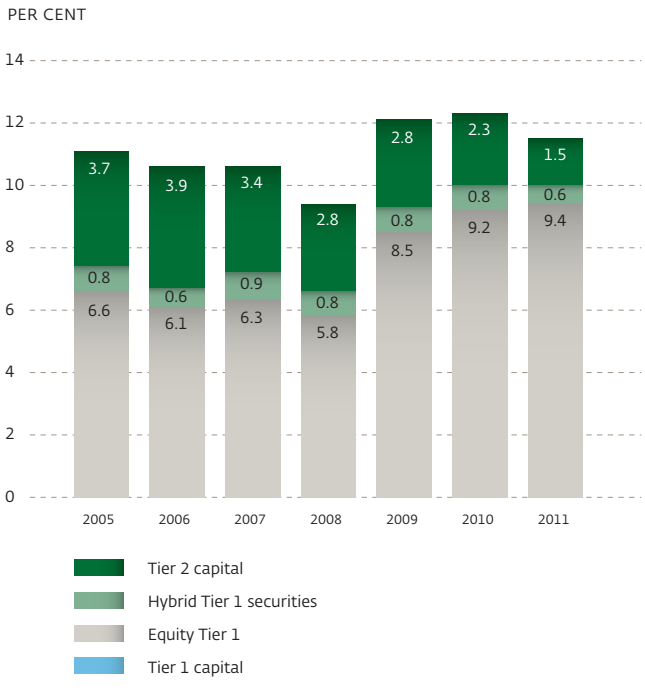
Assessment of risk profile and capital requirements
Pursuant to the Norwegian Public Limited Liability Companies Act, all companies must at all times have an equity which is sound, based on the extent of the company's activities and the risk they involve. The capital adequacy regulations set a minimum primary capital requirement, encompassing credit risk, market risk and operational risk. In addition, financial institutions are required to complete an Internal Capital Adequacy Assessment Process, ICAAP. Finanstilsynet (the Financial Supervisory Authority of Norway) has established guidelines for what such a process should include.

The capital adequacy assessment process should encompass risks which are not included in the calculation of the minimum requirement. In addition, it should reflect the fact that risk quantification and capital requirements are based on methods and data which entail uncertainty. Capital requirement assessments should be forward-looking and take account of business plans, growth and access to capital markets. The capital base should be adequate to get through a recession characterised by negative results and difficulties in obtaining new capital. The ICAAP is reported to Finanstilsynet. As part of the capital adequacy assessment process.

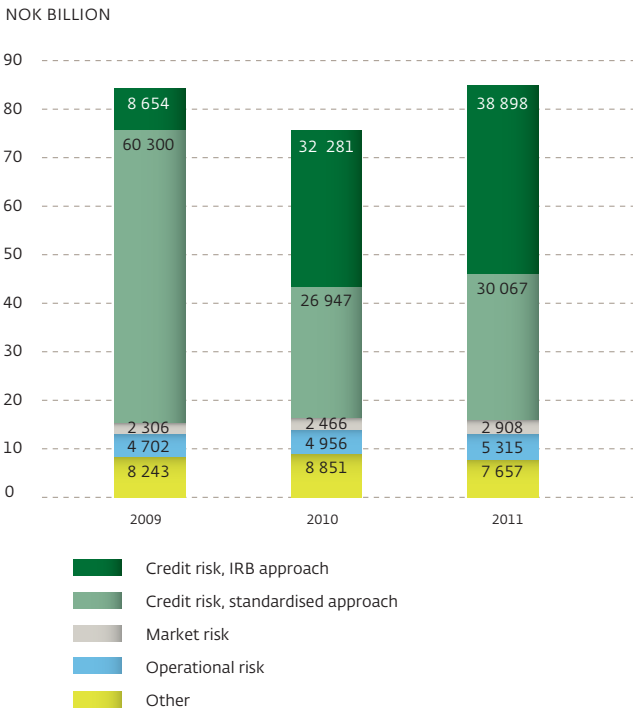
In 2011, the Board of Directors of DNB ASA approved a capitalisation policy which was adapted to the anticipated new requirements resulting from the Basel III proposals. The capitalisation policy is aimed at ensuring that DNB's equity is adequate to secure effective and optimal use of equity relative to the scope and risk profi le of operations. The capitalisation policy shall balance the need for a competitive return on equity with the need for stability required by the supervisory authorities, bondholders, market players and other takeholders, including rating companies.

The capitalisation policy sets out a target of minimum 8.5 per

CAPITAL ADEQUACY

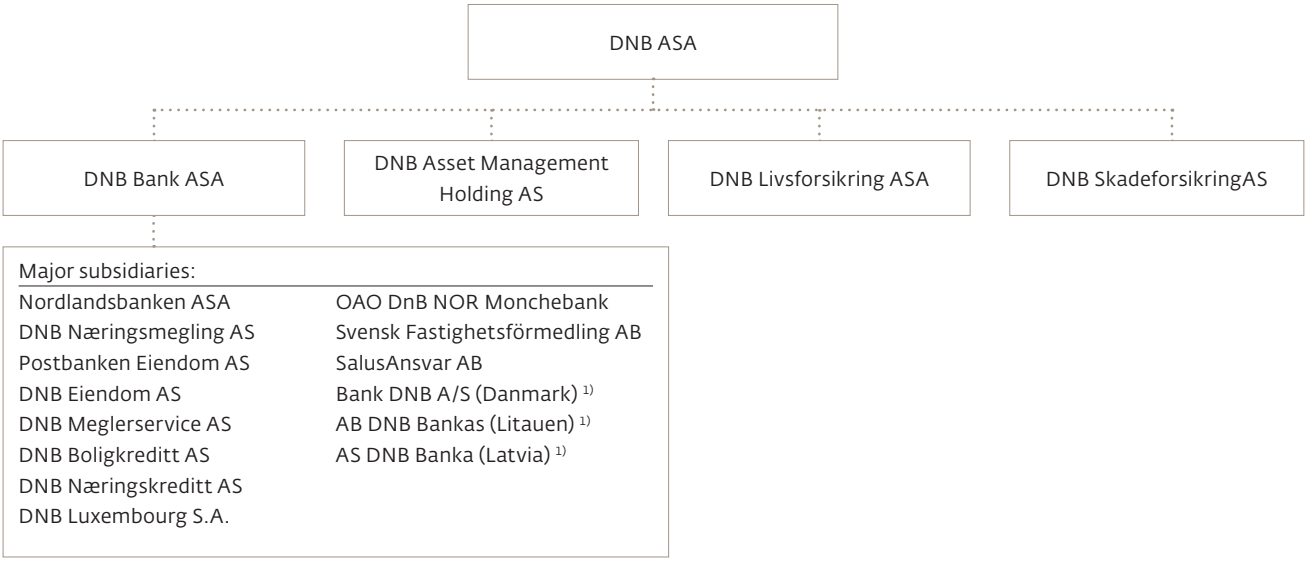


CAPITAL REQUIREMENT – 8 PER CENT OF RISK-WEIGHTED VOLUME



1) Internal Capital Adequacy Assessment Process, ICAAP.

DNB GROUP – LEGAL STRUCTURE AT END DECEMBER 2011



1) Operations in DNB Baltics and Poland will be integrated in DNB and are thus under restructuring. As part of the integration, ownership of the banks in Lithuania and Latvia was transferred to DNB at end-June 2011. Bank DNB A/S in Denmark still owns the operations in Poland and Estonia, but the ownership will be transferred as soon as possible in 2012. Following the restructuring, Bank DNB A/S in Denmark will only engage in investment activity.

cent common equity Tier 1 capital upon full implementation of the IRB system, Internal Ratings Based. As risk-weighted volume is affected by cyclical fluctuations, this means that the common equity Tier 1 capital ratio must be well over 8 per cent in good economic times and minimum 8.5 per cent during an economic downturn. Thus, the common equity Tier 1 capital ratio should normally be approximately 10 per cent.

In consequence of feedback from Finanstilsynet and more stringent future international regulatory requirements regarding the size and composition of financial institutions' primary capital, DNB will review its capitalisation policy during 2012, and the level of ambition will be raised.

As part of the capital adequacy assessment process in DNB, the Group's risk and capital situation is assessed and summarised in a separate risk report to the Board of Directors of DNB ASA every third month. The Group's capitalisation target is an important element in the budget and strategy process. Risk is quantified by calculating risk-adjusted capital. Capital required will generally exceed the measured risk. Based on the new regulatory requirements for the level of common equity Tier 1 capital, the Group's actual equity will be higher than risk-adjusted capital. The Group will take this into account in the return targets set for risk-adjusted capital.

A process for assessing the risk profiles and capital requirements of the parent company DNB ASA and all major subsidiaries is completed each year, based on risk-adjusted capital, regulatory requirements and qualitative assessments.

Stress tests for credit and market risk are other important references. The Boards of Directors of the subsidiaries make independent assessments of capital levels and future capital requirements based on guidelines in the Group's capitalisation policy. The results are verified with the specialist units in the respective subsidiaries and in DNB ASA. The process and the result thereof are documented in writing in an ICAAP report. DNB's ICAAP report was sent to Finanstilsynet in May 2011.

CAPITAL ADEQUACY

The consolidated accounts for DNB ASA ("DNB") include DNB Bank ASA, DNB Livsforsikring ASA, DNB Asset Management Holding AS and DNB Skadeforsikring AS, all including subsidiaries and associated companies. All subsidiaries are wholly owned.

DNB has prepared consolidated accounts for 2011 in accordance with IFRS, Inter¬national Financial Reporting Standards, as endorsed by the EU. When preparing consolidated accounts, intra-group transactions and balances along with unrealised gains or losses on these transactions between group units are eliminated.

Capital adequacy calculations are subject to special consolidation rules governed by the Consolidation Regulations. Primary capital and nominal amounts used in calculating risk-weighted volume will deviate from figures in the DNB Group's accounts, as associated companies which are consolidated in the accounts according to the equity method are consolidated according to the gross method in capital adequacy calculations. An overview of DNB investments in associated companies, including risk-weighted volume is shown in the table below.

INVESTMENTS IN ASSOCIATED COMPANIES

DNB GROUP

	Ownership share (%)	Assets	Risk-weighted[1] volume
Amounts in NOK million	31 Dec. 2011	31 Dec. 2011	31 Dec. 2011
Eksportfinans AS	40	213 929	11 864
Amports Inc.	30	894	214
Nordito Property AS	40	147	24
Relacom Management AB	31	5 215	482
Other associated companies	–	6 707	155

1) DNB's share

In accordance with Norwegian financial legislation, the raising and premature redemption of subordinated loans and repayment of subordinated loans between parent companies and subsidiaries require approval from Finanstilsynet.

Implementation of Basel II

Basel II, entered into force on 1 January 2007. The capital adequacy regulations are divided into three so-called pillars: 1. minimum capital requirements, 2. banks' own assessment of their risk profile, and capital requirements and 3. demand for disclosure of financial information. In Pillar 1, the capital requirements for credit risk, market risk and operational risk are described. Subject to approval from Finanstilsynet, the capital requirement for credit risk may be calculated based on internal classification models (IRB).

In 2007, DNB was granted permission to use the Group's own classification systems as a basis for capital adequacy reporting for parts of the credit portfolio. This has subsequently been extended to include use of the Group's own models for severity and credit exposure, and an increasing share of the portfolio is included.

DNB uses the IRB approach to calculate capital adequacy for approximately 70 per cent of the Group's credit risk, measured in terms of exposure at default. The table below shows the portfolios this applies to. Practically all of the Group's mortgages secured by real property are reported according to the IRB approach. When applying the IRB approach to mortgage loans, the bank's models for expected default frequency, loss given default and exposure at default are used for both internal management purposes and capital adequacy calculations. In the retail market, supervisory approval has been sought in order to apply the IRB approach for capital adequacy reporting for mortgage loans in Nordlandsbanken.

A large part of the portfolio for small and medium-sized businesses is reported according to the advanced IRB approach. The use of this approach implies that the bank's models for expected default frequency, loss given default, exposure and maturity are used for both internal management purposes and capital adequacy calculations. The Group has applied for approval to use the advanced IRB approach for simulation models in DNB Bank and for corporate clients in Nordlandsbanken and DNB Næringskreditt.

The Group has also applied for permission to use the advanced IRB approach for loans to banks. Moreover, such permission will be sought for additional small portfolios.

The basic indicator approach, the standardised approach and the advanced approach can all be used to measure operational risk under Basel II. DNB Bank ASA reports according to the standardised approach, while some subsidiaries use the basic indicator approach. A shift to the most advanced reporting standard, Advanced Measurement Approaches, AMA, will be considered at a later date. The use of the most advanced approach is subject to approval by Finanstilsynet.

Market risk can be reported according to the standardised approach or the VaR-based Internal Models Approach. DNB reports according to the standardised approach.

BASEL II-IMPLEMENTATION – FURTHER PROGRESS

	Reporting methods for credit risk in capital adequacy calculation	
Portfolios	31 Dec. 2011	31 Dec. 2012
Retail:		
- mortgage loans, DNB Bank and DNB Boligkreditt	IRB [1)]	IRB [1)]
- qualifying revolving retail exposures, DNB Bank [2)]	IRB [1)]	IRB [1)]
- mortgage loans, Nordlandsbanken	Standardised	IRB [1)]
- loans in Norway, DNB Finans, DNB Bank	IRB [1)]	IRB [1)]
Corporates:		
- small and medium-sized corporates, DNB Bank	Advanced IRB	Advanced IRB
- large corporate clients (scorecard models), DNB Bank	Advanced IRB	Advanced IRB
- large corporate clients (simulation models), DNB Bank	Standardised	Advanced IRB
- corporate clients, Nordlandsbanken	Standardised	Advanced IRB
- leasing DNB Bank	Advanced IRB	Advanced IRB
- corporate clients, DNB Næringskreditt	Standardised	Advanced IRB
Securitisation positions:		
- international bond portfolio	IRB [1)]	IRB [1)]
Institutions:		
- banks and financial institutions, DNB Bank	Standardised	Advanced IRB
Exceptions:		
- approved exceptions: government and municipalities, equity positions	Standardised	Standardised
- temporary exceptions: DNB Baltics and Poland, DNB Luxembourg, DnB NOR Monchebank and various other small portfolios	Standardised	Standardised

1) There is only one IRB approach for retail exposures and securitisation positions.

2) Reported according to the IRB category Other retail exposures.

PRIMARY CAPITAL AND MINIMUM CAPITAL REQUIREMENT

Specification of primary capital, including core capital, additions and deductions for DNB Bank ASA, the DNB Bank Group and the DNB Group as at 31 December 2011.

PRIMARY CAPITAL [1]	DNB Bank ASA		DNB Bank Group		DNB Group	
Amounts in NOK million	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
Share capital	18 314	17 514	18 314	17 514	16 260	16 232
Other equity	79 328	61 582	85 990	72 344	101 555	94 964
Total equity	97 643	79 096	104 304	89 859	117 815	111 196
Deductions						
Pension funds above pension commitments	0	0	(22)	(16)	(126)	(119)
Goodwill	(2 419)	(2 419)	(3 834)	(3 472)	(5 741)	(5 378)
Deferred tax assets	(3)	(481)	(644)	(324)	(651)	(977)
Other intangible assets	(1 130)	(1 159)	(2 028)	(1 963)	(2 270)	(2 219)
Dividends payable etc.	0	0	0	(6 000)	(3 258)	(6 515)
Unrealised gains on fixed assets	0	0	(30)	(30)	(30)	(30)
50 per cent of investments in other financial institutions	(1 022)	(1 024)	(1 022)	(1 024)	0	0
50 per cent of expected losses exceeding actual losses, IRB portfolios	(648)	(515)	(835)	(666)	(835)	(666)
Adjustments for unrealised losses/(gains) on debt recorded at fair value	(24)	94	(713)	(346)	(713)	(346)
Equity Tier 1 capital	92 396	73 592	95 177	76 018	104 191	94 946
Perpetual subordinated loan capital securities [2] [3]	5 973	8 241	6 159	8 423	6 159	8 423
Tier 1 capital	98 370	81 833	101 336	84 441	110 350	103 368
Perpetual subordinated loan capital	4 153	7 004	4 153	7 004	4 153	7 004
Term subordinated loan capital [3]	12 773	17 085	13 230	17 775	13 230	17 775
Deductions						
50 per cent of investments in other financial institutions	(1 022)	(1 024)	(1 022)	(1 024)	0	0
50 per cent of expected losses exceeding actual losses, IRB portfolios	(648)	(515)	(835)	(666)	(835)	(666)
Additions						
45 per cent of unrealised gains on fixed assets	0	0	18	18	18	18
Tier 2 capital	15 256	22 549	15 544	23 108	16 566	24 132
Total eligible primary capital [4]	113 625	104 382	116 879	107 548	126 916	127 500
Risk-weighted volume	874 786	738 194	1 018 586	918 659	1 111 574	1 028 404
Minimum capital requirement	69 983	59 056	81 487	73 493	88 926	82 272
Equity Tier 1 ratio (%)	10.6	10.0	9.3	8.3	9.4	9.2
Tier 1 capital ratio (%)	11.2	11.1	9.9	9.2	9.9	10.1
Capital ratio (%)	13.0	14.1	11.5	11.7	11.4	12.4
Risk-weighted volume, basis for transitional rules (Basel I)	1 013 353	899 340	1 273 232	1 148 324	1 269 037	1 144 757

1) This table is updated quarterly in the Annex to Pillar 3

2) Perpetual subordinated loan capital securities can represent up to 15 per cent of core capital. The excess will qualify as perpetual supplementary capital.

