Pillar III - risk and capital 2014

Eika Boligkreditt AS

1 INTRODUCTION

The purpose of this document is to provide the market with information about risk management and capital at Eika Boligkreditt AS. It is intended to fulfil the requirements for publication of financial information pursuant to chapter 45 of the capital requirement regulations.

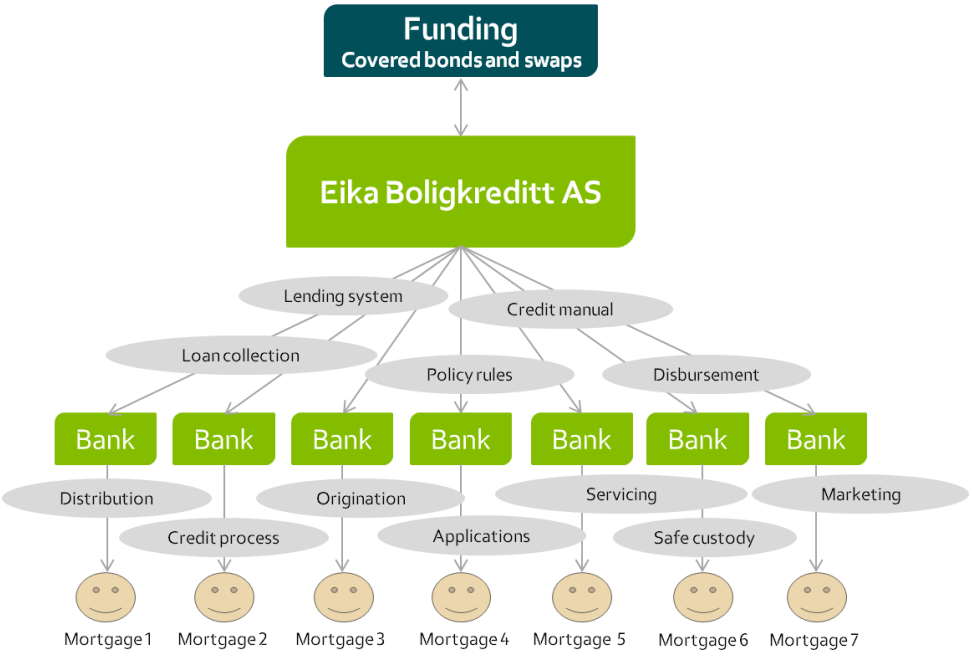
Eika Boligkreditt (hereafter **EBK**) is the Eika Alliance's covered bond company and is directly owned by 73 local banks and OBOS (known collectively as the owner banks). The company was demerged from Eika Gruppen AS in 2012, and no longer forms part of the Eika Gruppen group. In connection with the change of ownership, a strengthened mechanism was established to provide support for the company from the owner banks. This comprises commitments by the owner banks to provide the company with liquidity and capital in circumstances where such provision is necessary. In addition, the agreements require ownership of the company to be rebalanced on an annual basis. This is intended to ensure at least one annual adjustment so that the holding of each bank and OBOS corresponds to its share of the company's residential mortgage portfolio.

2 COMPANY STRUCTURE AND OPERATIONS

EBK's main purpose is to secure access for the owner banks in the Eika Alliance to long-term competitive funding by issuing covered bonds in the Norwegian and international financial markets. An important aspect of the company's business concept is to increase the competitiveness of the owner banks and reduce their risk – including refinancing risk.

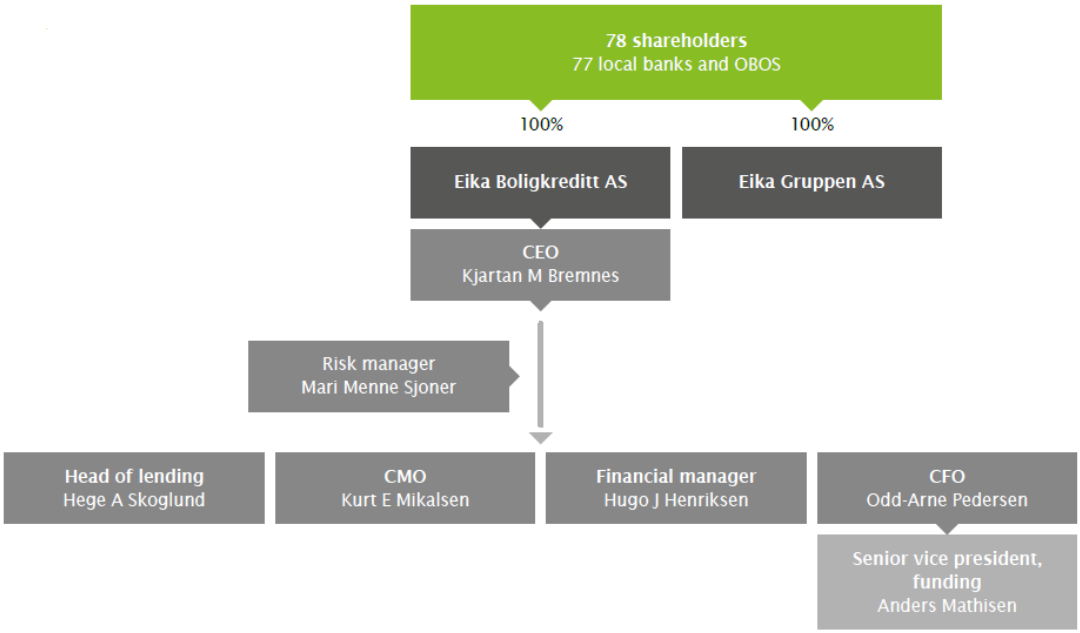
For EBK to be active as an issuer in both Norwegian and international financial markets, its covered bonds must have an international rating. An international rating from Moody's Investors Service (**Moody's**) gives EBK the opportunity to diversify its financing and to obtain funding at the best terms available in the market. The owner banks are prevented from issuing covered bonds directly, but through EBK, the owner banks can accordingly access very favourable financing and maintain their competitiveness in relation to large Norwegian and international banks.

Figure 1 The company's area of operation



The owner banks are EBK's local representatives, and make all the arrangements related to providing residential mortgages. That includes processing mortgage applications, establishing the loan, amending existing mortgages and borrowing, and so forth. As a result, a residential mortgage transferred to EBK will be wholly perceived by the mortgagee as one taken out with their local bank or OBOS-banken. That is because their local bank will always be the mortgagee's point of contact for the mortgage. EBK is responsible in the mortgage process for operating the IT system, credit policy and disbursals.

Figure 2 Company structure



EBK is organised in five departments:

- lending
- funding and investment
- marketing
- accounting and back office
- risk management and compliance.

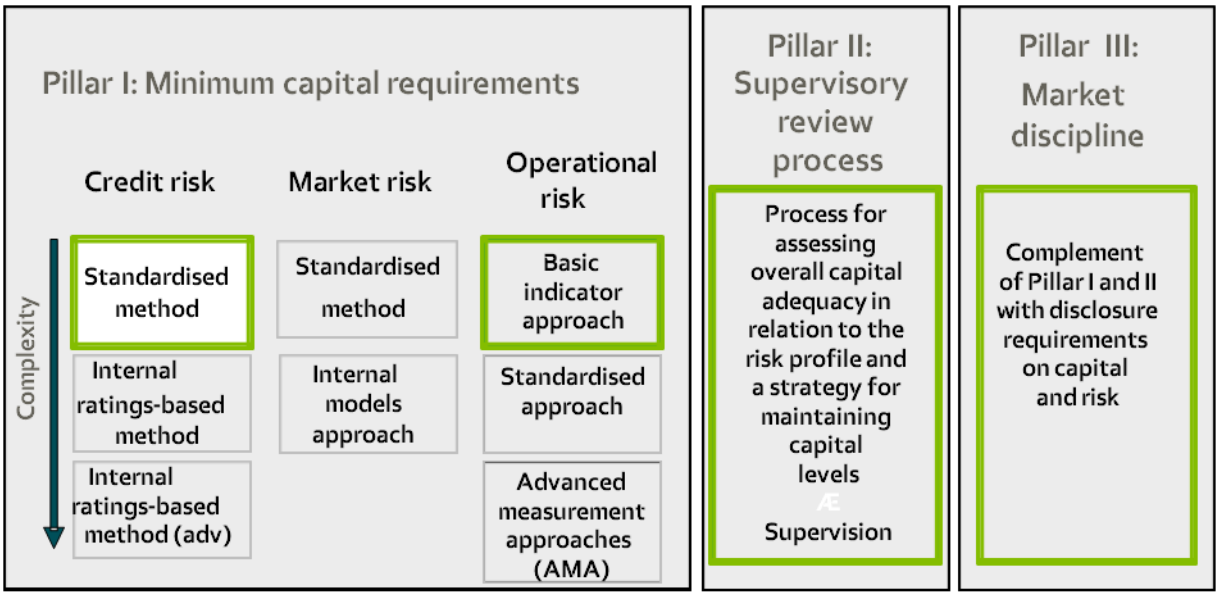
Company staffing at 31 December 2014 was the equivalent of 19.8 work-years. In addition, services are provided by Eika Gruppen in such areas as human resources, payroll, legal affairs, accounting and marketing. EBK's IT platform is also supplied by Eika Gruppen.

