Risk and capital management 2012

SpareBank 1 SR-Bank Group

Contents

INTRODUCTION

This document has been prepared to provide the market with the best possible information on SpareBank 1 SR-Bank's risk and capital management. It is also intended to cover the stipulated requirements for publication of risk information in accordance with the "Capital Requirements Regulations".

The Group’s information strategy emphasises an extended dialogue with the different stakeholder groups, where openness, predictability and transparency are vital factors. The information shall be correct, relevant and timely with regard to the Group's development and results, and it shall ensure that the Group's different stakeholder groups can keep continuously updated and create confidence in the investment market.

This document is updated each year with the exception of information on capital adequacy and the minimum regulatory capital requirements, which is updated quarterly. This will be updated in separate enclosures (Excel).

The core purpose of the banking industry is to create value by assuming deliberate and acceptable risk. SpareBank 1 SR-Bank therefore invests significant resources in the further development of risk management systems and processes in line with leading international practice. SpareBank 1 SR-Bank makes extensive use of risk models in its risk management. Risk and capital management in SpareBank 1 SR-Bank supports the Group’s strategic development and achievement of goals while ensuring financial stability and sound management of assets.

The overall risk exposure for SpareBank 1 SR-Bank is moderate. The pure core capital adequacy ratio for SpareBank 1 SR-Bank is 10.0 per cent at the end of 4th quarter of 2012, which is well above the Financial Supervisory Authority of Norway's minimum requirement of 9 per cent. SpareBank 1 SR-Bank is well-equipped to meet higher capitalisation requirements from the authorities and the market in the future.

SpareBank 1 SR-Bank considers its liquidity buffer to be sound, and the Group finds the liquidity in the European credit market to be good.

Credit risk represents a significant part of the Group's risk. The credit quality of SpareBank 1 SR-Bank's portfolio is good and has been stable over the last year. SpareBank 1 SR-Bank has a diversified portfolio.

The retail market represents 65 per cent of the total loan exposure of SpareBank 1 SR-Bank, which consists primarily of high-quality mortgage loans. The percentage of loans with a debt to asset ratio of over 85 per cent has declined over the last year as a result of stricter guidelines for home mortgages. The Group's largest sectoral concentration is in the area of commercial property, which represents around 10 per cent of the total loan portfolio (EAD), including the retail market. The property portfolio intended for rental consists primarily of long-term leases with financially solid tenants.

Experience from the financial crisis shows that focusing on operational risk and organisational culture is an important part of good risk management. SpareBank 1 SR-Bank has therefore prepared and conducted an organisational survey that measures the organisation's operational risk culture in partnership with the University of Stavanger (UiS). This survey is unique in a bank context and provides a basis for measuring and understanding how SpareBank 1 SR-Bank's organisational culture affects the Group's exposure to operational risk. The results from the survey confirm that SpareBank 1 SR-Bank has a good risk culture, in which the employees know what is expected of them and experience support from the organisation to act in an ethically proper manner.

SpareBank 1 SR-Bank is well-equipped to create value for the region the Group it is part of.