3) As at 31 December 2010, calculations of capital adequacy included a total of NOK 789 million in subordinated loan capital in associated companies, in addition to subordinated loan capital in the balance sheets of the banking group and the DNB Group.

4) Primary capital and nominal amounts used in calculating risk-weighted volume deviate from figures in the consolidated accounts since a different consolidation method is used. Associated companies are consolidated gross in the capital adequacy calculations while the equity method is used in the accounts.

RISK-WEIGHTED VOLUME

Specification of risk-weighted volume and capital requirements for DNB Bank ASA, the DNB Bank Group and the DNB Group as at 31 December 2011.

DNB BANK ASA

Specification of risk-weighted volume and capital requirements [1] *Amounts in NOK million*	Nominal exposure 31 Dec. 2011	EAD [2] 31 Dec. 2011	Average risk-weight	Risk-weighted volume 31 Dec. 2011	Capital requirements 31 Dec. 2011	Capital requirements 31 Dec 2010
IRB approach						
Corporate	814 640	682 465	55.5%	378 633	30 291	24 567
Specialised Lending (SL)	7 566	7 507	47.7%	3 580	286	117
Retail – mortgage loans	72 958	72 956	25.3%	18 457	1 477	1 444
Retail – other exposures	90 589	74 489	31.7%	23 641	1 891	1 778
Securitisation	95 062	95 062	9.9%	9 402	752	735
Total credit risk, IRB approach	1 080 815	932 479	46.5%	433 714	34 697	28 641
Standardised approach						
Central government	84 893	82 720	0.1%	77	6	143
Institutions	433 939	394 216	18.4%	72 442	5 795	5 323
Corporate	267 924	217 884	96.4%	210 088	16 807	14 235
Specialised Lending (SL)	0	0		0	0	476
Retail – mortgage loans	3 305	2 996	75.3%	2 255	180	293
Retail – other exposures	57 160	22 455	75.6%	16 972	1 358	1 078
Equity positions	40 162	40 162	100.5%	40 366	3 229	2 267
Other assets	3 878	3 878	100.0%	3 878	310	196
Total credit risk, standardised approach	891 260	764 310	45.3%	346 079	27 686	24 010
Total credit risk	1 972 075	1 696 789	46.0%	779 793	62 383	52 651
Market risk						
Position risk, equity instruments				1 183	95	37
Position risk, debt instruments				38 210	3 057	2 367
Currency risk				0	0	0
Total market risk				39 393	3 151	2 404
Operational risk				57 705	4 616	4 169
Deductions				(2 105)	(168)	(168)
Total risk-weighted volume and capital requirements before transitional rule				874 786	69 983	59 056
Additional capital requirements according to transitional rules [3]				0	0	0
Total risk-weighted volume and capital requirements				**874 786**	**69 983**	**59 056**

1) This table is updated quarterly in the Annex to Pillar 3
2) EAD, exposure at default.
3) Due to transitional rules, the minimum capital adequacy requirements for 2010 and 2011 cannot be reduced below 80 per cent relative to the Basel I requirements.

DNB BANK GROUP

Specification of risk-weighted volume and capital requirements [1] *Amounts in NOK million*	Nominal exposure 31 Dec. 2011	EAD [2] 31 Dec. 2011	Average risk-weight	Risk-weighted volume 31 Dec. 2011	Capital requirements 31 Dec. 2011	Capital requirements 31 Dec 2010
IRB approach						
Corporate	824 706	692 684	55.0%	380 666	30 453	25 103
Specialised Lending (SL)	7 566	7 507	47.7%	3 580	286	117
Retail – mortgage loans	538 910	538 908	12.8%	68 932	5 515	4 533
Retail – other exposures	90 589	74 489	31.7%	23 641	1 891	1 778
Securitisation	95 062	95 062	9.9%	9 402	752	735
Total credit risk, IRB approach	1 556 833	1 408 651	34.5%	486 222	38 898	32 266
Standardised approach						
Central government	93 841	110 044	0.1%	130	10	146
Institutions	140 500	118 851	21.9%	26 018	2 081	1 940
Corporate	392 019	293 720	96.1%	282 196	22 576	19 912
Specialised Lending (SL)	0	0		0	0	476
Retail – mortgage loans	47 575	45 614	45.9%	20 921	1 674	1 294
Retail – other exposures	85 324	46 589	76.6%	35 709	2 857	2 474
Equity positions	3 251	3 251	106.3%	3 455	276	361
Securitisation	9 349	9 349	19.2%	1 794	143	117
Other assets	11 495	11 495	100.0%	11 495	920	684
Total credit risk, standardised approach	783 354	638 913	59.7%	381 718	30 537	27 404
Total credit risk	2 340 187	2 047 564	42.4%	867 939	69 435	59 670
Market risk						
Position risk, equity instruments				1 183	95	37
Position risk, debt instruments				35 412	2 833	2 429
Currency risk				0	0	0
Total market risk				36 596	2 928	2 466
Operational risk				66 364	5 309	4 886
Deductions				(2 674)	(214)	(203)
Total risk-weighted volume and capital requirements before transitional rule				968 225	77 458	66 819
Additional capital requirements according to transitional rules [3]				50 360	4 029	6 673
Total risk-weighted volume and capital requirements				**1 018 586**	**81 487**	**73 493**

1) This table is updated quarterly in the Annex to Pillar 3

2) EAD, exposure at default.

3) Due to transitional rules, the minimum capital adequacy requirements for 2010 and 2011 cannot be reduced below 80 per cent relative to the Basel I requirements.

DNB GROUP

Specification of risk-weighted volume and capital requirements [1] *Amounts in NOK million*	Nominal exposure 31 Dec. 2011	EAD [2] 31 Dec. 2011	Average risk-weight	Risk-weighted volume 31 Dec. 2011	Capital requirements 31 Dec. 2011	Capital requirements 31 Dec 2010
IRB approach						
Corporate	824 706	692 684	55.0%	380 666	30 453	25 103
Specialised Lending (SL)	7 566	7 507	47.7%	3 580	286	117
Retail – mortgage loans	538 910	538 908	12.8%	68 932	5 515	4 533
Retail – other exposures	90 589	74 489	31.7%	23 641	1 891	1 778
Securitisation	95 062	95 062	9.9%	9 402	752	735
Total credit risk, IRB approach	1 556 833	1 408 651	34.5%	486 222	38 898	32 266
Standardised approach						
Central government	93 841	110 044	0.1%	130	10	146
Institutions	130 538	108 889	22.1%	24 026	1 922	1 783
Corporate	388 297	289 997	96.0%	278 473	22 278	19 607
Specialised Lending (SL)	0	0	0.0%	0	0	476
Retail – mortgage loans	47 575	45 614	45.9%	20 921	1 674	1 294
Retail – other exposures	85 324	46 589	76.6%	35 709	2 857	2 474
Equity positions	3 501	3 501	102.9%	3 602	288	372
Securitisation	9 349	9 349	19.2%	1 794	143	117
Other assets	11 266	11 266	100.0%	11 266	901	688
Total credit risk, standardised approach	769 690	625 249	60.1%	375 920	30 074	26 957
Total credit risk	2 326 523	2 033 900	42.4%	862 142	68 971	59 225
Market risk						
Position risk, equity instruments				1 183	95	37
Position risk, debt instruments				35 412	2 833	2 429
Currency risk				0	0	0
Total market risk				36 596	2 928	2 466
Operational risk				67 320	5 386	4 956
Net insurance, after eliminations				96 345	7 708	9 008
Deductions				(629)	(50)	(39)
Total risk-weighted volume and capital requirements before transitional rule				1 061 772	84 942	75 614
Additional capital requirements according to transitional rules [3]				49 802	3 984	6 658
Total risk-weighted volume and capital requirements				**1 111 574**	**88 926**	**82 272**

1) This table is updated quarterly in the Annex to Pillar 3

1) EAD, exposure at default.

2) Due to transitional rules, the minimum capital adequacy requirements for 2010 and 2011 cannot be reduced below 80 per cent relative to the Basel I requirements.

CREDIT RISK

Credit risk is the risk of losses due to failure on the part of the Group's counterparties or customers to meet their payment obligations towards the DNB Group. Credit risk refers to all claims against counterparties or customers, including credit risk in trading operations, country risk and settlement risk. The credit portfolio includes loans, liabilities in the form of other extended credits, guarantees, leasing, factoring, interest-bearing securities, approved, undrawn credits, as well as counterparty risk arising through derivatives and foreign exchange contracts. Settlement risk arises in connection with payment transfers as not all transactions take place in real time.

Credit policy

According to the Group's credit policy, approved by the Boards of Directors of DNB ASA and DNB Bank ASA, the principal objective for credit activity is that the loan portfolio should have a quality and a composition which secure the Group's profitability in the short and long term. The quality of the credit portfolio should be consistent with DNB's low risk profile target.

Credit risk management

The Group's credit policy regulates credit activity in DNB Bank. The customer's debt servicing capacity will be the key element when considering whether to approve a credit. If the customer has not proven a satisfactory debt servicing capacity, credit should normally not be extended even if the collateral is adequate. The value of collateral should be assessed based on estimated realisation value. The portfolio should be sufficiently flexible and liquid to permit sales, syndication and securitisation of credits and the use of credit derivatives.

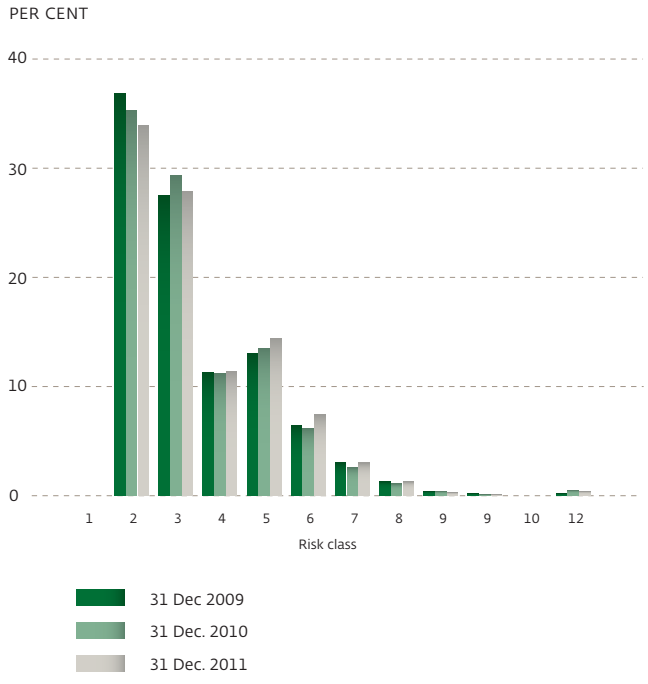
Credit operations must comply with business, credit and industry strategies approved by the Board of Directors. According to DNB's corporate social responsibility guidelines, DNB has undertaken not to offer products and services or perform acts representing a material risk of involvement in unethical conduct, infringement of human or labour rights, corruption or harm to the environment.

The Group aims to reduce large risk concentrations, whereby significant changes in one or a few risk drivers may markedly affect the Group's profitability. Risk concentrations include large exposures to a customer or customer group as well as clusters of commitments in high-risk classes, industries and geographical areas. Credit exposure within shipping and commercial property is monitored closely.

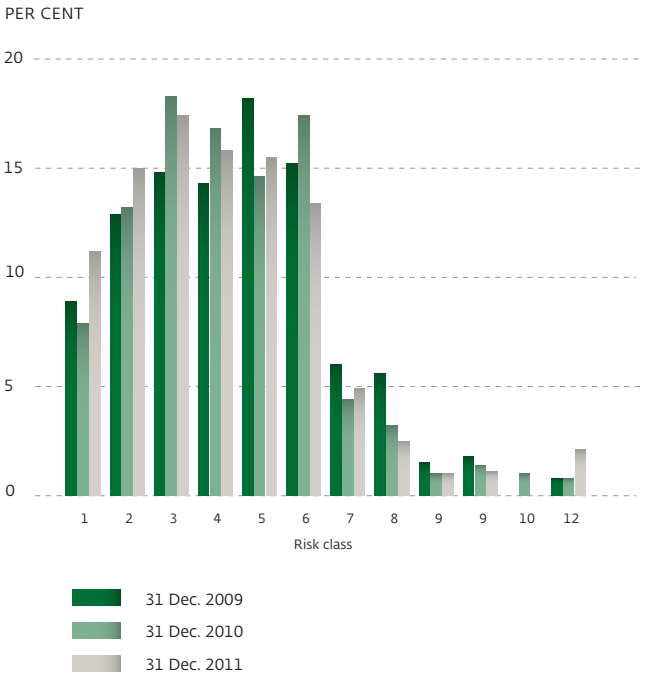
Credit approval authorisations are personal and graded on the basis of customers' risk class. For large credits, there is a two-layered decision-making procedure where credit approval authority rests with the business units while final credit approval requires endorsement by a credit officer who is organisationally independent of the business units. Commitments showing a negative development are identified and followed up separately.

All corporate customers granted credit must be classified according to risk in connection with every significant credit approval

RETAIL MORTGAGE LOANS IRB PORTFOLIO ACCORDING TO RISK CLASS



CORPORATE IRBA PORTFOLIO ACCORDING TO RISK CLASS



and, unless otherwise decided, at least once a year. In the personal banking market, where there is a large number of customers, the majority of credit decisions should be made on the basis of automated scoring and decision support systems. Risk classification should reflect long-term risk associated with each customer and the customer's credit commitment.

The unit responsible for the classification system is organisationally independent of the operative units. The classification models have been developed to cover specific loan portfolios. If a model is considered to place a commitment in a highly misleading risk class, the generated class may be overridden by a unit which is independent of the operative units, based on a recommendation from the business areas. All overrides must be well founded and be made only in exceptional cases based on a thorough assessment. The effect of overrides is tested by an independent unit once a year.

The risk classification systems are used as decision support, risk monitoring and reporting. The risk parameters used in the classification systems are an integrated part of the credit process and ongoing monitoring, including the follow-up of credit strategies.

Detailed rules are in place for the use and monitoring of collateral, including guidelines for the valuation of various pledged assets and guarantees. Such valuations are part of credit decisions and are reviewed in connection with the annual renewal of the commitments. A procedure has been established for the periodic control of collateral.

Classification models and the IRB system

The DNB Group has extensive experience with classification systems as support for credit decisions and monitoring. Data and analytical tools are an integrated part of risk management.

The Group's credit risk models provide a basis for statistically based calculations of expected losses in a long-term perspective and risk-adjusted capital in a portfolio perspective. The calculations are based on several risk parameters, with the most important being:

- Probability of default, PD, is used to measure quality. Customers are classified based on the probability of default.
- Exposure at default, EAD, is an estimated figure which includes amounts drawn under credit limits or loans as well as a percentage share of committed, undrawn credit lines.
- Loss given default, LGD, indicates how much the Group expects to lose if the customer fails to meet his obligations, taking the collateral provided by the customer and other relevant factors into consideration.

The risk classes are defined on the basis of the scales used by international rating agencies. There are ten risk classes for performing loans. In addition, impaired and non-performing commitments are placed in classes 11 and 12 respectively for reporting purposes.

DNB's models for risk classification of customers are subject to continual improvement and testing. The models are adapted to different industries and segments and are regularly upgraded to ensure that the variables used in the models have high explanatory power at all times based on key risk drivers for the individual parameters included in the models. If an external rating has been given, such rating may be taken into consideration when classifying individual commitments. The classification of institutional and country risk is based on classifications by external rating agencies.

Credit risk measurement

Credit risk is monitored by following developments in risk parameters, migration and distribution over the various risk classes. Developments in risk concentrations are monitored closely with respect to exposure, risk classes and allocated risk-adjusted capital. Large customers and customer groups are followed up based on risk class and allocated risk-adjusted capital. In the corporate segment, all commitments which are considered to require special follow-up during the credit approval process are identified. This ensures management attention and follow-up.

The models' calculations of estimated probability of default should show the average probability of default during a business cycle. This implies that the models overestimate the credit risk during a period of strong economic expansion and underestimate the credit risk during a recession. Consequently, stress testing is also used to assess the effects of a recession on capital requirements. The stress tests should identify possible future changes in economic conditions which could have a negative impact on the Group's credit exposure and ability to withstand such changes. These assessments are taken into account in the Group's risk and capital assessment process to determine the correct level of capital.

Risk-adjusted capital for credit risk is aggregated based on individual commitments, where each commitment is classified with respect to quality in the form of expected default frequency and the amount of loss experienced in the event of default. The portfolio classification provides a basis for statistically based calculations of normalised losses and risk-adjusted capital. Calculations of risk-adjusted capital include the effect of industry concentrations, diversification effects and large exposures.

Collateral

As a key principle, the bank requires security for all loans in the form of either mortgages or so-called negative pledges, where the customer is required to keep all assets free from encumbrances vis-à-vis all lenders. During the credit process, the bank will consider whether adequate collateral is provided.

The main principle for valuing collateral is that the expected realisation value at the time the bank may need to realise the collateral, should be used. The practical implementation is described in extensive rules, including maximum rates for all types of collateral and valuation guidelines. Valuations should be made when approving new loans and in connection with the annual renewal and are considered to be part of credit decisions. A procedure has been established for the periodic control of collateral.