3 BASEL II – CAPITAL ADEQUACY STANDARDS

The Basel II requirements on the calculation of capital adequacy by financial institutions were introduced in Norway at 1 January 2007. They are based on a new standard for calculating capital adequacy established by the Bank for International Settlements (BIS). The purpose of the capital requirement regulations is to strengthen the stability of the financial system through

- more risk-sensitive capital requirements
- better risk management and control
- closer supervision
- more information to the market.

Figure 3 The Basel II pillars



When calculating capital requirements, the company utilises the standardised method for credit and market risk and the basic indicator method with regard to operational risk. This means that the calculation of capital requirements for these risks accords with the categories and risk weighting rules in the capital requirement regulations.

PILLAR I

Pillar I addresses minimum capital adequacy requirements related to credit, market and operational risk. It also covers capital adequacy related to the creditworthiness of counterparties to derivatives (CVA risk).

PILLAR II

Pillar II is based on two main principles. EBK must have a process in place for assessing its total assets in relation to its risk profile and a policy for maintaining its capital adequacy. The Financial Supervisory Authority (FSA) of Norway as the regulator can also review and evaluate EBK's internal assessment of its capital requirements and policies, and monitor and ensure compliance with official capital requirements. The FSA has the authority to initiate appropriate supervisory measures if it is dissatisfied with the result of the process.

PILLAR III

Pillar III is intended to supplement the minimum requirements in Pillar I and the regulatory follow-up specified in Pillar II. It will help to enhance market discipline through requirements for the publication of information which make it possible for the market, including analysts and investors, to assess the institution's risk profile and capitalisation as well as its management and control. The publication requirements are particularly important when players can make greater use of their own systems and methods for calculating their capital requirement.

The capital requirement and targets are assessed on the basis of the international Basel II and Basel III regulations on capital adequacy as specified in the Act on Financing Activity and Financial Institutions and the capital requirement regulations. Pursuant to section 2, sub-section 9(b) of the

Act on Financing Activity and Financial Institutions, a financial institution must at all times have a primary capital (tier 2 capital) which is acceptable in relation to the risk and scope of the institution's business. This must be assessed for both the immediate future and the long term. Capital adequacy must accordingly be higher than the minimum requirement of eight per cent, as specified in detail in the capital requirement regulations. The FSA will evaluate both EBK's capital target and the documentation of the assessments on which the board's conclusions are based.

CONTINGENCY PLAN FOR CAPITAL ADEQUACY

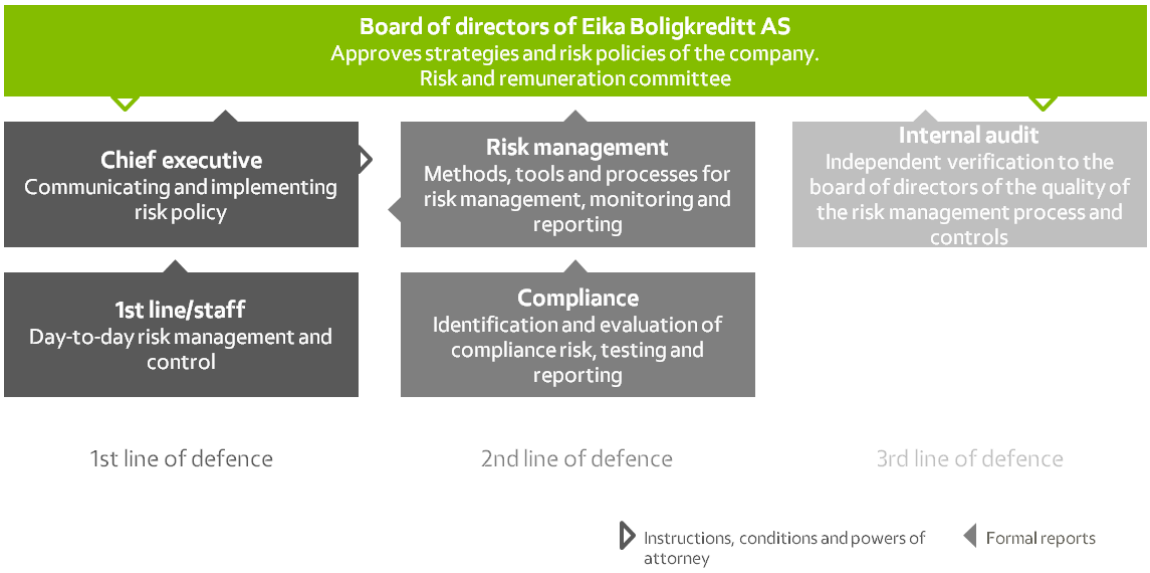
The company has established a contingency plan for capital adequacy which is intended to help ensure that good processes are in place for capital management. EBK's owner banks are all subject to capital requirements and all have good solvency. The owner banks are committed by agreements to participate in issues to strengthen the company's capital in accordance with each shareholder bank's share of EBK's residential mortgage portfolio.

4 OVERALL RISK AND CAPITAL MANAGEMENT

RISK MANAGEMENT IN EBK

Responsibility for conducting the company's overall management and control is organised as follows.

Figure 4 Governance and control



EBK has established a framework for management and control through risk policies determined by the board of directors, with quarterly reporting of status and developments. Overall professional responsibility for risk management in the company lies with the chief executive. The company's attention will be focused on maintaining sufficient resources to pursue risk management and compliance, and will assess available expertise and capacity on a continuous basis.

Quarterly risk and compliance reporting is conducted to provide an overview of exposure in relation to established parameters in the company, allowing the executive management and the board to verify that risk exposure falls within the defined willingness to accept risk. This reporting

quantifies and assesses all main risks relevant to the company, including strategic, credit, counterparty, market, interest rate, liquidity and refinancing, and operational risk.

A good internal control regime depends on entrenchment in the whole organisation, from the individual employees to the executive management and the board. PricewaterhouseCoopers is the company's internal auditor.

ICAAP

The business is required pursuant to section 2, sub-section 9 b of the Act on Financing Activity and Financial Institutions to conduct an internal capital adequacy assessment process (ICAAP). This process involves assessing capital requirements in relation to the company's goals, policies, current and anticipated risk exposures, and applicable risk parameters and regulatory provisions. The purpose of the ICAAP is to assess the company's capital targets and requirements in the short and long terms in order to ensure that the company has an adequate buffer in relation to regulatory minimum capital requirements.

Estimated budgets and forecasts for three years ahead are prepared by the management. On the basis of budgets and forecasts of anticipated developments in the company, the risk management and compliance department calculates capital needs for the coming three years.

Stress tests are also carried out by the department with what would be a reasonable but stringent downturn scenario where liquidity dries up for the banks. These scenarios are intended to reflect a worst-case scenario for EBK.

The preliminary ICAAP report is important for the board's assessment that the Company has adequate level of capital and liquidity, pursuant to section 3, sub-section 4 of the Act on Private Limited Liability Companies and possible opportunities to pay dividend, requirements for additional capital and so forth. The board process involves reviewing and discussing important assumptions in the ICAAP analysis, including

- significant assumptions in the budget and the three-year forecast
- an assessment of whether the stress tests are sufficiently conservative to cover a worst-case scenario
- an assessment of the capital adequacy – in other words, how much capital the company ought to have, including how large a buffer the board finds prudent/desirable.

Contributions from the initial ICAAP process, with assessments from the final board meeting for the year, and the final annual financial statements, form the basis for updating the ICAAP calculations. A report is prepared to summarise the company's ICAAP work. The final ICAAP is approved by the board and submitted to the FSA.

5 RISK APPETITE AND CAPITAL POLICY

Table 1 The company's risk appetite

Risk type	Risk appetite
Credit risk	Low
Market risk	Moderate
Operational risk	Low
Liquidity risk	Moderate
Interest rate risk on net interest income	Low
Strategic risk	Low
Reputational risk	Low

CAPITAL AND BUFFER REQUIREMENTS

In line with the increase in countercyclical buffer requirements from 1 July 2015, EBK has updated its capital targets to satisfy the applicable minimum and buffer requirements for capital. The company has resolved to meet capital targets in accordance with the pace of introduction specified in the table below while fulfilling applicable buffer requirements at all times.