SpareBank 1 SR-Bank

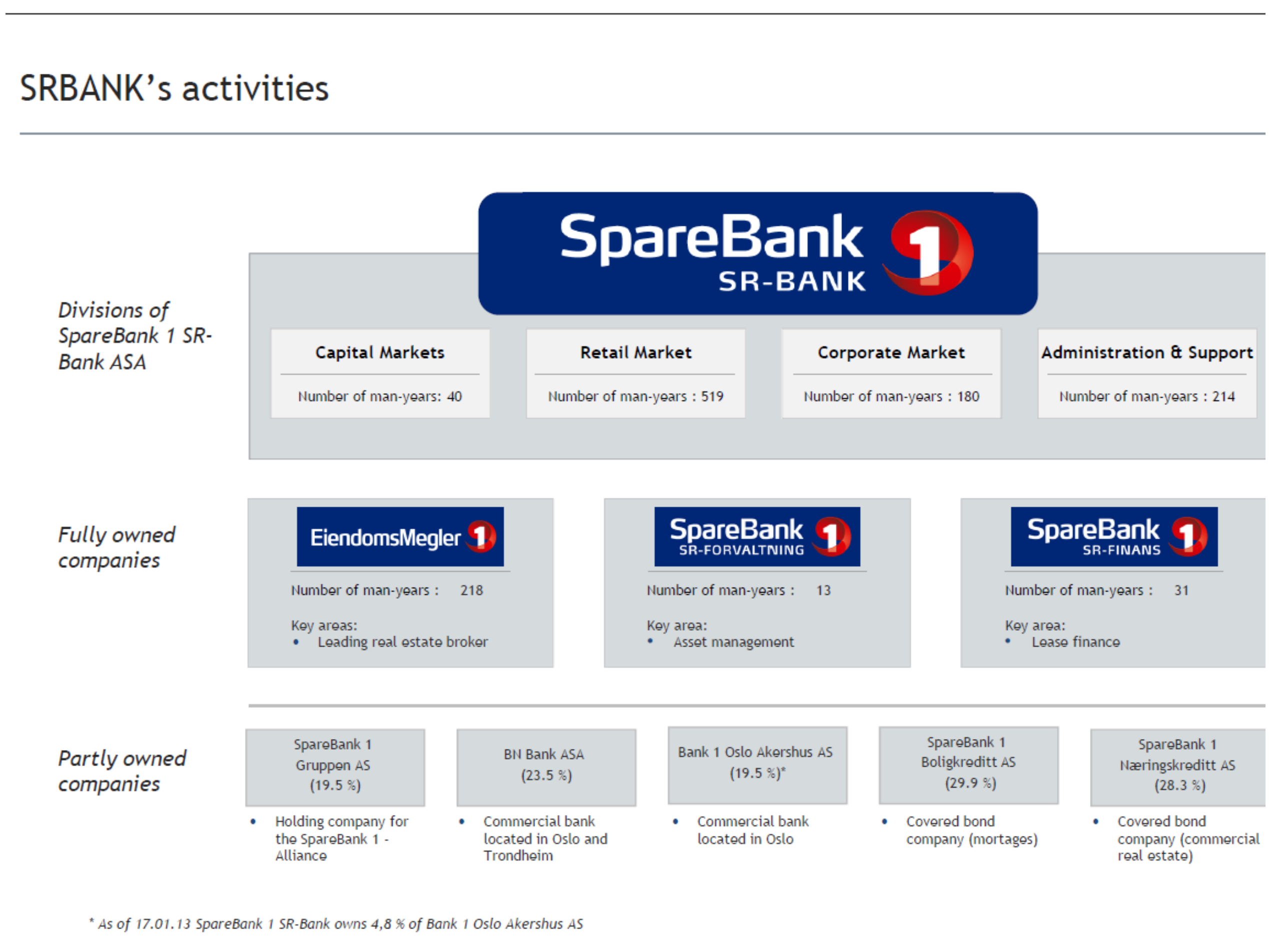
SpareBank 1 SR-Bank is currently Norway's leading limited savings bank with total assets of NOK 141 billion. SpareBank 1 SR-Bank has been one of the most profitable banks in the Nordic region over the past 15 years. Profit before tax was NOK 1.76 billion as at the 4th quarter of 2012. The Group's market area is Rogaland, Hordaland and the Agder counties, and it has approximately 300,000 customers. There are 1,330 employees.

SpareBank 1 SR-Bank is a financial group with a complete product range in the retail market, corporate market and the public sector.

In addition to the actual banking operations, the Group has expertise in funding, foreign exchange advice, funds management, securities trading, insurance, real estate brokering and financial advice.

The Group's headquarters are located in Stavanger. Summary of companies in the SpareBank 1 SR-Bank Group is illustrated in the figure below.

Figure 1: *Wholly-owned and partly owned companies in the SpareBank 1 SR-Bank Group*



SpareBank 1 Alliance

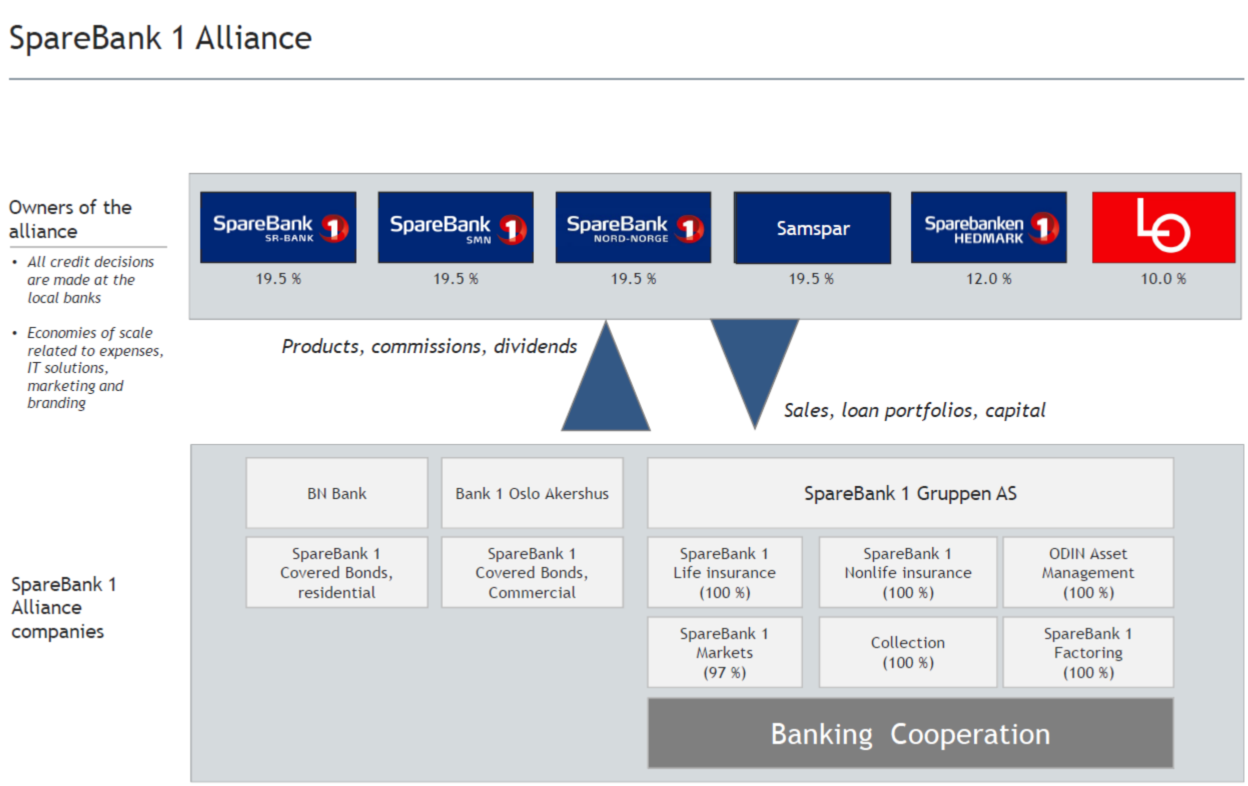
The SpareBank 1 Alliance is a banking and product alliance that consists of several independent banks. The SpareBank 1 Alliance represents one of the largest providers of financial products and services in the Norwegian market. The independent banks in the alliance are SpareBank 1 SR-Bank, SpareBank 1 SMN, SpareBank 1 Nord-Norge, SpareBanken Hedmark, and Samarbeidende Sparebanker. The banks in the SpareBank 1 Alliance distribute financial products from jointly owned companies and collaborate in key areas such as brands, work processes, skills development, IT operations, systems development and purchasing. The SpareBank 1 Alliance has entered into strategic agreements with the Norwegian Federation of Trade Unions (LO) and affiliated trade unions.