The main types of collateral used are mortgages on property, registrable movables, accounts receivable, inventories, plant and equipment, agricultural chattel and fish-farming concessions. The main categories of guarantors are private individuals (consumer guarantees), corporates (professionals), guarantee institutes and banks. Guarantors are classified according to risk based on the

bank's rating models. Debtors can only be assigned the guarantor's PD provided that the guarantor is placed in risk category 6 or higher and the guarantee applies to the entire commitment. Guarantees can only serve as collateral (affect LGD) if they are placed in risk category 6 or higher. Credit derivatives are not used for portfolios for which use of the IRB approach has been approved. Guarantees represent a limited part of such portfolios.

The Group's netting rights are in compliance with general rules in Norwegian legislation. Netting clauses have been included in all standard loan agreements in DNB Bank ASA and product agreements in DNB Markets. Netting rights have no value in risk and capital calculations, except for Markets products, where stipulations in the framework agreement (ISDA) open up for far more extensive netting.

Non-performing commitments and write-downs

On each balance sheet date, the Group will consider whether there are objective indications that the financial assets have decreased in value. Objective indications of a decrease in value of loans include serious financial problems on the part of the debtor, non-payment or other serious breaches of contract, the probability that the debtor will enter into debt negotiations or other special circumstances that have occurred. The renegotiation of loan terms to ease the borrower's position is regarded as objective indications of a decrease in value.

Impairment of other financial assets is recognised in the income statement according to the nature of the asset.

If objective indications of a decrease in value can be found, write-downs on loans are calculated as the difference between the value of the loan in the balance sheet and the net present value of estimated future cash flows discounted by the effective interest rate.

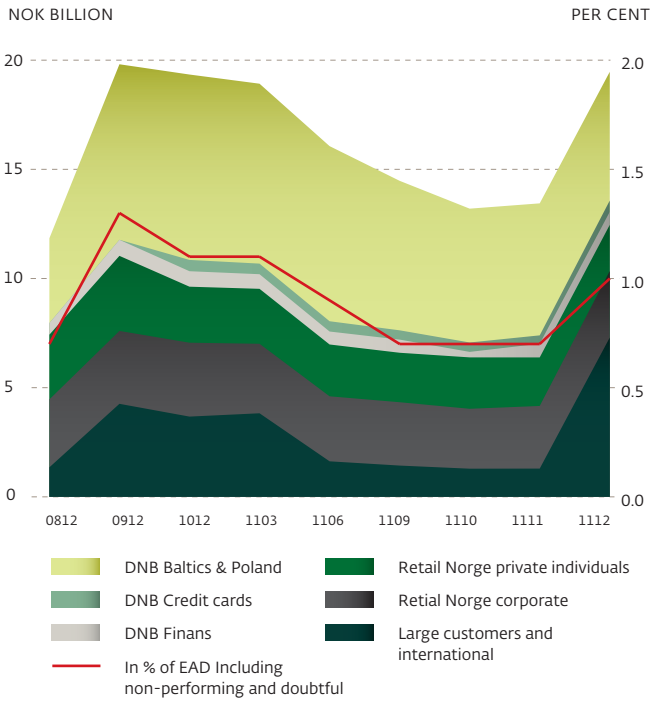
In accordance with IAS 39, the best estimate is used to assess future cash flows. Estimates of future cash flows are based on empirical data and discretionary assessments of future macroeconomic developments and developments in problem commitments, based on the situation on the balance sheet date. The estimates are the result of a process, which involves the business areas and central credit units and represents management's best estimate. When considering write-downs on loans, there will be an element of uncertainty with respect to the identification of impaired loans, the estimation of amounts and the timing of future cash flows, including collateral assessments.

The effective interest rate used for discounting is not adjusted to reflect changes in the credit risk and terms of the loan due to objective indications of impairment being identified.

Individual write-downs on loans reduce the value of the commitments in the balance sheet. Changes in the assessed value of loans during the period are recorded under "Write-downs on loans and guarantees".

Loans and other commitments where payment terms are not complied with are classified as non-performing, unless the situation is considered temporary. Commitments are classified as non-performing no later than 90 days past the formal due date.

NET NON-PERFORMING AND DOUBTFUL COMMITTMENTS



Guarantees are considered to be defaulted once a claim has been made against the bank. Loans, guarantees etc. classified as high risk, without being in default, are subject to special monitoring and loss risk assessment.

Loans, which have not been individually evaluated for impairment, are evaluated collectively in groups. Loans, which have been indivi¬du¬ally evaluated, but not written down, are also evaluated in groups. The evaluation is based on objective evidence of a decrease in value that has occurred on the balance sheet date and can be related to the group.

Loans are grouped on the basis of similar risk and value characteristics in accordance with the division of customers into main sectors or industries and risk categories. The need for write-downs is estimated per customer group based on estimates of the general economic situation and loss experience for the respective customer groups. The economic situation is assessed by means of economic indicators for each customer group based on external information about the markets. Various parameters are used depending on the customer group in question. Key parameters are production gaps, which give an indication of capacity utilisation in the economy, and developments in housing prices and in shipping freight rates. The economic indicators that are used show a high level of correlation with past write-downs.

Group write-downs reduce the value of the commitments in the balance sheet, and changes during the period are recorded under "Write-downs on loans and guarantees". Like individual write-downs, group write-downs are based on discounted cash flows.

Cash flows are discounted on the basis of statistics derived from individual write-downs. Interest is calculated on commitments subject to group write-downs according to the same principles and experience base as for commitments evaluated on an individual basis.

The tables below show the Group's commitment categories on and off the balance sheet and according to sector and geographical location. The tables also show total commitments including decreases in value and write-downs and average figures during the period. In addition, the commitment categories are broken down into residual maturities.

OVERVIEW OF CREDIT EXPOSURES

COMMITMENTS FOR PRINCIPAL SECTORS [1)] DNB GROUP

	Loans and receivables		Guarantees		Unutilized credit lines		Total commitments	
Amounts in NOK million	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
Retail customers	599 941	559 062	243	283	98 125	99 357	698 309	658 701
Transportation by sea and pipelines and vessel construction	143 921	133 926	10 980	9 748	41 167	38 430	196 067	182 104
Real estate	187 992	175 806	2 975	2 173	24 751	19 828	215 718	197 807
Manufacturing	51 643	47 897	14 100	10 438	50 446	38 856	116 190	97 191
Services	86 493	73 961	5 233	5 105	34 511	23 941	126 237	103 007
Trade	36 419	33 942	4 696	4 413	26 948	20 662	68 062	59 016
Oil and gas	24 502	18 076	14 357	8 439	42 470	26 653	81 329	53 168
Transportation and communication	34 273	29 421	4 205	4 139	18 813	17 418	57 292	50 979
Building and construction	43 108	35 790	12 201	8 931	18 040	15 222	73 348	59 943
Power and water supply	28 801	22 843	16 206	12 355	26 740	17 287	71 746	52 485
Seafood	16 934	13 893	299	191	6 166	4 652	23 399	18 737
Hotels and restaurants	4 089	5 121	230	127	887	1 053	5 206	6 300
Agriculture and forestry	8 856	7 499	52	37	1 420	900	10 328	8 437
Central and local government	6 708	6 042	1 844	2 844	4 362	5 137	12 914	14 023
Other sectors	5 242	6 731	6 663	4 848	32 936	20 637	44 841	32 216
Total customers, nominal amount after individual write-downs	1 278 922	1 170 011	94 282	74 071	427 782	350 033	1 800 986	1 594 115
– Collective write-downs, customers	2 119	1 872		-	-	-	2 119	1 872
+ Other adjustments	2 456	2 202	(98)	(95)	-	-	2 359	2 107
Lending to customers	**1 279 259**	**1 170 341**	**94 185**	**73 976**	**427 782**	**350 033**	**1 801 226**	**1 594 350**
**) Average*	*1 224 467*	*1 142 851*	*84 177*	*67 807*	*388 908*	*324 204*	*1 697 551*	*1 534 860*
Credit institutions, nominal amount after individual write-downs	28 748	47 714	2 204	2 085	7 577	11 484	38 529	61 283
+ Other adjustments	6	77	0	0			6	77
Lending to and deposits with credit institutions	**28 754**	**47 792**	**2 204**	**2 085**	**7 577**	**11 484**	**38 535**	**61 360**
**) Average*	*38 231*	*54 971*	*2 145*	*3 488*	*9 531*	*11 209*	*49 906*	*69 668*

1) The breakdown into principal sectors is based on standardised sector and industry categories set up by Statistics Norway.

Non-performing and doubtful commitments for principal sectors

Net non-performing and doubtful commitments totalled NOK 19.5 billion at end-December 2011, increasing from NOK 18.4 billion at year-end 2010. Towards the end of 2011, a somewhat higher risk of individual losses relating to certain large commitments was identified, requiring limited write-downs. In such cases, the entire commitments are classified as non-performing and doubtful, which explains the rise from 2010. There was no general deterioration in the Group's loan portfolio. Net non-performing and doubtful commitments represented 1.55 and 1.50 per cent, respectively, of lending volume at end-December 2010 and 2011.

DNB GROUP

	Gross impaired commitments		Total individual write-downs		Net impaired commitments	
Amounts in NOK million	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
Retail customers	6 557	6 727	2 786	2 246	3 771	4 481
Transportation by sea and pipelines and vessel construction	4 045	1 144	494	335	3 551	810
Real estate	5 121	3 742	1 546	1 239	3 575	2 503
Manufacturing	3 676	4 865	1 604	1 700	2 072	3 165
Services and management	1 410	2 378	838	857	572	1 521
Trade	1 671	1 515	817	817	854	698
Oil and gas	0	0	0	0	0	0
Transportation and communication	761	977	427	487	334	490
Building and construction	1 349	2 777	702	1 067	647	1 710
Power and water supply	80	188	80	162	0	25
Seafood	100	52	33	41	67	10
Hotels and restaurants	429	481	131	130	298	351
Agriculture and forestry	388	441	128	162	260	279
Central and local government	0	0	0	0	0	0
Other sectors	35	81	13	29	22	53
Total customers	25 622	25 368	9 599	9 272	16 023	16 097
Credit institutions	46	1	25	1	21	0
Total impaired loans and guarantees	25 667	25 369	9 624	9 273	16 043	16 097
Non-performing loans and guarantees not subject to write-downs	3 422	2 313	–	–	3 422	2 313
Total non-performing and impaired commitments	**29 089**	**27 682**	**9 624**	**9 273**	**19 465**	**18 409**

Commitments according to geographical location [1)]

The table below shows the Group's exposure in different geographical areas.

DNB GROUP

	Loans		Guarantees		Unutilised credit lines		Total commitments	
Amounts in NOK million	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
Oslo	227 229	211 013	20 845	19 648	93 770	72 656	341 844	303 317
Eastern and southern Norway	418 195	386 727	23 109	17 261	112 070	106 159	553 374	510 147
Western Norway	154 741	146 273	9 342	7 450	41 330	37 270	205 414	190 992
Northern and central Norway	169 817	156 597	11 265	7 378	32 818	32 625	213 899	196 599
Total Norway	969 981	900 609	64 561	51 737	279 989	248 710	1 314 531	1 201 055
Sweden	68 910	68 062	4 882	3 620	29 187	19 954	102 980	91 637
United Kingdom	28 183	25 094	6 617	4 450	5 438	1 147	40 238	30 691
Other Western European countries	59 954	60 229	4 651	5 476	39 376	28 987	103 982	94 693
Russia	1 660	1 360	204	43	175	131	2 040	1 533
Estonia	1 971	2 841	53	29	168	80	2 193	2 951
Latvia	17 352	18 242	554	492	1 593	844	19 499	19 577
Lithuania	21 503	22 690	612	441	1 117	1 806	23 233	24 938
Poland	19 600	14 408	722	690	2 680	1 786	23 001	16 884
Other Eastern European countries	269	251	246	73	9	3	523	326
Total Europe outside Norway	219 403	213 177	18 541	15 313	79 744	54 738	317 688	283 229
USA and Canada	33 793	25 573	8 127	5 017	32 610	33 076	74 531	63 665
Bermuda and Panama [2)]	18 903	17 828	497	324	5 535	7 449	24 935	25 601
South and Central American countries	9 586	6 109	2 467	2 353	6 125	6 004	18 178	14 466
Total America	62 283	49 510	11 091	7 694	44 270	46 529	117 644	103 733
Singapore [2)]	14 706	14 845	555	332	3 535	2 301	18 796	17 479
Hong Kong	3 613	3 780	0	7	726	856	4 339	4 643
Asian countries	14 145	13 067	999	386	6 233	990	21 377	14 443
Total Asia	32 465	31 692	1 554	725	10 493	4 147	44 512	36 565
Liberia [2)]	12 191	10 919	335	255	3 949	3 128	16 475	14 301
African countries	399	2 394	104	112	1 263	398	1 767	2 905
Australia, New Zealand and Marshall Islands [2)]	20 494	18 632	379	385	15 653	3 867	36 526	22 884
Lending and guarantees [3)]	1 317 216	1 226 935	96 564	76 220	435 359	361 517	1 849 138	1 664 671
- Individual write-downs	9 546	9 208	78	65	–	–	9 624	9 273
- Collective write-downs	2 119	1 872	–	–	–	–	2 119	1 872
+ Other adjustments	2 462	2 279	(98)	(95)	–	–	2 365	2 184
Lending and guarantees	1 308 013	1 218 133	96 389	76 061	435 359	361 517	1 839 760	1 655 710

1) Based on the customer's address.
2) Represents shipping commitments.
3) All amounts represent gross lending and guarantees respectively before individual write-downs.

Non-performing and doubtful commitments according to geographical location [1)]

The table below shows gross and net non-performing and doubtful commitments according to geographical location.

DNB GROUP

	Gross non-performing and doubtful commitments		Total individual write-downs		Net non-performing and doubtful commitments	
Amounts in NOK million	31 Dec. 2010		31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
Oslo	1 693	1 518	763	487	930	1 031
Eastern and southern Norway	4 403	6 183	1 432	1 563	2 970	4 620
Western Norway	2 377	1 596	564	601	1 813	995
Northern and central Norway	2 427	2 356	607	709	1 820	1 647
Total Norway	10 899	11 654	3 366	3 360	7 533	8 294
Sweden	397	1 531	292	420	104	1 111
United Kingdom	191	158	43	33	148	125
Other Western European countries	1 774	2 344	865	942	909	1 402
Russia	98	143	28	69	70	74
Estonia	519	516	204	193	316	323
Latvia	4 122	4 290	2 287	1 645	1 834	2 645
Lithuania	4 464	5 551	1 791	1 978	2 673	3 572
Poland	1 750	1 153	550	548	1 200	605
Other Eastern European countries	0	0	0	0	0	0
Total Europe outside Norway	13 314	15 687	6 060	5 829	7 254	9 858
USA and Canada	507	124	0	59	507	65
Bermuda and Panama [2)]	1	1	1	1	0	0
Other South and Central American countries	4	0	1	0	3	0
Total America	512	125	2	60	510	65
Singapore [2)]	11	0	2	0	10	0
Hong Kong	3	7	0	2	2	6
Other Asian countries	6	2	1	0	6	1
Total Asia	20	9	3	2	17	7
Liberia [2)]	0	0	0	0	0	0
Other African countries	7	6	3	2	5	3
Australia, New Zealand and Marshall Islands [2)]	4 337	201	191	19	4 146	182
Lending and guarantees	**29 089**	**27 682**	**9 624**	**9 273**	**19 465**	**18 409**
Herav: Kredittinstitusjoner	112	65	25	1	87	64

1) Based on the customer's address.
2) Representing shipping commitments.

Total commitments according to residual maturity

DNB GROUP

31 Dec. 2011

Amounts in NOK million	Up to 1 month	From 1 month to 3 months	From 3 monts to 1 year	From 1 year to 5 years	Over 5 years	No fixed maturity	Total
Lending to and deposits with credit institutions	14 737	5 645	5 896	2 393	125		28 796
Net lending to customers	213 708	109 709	78 904	165 562	714 930	(2 119)	1 280 694
Unutilised credit lines under 1 year							275 428
Unutilised credit lines over 1 year							246 309
Guarantees							96 565

DNB GROUP

31 Dec. 2011

Amounts in NOK million	Up to 1 month	From 1 month to 3 months	From 3 monts to 1 year	From 1 year to 5 years	Over 5 years	No fixed maturity	Total
Lending to and deposits with credit institutions	22 164	19 993	5 603				47 760
Net lending to customers	167 095	86 549	87 254	181 956	648 961	(1 872)	1 169 943
Unutilised credit lines under 1 year							224 024
Unutilised credit lines over 1 year							191 825
Guarantees							76 221

Past due loans not subject to write-downs

The table below shows overdue amounts on commitments. Past due loans, subject to impairment are not included in the table.

DNB GROUP

Amounts in NOK million	31 Dec. 2011	31 Dec. 2010
No. of days past due/overdrawn		
1 - 29	208	1 238
30 - 59	263	466
60 - 89	95	103
> 90	213	261
Past due loans not subject to write-downs	779	2 068

Developments in write-downs on loans and guarantees

The table below shows write-downs on loans and guarantees in the balance sheet and income statement of the DNB Group and write-downs in the income statement for principal sectors.