Table 2 Capital targets for EBK in the ICAAP period

Capital targets	1 July 2014	1 July 2015	1 July 2016
Core tier 1 capital ratio	10.0 %	11.0 %	11.0 %
Tier 1 capital ratio	11.5 %	12.5 %	12.5 %
Tier 2 capital ratio	13.5 %	14.5 %	14.5 %

In its capital planning, company operates with a buffer of 0.5 percentage points on its capital targets. However, it is important for the owner banks that EBK continues to save capital, since it is the assets with the best quality and lowest risk which are transferred from the banks to the covered bond institution. Should the need for capital change, the shareholder agreement provides considerable predictability over the provision of capital from the owner banks. The company's capital targets will be adjusted if countercyclical buffers change and, in the event of an increase in buffers, will have a minimum of 12 months to adjust to a new requirement.

New buffer requirements which exceed the company's minimum requirements must be met with core tier 1 capital, and comprise system-risk, capital-conservation and countercyclical buffers. In addition, an increased requirement has been set for core tier 1 capital in systemically important financial institutions (SIFI). A common denominator for the new buffer requirements is the restrictions imposed on opportunities to make dividend and bonus payments in circumstances where the company fails to satisfy the requirements.

Table 3 Capital buffer requirements at 31 December 2014 (amounts in NOK 1 000)

Buffer types		Core tier 1 requirements
Capital conservation buffer	2.5 %	628,866
Systemic risk buffer	3.0 %	754,640
Countercyclical buffer	0 %	-
Combined buffer requirements		**1,383,506**

The company had a combined buffer requirement of about NOK 1.4 billion at 31 December 2014, which is covered by core tier 1 capital.

6 CAPITAL

The company applies the standardised method for calculating capital requirements for credit and market risk and the basic indicator method for calculating operational risk. The standardised method for credit risk is used in calculating capital requirements for market risk, including capital requirements for liquidity investments.

Pursuant to the capital requirement regulations, the following weighting rules are significant for credit risk in the company:

Commitment	Risk weighting	Assessment of capital in relation to risk
Residential mortgages secured on the property with an LTV of at least 80 per cent	35%	Credit risk
Mortgage loan approvals and partly disbursed loans with an LTV of at least 60 per cent. Conversion factors of 20 and 50 per cent	35%	Credit risk
Bank deposits without fixed terms	20%	Counterparty risk
Derivatives, depending on rating	20%/50%	Counterparty risk
Local and regional government, including local authorities	20%	Market risk
Covered bonds	10%	Market risk

Capitalised assets and other credit risk are basically weighted at 100 per cent unless special rules have been specified. In addition, the company has items in its balance sheet with the following weighting:

- enterprises with an approved rating are assigned a 50 per cent risk weight
- deferred tax assets resulting from temporary differences, which are below 10 per cent of core tier 1 capital, will be assigned a 250 per cent risk weight.

Calculating the capital requirement for operational risk using the basic indicator method means that the capital requirement is determined in relation to the company's net interest income and other revenues. Assessment of the operational risk is based on incidents experienced, events in the rest of the banking industry, and intrinsic risks.

Calculating the capital requirement for counterparty risk, including the risk of a reduction in the counterparty's creditworthiness (CVA risk) is calculated in accordance with the standardised method for CVA risk. See section 20a, sub-section 3 of the capital requirement regulations. Calculated on the basis of the counterparty's creditworthiness, this supplementary requirement is known as the credit valuation adjustment (CVA). The CVA became part of the calculation basis from 30 September 2014.

Risk types not covered by Pillar I – minimum primary capital requirement – have been calculated on the basis of overall exposure and the company's risk management and control.

Table 4 Capital adequacy status at 31 Dec 14 (amounts in NOK 1 000)

Capital status	31 December 2014
Share capital	713,455
Share premium reserve	1,746,928
Other paid-in equity	477,728
Other equity	999
Total equityl	**2,939,109**
Intangible assets	-4,609
Prudent valuation	-9,206
Total core tier 1 capital	**2,925,294**
Hybrid capital	448,315
Total tier 1 capital	**3,373,609**
Subordinated loan capital	249,661
Total primary capital (tier 2 capital)	**3,623,270**
Risk-weighted assets and capital adequacy ratio	
Credit risk	23,125,227
CVA risk	1,717,691
Operational risk	311,738
Total risk-weighted assets	**25,154,656**
Capital requirement corresponding to 8% of risk-weighted	2,012,372
Surplus equity and subordinated capital	1,610,898
Core tier 1 capital ratio	**11.63 %**
Tier 1 capital ratio	**13.41 %**
Tier 2 capital ratio	**14.40 %**

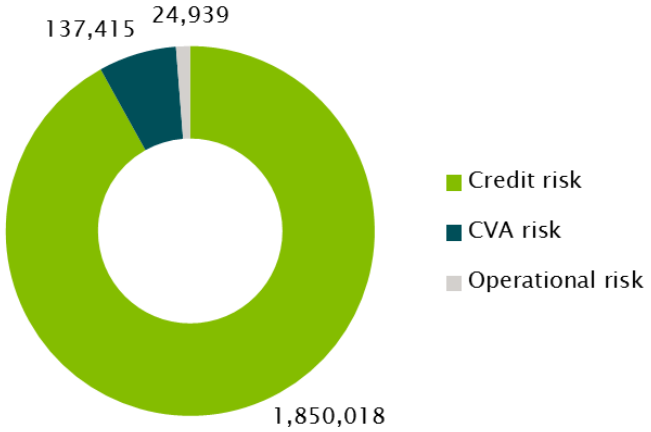
The company's capital adequacy status at 31 December 2014 comprised a core tier 1 capital adequacy of 11.63 per cent, a tier 1 capital ratio of 13.41 per cent and a tier 2 capital ratio of 14.40 per cent. EBK issued a new subordinated loan during 2015 which is treated as NOK 200 in supplementary capital.

SUMMARY OF MINIMUM CAPITAL REQUIREMENT

Table 5 Capital adequacy by risk type (amounts in NOK 1 000)

Capital status	31 December 2014
Core tier 1 capital ratio	11.63 %
Tier 1 capital ratio	13.41 %
Capital ratio	14.40 %
Credit risk	1,850,018
CVA risk	137,415
Operational risk	24,939
Total Pillar I	**2,012,372**

Figure 5 Capital requirements on Pillar I (amounts in NOK 1 000)



LEVERAGE RATIO

Implementing CRD IV in the Norwegian regulations means that the leverage ratio must be reported and incorporated in the assessment of overall capital requirements under Pillar II before a minimum requirement in Pillar I is introduced in 2018. Pursuant to the Act on Financing Activity and Financial Institutions, regulations may be introduced which specify that minimum core tier 1 or tier 1 capital in financial institutions must be a specific percentage of the value of the company's assets and off-balance sheet commitments, calculated without risk weighting (leverage ratio). This is intended to act as a safeguard against setting the calculation basis too low when calculating capital adequacy.

Reporting of the leverage ratio under CRD IV in Norway will be in line with EU standards. The Financial Supervisory Authority has been charged with assessing when and how a requirement for an unweighted equity ratio, with associated definitions, is to be introduced in Norway. This work includes preparing proposals for possible regulations by June 2015.

EBK has reported its leverage ratio to the regulators from 30 September 2014. Reporting is done on a standardised form, but without any indicator requirements being specified for the moment. The proposed requirement for the leverage ratio is three per cent. EBK has produced estimated projections of the ratio on the basis of the Financial Supervisory Authority's calculation method, and fulfils a potential three per cent requirement.

Table 6 Leverage ratio at 31 Dec 14

Leverage ratio	2014
Balance sheet items (excluding derivatives)	72,689,405
Assets deducted from core tier 1 capital	(4,609)
Prudent valuation	(9,206)
Preliminary results/dividends	(84,620)
Derivative exposure	11,164,827
Loan commitments to customers	1,159,431
Total on- and off-balance sheet exposures	84,915,228
Core tier 1 capital	2,925,293
Tier 1 capital	3,373,609
Leverage ratio (core tier 1)	3.44 %
Leverage ratio (tier 1)	**3.97 %**

7 STRATEGIC AND BUSINESS RISK

Definition: *Business risk is the risk that covariation between income and expenses will be absent over time. Strategic risk is defined as the risk of weakened profitability owing to changes in competitive terms, operating parameters, external factors and so forth. Reputational risk is also addressed under business risk, and consists of the risk of loss owing to reputational damage from negative publicity.*

RISK APPETITE AND EXPOSURE

Strategic and business risk in the company must be low. EBK has established a good business strategy and comprehensive risk policies for managing strategic risk. Goals have been set in the business strategy, and other policies have overarching parameters related to risk appetite. The company's business concept is to improve the competitiveness of the banks and reduce their risk by issuing covered bonds in the Norwegian and international financial markets. Through professional cultivation of the financial markets, good international ratings and high-quality collateral, EBK will thereby secure long-term and competitive funding for the owner banks. To achieve this strategy, the priority areas relate to:

- sustainable development
- good international ratings
- profitability and cost-effectiveness
- quality at every level.