Balance sheet

DNB GROUP

	2011				2010			
Amounts in NOK million	Lending to credit institutions	Lending to cusstomers	Guarantees	Total	Lending to credit institutions	Lending to cusstomers	Guarantees	Total
Write-downs as at 1 January	1	11 737	65	11 803	1	11 249	76	11 325
New write-downs	26	2 320	53	2 399	0	3 305	16	3 321
Increase in write-downs	0	1 701	21	1 722	0	1 824	(3)	1 821
Reassessed write-downs	0	968	47	1 015	0	1 093	16	1 109
Write-offs covered by previous write-downs	0	2 740	13	2 753	0	2 209	8	2 217
Changes in individual write-downs of accrued interest and amortisation	0	52	–	52	0	51	–	51
Changes in collective write-downs	0	227	–	227	0	(1 077)	–	(1 077)
Changes in group structure	0	0	0	0	0	0	0	0
Changes due to exchange rate movement	(1)	20	0	19	0	(313)	0	(313)
Write-downs as at 31 December	25	12 350	78	12 453	1	11 737	65	11 803
Of which: Individual write-downs	*25*	*9 521*	*78*	*9 624*	*1*	*9 207*	*65*	*9 273*
Individual write-downs of accrued interest and amortisation	*0*	*710*	–	*710*	*0*	*658*	–	*658*
Collective write-downs	*0*	*2 119*	–	*2 119*	*0*	*1 872*	–	*1 872*

Income statement

DNB GROUP

	2011			2010		
Amounts in NOK million	Lending [1)]	Guarantees	Total	Lending [1)]	Guarantees	Total
Write-offs	550	0	550	459	0	459
New individual write-downs	4 047	73	4 120	5 128	13	5 141
Total new individual write-downs	4 597	73	4 670	5 587	13	5 600
Reassessed individual write-downs	968	47	1 015	1 092	16	1 109
Recoveries on commitments previously written off	437	0	437	418	0	418
Net individual write-downs	3 192	26	3 217	4 077	(3)	4 074
Changes in collective write-downs on loans	227	227	227	(1 077)	0	(1 077)
Write-downs on loans and guarantees	**3 419**	**253**	**3 445**	**3 000**	**(3)**	**2 997**
Write-offs covered by individual write-downs made in previous years	2 740	13	2 753	2 209	8	2 217

1) Including write-downs on loans at fair value.

Write-downs on loans and guarantees for principal sectors [1)]

DNB GROUP

	2011				2010			
Amounts in NOK million	New individual write-downs	Reassessed individual write-downs	Recoveries on commitments reviously written of	Net write-downs	New individual write-downs	Reassessed individual write-downs	Recoveries on commitments reviously written of	Net write-downs
Retail customers	1 758	225	360	1 174	1 830	110	307	1 414
Transportation by sea and pipelines and vessel construction	417	77	4	336	356	63	12	281
Real estate	917	167	12	738	805	335	8	462
Manufacturing	281	109	1	171	835	98	1	736
Services and management	213	73	4	135	345	161	61	123
Trade	316	105	7	203	368	126	3	240
Oil and gas	1	0	0	1	3	0	0	3
Transportation and communication	74	52	7	15	192	87	2	103
Building and construction	527	105	5	416	487	86	8	393
Power and water supply	3	10	0	(7)	158	1	0	158
Seafood	24	20	0	3	9	0	0	9
Hotels and restaurants	48	27	0	20	92	16	0	76
Agriculture and forestry	59	43	1	16	95	25	1	69
Central and local government	0	0	0	0	0	0	0	0
Other sectors	8	1	5	2	22	0	14	9
Total customers	4 644	1 015	406	3 222	5 600	1 109	416	4 076
Credit institutions	26	0	31	(5)	0	0	2	(2)
Changes in collective write-downs on loans	–	–	–	227	–	–	–	(1 077)
Write-downs on loans and guarantees	**4 670**	**1 015**	**437**	**3 445**	**5 600**	**1 109**	**418**	**2 997**
Of which individual write-downs on guarantees	*73*	*47*	*0*	*26*	*13*	*16*	*0*	*(3)*

1) The breakdown into principal sectors is based on standardised sector and industry categories set up by Statistics Norway.

CREDIT RISK – STANDARDISED APPROACH

Estimated risk-weighted volume and capital requirements for the portfolios reported according to the standardised approach are shown in tables on pages 12 too 14.

As an IRB bank, DNB reports all portfolios which are not qualified to be reported according to the IRB approach according to the standardised approach, though the portfolios are grouped in IRB categories. In addition, commitments which qualify for being reported according to the IRB approach, but where there is not adequate available data, are reported according to this approach. The following categories and risk weights are used in reporting according to the standardised approach.

Risk class	Standard & Poor's	Moody's	Fitch	Risk weights for different exposure classes (main rule) ie. the Capital Adequacy Regulations	
	0%	20%	50%	Governments and central banks	Institutions
1	AAA to AA-	Aaa to Aa3	AAA to AA-	0%	20%
2	A+ to A-	A1 to A3	A+ to A-	20%	50%
3	BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-	50%	100%
4	BB+ to BB-	Ba1 to Ba3	BB+ to BB-	100%	100%
5	B+ to B-	Bi to B3	B+ to B-	100%	100%
6	CCC+ and below	Caa1 and below	CCC+ and below	150%	150%

- Governments and central banks – long-term ratings from approved rating agencies are used for assigning risk classes and applicable risk weights.
- Institutions – banks, mortgage institutions and financial institutions, regional governments and local authorities. Country ratings are used. The institutions are assigned a risk class which is higher than the risk class for the country rating.

- Corporates – includes life and non-life insurance companies – 100 per cent risk weight.
- Corporates, specialised lending – 100 per cent risk weight.
- Retail exposures – in order to qualify for inclusion in the retail portfolio, the borrower must be an individual. Alternatively, individual exposures must be classified as "Corporate as retail exposure". Retail exposures are divided into the following three sub-categories:
  - Mortgages backed by real property - as a main rule, commitments secured by mortgages on residential property within 80 per cent of appraised value will be assigned a risk weight of 35 per cent, while commitments backed by collateral exceeding 80 per cent of appraised value will be assigned a 75 per cent weight
  - Qualifying revolving retail exposures - 75 per cent risk weight
  - Other retail exposures – 75 per cent risk weight
- Equity positions – equities and instruments with corresponding financial characteristics, including mutual funds and loans which can be converted to equities. Risk weight according to counterparty, as above. In addition, a 150 per cent risk weight is applied to high-risk commitments, e.g. investments in Private Equity and venture capital.
- Securitisation – DNB's securitisation investments are reported according to the IRB approach, while Eksportfinans' portfolio is reported according to the standardised approach.

Rated positions under the standardised approach should be assigned the following risk weights:

Risk Class	Standard & Poor's	Moody's	Fitch	Risk-weight
1	AAA to AA-	Aaa to Aa3	AAA to AA-	20%
2	A+ to A-	A1 to A3	A+ to A-	50%
3	BBB+ to BBB-	Baa1 to Baa3	BBB+ to BBB-	100%
4	BB+ til BB-	Ba1 to Ba3	BB+ to BB-	350%
5-6	B+ and below	B1and below	B+ and below	1250%

Other assets – fixed assets and receivables which are not classified by debtor sector are assigned a risk weight of 100 per cent.

Covered bonds are reported under the institutions category and assigned a 10 per cent risk weight.

Past due commitments are not reported as a separate category, but under the categories specified above. The applicable risk weights are 100 per cent and 150 per cent depending on whether write-downs represent more or less than 20 per cent of the unsecured part of the assets before write-downs.

External ratings are used for foreign government risk and public administration outside Norway as well as international banks and credit institutions included in the commitment categories governments and institutions. As a main principle, a country's rating is used, based on the average of ratings from Moody's, Standard & Poor's and Fitch. If there is no rating from one of the rating agencies, the average rating from the two other agencies should be used. If there is no rating from two of the rating agencies, the rating the third agency should be used. If none of the above-mentioned rating agencies have issued a rating for the country in question, a rating from The Economist Intelligence Unit, or alternatively Euromoney or Institutional Investor is used.

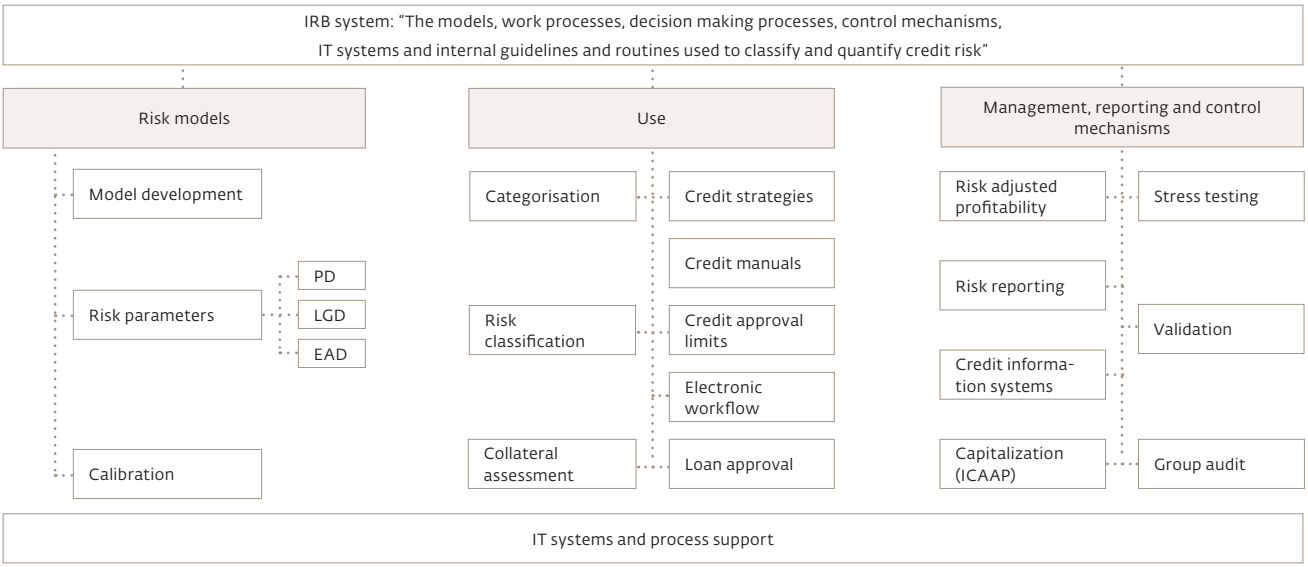
CREDIT RISK – IRB APPROACH

Estimated risk-weighted volume and capital requirements for the portfolios reported according to the IRB approach are shown in tables on pages 12 too 14.

The principle diagram below shows the extensive nature of the IRB regime. The aim is to ensure that the capital adequacy requirements for banks are adequately fulfilled. To succeed, quality and transparency must be secured throughout the value chain up until the Board of Directors' stipulation of a satisfactory level of capitalisation for operations. This value chain comprises both quantitative risk measurement systems, high-quality administrative processes generating data for the quantitative risk estimates and requirements to ensure that the organisation integrates and uses this data at all relevant organisational levels. The Group's Board of Directors assesses the capital adequacy requirement on the basis of risk measurements and an overall evaluation of external parameters and business and strategic targets. All elements in the value chain must be validated with respect to whether the authorities' requirements and internal quality requirements have been met. The validation will thus both verify the adequacy of the system and reveal improvement needs.

Use of the Group's own calculations of risk parameters in capital adequacy reporting is part of the IRB system, defined as the models, work processes, decision-making processes, control mechanisms, IT systems and internal guidelines and routines used to classify and quantify credit risk. The IRB system thus affects a major part of the Group's operations, also across business areas and support and staff units. Extensive efforts have been made over a number of years to establish the IRB system. In addition, the bank has long and extensive experience from the use of risk models and systems and maintains sound credit control. The introduction of the IRB system has contributed to better credit risk management through improved follow-up systems.

Group Audit prepares an annual IRB compliance report. The report is considered by the bank's Board of Directors. In addition, Group Audit audits the IRB system on a regular basis during the year.



CLASSIFICATION, QUANTIFICATION AND VALIDATION

Classification and quantification

The bank divides its portfolio into 10 risk categories based on the probability of default for each commitment. All credit clients are risk classified before any credit allowance. In addition, all credit exposures should be classified at least once a year. Clients that are considered to be doubtful are given risk grade 11, while exposures that are overdue more than 90 days are classified as risk grade 12. In both cases, the exposures are categorised as non-performing and assigned a probability of default of 100 per cent.

RELATIONSHIP BETWEEN RISK CATEGORIES AND PROBABILITY OF DEFAULT

	Probability of default (per cent)	
Risk class	As from	Up to
1	0.01%	0.10%
2	0.10%	0.25%
3	0.25%	0.50%
4	0.50%	0.75%
5	0.75%	1.25%
6	1.25%	2.00%
7	2.00%	3.00%
8	3.00%	5.00%
9	5.00%	8.00%
10	8.00%	40.00%
For reporting		
11		Impaired
12		Non-performing 90 days

1) For the Basel II capital calculation, the lowest permissible PD is 0.03 per cent for each risk class, excluding commitments with governments

MODELS USED FOR PORTFOLIOS WITH IRB APPROVAL AS OF 31 DECEMBER 2011

Commitment category	Customer segment	Risk models		
Residential mortgage exposure	Residential mortgage financing	PD RM Application	EAD RM	LGD RM
		PD RM Behavior		
Other Retail	Other retail exposure within DNB Finans	PD Application/ Behavior	EAD	LGD
	Qualifying Revolving Retail Exposure	PD Application	EAD QRRE	LGD QRRE
		PD Behavior		
	Limited companies with turnover < 1000 MNOK. Property companies with a balance sheet < 200 MNOK	PD SME	EAD SME/GP/SP	LGD SME/GP/SP
	General Parnterships with commitment < 50 MNOK	PD GP		
	Sole Proprietorship with commitment < 20 MNOK	PD SP		
	Limited companies with turnover < 1000 MNOK. Property companies with with a balance sheet < 200 MNOK. Exposure in DNB Finans	PD SME	EAD SME/SP	LGD SME/SP
	Sole Proprietorship with commitment < 5 MNOK. Exposure in DNB Finans	PD SP		
	Large Corporates with a turnover > 1000 MNOK	PD GC	EAD LC	LGD GC
	Shipping General Corporates (SPV's excl.)	PD SGC		LGD SGC
	Leveraged Buyouts (LBO)	PD LBO		LGD LBO

Validation

Validation is a key element in assuring the quality of DNB's IRB system. In accordance with Section 48-1 (3) of the capital adequacy regulations and DNB's validation guidelines, a validation report should be presented to the Board of Directors at least once a year as a basis for assessing whether the Group's credit risk is adequately classified and quantified.

The quantitative validation includes tests of the models' ranking power/discriminatory power, ability to determine the correct level (calibration) of risk parameters and the stability of the risk parameters.

- With respect to calibration, tests are implemented to assess whether probability of default (PD), exposure at default (EAD) and loss given default (LGD) are at the right levels. The criterion is that predicted values are consistent with observed outcomes or that the deviations are anticipated and/or acceptable. PD should reflect the average expected default rate during a business cycle. In practice, this means that the model should give a too high PD relative to observed values in good times and vice versa during less favourable periods. LGD should reflect the loss ratio during a downturn. The predicted EAD should also reflect an economic downturn if this is more conservative than the average exposure during a business cycle.
- With respect to ranking power, the PD model's ability to differentiate between "bad" customers (customers with a high probability of default) and "good" customers (customers with a low probability of default) is tested, along with its ability to make the correct ranking. A measure of explanatory power called ROC is used for the PD models, expressed in per cent. DNB's minimum explanatory power requirement is 70 per cent in the retail market and 75 per cent for corporate customers. In comparison, a random model would have a ROC of 50 per cent, while a perfect model would have had a ROC of 100 per cent. With respect to LGD models, we test the models' ability to rank loss given default by using a test with approximately the same characteristics as ROC.

In the qualitative validation, both the design of the IRB system and the IRB process are tested. When validating the design of the IRB system, the assumptions underlying the IRB models are reviewed, including the development of the classification method, data quality and the stability of the classification system. Furthermore, checks are carried out to make sure that the IRB system is used as intended. Testing of how the risk models are used in decision-making processes and external reporting is thus an important part of the qualitative validation.

Definition of non-performing commitments

A commitment should be defined as non-performing if a claim is more than 90 days overdue, the overdue

amount exceeds NOK 2 000 and the event of default is not due to delays or incidental factors on the part of the

counterparty. A commitment should also be classified as non-performing if the bank:

- due to a weakening of the counterparty's creditworthiness makes write-downs representing a not insignificant amount.
- due to a weakening of the counterparty's creditworthiness sells a claim at a reduced price and the reduction represents a not insignificant amount.
- agrees on changes in terms due to the counterparty's payment problems, and this must be considered to reduce the value of the cash flow by a not insignificant amount
- expects that debt settlement or bankruptcy proceedings will be opened against the counterparty or that the counterparty will be placed under administration
- does not expect the obligations to be met for other reasons.

The above definitions apply in both the retail and corporate markets. However, the 90-day rule applies for segments where no individual assessments are made.

Guarantees are considered to be defaulted once a claim has been made against the bank.

2) Write-downs made on the basis of portfolio analysis should not be classified as events of default.