The company is exposed to reputational risk related to Eika as a brand. Adverse developments related to the Eika Alliance, Eika Gruppen As and/or companies in the Eika Gruppen group may have detrimental effects on EBK's reputation, particularly in the funding market. The risk of damage to the Eika brand's reputation with customers for residential mortgages is smaller, since the customer's relationship is with their local bank.

In addition, EBK is exposed to reputational risk related to the reputation of Norwegian issuers of covered bonds. International investors often treat all Norwegian issuers of covered bonds as a single category. Statements by the Norwegian authorities which might indicate, for example, a lack of government support could adversely affect the reputation of other Norwegian issuers. Reputational risk could have significant consequences for the company as a funding instrument – by damaging its credit rating, for example. Such risk is accordingly closely related to EBK's liquidity and refinancing risk.

MANAGEMENT AND CONTROL

Good policy processes are important for ensuring management and control of business and strategic risk. EBK has an annual cycle in which revision of business and risk policies plays a fixed role. Changes made to the company's support structure, whereby the shareholders have undertaken to provide liquidity and capital support when required in a crisis, form part of the management and control of business risk.

Focusing attention on good risk management, compliance, business ethics, whistleblowing, managing conflicts of interests, and other policies, strategies and routines will help the company to handle processes in a positive way.

CAPITAL REQUIREMENTS

Strategic and business risk is not included in the calculation of Pillar I capital requirements. An assessment of capital requirements for strategic and business risk is included in the assessment of Pillar II requirements, and the company's capital targets are considered adequate to cover risks over and above the minimum requirements in Pillar I.

8 CREDIT RISK

Definition: *Credit risk is the risk of loss posed by customers or counterparties failing to meet their payment obligations. Credit risk affects all claims on customers/counterparties, lending, credits, guarantees, open trades, residential mortgage approvals to customers, and the counterparty risk arising through derivatives and foreign-exchange contracts. Credit risk depends in part on the size of the claim, the time to maturity, the probability of default and possibly the value of collateral. Credit losses can also be incurred as a result of operational errors.*

RISK APPETITE AND EXPOSURE

Credit risk accounted for 92 per cent of the company's capital requirement under Pillar I at 31 December 2014, making this its most significant risk. The company has never experienced defaults exceeding 90 days or losses related to its mortgage business.[1]

The credit risk related to lending must be low. In its credit policy and lending activity, EBK will take account of the applicable regulations which govern credit companies issuing covered bonds at any given time. See section 2, sub-section 25 and subsequent sub-sections of the Act on Financing Activity and Financial Institutions. The company's policy for credit risk on lending is intended to minimise the risk of defaults and to keep credit risk below the level in comparable companies. This will ensure that the company's bonds are a preferred choice for investors.

The company's credit risk is strictly limited through the company's business purpose, policies, credit guarantees from the owner banks and the company's credit risk policy. At 31 December 2014, EBK's credit risk related primarily to balance sheet items, but it is also exposed to off-balance sheet credit risk.

Credit risk in the company consists mainly of residential mortgages secured on the property plus a counterparty risk in bank deposits and derivatives. The counterparty risk is limited by parameters and requirements concerning the issuers who are the company's counterparties, and the capital requirement related to this risk is calculated under counterparty risk. EBK is also exposed to credit risk in its management of investments in securities other than those issued by the Norwegian government. This credit risk is limited through defined investment parameters. Capital requirements related to this risk are calculated under market risk.

The company reports pursuant to the International Financial Reporting Standards (**IFRS**), and measures mortgages at fair value. Floating-rate mortgages are measured as equal to amortised

[1] A mortgage is defined as being in default when payments are delayed by more than 90 days, and the delay is not the result of random circumstances affecting the borrower. Doubtful loans are not necessarily in default, but the customer's financial position and the value of the collateral indicate a risk of loss.

cost. The fair value of fixed rate loans is correspondingly measured as equal to amortised cost adjusted for the difference between the loans' fixed rate of interest and the interest rate at the balance sheet day. The fair value of mortgages with a fixed interest rate is determined pursuant to the regulations on credit agreements. The fair value of each individual fixed-interest mortgage is determined on the basis of the discount or premium which the customer will receive or have to pay in the event of early redemption. This value is therefore contingent on interest-rate developments, and value fluctuations will affect the financial results. The company also provides mortgages for residential cooperatives.

GENERAL CONSIDERATIONS RELATED TO CREDIT RISK IN EBK

EBK has never experienced accounting defaults on its lending or losses related to its mortgage business. The guarantee structure between EBK and its distributors reduces the company's credit risk, and it therefore also expects no bad debts in the future. Consequently, the company has never taken an impairment charge on mortgages.

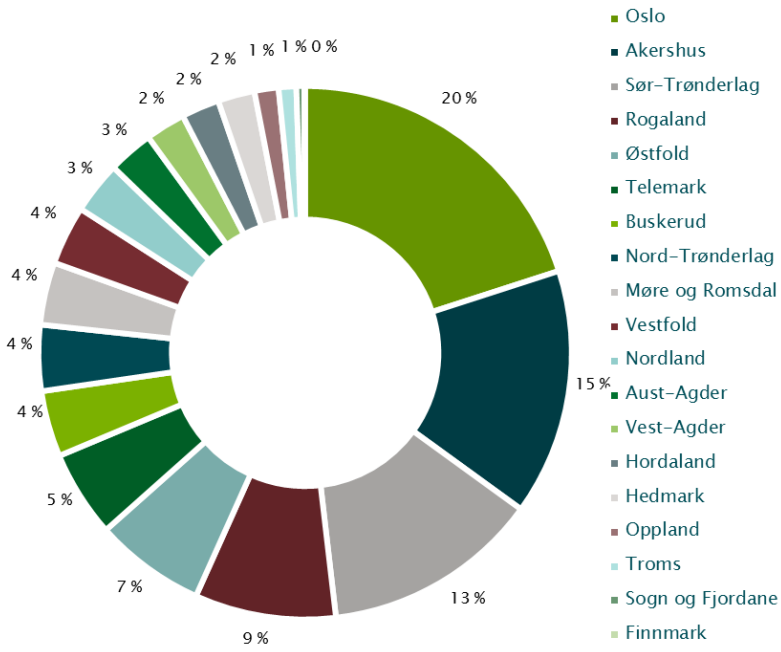
Table 7 Credit risk: specification of risk-weighted volume and capital requirement (amounts in NOK 1 000)

Credit risk	Section	CCF	Balance sheet	Off-balance sheet items	Risk weight	Calculation basis	Capital requirement
Government bonds	§ 5-1		1,888,702		0 %	-	-
Regional or local government	§ 5-2		1,230,362		20 %	246,072	19,686
Banks and institutions (deposits in other banks)	§ 5-6		3,708,022		20 %	741,604	59,328
Credit guarantees from the shareholders	§ 5-6			6,748,842	20 %	1,349,768	107,981
OTC derivatives AA rating (standardised method)	§ 5-7 og § 23			1,181,366	20 %	236,273	18,902
OTC derivatives A rating (standardised method)	§ 5-7 og § 23			1,702,478	50 %	851,239	68,099
Claims on corporates (unrated)	§ 5-7		15,000		100 %	15,000	1,200
Claims or contingent claims secured on real property	§ 5-9		60,966,428	-6,748,842	35 %	18,976,155	1,518,092
Loan commitments to customers (duration 30 days)	§ 5-9 og § 6-1 (9)	0.2		461,651	7 %	32,316	2,585
Loan commitments to customers	§ 5-9 og § 6-1 (8)	0.5		622,293	18 %	108,901	8,712
Covered bonds	§ 5-13		4,842,004		10 %	484,200	38,736
Other assets	§ 5-15		2,650		100 %	2,650	212
Other assets (deferred tax assets)	§ 18 (beregningsforskrifte		32,419		250 %	81,047	6,484
Total credit risk			**72,685,587**	**3,967,788**		**23,125,227**	**1,850,018**

Table 8 Credit risk by commitment category (amounts in NOK 1 000)

Claims	Capital requirement
Claims on regional or local government	19,686
Claims on institutions	254,311
Claims on corporates	1,200
Claims or contingent claims secured on real property	1,529,390
Covered bonds	38,736
Other items	6,696
Total capital requirement credit risk	**1,850,018**

Figure 6 Residential mortgages by Norwegian county as % of total mortgage volume at 31 Dec 14



Having the owner banks as the distributor channel means that customers are well spread geographically. The company's customers are primarily private individuals, each of whom accounts for a relatively small proportion of the company's total portfolio.

Table 9 Residential mortgages by commitment type and residual time to maturity (amounts in NOK 1 000)

Expected maturities on lending and investments	31 December 2014	0-1 month	1-3 months	3-6 months	6-12 months	1-3 years	3-5 år	5-10 years	Over 10 years
Lending:									
Residential cooperatives	52,047,002	41	214	770	5,760	88,499	361,635	2,280,504	49,309,577
Residential	8,791,895	39	-	567	3,085	27,989	60,414	287,937	8,411,865
Investments:									
Government bonds	1,869,041	-	226,300	1,412,314	230,428	-	-	-	-
Municipalities	1,225,999	290,031	760,768	75,050	100,149	-	-	-	-
Covered bonds	4,825,490	90,040	-	212,963	536,459	3,833,787	152,241	-	-
Bank deposits	3,708,022	3,708,022	-	-	-	-	-	-	-
Total	72,467,449	4,088,174	987,282	1,701,665	875,881	3,950,275	574,290	2,568,441	57,721,442

Table 9 shows that EBK has a good spread of maturities on its mortgages and other lending, which helps to reduce the company's credit risk.

EBK has a diversified mortgage portfolio in terms of geographical distribution and individual customers. The Herfindahl-Hirshman index (HHI) is applied when assessing the concentration risk. This index will expose an inadequately diversified portfolio in terms of individual customers, business sectors or geographical distribution through high α and β values. Premium levels are fixed on the basis of the sector standard.

CREDIT RISK – THE STANDARDISED METHOD

As an issuer of covered bonds, EBK must ensure that all loans and advances in its cover pool comply with credit quality step 1 or 2. When assessing ratings, only those from Standard & Poor's, Moody's and Fitch are utilised. Where a counterparty has been rated by all three agencies, the

median is used to assess the credit quality step. The mean value is applied when it has been rated by two accredited agencies, and a rating from just one is used directly.

- States and central banks: long-term ratings by an accredited agency are used to assign the credit quality step.
- Local and regional government: the national long-term rating is applied.
- Institutions: long-term rating of institutions rated by approved rating agencies will be utilised to determine the credit quality step for banks and for credit and financial institutions.
- Enterprises: long-term ratings from an accredited agency are used to assign the credit quality step, with a 100 per cent weighting applied to relevant claims if no approved rating exists.

GUARANTEES

All residential mortgages transferred to EBK must have a loan-to-value (LTV) ratio of up to 60 per cent at origination. A further requirement is that collateral must be secured in completed residential properties or holiday homes. EBK's collateral requirements satisfy the provision in the capital requirement regulations calling for 35 per cent risk weighting of mortgages and advances with collateral in residential properties. Documentation of value must be an approved appraiser's valuation, an estate agent's valuation, a purchase contract or a valuation by Eiendomsverdi AS, which must not be more than six months old when the mortgage is approved.

Upon transfer to Eika Boligkreditt, the distributors assume mandatory guarantees for the mortgages they have transferred. The main features of these guarantees are as follows.

- *Case guarantee*, covering the entire amount of the mortgage over the period from the distributors request for payment until the mortgage's collateral has been perfected (legally registered) and the custody department of the distributor has checked the documentation.
- *Loss guarantee,* covering the portion of the principal upon payment which exceeds 50 per cent of the reasonable value of the mortgaged property or properties (determined upon payment). The minimum loss guarantee liability of the distributor will be NOK 25 000 per mortgage, irrespective of the mortgaged amount and the value of the collateral. The guarantee will remain in force for a period of six years from the date on which the collateral has been perfected (legally registered) or on which payment is requested, if later. The loss guarantee comes into effect when the case guarantee expires.
- *Proportion of a framework guarantee*, covering a total of one per cent of the mortgage portfolio transferred by the distributors at any given time. The distributor share in the framework guarantee will be calculated on the basis of the distributor actual share of the mortgage portfolio transferred by the distributors at any given time. The framework guarantee can be used if losses incurred in excess of the above-mentioned guarantees, or if the shareholder banks default on their guarantee commitments.

The total guarantee liability for the distributors is the total of all three guarantees mentioned above. This part of the residential mortgage portfolio is assigned a 20 per cent risk weighting.

In addition to the above-mentioned guarantees, EBK has the right to offset commission payments to the shareholder banks for up to 12 quarters. This offsetting can be used to cover losses which exceed the above-mentioned guarantees, and will apply to commission payments to the bank transferring the mortgage which may have gone into default.

An overview was established at 31 December 2014 of the outstanding residential mortgage portfolio compared with the valuation of the mortgage collateral at origination. This shows that the company has mortgages within the following collateral bands.

Table 10 Distribution of LTV at origination (amounts in NOK 1 000)

Loan to value (LTV)	Unindexed values			
	Residential	Residential cooperatives	Total	Share of total
0 <= 40	8,127,854	7,921,708	16,049,562	26 %
40 < x <= 50	8,081,159	617,817	8,698,976	14 %
50 < x <= 60	35,837,989	252,371	36,090,360	59 %
Total	**52,047,002**	**8,791,895**	**60,838,897**	**100 %**
Average LTV	**51.1 %**	**18.2 %**	**46.4 %**	

EBK's residential mortgages have a maximum loan-to-value (hereafter **LTV**) ratio of 60 per cent of the property at origination. The collateral is accordingly regarded as very good and the risk considered small.

CONTINUOUS VALUATION OF COLLATERAL

The portfolio is indexed on a quarterly basis against market values estimated by Eiendomsverdi AS. Eiendomsverdi indexes against objects sold over time in the immediate vicinity and makes adjustments for price developments and the valuations registered by EBK on the mortgaged property at origination. Were residential property prices to fall, the company would have a good margin before possible repossessions might lead to loss. The table below presents indexed market values for EBK's mortgage portfolio.

Table 11 Distribution of indexed LTV (amounts in NOK 1 000)

Loan to value (LTV)	Indexed values			
	Residential	Residential cooperatives	Total	Share of total
0 <= 40	11,725,523	8,317,053	20,042,576	33 %
40 < x <= 50	11,886,936	195,277	12,082,213	20 %
50 < x <= 60	25,996,566	254,565	26,251,131	43 %
60 < x <= 70	2,333,435	25,000	2,358,435	4 %
70 < x <= 75	104,543	-	104,543	0 %
75 < x	-	-	-	0 %
Total	**52,047,002**	**8,791,895**	**60,838,897**	**100 %**
Average LTV	**48.1 %**	**15.5 %**	**43.4 %**	

The weighted average indexed LTV at 31 December 2014 was 43.4 per cent, compared with a non-indexed LTV of 46.4 per cent. Indexing of residential cooperatives shows a weighted average LTV of 15.5 per cent, compared with a non-indexed weighted average LTV of 18.2 per cent. This indicates that house prices have risen across the board since the mortgages were granted.

Some mortgages are indexed with a higher LTV than at origination. The table above shows that no loans exceed the limit of 75 per cent of the property's value, which is the maximum permitted LTV pursuant to section 2, sub-section 28 of the Act on Financing Activity and Financial Institutions. This indexing is performed quarterly and, where mortgages and advances exceed the limit of 75 per cent of LTV, valuation documentation is obtained from the bank to establish that EBK has satisfactory collateral. If satisfactory valuation documentation cannot be obtained for the mortgaged collateral, the bank will have to reduce the mortgage or possibly transfer the mortgage back to its own balance sheet.

RISK OF DEFAULT IN THE COVER POOL

EBK's covered bonds are rated by Moody's. The latter calculates a quarterly collateral score which informs investors about its modelling of the risk of loss related to the credit quality of the cover pool in an Aaa scenario. The higher the credit quality, the lower the collateral score. This score determines the level of loss which Moody's estimates will affect investors in the company's covered bonds in the event of default on these, based on the credit quality of the cover pool. The collateral score presents Moody's analysis of the amount of risk-free assets which must be added to the cover pool in order to offset the negative effect of the stress test scenario as defined by the rating agency. For further information, see Moody's methodology for the definition of the collateral score and the way it is calculated.

In its report covering the third quarter of 2014, published 25 February 2015, Moody's specified a collateral score of two per cent, which is the lowest figure for global issuers of covered bonds rated by the agency. The table presents EBK's covered bonds as the Eika BoligKreditt Mortgage Covered Bond Programme.