RISK PARAMETERS VERSUS ACTUAL OUTCOME

PD-models	2008		2009		2010	
	Predicted	Observed	Predicted	Observed	Predicted	Observed
Small and medium-sized limited corporations [1]	1.83%	2.06%	1.84%	2.52%	2.22%	2.49%
One-man businesses [1]	2.33%	1.88%	2.21%	1.56%	3.62%	1.89%
General partnerships	2.60%	1.34%	1.84%	1.76%	2.41%	1.85%
Other retail – Residential mortgage financing	0.80%	0.34%	0.77%	0.46%	0.65%	0.36%
Other retail – Revolving credit					2.24%	1.70%
Other retail – Exposures within DnB NOR Finans					2.74%	1.74%
Large corporates					1.92%	0.94%

LGD-models [2]	2009		2010	
	Predicted	Observed	Predicted	Observed
Small and medium-sized limited corporations	30.40%	19.70%	31.80%	20.60%
One-man businesses	23.00%	9.10%	24.70%	9.60%
General partnerships	23.30%	8.10%	32.40%	26.30%
Other retail – Residential mortgage financing			16.40%	8.60%
Other retail – Revolving credit [3]			39.00%	33.50%
Other retail – Exposures within DnB NOR Finans			25.20%	17.90%
Large corporates			29.50%	8.80%

EAD-models	EAD-measures	2008	2009	2010
Small and medium-sized limited corporations	Observed/predicted EAD	89.30%	82.00%	77.60%
	Acceptance ratio			47.40%
One-man businesses	Observed/predicted EAD	89.30%	82.00%	77.60%
	Acceptance ratio			36.60%
General partnerships	Observed/predicted EAD	89.30%	82.00%	77.60%
Other retail – Residential mortgage financing	Observed/predicted EAD		97.80%	96.90%
	Acceptance ratio	93.40%	94.70%	93.10%
Other retail – Revolving credit	Observed/predicted EAD			95.50%
Other retail – Exposures within DnB NOR Finans	Acceptance ratio			44.10%

1) Exposures within DNB Finans included in 2010.
2) Predicted LGD is normally higher for a defaulted portfolio compared to the total portfolio. Both predicted and observed LGD above are based on defaulted exposures.
3) Predicted LGD reflects the calibration level in absence of predictions from the newly developed LGD-model implemented 2010-Q3.

Total exposure for approved IRB portfolios

The table below shows exposure at default (EAD) for the retail market and corporate portfolios according to risk category. In addition, loss ratios and conversion factors are shown, calculated according to internal models. The LGD ratio is a calculation of expected losses at default. The conversion factor (CF) indicates how much of the credit risk represents unpaid amounts on, for example, undrawn credit lines, loan commitments and guarantees. This factor is used to estimate the expected utilisation of a given limit at the time of default.

	Retail, mortgage loans					Other retail					Corporate				
	Unutilised credit lines	KF	EAD	LGD	RW	Unutilised credit lines	KF	EAD	LGD	RW	Unutilised credit lines	KF	EAD	LGD	RW
Risk class 1											60 766	67 %	59 304	31 %	14 %
Risk class 2	19 686	100 %	182 650	13 %	5 %	29 608	71 %	28 413	33 %	13 %	83 983	62 %	102 043	30 %	27 %
Risk class 3	13 095	100 %	150 505	13 %	9 %	6 291	76 %	10 048	34 %	22 %	66 157	65 %	117 783	27 %	37 %
Risk class 4	3 915	100 %	61 487	14 %	13 %	2 734	79 %	5 509	36 %	31 %	42 984	60 %	87 997	25 %	47 %
Risk class 5	4 277	100 %	77 569	14 %	19 %	2 505	77 %	5 216	35 %	38 %	44 411	62 %	128 268	27 %	59 %
Risk class 6	1 902	100 %	39 699	15 %	26 %	15 061	73 %	13 572	34 %	44 %	28 193	69 %	98 566	28 %	70 %
Risk class 7	535	100 %	15 944	16 %	38 %	964	84 %	2 410	37 %	53 %	10 977	60 %	48 742	28 %	79 %
Risk class 8	170	100 %	6 915	16 %	50 %	1 276	83 %	3 159	37 %	56 %	2 840	59 %	19 596	28 %	86 %
Risk class 9	33	100 %	1 482	16 %	63 %	339	84 %	1 258	34 %	55 %	1 268	54 %	8 351	29 %	104 %
Risk class 10	17	100 %	549	16 %	80 %	885	85 %	3 428	39 %	85 %	1 027	72 %	7 668	29 %	138 %
Risk class 11	0	100 %	51	19 %	103 %	13	75 %	83	47 %	128 %					
Risk class 12	21	100 %	2 058	20 %	122 %	244	84 %	1 393	38 %	106 %	1 032	51 %	14 366	20 %	290 %
Total/average	43 650	100 %	538 908	13,5 %	12,8 %	59 920	73,1 %	74 489	34,4 %	31,7 %	343 639	63,8 %	692 684	27,7 %	55,0 %

Actual value adjustments according to risk parameters

Expected loss estimated value adjustments compared with actual value adjustments.

DNB GROUP

	Retail, mortgage loans		Other retail		Corporates		Corporates, SL	
Amounts in NOK million	2011	2010	2011	2010	2011	2010	2011	2010
Value adjustments and write-downs	310	335	554	510	2 851	2 993	0	0
Expected loss, EL	929	838	1 012	1 030	5 019	4 772	12	7

COUNTERPARTY RISK FOR DERIVATIVES

Derivatives are traded in portfolios where balance sheet products are also traded. The market risk of the derivatives is handled, reviewed and controlled as an integral part of market risk in these portfolios. Derivatives are traded with a number of different counterparties, and most of these are also engaged in other types of business. The credit risk that arises in connection with derivative trading is included in the DNB Group's overall credit risk. For a number of counterparties, netting agreements or bilateral guarantee agreements have been entered into, thus reducing credit risk. The authorities' capital adequacy requirements take such agreements into account by reducing the capital requirement.

CSA agreements (Credit Support Annex) have been entered into with most major banks. This implies that the market value of all derivatives entered into between DNB and the counterparty is settled either daily or weekly, which implies that counterparty risk is largely eliminated. If the collateral is impaired (i.e. weaker rating) the minimum amount for the exchange of money will be reduced.

Moreover, products such as equity forward contracts, securities issues and currency trading for private individuals are monitored and margined on a daily basis.

Counterparty risk, financial derivatives	Nominal amount		Credit equivalent		Weighted amount	
Amounts in NOK million	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
Gross amount before netting	6 640 645	5 389 200	189 705	160 426	71 984	54 740
Net amount after netting	608 481	446 241	98 909	82 294	48 622	39 259

Credit derivatives used for hedging	Bought	Sold	Bought	Sold
Amount in NOK million	31 Dec. 2011	31 Dec. 2011	31 Dec. 2010	31 Dec. 2010
CDS – Credit Default Swaps	115	103	68	193
CLN – Credit Linked Notes	65	0	122	0
Total credit derivatives	180	103	190	193

INVESTMENT IN SECURITISATION

The topic is discussed in Chapter 9, Liquidity risk.

MARKET RISK

Market risk is the risk of losses or reduced future income due to fluctuations in market prices or exchange rates. The risk arises as a consequence of the bank's unhedged positions and exposure in the foreign exchange, interest rate, commodity and equity markets. The risk level reflects market price volatility and the positions taken.

A distinction is made between trading and banking activities. Trading activities include trading and positions in financial instruments, aiming to achieve a profit by capitalising on differences and fluctuations in interest rates and exchange rates, typically in a short-term perspective. Banking activities include the Group's ordinary funding and lending operations, where mismatches in fixed-rate periods for assets and liabilities represent sources of market risk. In addition, DNB also had investments in equity instruments which are included in banking activities. The portfolio of fixed income securities in DNB Markets, the majority of which are classified as held-to-maturity investments, is defined as credit risk in the internal measurement of risk-adjusted capital.

Market risk in the trading portfolio arises through trading activities in the interest rate, foreign exchange, commodity and equity markets. The risk relates partly to customer business, though there is scope for moderate risk-taking within proprietary trading in foreign exchange and financial instruments. Positions will be generated by trading in balance sheet products such as bonds and commercial paper, as well as financial derivatives such as interest rate swaps, options, forward contracts and future rate agreements. Such instruments are used to hedge positions in the trading portfolio. Hedging of positions by use of derivatives may also entail basis risk due to a mismatch between the position which is hedged and the derivative used for hedging.

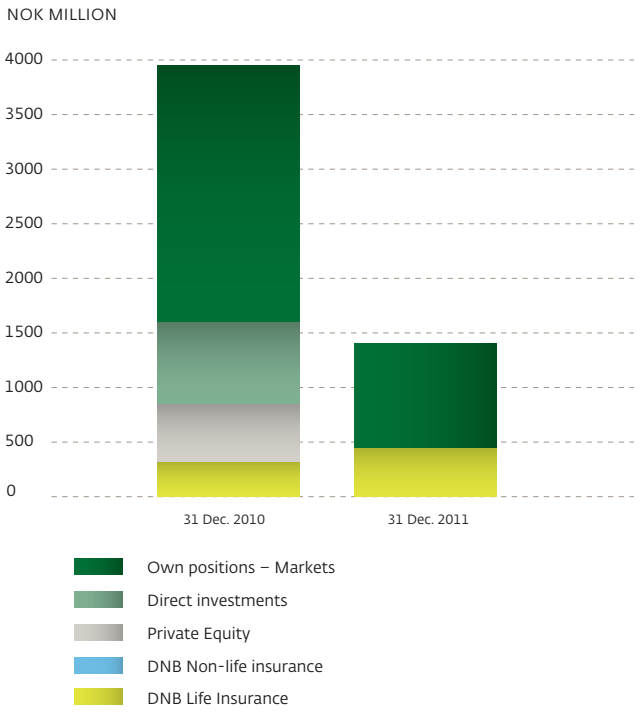
Market risk arising in DNB Livsforsikring is defined as market risk related to the ownership of the life insurance company. Due to the current regulatory framework for life insurance operations, which entail risk sharing between policyholders and the owner of the life insurance company, it is necessary to measure market risk in life insurance separately. Market risk arising in DNB Skadeforsikring is insignificant and is thus included in the insurance risk measurements.

Overall, market risk represents a small share of the Group's total risk.

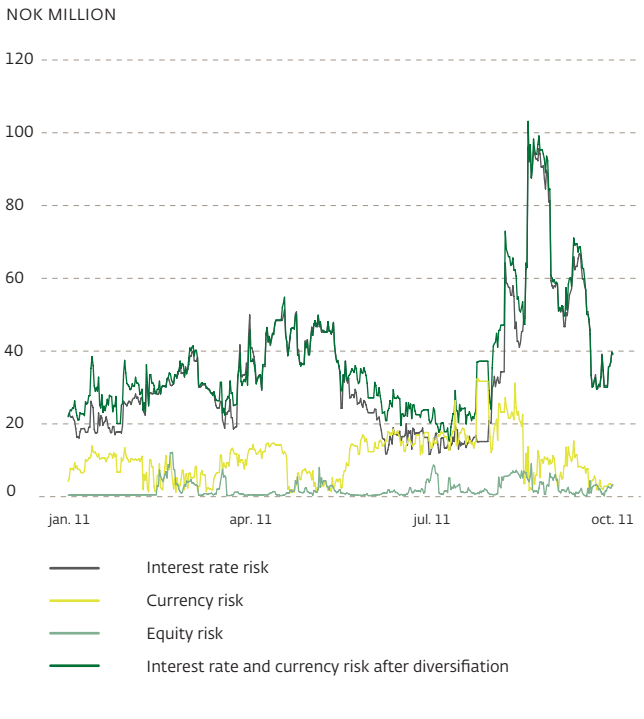
Market risk management
Limits established for the Group's market risk exposure also encompass market risk in DNB Livsforsikring and in DNB Skadeforsikring.

Responsibility for all trading activities in the DNB Bank Group rests with DNB Markets. Limits and guidelines for managing market

EQUITY EXPOSURE, DNB ASA



DAILY RISK EXPOSURE (VALUE-AT-RISK), ONE DAY HOLDING PERIOD, CONFIDENCE LEVEL 99 PER CENT



risk on trading activities are reviewed at least once a year and are determined by the Board of Directors of DNB Bank. A unit independent of brokerage operations checks positions in relation to limits and results on a daily basis. Limit utilisation is reported through the Group's risk report. Hedging activities which entail significant basis risk are subject to risk limits in line with other types of risk.

The Treasury function in the DNB Bank Group handles interest rate risk on the banking book. As for trading activities, limits and guidelines for managing market risk are reviewed by the bank's Board of Directors once a year. Principles, methods, limits and follow-ups are based on the same guidelines as trading activities, which includes daily measurement of interest rate risk. Interest rate and currency risk in the banking group is centralised, as all units in the banking group must hedge their positions through the Treasury function. DNB Baltics and Poland and DnB NOR Monchebank have their own risk limits. This ensures the quality and transparency of position-taking both locally and in the Group as a whole.

Limits for equity instruments are determined by the Board of Directors of DNB Bank ASA. The limits are reviewed at least once a year.

Primary responsibility for following up, further developing and reporting all types of investments in and purchases of equity instruments, including the monitoring of mutual fund holdings invested in through DNB Asset Management, rests with Group Investments, which is organised under Group Finance and Risk Management. The unit is part of the bank's contingency team handling non-performing commitments as it is also responsible for credit commitments where the bank takes ownership positions. Follow-ups take place on a monthly basis.

Market risk measurement

When measuring market risk, a distinction is made between measurements of risk under normal market conditions and measurements which focus on extreme market conditions.

Several tools have been established to quantify and measure the Group's total market risk exposure under normal conditions. Interest rate risk is measured as the change in value resulting from an interest rate adjustment of one basis point. Limits for foreign exchange, equity and commodity risk represent nominal amounts for individual positions. In addition, Value-at- Risk calculations are used in operational management and control in DNB Markets.

Risk measurement under extreme market conditions includes stress tests and calculations of risk-adjusted capital. Stress tests are also used to follow up non-linear instruments and interest rate risk.

Risk-adjusted capital for market risk is calculated by simulating potential losses on the basis of expected maximum exposure, liquidation periods for positions and correlations between the portfolios. Correlations are based on a stressed scenario. The liquidation period ranges from 250 trading days for equity instruments in the banking book to two trading days for positions in the most commonly traded currencies. Calculations of risk-adjusted capital distinguish between trading and banking activities.

EQUITY RISK (EQUITY POSITIONS OUTSIDE THE TRADING PORTFOLIO)

Equity risk outside the trading portfolio is handled by the Group Investments division. The investments can be divided into four categories:

- Strategic investments: Investments which are defined as strategic for the Group.
- Financial investments: Financial investments comprise venture investments in cooperation with customers. Apart from financial returns, the purpose of financial investments is to create new business opportunities for DNB. The investments are divided into categories depending on investment horizon (medium and long-term). Since the decision-making responsibility for this type of investments rests with the business units, the investments are subject to limits which are determined on an annual basis.
- Credit portfolio: The credit portfolio comprises holdings in companies which have defaulted on their obligations to the bank. The purpose of the portfolio is to secure the value of repossessed assets until they are sold.
- Property portfolio: The property portfolio comprises properties and property projects taken over by DNB in consequence of default. The purpose of the portfolio is to secure the value of repossessed properties until they are sold.

Limits for the investment category financial investments are determined by the bank's Board of Directors each year. Due to their characteristics, there are no limits for the other categories. Equity exposure is measured and reported to the head of Group Investments on a monthly basis by the division's Internal Control department.

Exposure to limits and market risk is measured based on the investments' market value plus any future committed amounts. With respect to derivatives, risk exposure is measured as the equivalent exposure in the underlying instruments. Guarantees for share issues and secondary investments in the equity markets are included in full in the limit utilisation. Shares in subsidiaries and associated companies are not included, as they are consolidated in full or in part in the accounts.

Accounting principles

Shareholdings are classified as shareholdings in the trading portfolio or as shareholdings and mutual funds designated as at fair value. As at 31 December 2010 and 2011, none of the Group's shareholdings were classified as available for sale.

Investments in shares are measured at fair value. Changes in value of shareholdings are recorded under "Net gains on financial instruments at fair value".

Measurement

Financial instruments measured at fair value are according to IFRS 7 required to be classified in a three level hierarchy by reference to the inputs used in the valuation: quoted prices from active markets, observable market data and inputs not based on observable market data.

Valuation based on prices in an active market – level 1
Classified as level 1 are financial instruments valued by using quoted prices in active markets for identical assets or liabilities. Instruments in this category include listed shares.

Valuation based on observable market data – level 2
Classified as level 2 are financial instruments which are valued by using inputs other than quoted prices, but where prices are directly or indirectly observable for the assets or liabilities, including quoted prices in nonactive markets for identical assets or liabilities.

Valuation based on other than observable market data – level 3
Equities which are classified as level 3 essentially comprise property funds, limited partnership units, private equity investments, as well as hedge fund units and investments in unlisted equities.

The table below specifies the equity positions reported in the Group's capital adequacy calculations.