Table 12 Collateral score in Moody's global CB performance overview at 30 September 2014

EXHIBIT 11

Deals with lowest (best) Collateral Scores

Name of Programme	Type of Programme	Country	Collateral Score
Eika Boligkreditt - Mortgage - Covered Bond Programme	Mortgage	Norway	2.0%
Nordea Bank Finland PLC - Covered Bond Programme	Mortgage	Finland	2.3%
HSBC - Covered Bond Programme	Mortgage	UK	2.4%
OP Mortgage Bank Mortgage II - Covered Bond Programme	Mortgage	Finland	2.4%
OP Mortgage Bank - Mortgage - Covered Bond Programme	Mortgage	Finland	2.5%
Sparebanken Oest Boligkreditt AS - Covered Bond Programme	Mortgage	Norway	2.6%
Coventry Building Society - Covered Bond Programme	Mortgage	UK	2.7%
SpareBank 1 Boligkreditt AS Mortgage - Covered Bond Programme	Mortgage	Norway	2.7%
Aktia Mortgage (MT) - Covered Bond Programme	Mortgage	Finland	2.8%
Royal Bank of Scotland Plc - Mortgage - Covered Bond Programme	Mortgage	UK	2.8%

STRESS TESTS FOR RESIDENTIAL PROPERTY PRICES

EBK conducts stress tests for falls in residential property prices in order to identify the company's mortgage credit risk. The capital requirement regulations require residential mortgages to have an LTV of at least 80 per cent before the mortgage can be assigned a risk weight of 35 per cent. If this is not the case, the company's capital requirement will be increased for that part of the mortgage portfolio which must be weighted at 75 per cent[2] rather than 35 per cent when calculating capital requirements. Calculations are carried out when residential property prices fall by 15, 25 and 35 per cent respectively. Before the worst-case scenario with a price fall of 35 per cent could occur, for example, EBK would already have taken a number of steps to improve the quality of its cover pool, including initiating its emergency response plan for a fall in residential property prices. If certain mortgages in the cover pool acquire an LTV greater than 75 per cent (60 per cent for holiday homes), this part of the mortgage can no longer be included when

[2] The mortgages are assumed to satisfy the requirements for the retail exposures class and can accordingly be weighted at 75 per cent pursuant to the capital requirement regulations.

determining the overall value of the cover pool. That will be significant for the company's compliance with the balance-sheet requirements in the legislation and its obligations related to overcollateralisation.

The company has better security in its portfolio and a lower minimum for LTV than is usual among covered-bond issuers in Norway, and is accordingly well equipped to handle the risk related to a fall in residential property prices. Reactions to such a fall would generally be swift because of the guarantee structure and the need to comply with legislation governing covered bonds. No increased Pillar I requirement has accordingly been incorporated for a worst-case scenario, since the risk associated with a general fall in residential property prices is adequately covered by the company's guarantee structure and by maintaining requirements for overcollateralisation of the cover pool.

MANAGEMENT AND CONTROL

EBK's distribution channel runs through the owner banks. These banks are locally entrenched with a high proportion of loyal customers and good knowledge of their markets. Customer selection through the distributor banks is regarded as helping to ensure that the company's customers are generally good and loyal.

The company has established policies for credit risk on mortgages, counterparty risk and capital management, which form the basis for management and control of credit and counterparty risk. The status of compliance with the company's credit policy is assessed continuously, and the position in relation to the approved level of risk acceptance is reported quarterly to the board in the risk and compliance report. Compliance with the credit handbook, including safe custody department checks, is monitored on a continuous basis. Overall management and control of risk is described in more detail in chapter 4 above.

CAPITAL REQUIREMENTS

EBK applies the standardised method to calculate the capital requirement for credit risk. This was calculated to be NOK 1 850 million at 31 December 2014. The company's capital targets are considered to be adequate for possible credit risk assessed to be over and above the minimum capital requirements in Pillar I.

9 COUNTERPARTY RISK

Definition: *Counterparty risk is the risk of loss because counterparties are unable to meet their payment commitments and accordingly represent a credit risk. It relates to all claims with counterparties, including guarantees, unsettled transactions and undrawn credits, and to the counterparty risk which arises from exposure to derivatives. Counterparty risk depends in part on the size of the claim, time to maturity, probability of default and value of possible collateral.*

RISK APPETITE AND EXPOSURE

The company has established a policy for counterparty risk to ensure that overall requirements for management and control of such risk are met. This policy is intended to meet the company's need for control over large exposures, including the total exposure with a single counterparty. It will ensure that counterparty risk is manageable at all times by establishing parameters for such risk,

ensuring the establishment of an ISDA with associated CSA for counterparties to derivatives, and providing a clear division of responsibility and authority.

EBK has established the following risk parameters for counterparty risk:

- maximum limit for total exposure (regulations on large exposures)
- internal maximum limit for total exposure
- entering into derivative contracts and defining maximum exposure to a counterparty.

The company is exposed to counterparty risk through lending, investment of surplus liquidity and derivatives. Attention in this chapter is focused on counterparty risk related to derivatives and bank deposits, since this does not belong naturally with the assessment of other risk factors. Counterparty risk is treated as part of credit risk when it relates to lending, and as part of market risk when it relates to investment of surplus liquidity.

- **Counterparty risk related to bank deposits in credit institutions**

EBK uses bank deposits when investing surplus liquidity, and is accordingly exposed to counterparty risk in relation to the various banks concerned. Deposits must be confined to banks with a low credit risk, and must fall within the requirements for inclusion in the cover pool (minimum credit quality step 2, rating A-/A3 for tenors up to 100 days). Parameters for counterparty risk per bank are defined in the company's policy for capital management, including the investment mandate.

- **Counterparty risk related to derivatives**

Activities in EBK are subject to strict regulations for risk exposure, and the company is obligated to refrain from accepting greater interest-rate and foreign-exchange risk than is prudent at any given time.[3] This means that the company uses both interest-rate and foreign-exchange derivatives when borrowing in foreign currencies and/or fixed interest rates in order to keep risk at a minimum. The same applies to hedging interest-rate risk relative to lending at fixed interest rates.

Derivative contracts can only be entered into with counterparties which have a low credit risk, and must fall within the requirements for inclusion in the cover pool (minimum credit quality step 2, rating A-/A3).[4] EBK will only enter into derivative contracts within the framework established by the International Swaps and Derivatives Association (ISDA). ISDA master agreements with credit support annex (CSA) are based on a standardised template utilised by most of the Norwegian covered-bond issuers who enter into derivative contracts. They are used with each individual counterparty and, for the latest version of the template, for each currency in the underlying covered bond issue.

The company calculates counterparty risk in derivatives using standardised methods.[5] Account is taken of financial collateral in the form of cash and securities[6] when calculating capital

[3] FOR-2007-05-25-550 Regulations on bonds in credit institutions, sections 5 and 7.
[4] Should the derivatives be downgraded below credit quality step 2, they can still be included in the cover pool providing the counterparty provides satisfactory collateral.
[5] FOR-2006-12-14-1506 Capital requirement regulations, chapter 23.
[6] FOR-2006-12-14-1506 Capital requirement regulations, chapters 17 and 18.

requirements related to the counterparty risk in derivatives. At 31 December 2014, the company had the following counterparty exposure in derivatives by rating category.

Table 13 Counterparty risk in derivatives pursuant to the standardised method (amounts in NOK 1 000)

Rating on derivative counterparty	EAD*	Credit quality step	Risk weight	Risk weighted assets
AA	1,181,366	1	20 %	236,273
A	1,702,478	2	50 %	851,239
	2,883,844			**1,087,512**

*Exposure at default, the company's exposure to derivatives, is calculated as the maximum of the derivative's potential for exposure and market value less collateral received in the form of cash or

CSA agreements have been signed with all the company's derivatives counterparties. The company's contracts with derivative counterparties specify that the company has the unilateral right to collateral for the market values of derivatives which exceed the predetermined rating limits. Since the CSA agreements are unilateral, EBK will avoid finding itself in a position where it needs to post collateral in the event of a possible downgraded rating. Market values are normally calculated weekly in the existing agreements. EBK has established daily valuation and cash posting with some counterparties and is working to do the same with additional counterparties, which helps to reduce the company's credit risk even further. During 2014, EBK entered into agreements which also permit securities to be accepted as collateral from some counterparties. Underlying securities are not regarded as part of the company's counterparty risk, since they are off the balance sheet. Nevertheless, limits must be set on the securities considered acceptable as collateral, and a spread sought between different counterparties. This is regulated in the agreement with the counterparties.

- **CVA risk**

CRD IV introduced a new requirement intended to cover the risk related to changes in the fair value of bilateral derivative contracts which are not traded on a stock exchange.[7] This additional requirement is calculated on the basis of the counterparty's creditworthiness and is called the credit valuation adjustment (CVA).[8] The CVA supplement became part of the calculation basis from 30 September 2014, and was calculated to be NOK 1.7 billion at 31 December.