	DNB Group excluding DNB Livsforsikring	
Amount in NOK million	31 Dec. 2011	31 Dec. 2010
Financial institutions	2	2
Norwegian companies [1)]	851	929
Companies based abroad	1 774	1 971
Mutual funds [2)]	872	1 658
Shareholdings, designated as at fair value	3 501	4 561
Net gains on shareholdings, designated as at fair value	(11)	624
1) Of which: Exchange traded	*39*	*149*
2) Of which.: Investments in Private Equity	*409*	*378*

INTEREST RATE RISK OUTSIDE THE TRADING PORTFOLIO

Interest rate risk outside the trading portfolio arises through traditional banking activities such as customer lending and deposits, stemming from differences in fixed-rate periods for assets and liabilities, including fixed-rate loans and fixed-rate deposits. Interest rate risk from loans and deposits is based on contractual maturities. Interest rate risk outside the trading portfolio includes NOK denominated securities in the Treasury's portfolio and the bank's debt denominated in NOK. Derivatives and interest rate swaps, future rate agreements (FRAs) and futures are used to hedge interest rate risk.

Interest rate and currency risk in the banking group is centralised, whereby all units in the banking group, with the exception of Bank Baltics and Poland and DnB NOR Monchebank, must hedge their positions through the Treasury function. Bank Baltics and Poland and DnB NOR Monchebank have their own risk limits. The limits for interest rate risk represent changes in value resulting from an interest rate adjustment of one basis point. Interest rate risk is measured and reported to the Treasury every day, to the head of DNB Markets once a week and to the group chief executive/ALCO (Asset and Liability Committee) once a month. Limits for interest rate risk are review by the bank's Board of Directors every year.

The table shows changes in income during the year resulting from interest rate risk outside the trading portfolio, as well as unrealised gains or losses as at year-end.

	Change income		Unrealised gian/loss	
Amounts in NOK million	31 Dec. 2011	31 Dec. 2010	31 Dec. 2011	31 Dec. 2010
NOK	587	(1 868)	(590)	(1 177)
EUR	(13)	111	98	111
SEK	(17)		(17)	
TOTAL	557	(1 757)	(509)	(1 066)

MARKET RISK IN LIFE INSURANCE

Market risk in life insurance is the risk that the return on financial assets will not be sufficient to meet the obligations specified in insurance policies. In addition, management of the corporate portfolio also entails market risk.

According to current parameters for life insurance operations in Norway, DNB Livsforsikring carries the risk of fulfilling the company's commitments in contracts with policyholders. The return on financial assets must be sufficient to meet the guaranteed annual return to the company's policyholders. If this is not the case, additional allocations will have to be used, representing buffer capital built up from profits in previous years. Alternatively, the shortfall could be charged to equity. Market risk in life insurance is the chief risk category in DNB Livsforsikring.

Management of market risk in life insurance

Risk management in DNB Livsforsikring is part of the company's strategy, which has been approved by the Board of Directors. Through regular assessments by the Group's Asset and Liability Committee, ALCO, the risk situation in DNB Livsforsikring is reviewed relative to the Group's overall risk profile. DNB Livsforsikring's chief executive and Board of Directors are to help ensure that DNB Livsforsikring's strategy and risk management are consistent with the DNB Group's risk profile. The Risk Analysis and Control unit is organised independent of the company's financial management and business areas and is responsible for reporting, monitoring and follow-up of the company's total risk. The unit regularly prepares a risk report for the company's management and Board of Directors.

Risk reports to DNB Livsforsikring's management and Board of Directors include stress tests and sensitivity tests to enable continual monitoring of the company's total risk. The Risk Analysis and Control unit oversees financial market developments on a daily basis and issues weekly reports on the level of risk relative to the risk limit for asset management. Compliance with laws and regulations and internal guidelines is reported monthly.

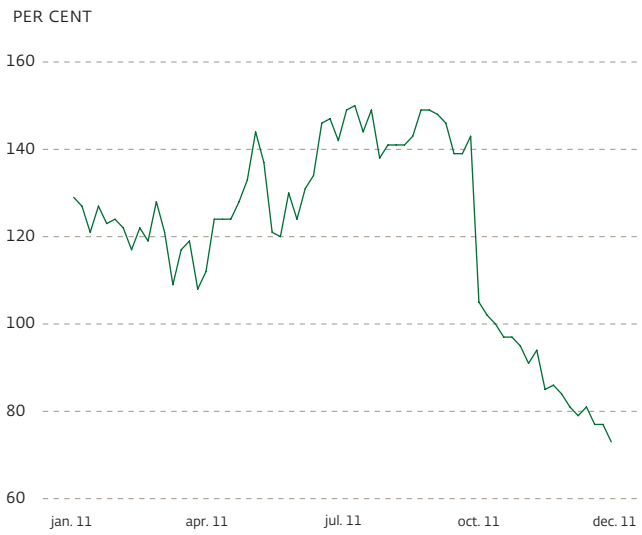
The asset management strategy aims to reduce earnings fluctuations. In order to comply with the need for minimum diversification, limits have been set for each asset class. The limits also restrict concentration risk relative to individual issuers. Separate limits have been established for derivatives within asset management. All asset management limits are determined each year by the Boards of Directors of DNB ASA and DNB Livsforsikring.

Solvency II

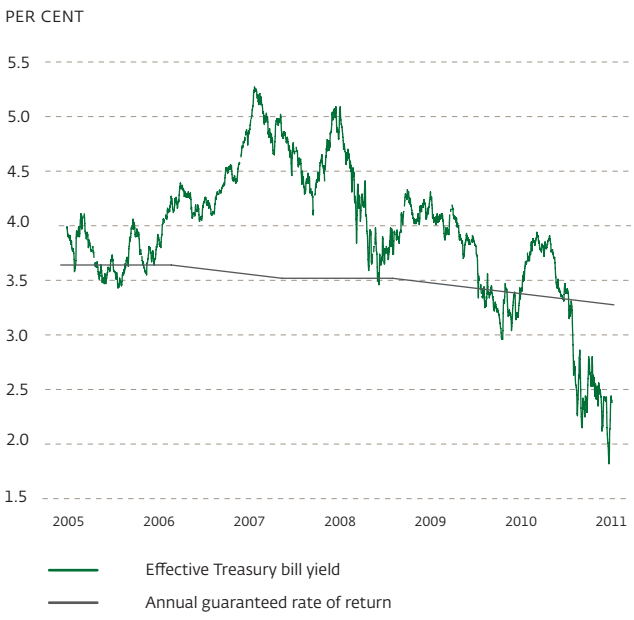
Solvency II are new EU regulations which, among other things, will replace the current minimum requirements for capital adequacy and solvency margin. The framework directive was approved in May 2009, and final implementation in national regulations is scheduled to take place by 1 January 2013. Due to a general transitional scheme, the capital requirements will not enter into force until 1 January 2014. A good dialogue has been established with the authorities and industry bodies to ensure an expedient adaptation of the new regulations until they enter into force.

The regulations are based on the same structure as Basel II, with three pillars. This means that in addition to minimum capital requirements, Solvency II will also include qualitative requirements regarding operational and risk management, the internal capital adequacy assessment process and more stringent external reporting requirements. The new requirements will be more risk-sensitive and ensure better insight into insurance companies' actual risk profiles.

DEVELOPMENT IN INVESTMENT RISK – MEASURED WEEKLY



DEVELOPMENT IN ANNUAL GUARANTEED RATE OF RETUR AND 10-YEAR TREASURY BILL YIELD



DNB Livsforsikring has participated in the quantitative studies implemented for the European insurance industry. DNB Livsforsikring has implemented a Solvency II programme to ensure that the company will meet the requirements on the implementation date. A Risk Management section was established in the autumn of 2011 in order to transfer the Solvency II programme to an operational unit.

Measurement of market risk in life insurance

Measurement of market risk in DNB Livsforsikring includes stress tests and sensitivity analyses. The internally developed stress test calculates the total loss potential for market, insurance, credit, operational and business risk. When determining the overall investment risk tolerance, this loss potential is measured against the company's buffer capital in excess of the regulatory requirement. This method is also used as a basis for measuring and determining the limit for market and credit risk in asset management. Calculations of the loss potential associated with market and credit risk include stress tests for equity, interest rate, property, spread and counterparty risk, respectively.

Sensitivity analyses have been established which estimate the change in value and effects on profits of a 20 per cent fall in equity prices, a 1.5 percentage point rise in interest rates and a 12 per cent reduction in property prices. The sensitivity analyses are carried out separately.

Risk-adjusted capital reflects the ownership risk associated with the DNB Group, as owner of the life insurance company, having to report a net loss from these operations and possibly being required to inject new equity. In the calculations of risk-adjusted capital, developments in the value of the insurance company's financial assets are simulated. In the simulations, a distinction is made between policyholders' funds and company funds, whereby the company's capital is managed separately at the owner's expense and risk. Value developments are simulated on a daily basis for all portfolios, taking account of the level of correlation between the sub-portfolios. The values are tested against limits which indicate when DNB will have to record losses. These limits are affected by the securities adjustment reserve, interim profits, additional allocations and the guaranteed rate of return. The calculations also include the effect of a possible rebalancing of the portfolio, i.e. dynamic adaptation of risk.

INSURANCE RISK

Insurance risk in DNB comprises insurance risk in DNB Livsforsikring and risk in DNB Skadeforsikring.

Insurance risk in life insurance is the risk related to changes in future insurance payments due to changes in life expectancy and disability rates.

Risk in DNB Skadeforsikring includes insurance, market, credit, operational and business risk. Insurance risk is the risk of losses if insurance premiums fail to cover future claims payments. The non-life insurance company is exposed to market and credit risk in investment operations, and reassurance agreements encompass credit risk. However, based on the current business model for DNB Skadeforsikring, these risk categories are of little significance compared with pure insurance risk.

Management of insurance risk

In 2010, DNB Livsforsikring worked out a special strategy for insurance risk management, which includes the scope and type of reassurance contracts to be entered into and measures to meet higher life expectancy. The risk results are periodically monitored, and in the longer term, developments will be reflected in prices, products and market strategies. DNB Skadeforsikring's Board of Directors has established a strategy and principal guidelines for market and insurance risk, including the premises for the company's reinsurance hedging. Through the reassurance programme, the total risk is geared to the capital base. The reassurance programme also contributes to profit equalisation by hedging catastrophe risk. Credit and market risk is managed through the investment plan, which is considered by the company's Asset and Liability Committee and Board of Directors once a year. Insurance risk in DNB Skadeforsikring is continually monitored by tracking profitability on all products. In addition, the claims reserve is reviewed on a quarterly basis.

Measurement of insurance risk

Risk-adjusted capital for insurance risk in life insurance is measured as the potential need to strengthen insurance provisions due to changes in life expectancy, mortality and disability. Risk-adjusted capital for non-life insurance risk is measured on the basis of Finanstilsynet's stress test for calculating total risk and is also calibrated against DNB's confidence level.

OPERATIONAL RISK

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk is a consequence of DNB's operations.

Operational risk management
The Board of Directors has laid down a policy for the management of operational risk in the Group. Operational risk should be low, and risk management should ensure that the risk of unwanted losses is reduced.

All managers are responsible for knowing and managing operational risk within their own area of responsibility. This is to be ensured through risk assessments of everyday operations, of all major changes in operations as well as of particularly critical functions. When a need for improvement measures is identified, special follow-ups are initiated. In order to limit the consequences of serious events, operational disruptions etc., comprehensive contingency and business continuity plans have been drawn up to be able to handle a crisis situation in a rational and effective manner, thus contributing to limiting damage and restoring a normal situation.

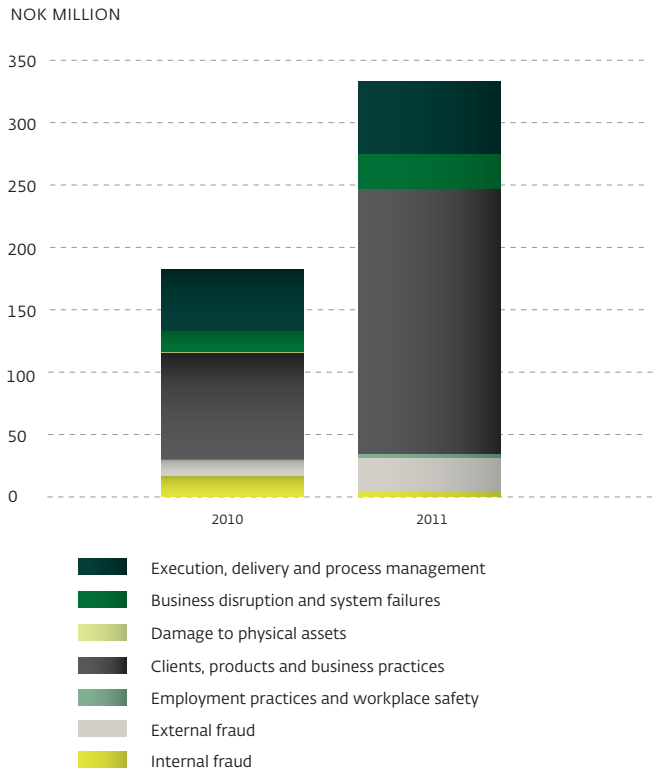
In all business areas, special groups have been established to support management in managing operational risk.

Responsibilities include assessing and reporting identified risks and helping to prevent operational losses. To ensure independence relative to business operations, these persons are organised in the business areas' respective staff units. Their work also includes making sure that operations are in compliance with relevant laws and regulations. All reporting is a two-way process, both through the line organisation and through the Group's central risk unit. Operational risk management and compliance at group level is organised in a separate unit within Group Risk Management, which is organised under the staff area Group Finance and Risk Management.

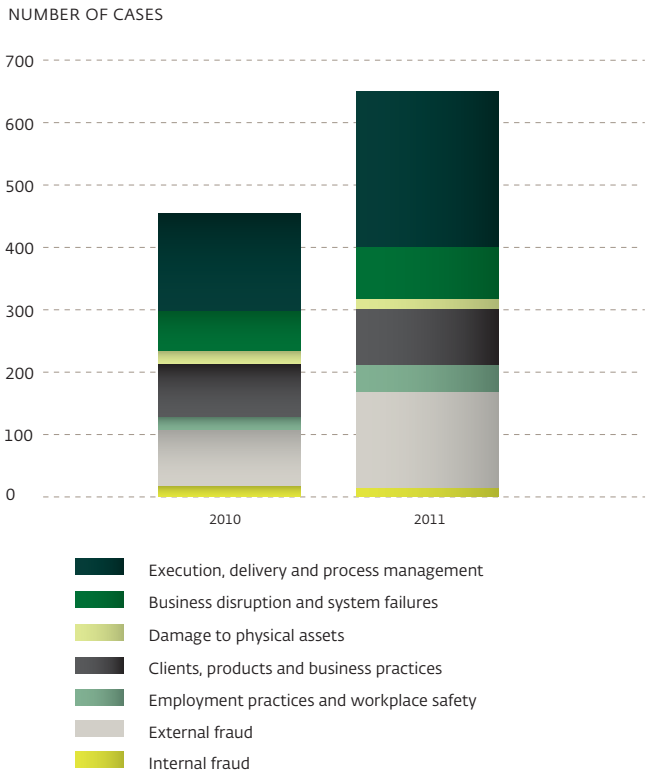
The Group's insurance coverage is an element in operational risk management. Insurance contracts are entered into to limit the financial consequences of undesirable events which occur in spite of established security routines and other risk-mitigating measures. The insurance programme also covers legal liabilities the Group may face related to its operations, The insurance programme is cost-effective and primarily aims to cover serious loss events in line with the Group's insurance policy

Operational risk measurement
Operational loss events in the Group which result in losses of more than NOK 50 000 and near-events with a loss potential of more

OPERATIONAL LOSSES ACCORDING TO CATEGORY



OPERATIONAL LOSSES, NUMBER OF CASES PER CATEGORY



than NOK 100 000 are registered, reported and followed up on an ongoing basis in the Group's event database. Information about perational risk and loss events in the Group is provided in the Group's risk report. Undesirable events which cause, or could have caused, financial losses for the Group, represent valuable information and learning about necessary improvement needs. As from 2011 the Group is a member in an external database, Operational Risk Exchange, ORX, which will ensure access to external events which will strengthen the work on operational risk management.

The Board of Directors is kept updated on the status of operational risk through the Group's periodic risk report, which provides a basis for analysing the risk situation and for considering the capitalisation of the Group. In addition, the Board of Directors is kept updated on the Group's operational risk in the annual status report on ongoing management and control of operational and business risk. The status report includes a presentation of key group-wide risks, relevant improvement measures and a detailed qualitative assessment based on the Group's ambitions within key areas for risk management and quality assurance. The conclusion in the report for 2010 was that the Group's operational risk was at a satisfactory level and that operations, management and control were of high quality.

Risk-adjusted capital for operational risk is calculated based on external capital requirements, where income and the type of business operations are the drivers for capital volumes, and is adjusted upward to reflect DNB's risk tolerance. DNB is qualified for using the standardised approach for operational risk.

BUSINESS RISK

Business risk is the risk of losses due to external factors such as the market situation or government regulations. Such risk includes loss of income due to a weakened reputation.

Business risk is manifested in an unexpected decline in profits. Such a decline can be caused by competitive conditions resulting in lower volumes and pressure on prices, competitors introducing new products, government regulations or negative media coverage. Losses arise if the Group fails to adapt its cost base to such changes.

Negative media coverage may be a consequence of other risk factors, but is handled as business risk in DNB. A damaged reputation can have an adverse impact on all business areas, independent of where in the Group or in the rest of the financial industry the original incident occurred.

Business risk management and measurement
Sound strategic planning is instrumental in reducing business risk. The Group's active commitment to corporate social responsibility and the code of ethics for employees also have a positive impact on business risk.

Reputational risk is managed through policies and business activities, including compliance. Reputational risk is followed up by monitoring media coverage, while the competitive situation is followed up by analysing market trends and developments in market shares.

The Group has developed a model for calculating business risk per business area. The model is based on past fluctuations in income and costs and is structured so that if all other factors are kept constant, high income volatility raises the risk level and thus risk-adjusted capital. Vice versa, a highly flexible cost structure will reduce risk-adjusted capital.

See also chapter 10, new regulatory framework.

LIQUIDITY RISK

Liquidity risk is the risk that the Group will be unable to meet its obligations as they fall due, and risk that the Group will be unable to meet its liquidity obligations without a substantial rise in appurtenant costs. In a broader perspective, liquidity risk also includes the risk that the Group will be unable to finance increases in assets as its funding requirements rise.

Risk profile

In line with the bank's other operations, liquidity risk should be low and promote the bank's financial strength and ability to withstand various events and developments. This implies that the bank should seek to have a balance sheet structure that reflects the liquidity profile of an international bank with an Aa level long-term credit rating from recognised rating agencies.

Liquidity risk management

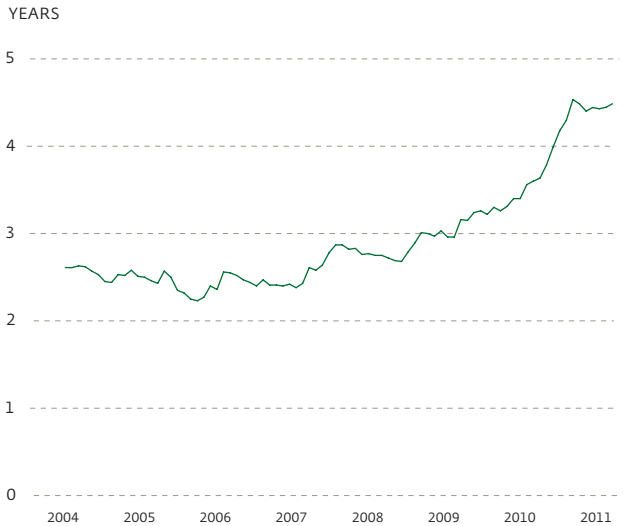
The Board of Directors regularly reviews the bank's liquidity risk and determines limits and guidelines. The Board reviews the limits each year, or more frequently if required.

The bank's liquidity management is organised based on a clear authorisation and reporting structure. In accordance with the regulations on prudent liquidity management, the bank makes a distinction between premise-setting and performing units. The premise-setting units are generally organised in the group staff unit and report to the CFO, while the performing units are organised in Markets and report to the head of Markets.

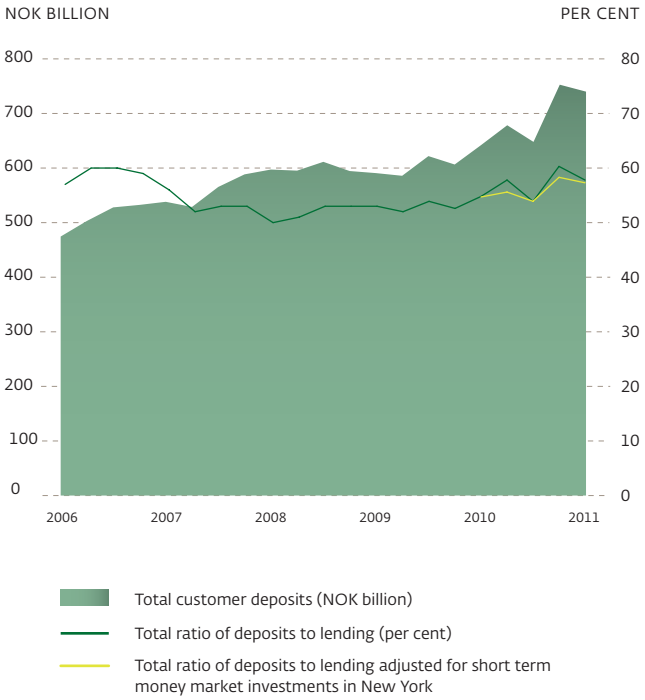
Group Finance and Risk Management has assigned responsibility for determining principles and limits for liquidity management to the Asset and Liability Management unit and responsibility for long-term funding to the IR/Long-term Funding unit. The Treasury function is responsible for modifying the Group's total short-term liquidity risk and for ensuring that liquidity requirements are within the short-term limits established by the Board of Directors. The unit also has operative responsibility for long-term bond debt in Norwegian kroner. The Asset and Liability Committee, ALCO, is the advisory body for DNB's CFO with respect to principles and methods for liquidity risk measurement.

Overall liquidity management in the DNB Bank Group is based on DNB Bank ASA providing funding for subsidiaries such as Nordlandsbanken and international branches and subsidiaries. Liquidity risk is managed through both short-term limits which restrict the net refinancing requirement within one week and one month, along with a long-term management target which specifies the share of lending to be financed by customer deposits or funding with a residual maturity of minimum 12 months. Liquidity risk

AVERAGE TERM TO MATURITY FOR THE BOND PORTFOLIO, SENIOR DEBT AND COVERED BONDS



CUSTOMER DEPOSITS AND RATIO OF DEPOSITS TO LENDING



limits reduce the bank's dependence on short-term funding from the money and capital markets in Norway and abroad. The limits have been established as funding from such sources is generally more unstable than ordinary deposits. See the paragraph on liquidity risk measurement below regarding changes in the limit structure.

Liquidity management in DNB implies maintaining a broad deposit and funding base, representing both retail and corporate customers, along with diversified funding of other operations. As an element in this strategy, a number of funding programmes have been established in different markets.

Senior debt is mainly issued through the European Medium Term Note programme of Euro 45 billion. In 2011, a senior program was established in the Japanese JPY. DNB has a commercial paper programme in USA and Europe of USD 18 billion and Euro 10 billion. The short-term funding sources are further diversified through a so-called Yankee CD programme for USD 12 billion, where commercial paper are issued by DNB's New York branch. The bank also has a European Medium Term Note Programme of EUR 45 billion and a USD 8 billion long-term funding programme in the US market. In addition, debt programs are established in the covered bonds market, in Europe, the US and in Australia

An important instrument for long-term funding is the issue of covered bonds. The bonds are issued by the bank's subsidiaries DNB Boligkreditt AS and DNB Næringskreditt AS, and are secured by the companies' home mortgage and commercial mortgage portfolios, respectively. During the financial market turmoil, covered bonds proved to be a more robust and considerably lower priced funding instrument than ordinary bonds. Over the next few years, DNB will thus seek to cover a large share of its long-term funding requirement through the issue of covered bonds.

As an element in ongoing liquidity management, DNB Bank needs to have a holding of securities that can be used in various ways to regulate the Group's liquidity requirements and serve as collateral for operations in the main currencies in which the bank is active. The securities are used, among other things, as collateral for short-term loans in a number of central banks and serve as liquidity buffers to fulfil regulatory requirements. The bank has chosen to meet its need for liquid securities by holding international bonds of superior credit quality.

DNB gives priority to maintaining sound business relations with a large number of international investors and banks and to promoting the Group in international capital markets.

Liquidity risk measurement

Liquidity risk is managed and measured using various measurement techniques, as no single technique can quantify this type of risk. The techniques include monitoring refinancing needs, balance sheet key ratios, average residual maturity and future funding requirements. DNB also uses stress testing, simulating the liquidity effect of a downgrading of the bank's international credit rating following one or more negative events. The results of such stress testing are included in the banking group's contingency plan for liquidity management during a financial crisis.

The refinancing requirement limits reflect that the bank should be self-sufficient with regard to liquidity for a minimum period of one month in an acute situation. The limit for structural liquidity risk implies that minimum 90 per cent of lending to the general public should be financed through customer deposits, long-term funding and primary capital.

With effect from 2012, the limit structure for liquidity risk will be changed to ensure that it is consistent with the structure in the Basel III regulations. Short-term and long-term liquidity risk limits are measured by the new international standards, Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR). The observation periods will ensure a gradual adaptation to the minimum requirements within the deadlines, as described by the Basel Committee.

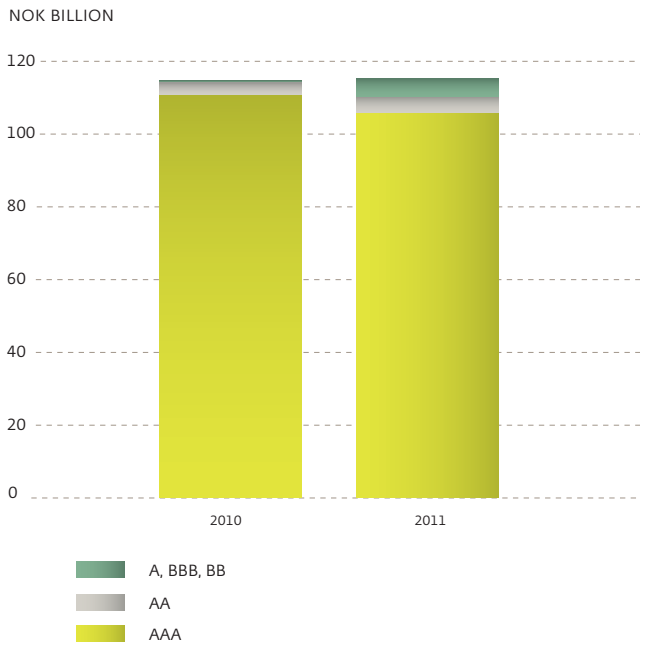
Parallel to this, the limit structure will be extended, whereby there will also be short-term limits for one week and three months, in addition to the LCR, which has a time horizon of one month. The short-term and long-term limits apply for each main currency and in total.

The bank regularly reviews the premises underlying liquidity management. This includes considering whether assets which are classified as liquid, may be realised or used as collateral in accordance with the underlying premises, and to what extent assumptions regarding stable funding are realistic in a bank-specific crisis or in a deteriorating market.

Liquidity portfolio

The liquidity portfolio is used to regulate the Group's need for liquidity and as a basis for collateral for liquidity operations in various currencies. Among other things, the securities are used as collateral for short-term and long-term loans in a number of

INTERNATIONAL BOND PORTFOLIO AT THE END OF 2010 AND 2011



central banks and serve as liquidity buffers to fulfil regulatory requirements. A major part of the international liquidity portfolio is classified as "hold-to-maturity, is carried at amortised cost and will be subject to impairment if there is objective evidence of a decrease in value. With effect from 2011, however, new investments in securities which have been approved for use in LCR calculation will be recorded as part of the trading portfolio. At year-end 2011, this international liquidity portfolio totalled NOK 115.3 billion.

The Norwegian liquidity portfolio mainly comprises Norwegian Treasury bills and totalled NOK 66.2 billion at year-end 2011.

More about the "hold-to-maturity" portfolio

As at 31 December 2011, the portfolio represented NOK 95 billion. 90 per cent of the securities in the portfolio had an AAA rating, while 4.7 per cent were rated AA. There were no synthetic securities in the portfolio and no investments in US sub-prime bonds or Collateralised Debt Obligations, CDOs. The average maturity of DNB Markets' liquidity portfolio is 3 years, and the change in value resulting from an interest rate adjustment of one basis point was NOK 29 million at end-December 2011. The structure of the portfolio at year-end 2011 is shown below.

DNB GROUP

	Per cent 31 Dec. 2011	NOK billion 31 Dec. 2011	Per cent 31 Dec. 2010	NOK billion 31 Dec. 2010
Asset class				
Consumer credit	1	1 019	2	2 190
Residential mortgages	60	58 067	64	73 387
Corporate loans	1	1 247	2	2 578
Government-related	37	35 663	31	35 909
Total international bond portfolio DNB Markets, nominal values	100	95 996	100	114 064
Accrued interest, including amortisation effects		(934)		(1 497)
Total internatioal bond portfolio DNB Markets, held to maturity	**100**	**95 062**	**100**	**112 567**

In the capital adequacy calculations this portfolio is reported as an investment in securitisation. From the third quarter of 2010 the portfolio has been reported according to the IRB approach.

DNB GROUP

Amounts as at 31 December 2011	NOK millions	Risk weight	Factor	NOK million RWA
Rating				
AAA	85 415	7 %	1,06	6 338
AA	4 516	8 %	1,06	383
A	2 816	12 %	1,06	358
BBB	2 144	60 %	1,06	1 364
BB	147	425 %	1,06	664
	24	1250 %	–	296
Total	**95 062**			**9 402**

NEW REGULATORY FRAMEWORK

Over the last few years, a number of new regulations and requirements for the financial services industry have been introduced or announced. They have different backgrounds, but a common factor is that they will have serious financial consequences for the industry.

The changes are so extensive that they will have a profound impact on how the institutions will have to organise important parts of their operations. In addition, they will increase costs, both because the regulations in themselves will entail higher costs and because compliance with the regulations will be more complicated and require additional resources.

The most far-reaching requirements arise from the financial crisis and reflect the supervisory authorities' ambitions to strengthen the capital adequacy, liquidity and funding of financial institutions. Other requirements derive from changes in international accounting rules. In addition, changes have been proposed to the taxation of financial institutions, which will affect their profitability and product pricing. The framework conditions need to be balanced in order to be able to offer customers good and relevant products in a financially sustainable manner. It is vital that the introduction of such changes is transparent, thus enabling investors, customers and other stakeholders to understand the effects of the regulations. Moreover, it is critical that changes in the individual countries are implemented in step with international developments to ensure uniform framework conditions and equal competitive terms.

CAPITAL REQUIREMENTS DIRECTIVE, CRD IV

On 20 July 2011, the European Commission launched its proposal for new regulations for credit institutions and investment firms, CRD IV, which is based on the Basel Committee's recommendations from December 2010 on new and stricter capital and liquidity standards, Basel III. CRD IV is intended to apply to all banks and investment firms within the EEA. Even though the draft regulations are aimed at ensuring optimal harmonisation within the EU, scope is given for a certain level of national discretion. For example, national authorities will be given the opportunity to adjust the risk weighting of commitments secured by real estate, determine counter-cyclical capital buffers, introduce additional buffer requirements and opt for an early introduction of the capital adequacy requirements.

The draft proposal has been submitted to the EU for further consideration and must be approved by the European Council and the EU Parliament before becoming final legislation. The draft proposal will follow the implementation plan proposed by the Basel Committee, whereby it will enter into force on 1 January 2013 and be fully implemented by 1 January 2019.

In Norway, the regulations will apply to all financial institutions, also those that are not credit institutions, and to financial services groups. Finanstilsynet (the Financial Supervisory Authority of Norway) has prepared a consultation paper to the Ministry of Finance, proposing legislative amendments due to enter into force on 1 January 2013.

Liquidity requirements for banks

The Basel Committee has proposed new liquidity requirements for banks: a short-term requirement, Liquidity Coverage Ratio, LCR, and a long-term requirement, Net Stable Funding Ratio, NSFR. The LCR requires that banks hold sufficient eligible liquid assets to cover, as a minimum, total net payments over a 30-day period. Net payments reflect key stress assumptions, such as the loss of deposits from customers, public entities and central banks. This requirement must be met by 1 January 2015.

The NSFR requires banks to have an amount of stable funding (12-month horizon) which, as a minimum, corresponds to the so-called "required amount of stable funding". Banks are thus required to use stable funding to finance their assets, such as loans and securities. Stable funding is defined as deposits and funding with residual maturities of 12 months or longer. There are weighting rules for both assets and deposits which reflect the items' liquidity characteristics. According to the proposal, the NSFR requirements must be met by 1 January 2018.

Uncertainty still prevails regarding the final details in the new liquidity requirements, and observation periods have therefore been established to prevent unintended consequences from the regulations. In order to help reduce market uncertainty, the Basel Committee has announced that LCR modifications and specifications will be published in 2012. The updates will apply to the criteria for eligible liquid assets, stress assumptions relating to cash flows, and a description of how the banks can use the liquidity buffer in times of stress. With respect to the NSFR, the Basel Committee is still in constructive dialogue with the financial sector regarding the details, based on facts and analyses.

Capital adequacy requirements for banks

The proposed new capital adequacy requirements imply that the minimum common equity Tier 1 requirement will be increased to 4.5 per cent. In addition, there will be a 2.5 per cent capital conservation buffer which in practice will be regarded as part of the minimum requirement. The total minimum common equity Tier 1 requirement will thus be 7 per cent. Common equity Tier 1 capital must be fully loss absorbing and can only consist of common share capital or retained earnings. The minimum capital adequacy requirement will be increased from 8 to 10.5 per cent, of which minimum 8.5 per cent must represent Tier 1 capital and Tier 2 capital can represent maximum 2 per cent. Furthermore, up to 1.5 per cent of Tier 1 capital may consist of hybrid capital. Under Basel III, there are much stricter requirements governing the actual loss absorbing capacity of hybrid capital than under the current regulatory framework. In addition, a counter-cyclical capital element will be introduced, ranging between 0 and 2.5 per cent. This element should consist exclusively of common equity

Tier 1 capital, and the size of the buffer will be determined by the national supervisory authorities. The total common equity Tier 1 requirement will thus range between 7 and 9.5 per cent. With respect to systemically important banks, additional capital buffers will probably be required. The G20 countries have agreed on an additional buffer of between 1 and 2.5 per cent of common equity Tier 1 capital for global systemically important banks. Corresponding supplementary requirements are expected to be incorporated in the EU's rules for domestic systemically important banks. The capital adequacy requirements will be phased in from 1 January 2013 and be fully implemented no later than 1 January 2019. The proposed EU directive opens up for introducing the requirements more quickly than recommended by the Basel Committee.