Table 14 Total calculation basis for counterparty risk related to derivatives and bank deposits at 31 Dec 14 (amounts in NOK 1 000)

Risk-weighted assets		Amount
Bank deposits		741,622
Derivatives		1,087,512
Credit value adjusment (CVA)		1,717,691
Total		**3,546,825**
Pillar I capital requirement 8%	**8 %**	**283,746**

MANAGEMENT AND CONTROL

The company has established a policy and associated parameters for counterparty risk which forms the basis for management and control of this risk in EBK. The status of compliance with the

[7] Bilateral derivative contracts are also called over-the-counter or OTC derivatives.
[8] FOR-2006-12-14-1506 Capital requirement regulations, chapter 20a.

company's policy for counterparty risk is assessed continuously, and the position in relation to the approved level of risk acceptance is reported quarterly to the board in the risk and compliance report.

CAPITAL REQUIREMENTS

No buffer is assumed to be required by the company for handling a loss related to counterparty risk. This is because the capital requirement calculated in accordance with Pillar I is considered to cover the potential risk of loss in the portfolio.

10 MARKET RISK

Definition: *Market risk is the risk of loss on the market value of portfolios of financial instruments as a consequence of fluctuations in interest rates, credit spreads and exchange rates.*

RISK APPETITE AND EXPOSURE

The company's business purpose is to obtain favourable funding by issuing covered bonds. This means that its excess liquidity must satisfy legal and regulatory requirements concerning what may be included in the cover pool. The objective of the company's investment of surplus liquidity is to have liquidity available at all times to secure the financing of growth and maturation, and to secure the highest possible return within specified risk parameters. Surplus liquidity is held in bank deposits or fixed-income securities in Norwegian kroner and euros. Liquidity in euros reflects the receipt of cash collateral in this currency from counterparties to derivatives in line with the requirements in the derivative agreements. The company's surplus liquidity will be invested at low to moderate risk. Risk will normally comprise credit-spread and interest-rate risk.

The company has established parameters for the liquidity portfolio.

- Interest-rate risk: the average duration of all surplus liquidity investments will be less than six months. The duration of the individual security must be less than one year when derivatives are taken into account. For repurchase agreements, the duration of the underlying security must be less than three years.

- Credit/spread risk: the average tenor for all surplus liquidity investment must be less than two years. The tenor of an individual security must be less than 3.5 years. The tenor for repurchase agreements must be less than 100 days.

- Foreign-exchange risk: the liquidity portfolio will not accept unsecured foreign-exchange risk

The company's total risk parameter for credit-spread and interest-rate risk will be five per cent of its total tier 2 capital, with an expected composition of two per cent interest-rate risk and three per cent credit-spread risk. The interest-rate risk, including the maximum permitted value change, is calculated as the consequence of a one percentage point parallel change in interest rates. The credit-spread risk with the issuer is calculated primarily on the basis of the Financial Supervisory Authority's module for market risk. The model is based on rating and credit quality step. The company calculates capital requirements related to market risk pursuant to part II of the capital requirement regulations, standardised method for credit risk.

EBK's portfolio of securities totalled NOK 7.96 billion at 31 December 2014 and constituted about 10 per cent of the company's total assets. It is invested in government bills, covered bonds and municipal bills, where all counterparties had an AAA rating at 31 December. The portfolio varies in size in line with the company's liquidity requirements over the coming year. The company calculated the position risk for debt instruments at 31 December 2014, based on the standardised method for credit risk (Pillar I).

Table 15 Calculation basis and capital requirement for market risk (amounts in 1 000s)

Assets (amount in NOK 1 000)	Amount	Risk weight	Risk-weighted assets	Capital requirement
Government bonds	522,911	0 %	-	-
Government bonds EUR	1,365,791	0 %	-	-
Covered bonds	4,626,065	10 %	462,607	37,009
Covered bonds EUR	215,939	10 %	21,594	1,728
Regional or local government	1,230,362	20 %	246,072	19,686
Total	**7,961,068**			**58,422**

The company is also exposed to market risk in the form of interest-rate risk which arises from differences between interest terms for borrowing and lending. This risk is treated in detail in section 11 on interest-rate risk related to net interest income.

MANAGEMENT AND CONTROL

The company has established policies for asset liability and for investment management with an associated investment mandate, which form the basis for management and control of market risk. The company's risk management and compliance function continuously assesses exposure in relation to approved risk acceptance and parameters. It prepares quarterly risk and compliance reports for the board, which quantify and assess market risk exposure in relation to risk appetite. The board-approved parameter as a percentage of tier 2 capital is meant to cover the interest-rate risk of a one percentage point parallel change in the interest-rate curve and a 0.5 percentage point increase in credit spread outcomes in the company's portfolio of securities. Market risk in the liquidity portfolio is managed on a daily basis by the funding department.

CAPITAL REQUIREMENTS

EBK applies the standardised method for credit risk to calculate market risk. The capital requirement was calculated to be about NOK 58 million at 31 December 2014, and is included in the total capital requirement for credit risk.

Further evaluation of capital requirements for market risk is incorporated in the assessment of the Pillar II buffer, and the company's capital targets are considered to be sufficient to meet risks over and above the minimum regulatory requirements.

11 INTEREST-RATE RISK RELATED TO NET INTEREST INCOME

Definition: *Risk associated with net interest income arises from differences between interest terms for borrowing and/or lending, and from borrowing by the company in different markets than those it lends to, so that the borrowing interest rate may change without the company being able to adjust the lending rate equally quickly.*

RISK APPETITE AND EXPOSURE

Interest-rate risk will be limited by ensuring that lending on floating interest-rate terms is financed by borrowing/derivatives at floating interest rates, and that lending at fixed interest rates is hedged with derivatives at floating rates. The company will make active use of derivatives to reduce interest-rate risk. Interest-rate risk related to net interest income must be low.

The bulk of the residential mortgages in EBK's portfolio have a variable interest rate. Pursuant to the Financial Contracts Act, interest rates on such mortgages can be adjusted at six weeks notice in line with the development of the company's borrowing costs. EBK is not subject to such notice in relation to the interest rates it charges to the owner banks. Interest-rate changes can therefore be implemented more quickly, which ensures efficient adjustment to changes in EBK's funding costs.

EBK permits the addition of fixed-rate mortgages to the cover pool, and this is regulated by separate agreements with the banks. EBK establishes the interest rate for fixed-interest mortgages, while the owner banks specify customer terms and interest rates based on borrowing costs and risk assessment for the advance.

EBK uses hedge accounting pursuant to the IFRS on borrowing at fixed interest rates, and an interest swap must be assessed as very effective when entered into. The company measures interest-rate risk on the balance sheet quarterly, based on the duration of the various claims and commitments. Duration means the number of years until the next interest-rate adjustment.

Table 16 Interest-rate sensitivity in the balance sheet (amounts in NOK 1 000)

Interest rate sensitivity	Duration	Amount	Effect
Funding	0.14	64,850,698	91,140
Lending with floating rate	-0.12	59,817,636	(71,781)
Lending with fixed rate	-3.23	1,021,261	(32,970)
Derivative lending	2.91	1,969,578	28,627
Government bonds*	-0.35	1,869,041	(6,622)
Covered bonds*	-0.13	4,825,490	(6,110)
Municipalities*	-0.13	1,225,999	(1,643)
Bank deposits*	-0.01	3,708,022	(254)
Total including liquidity portfolio*			**387**
Total effect lending			**15,016**

Fixed interest rates on the company's borrowing have longer periods than on its lending. Circumstances where the interest rate for funding costs increase by one percentage point will in reality produce a gain for the company as long as the asset side of the balance sheet has a shorter fixed-interest period than the liability side. Other factors may nevertheless exist which prompt the company to reduce its lending margin and net interest income, but these will be independent of the interest-rate risk.

MANAGEMENT AND CONTROL

The company has established a policy for asset liability management which forms the basis for total interest-rate risk in its balance sheet. This also includes the liquidity portfolio, and interest-rate risk associated with net interest income relates to the company's total interest terms.

In the event of an increase in financing costs or money market interest rates, a decision to adjust the interest-rates charged to the owner banks will be made by the CEO in consultation with the rest of the company's executive management and based on forecasts of anticipated interest-rate developments and planned new funding. Such forecasts are made by the finance and accounting department.

Interest-rate risk is measured quarterly as the change in value arising from a one percentage point adjustment to the level of interest rates, and the company has defined maximum exposure related to this. The exposure is reported quarterly in the risk and compliance report submitted to the board.

CAPITAL REQUIREMENTS

Interest-rate risk related to net interest income is not included in Pillar I capital requirements. An assessment of capital requirements for interest-rate risk is included in the assessment of the Pillar II buffer, and the company's capital targets are considered adequate to cover risks over and above the minimum regulatory requirements.

12 LIQUIDITY AND REFINANCING RISK

Definition: The risk that the company will be unable to meet its commitments as and when they fall due without incurring substantial costs in the form of expensive refinancing or the need for premature realisation of assets. In the worst case, liquidity risk is the risk that the company will be unable to refinance itself sufficiently in order to meet commitments as and when they call due.

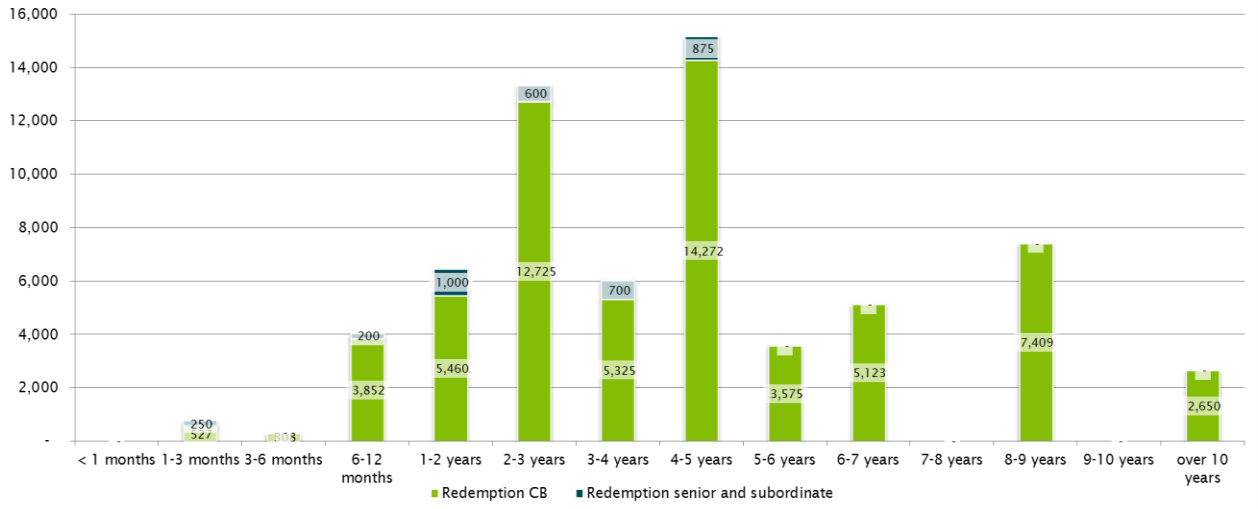
RISK APPETITE AND EXPOSURE

EBK finances lending primarily through the issue of covered bonds. Through its opportunity to make such issues, the company achieves lower borrowing costs than its owner banks. The company will also raise ordinary senior unsecured bonds and certificate loans, primarily involving the issue of certificate loans to cover overcollateralization related to the Euro Medium Term Covered Note (EMTCN) programme. EBK has entered into an international borrowing programme for its bonds. This EMTCN programme was signed and listed on the London Stock Exchange on 10 August 2007, and is revised annually.

The company has established parameters for financing and liquidity risk to keep financing and liquidity risk satisfactorily low, and to comply with section 2, sub-section 32 of the Act on Financing Activity and Financial Institutions, the regulations for credit institutions issuing covered bonds and the regulations on sound liquidity management.

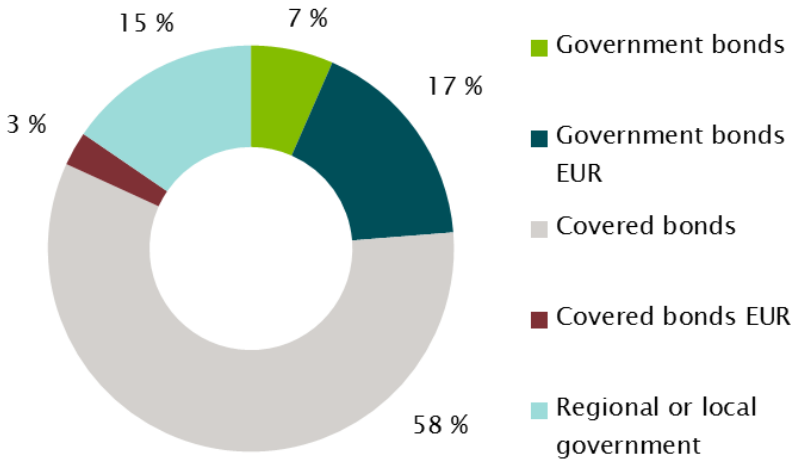
EBK had a good liquidity position at 31 December 2014, and issued a total of NOK 10 billion in bonds and certificates during 2014. The company complied with all parameters for risk exposure during the year. Because funding activity was low through 2014, the average remaining tenor on total funding and covered bonds declined somewhat. However, attention has been devoted to increasing the tenor for funding in the market for senior unsecured bonds. Nevertheless, activity in 2014 and the status at 31 December were in line with targets and parameters for liquidity management.

Figure 7 Redemption profile at 31 December 2014 (amounts in NOK million)



The company's need for funding was limited in 2014 because of low growth in lending. Credit reports from brokers indicate that EBK could have obtained funding at very advantageous terms compared with earlier years. Investor interest in subscribing to the company's covered bonds was again very high in 2014, and the company has also achieved good terms for its borrowing.

Figure 8 Composition of the liquidity buffer



MANAGEMENT AND CONTROL

EBK has established a separate risk policy for financing risk, including defined risk appetite, risk parameters and a crisis plan in the event of insufficient liquidity. This risk policy forms the basis for liquidity management.

Financing and liquidity risk is managed through parameters for financing structure, requirements for diversification of instruments, markets and tenors, and the establishment of contingency facilities. An agreement has also been entered into between the shareholders and EBK to ensure that the company can access liquidity in a crisis. The agreement commits the owner banks, under given circumstances, to purchase the company's covered bonds limited to the maturity of the

company's covered bonds issued under the EMTCN programme and the associated swap agreements over the coming 12 months. EBK's own liquidity is deducted when calculating the liquidity obligation. The owner banks can deposit these covered bonds as collateral with the Central Bank of Norway in exchange for a haircut. EBK is not permitted to make such deposits in the Central Bank of Norway.

The company has a separate funding department headed by the CFO, who is responsible for operational liquidity management and reports to the CEO. The funding department utilises liquidity forecasts, particularly when obtaining new funding. The future liquidity holding, refinancing indicators and the average time to maturity of funding are then simulated. The board receives a quarterly overview of the maturity structure of the company's assets and liabilities, in addition to the development of the company's liquidity indicators in order to evaluate liquidity risk.

EBK's risk and compliance function measures exposure linked to financing and liquidity risk in relation to approved parameters on a continuous basis, and reports quarterly on the actual exposure in the risk and compliance report to the board. These reports provide a basis for the executive management and the board to assess the exposure status in relation to established parameters and targets. The company performs stress tests which simulate the effect of possible liquidity crises, including market-specific, company-specific and combined market/company crises.

CAPITAL REQUIREMENTS

Liquidity and refinancing risk is not included in the capital requirements defined under Pillar I. The assessment of capital requirements for liquidity risk is included in the assessment under ICAAP, and the company's capital targets are considered adequate to cover risks over and above the minimum regulatory requirements.

13 OPERATIONAL RISK

Operational risk is the risk of loss as a result of inadequate or deficient internal processes or systems, human error, or external events. Operational risk also comprises compliance and legal risk.

RISK APPETITE AND EXPOSURE

EBK has a simple and readily comprehensible organisation, and has therefore adopted the basic indicator method for calculating capital requirements. With this approach, the calculation basis for the minimum primary capital requirement is 15 per cent of average income over the past three years multiplied by 12.5. See section 42, sub-section 1 of the capital requirement regulations.

Table 17 Calculation basis and capital requirement for operational risk (amounts in NOK 1 000)

Operational risk	2012	2013	2014
Net income	137,460	194,789	166,531
Average income			166,260
Calculation basis			311,738
Capital requirement			**24,939**

The company will have a low-risk profile for operational risk. Operational risk which could expose EBK to loss consists virtually entirely of a failure to establish adequate collateral, deficient internal control or failure of IT systems.

MANAGEMENT AND CONTROL

EBK has established a policy for operational risk which forms the basis for its management and control. A number of guidelines and routines have been implemented for all significant processes in the company. These are intended to help identify that operational risk is being handled in a way which ensures an acceptable level of residual risk. The company will have an updated business continuity plan at all times, which ensures that it can maintain its operations, while functions will have adequate back-up. Relevant contingency plans have also been drawn up to deal with crises.

The company monitors operational risk through reporting and registering undesirable events, pursuing compliance activities, internal auditing and so forth. The company's risk and compliance department prepares quarterly risk and compliance reports, which quantify and assess operational risk through event reporting. These reports provide the executive management and the board with the basis for assessing the status of exposure in relation to established parameters and targets.

CAPITAL REQUIREMENTS

EBK applies the basic indicator method to calculate the capital requirement for operational risk. The capital requirement was calculated to be about NOK 25 million at 31 December 2014.