As a supplement to the risk-weighted capital requirements and as a measure to counter creative adjustments and gaps in the regulations, a non-risk based capital requirement, "leverage ratio", will also be introduced. This requirement implies that Tier 1 capital must be minimum 3 per cent of the total of balance sheet items and off-balance sheet risk exposure. Off-balance sheet items are converted to on-balance sheet items according to further specified rules. Public reporting of the non-risk based capital requirement is expected to start on 1 January 2015 and may become a binding minimum requirement on a level with the capital adequacy requirements with effect from 2018.

Temporary, stricter capitalisation requirement for banks
On account of the European sovereign debt crisis, the European Banking Authority, EBA, published an additional plan for the recapitalisation of European banks in October 2011 to increase confidence in the European banking system. Banks are required to hold common equity Tier 1 capital of minimum 9 per cent after any adjustments for latent sovereign debt write-downs. As opposed to the supervisory authorities in Sweden and Denmark, Finanstilsynet has chosen to use the Basel II transitional rules, which set a floor for how low a bank's risk-weighted volume can be relative to the Basel I rules, the so-called "80 per cent floor". Banks in Sweden and Denmark are thus not subject to any recapitalisation requirement, which they would have been if the Norwegian calculation method had been used.

In the fourth quarter of 2011, the Swedish authorities launched a special initiative for the national implementation of Basel III and CRD IV. Based on the IRB approach for determining risk-adjusted volume, large Swedish banks will be required to have a common equity Tier 1 capital ratio of 10 per cent from 1 January 2013, increasing to 12 per cent from 1 January 2015. This means that the Swedish authorities are opting for a 3 per cent (5 per cent from 2015) increase in the minimum common equity Tier 1 capital requirements for systemically important banks, but will consider other solutions if this will not be consistent with EU legislation.

Different requirements and measurement rules in the Nordic region make it difficult to communicate financial strength and capital adequacy to the international capital market, which frequently regards the Nordic region as one and the same market. It is a paradox that stricter national rules for determining risk-weighted volume could result in Norwegian banks appearing to be less sound and have negative consequences for ratings and the price of market funding.

DNB is of the opinion that there should be equal framework conditions for competition in the market and urges the Norwegian authorities to work for optimal harmonisation in line with the intentions behind the new regulatory framework for the EEA. It is positive that the Basel Committee supports a harmonised international implementation of the Basel regulations. A possible tool in this connection will be the publication of peer reviews showing how the individual countries implement the rules, using the measurement of risk-weighted assets to demonstrate the need for consistency to avoid the distortion of competition. The first reviews will be published during the first quarter of 2012 and will encompass the EU countries plus Japan and the US. DNB encourages the Norwegian authorities to participate in these processes.

IMPROVED WINDING-UP AND CRISIS SOLUTIONS FOR BANKS

The financial crisis demonstrated the need for better solutions for the winding-up and restructuring of banks. In line with recommendations from the Basel Committee, the EU has announced a future directive on this subject. A draft directive was circulated for comments in 2011. The intention is to facilitate the winding-up of even the largest banks without an injection of government funds. It should be possible to ensure the continuity of systemically important functions through the recapitalisation of the entire or parts of a bank by writing down or converting into share capital the bank's subordinated loans and unsecured senior debt. The authorities will be given extensive powers to restructure banks which are considered to be "non-viable".

IMPORTANT IFRS AMENDMENTS

A number of new International Financial Reporting Standards, IFRSs, must be expected to be introduced over the coming years. Some of the standards have already been approved by standard-setting bodies, as described under Accounting principles to the annual accounts, item 21 Approved standards and interpretations that have not entered into force. The amendments are expected to become effective for Norway after being considered by the EU Commission and the Norwegian authorities. Some of the new accounting requirements ensue from a wish for improvements expressed in the wake of the financial crisis, while others are based on other improvement initiatives, not least in connection with the convergence between IFRS and US GAAP.

Future amendments which are expected to have the most pronounced impact on the Norwegian financial market are new accounting requirements for the assessment of loans and new accounting requirements for insurance contracts. In addition, the IASB has issued amendments to IAS 19 Employee Benefits which will affect the accounting treatment and presentation of defined benefit pension schemes.

New accounting requirements for the assessment of loan losses
The International Accounting Standards Board, IASB, a standard-setting body, has drawn up an exposure draft for the assessment of credit losses, issued in November 2009. At end-January 2011,

the IASB and the US Financial Accounting Standards Board, FASB, published a supplement to the original exposure draft on an impairment model for financial assets measured at amortised cost. The model was further refined during 2011, and at the beginning of 2012, the standard-setting bodies were still discussing the rules for the impairment of financial assets measured at amortised cost. Additional changes to the original exposure draft are expected. The final draft for a new IFRS standard on the impairment of financial assets measured at amortised cost is expected to be presented by end-June 2012. The amendments are likely to have a major impact on the banking industry and the market in general.

Current requirements for measuring loan losses
According to prevailing requirements, the value of a financial asset shall be written down if there is objective evidence of impairment, i.e. when a loss event has occurred. Standard-setting bodies, auditors and users have criticised certain aspects of the impairment rules, including the fact that in some cases, the current rules have resulted in delayed recognition of losses, as a loss event must have occurred in order for the loss to be recognised. In addition, it is sometimes difficult to determine when a loss has actually occurred, which may result in inconsistent application of the requirements.

New requirements for measuring loan losses
In the exposure draft issued in November 2009, the IASB proposed an expected loss model which entailed that expected losses were to be included in the computation of the effective interest rate upon initial recognition of a financial asset, including loans. The proposal implied that the part of the interest rate which compensates for expected losses, should not be recognised as income.

In the supplement issued on 31 January 2011 and in subsequent discussions, the IASB and the FASB presented a joint model for recognising impairment of financial assets. This model received little support and the standard-setting bodies have made further adjustments to the model in 2011 and 2012. The impairment model which is being discussed in early 2012 includes elements of the IASB's original proposal, as well as adjustments which are intended to make the model easier to use. Among other things, expected losses are not included in the computation of effective interest rates used as a basis for interest income recognition. In addition, it is assumed that the model which is being discussed will be applicable for all types of loans and securities.

According to the model which is being discussed in early 2012, the accrual of expected losses over the life of the assets should be determined by the characteristics of the assets. Financial assets measured at amortised cost should be divided into three categories. In principle, at initial recognition, all commitments shall be classified in category 1 and thereafter be transferred to the other two categories according to specific criteria. Expected losses relating to doubtful commitments, which according to given criteria are transferred from category 1, shall be calculated for the total lifetime of the commitment and be recognised immediately (category 2 at portfolio level or category 3 at an individual level). Provisions for losses on commitments in category 1 shall be based on expected losses within a 12-month period.

The intention behind the new approach is to better reflect the underlying economics in a lending transaction. There should be no need to identify triggering loss events in order to estimate changes in expected losses. According to the IASB, this method is intended to ensure greater consistency between various reporting entities. The standard-setting bodies expect that the new requirements will present useful information to users of financial statements for their assessment of original loss estimates and possible changes in estimates over the life of an asset.

It remains highly questionable whether the new requirements will actually have the desired effect. A high degree of judgement will be required when assessing when commitments should be defined as doubtful and transferred from a category where provisions are based on expected losses during a 12-month period to a category where expected lifetime losses should be calculated. It will also be very challenging to assess future expected cash flows and lifetimes, as well as arrive at good and stable expected loss estimates. There will therefore be a high degree of uncertainty related to these estimates.

The new requirements are expected to cause greater volatility in financial reporting. Due to limited experience and the lack of relevant and reliable statistics, adjustments will regularly be made to the assumptions underlying expected loss measurements. Such changes will be reflected in the accounts on a cumulative basis, which means that the full effect of new estimates must be recognised immediately for all commitments affected by the changes. Adjustments in the new model may nevertheless result in somewhat lower volatility in financial reporting.

Once the new requirements are implemented, a reduction in equity is expected for most financial institutions, as there will probably be a need for higher impairment allowances on loans. In light of the introduction of Basel III and the amended IAS 19, the consequences may be challenging unless capital adequacy requirements and accounting rules are coordinated. The expected effective date for the new loss reporting requirements is 1 January 2015.

New accounting requirements for insurance contracts
In July 2010, the IASB published an exposure draft for a revised IFRS 4 Insurance Contracts, which represented the first extensive proposal from the IASB on the accounting treatment of insurance contracts. Subsequent to this, there have been many discussions concerning the new requirements, and a number of tentative decisions have been made regarding amendments to the original exposure draft. As a consequence, a revised exposure draft or a supplement to the original exposure draft is expected to be presented in the second quarter of 2012. The exposure draft proposes that insurance liabilities be measured at the fair value of the cash flows arising from the insurance contracts, plus a risk margin. However, the wording of the final standard remains uncertain. Under the current standard, liabilities are measured according to requirements which are further defined in the Act on Insurance Activity. The assets are thus measured at a combination of amortised cost and fair value, depending on the characteristics of the assets. The accounting requirements are expected to result in greater volatility in profit measurements for life insurance companies in the longer term. The original effective date for the revised IFRS 4 Insurance Contracts was 1 January 2013, but has been indefinitely postponed.

Revised accounting requirements for defined benefit pension schemes

In 2011, the IASB issued amendments to IAS 19 Employee Benefits. One of the amendments is the removal of the corridor approach for recognising actuarial gains and losses. Actuarial gains and losses should now be recognised in other comprehensive income in the period in which they occur. Furthermore, the amendments imply that pension expenses are to be split between profit or loss and other comprehensive income. The expected return on pension funds should be computed using the discount rate used to measure the pension liability. The current service cost and net interest expenses are to be recognised in profit or loss, while remeasurements, such as actuarial gains and losses, are to be recognised in other comprehensive income. Pension entitlements earned during the period and net interest expenses should be recognised in profit or loss, while remeasurements are to be recognised in other comprehensive income. Furthermore, the disclosure requirements for defined benefit pension schemes have been changed. The amendments will be effective for the accounting year starting on 1 January 2013, but have not yet been endorsed by the EU. See also Accounting principles to the annual accounts, item 21 Approved standards and interpretations that have not entered into force.

TAX EXEMPTION METHOD FOR LIFE INSURANCE COMPANIES

On 1 January 2012, the Norwegian Ministry of Finance made public a consultation paper proposing more restrictive use of the tax exemption method (Section 2-38 of the Norwegian Taxation Act) for life insurance and pension companies. The proposal concerns income on shares, including dividends and capital gains generated in group and unit-linked portfolios (policyholders' funds). Income on shares will still be included in the deduction for allocations to insurance funds etc. in accordance with Section 8-5 of the Taxation Act. The exemption method will still apply to income from shares etc. in the corporate portfolios of life insurance and pension companies.

In the opinion of the Ministry of Finance, there is a certain asymmetry in prevailing legislation, as a rise in the value of or the income on policyholders' funds gives tax deductions, while the exemption method permits that parts of such income be exempt from taxation.

The proposed legislative amendment aims to reduce the apparent asymmetry by restricting the use of the exemption method for these companies. The proposal was launched without any prior notification or dialogue with the industry. In a letter dated 4 January 2012 to the Ministry of Finance, Finance Norway (FNO) pointed out that the proposal came as a surprise to the industry and that the timing was unfortunate. If the proposal is approved, it may entail higher taxes for DNB.

It has been proposed that the new rules enter into force with effect from 1 January 2012. The deadline for comments on the consultation paper is 2 April 2012. DNB, FNO and other industry players will be active during the consultation round in an effort to limit the negative effects of the proposal. At present, there are still a number of unresolved questions regarding the proposal.

FINANCIAL ACTIVITIES TAX

According to the Norwegian National Budget for 2012, the Ministry of Finance has carried out a preliminary feasibility assessment of the introduction of an activities tax for the financial sector.

The Norwegian government's assessment of possible changes to the taxation of the financial sector is based on the report from the Financial Crisis Commission, c.f. Official Norwegian Report no. 2011: 1, Better positioned against financial crises, where one of the proposals was to consider the feasibility of an activities tax for the financial sector.

In Norway and most other countries, financial services are normally exempt from value added tax (VAT). The reason for this exemption is the difficulty in determining an appropriate tax base for VAT calculation in the financial sector. Furthermore, this would lead to an extremely complex relationship between VAT rules for financial services in Norway and for international ones. As a result of this exemption, outgoing VAT is not charged on the sale of financial services, while financial undertakings are not entitled to deduct incoming VAT on products procured for use in such operations.

The government has stated that the intention of the activities tax is to remedy the situation that the financial sector does not pay VAT. It has been claimed that the financial sector is undertaxed as a result of the VAT exemption. However, this must be seen in relation to the fact that paid VAT (non-deductible incoming VAT), seen in isolation, represents a surtax for the financial sector.

The Ministry of Finance has considered two principal methods for drawing up an activities tax as an alternative to VAT in the financial sector: the addition method and the subtraction method. The tax basis for an activities tax based on the addition method will be the sum of wages and profits. Based on the subtraction method, the added value is instead determined by the difference between income and intermediate consumption (goods and services consumed as inputs).

DNB considers the introduction of an activities tax for the financial sector to be an unfortunate measure. An activities tax lacking the neutrality characteristics of the VAT system would represent an extra tax on the financial sector. This will create a distortion of competition vis-à-vis similar market players within the EU. Moreover, an activities tax which is not internationally harmonised will create an imminent danger of double taxation for financial institutions with international activities.

Furthermore, the financial sector is facing a number of far-reaching regulatory requirements. In such a scenario, a possible introduction of an activities tax will create added uncertainty and reduce the financial sector's ability to satisfy the new requirements. Finanstilsynet has stated that it would not welcome the introduction of an activities tax. Norges Bank has recommended that further exploration of an activities tax in Norway be put on hold until a proposal for such a tax is presented by the European Commission. DNB agrees that an exclusively Norwegian surtax should not be introduced for the financial industry. As of today, no other country has introduced a tax equivalent to the activities tax which has been evaluated in Norway.

The background for the activities tax assessment is also based on the false premise that Norwegian financial institutions pay too little tax. In fact, the financial industry is second only to the petroleum industry with respect to who pays most corporate income tax in Norway.

REPORTING OF CUSTOMERS OR ENTITIES LIABLE TO US TAXATION

In 2010, the Foreign Account Tax Compliance Act, FATCA, was passed by the US authorities to combat tax evasion by persons or entities liable to US taxation. The rules and the implementation timetable have been made public in several statements by the US tax authorities, i.e. the Internal Revenue Service, IRS, most recently in February 2012. A number of individual countries and the EU have raised the issue of the reporting requirements with the American authorities to achieve an implementation which is cost-effective, business-friendly and in conformity with their national legislation.

The final regulatory framework has not been adopted, and the details of the reporting requirements have not yet been finalised. The rules proposal made public in February 2012 relaxes the original requirements and extends the implementation period. Notification has been given of a US public hearing about the rules in May 2012. According to the proposed rules, non-American financial undertakings must report to the American tax authorities, either directly or via the local authorities in the country concerned. The latter requires the conclusion of a separate agreement between the country concerned and the US. In February 2012, the authorities in the US, the UK, Germany, France, Italy and Spain published a joint statement with a view to achieving better compliance with international tax rules and the implementation of FATCA. The statement entails a relaxation of the FATCA requirements for financial undertakings in the countries concerned.

The definition of financial undertakings is broad and comprises banks, insurance companies, brokerage companies, and investment and mutual fund structures. The reporting requirement includes customer relationships with customers who are liable to US taxation or with units where such customers have a significant ownership interest. It is also presumed that the financial undertakings will collect American withholding tax on behalf of the IRS. The rules are intended to be gradually introduced from 2013.

Non-American financial undertakings are expected to establish processes to identify and verify customer relationships falling within the scope of FATCA, report such customer relationships annually to the IRS and collect 30 per cent withholding tax on payments of US-source income or gross sales proceeds for financial instruments which generate income which is taxable in the US. Such withholding tax includes payments to financial undertakings which have not entered into an agreement with the IRS, customers who have not submitted sufficient information for their tax liability to the US to be clarified, or units with large American owners which have not submitted information about these owners.

FATCA represents large challenges for financial undertakings around the world and will require, among other things, that identification and reporting procedures are established. The IRS reporting could also come into conflict with local legislation on the protection of customer information that applies to the financial undertakings. For the above-mentioned countries, the intention is to incorporate the FATCA rules into local legislation and that the reporting is made to the local tax authorities in each country, who in turn forward the information to the IRS. FATCA may potentially have significant negative consequences for financial undertakings failing to comply with the identification and reporting requirements. It is important that the Norwegian authorities ensure that Norwegian financial undertakings have equal framework conditions in this area.

DNB is following developments and planning how to adapt in order to satisfy the requirements within a framework which is cost-effective, takes commercial aspects into account and is in conformity with the legislation of the countries where the Group has operations.