The SpareBank 1 Alliance's main goal is to ensure each bank's independence and regional affiliation through strong competitiveness, profitability and financial strength.

The product companies in the SpareBank 1 Alliance are owned by the banks through the holding company SpareBank 1 Gruppen AS. The banks in the SpareBank 1 Alliance also own SpareBank 1 Boligkreditt AS, SpareBank 1 Næringskreditt AS, Eiendomsmegler 1, Alliansesamarbeidet SpareBank 1 Utvikling DA, SpareBank 1 Oslo Akershus and BN Bank ASA.

The figure below provides a summary of the ownership structure of the SpareBank 1 Alliance.

Figure 2: SpareBank 1 Alliance



Objective of risk and capital management in SpareBank 1 SR-Bank

The core purpose of the banking industry is to create value by assuming deliberate and acceptable risk. The Group therefore invests significant resources in the further development of risk management systems and processes in line with leading international practice.

SpareBank 1 SR-Bank's risk and capital management underpins the Group's strategic development and goal attainment, while ensuring financial stability and prudent asset management. This is achieved through a strong organisational culture that is characterised by:

- A high awareness of risk management
- A good understanding of which risks drive earnings
- Striving for optimal capital application within the adopted business strategy
- Preventing unexpected single events from damaging the Group's financial position to a serious extent.
- Exploiting synergies and diversification effects

Overall framework for management and control

SpareBank 1 SR-Bank shall have a moderate risk profile and no single event shall be capable of seriously harming the Group's financial position either. The overall risk exposure for SpareBank 1 SR-Bank is deemed to be moderate.

SpareBank 1 SR-Bank is exposed to various types of risk. The most important risk groups are:

- **Credit risk:** the risk of loss resulting from the customer's or counterparty's inability or unwillingness to fulfil his obligations
- **Market risk:** the risk of loss due to changes in observable market variables such as interest rates, foreign exchange rates and securities markets
- **Operational risk:** the risk of losses due to weak or inadequate internal processes or systems, human error or external incidents
- **Liquidity risk:** the risk that the Group is unable to refinance its debt or does not have the ability to fund increases in assets without significant additional costs
- **Ownership risk:** the risk that SpareBank 1 SR-Bank bears if it suffers negative results from stakes in strategically owned companies and/or the need to inject fresh capital into these companies. Owned companies are defined as companies where SpareBank 1 SR-Bank has a significant stake and influence.
- **Business risk:** the risk of unexpected income and cost variations due to changes in external factors such as market conditions or government regulations
- **Reputation risk:** the risk of a failure in earnings and access to capital because of lack of trust and reputation in the market, i.e. customers, counterparties, stock market and authorities
- **Strategic risk:** the risk of losses resulting from the wrong strategic decisions.
- **Compliance risk:** the risk that the Group incurs public sanctions/penalties or financial loss as a result of failure to comply with legislation and regulations.

In order to ensure an effective and adequate process for risk and capital management, the framework is based on a variety of elements that reflect the manner in which the Board and the executive management team run the Group. The principal elements are described below:

The Group's strategic targets: SpareBank 1 SR-Bank shall be Southern and Western Norway's most attractive supplier of financial services based on:

- Good customer experiences
- A strong team spirit and professionalism
- Local roots and decision-making authority
- Financial strength, profitability and confidence in the market

Risk identification and analysis: The process for risk identification is based on the Group's strategic targets. The process is forward-looking and covers all of the Group's significant risk areas. In areas where the effect of the established control and management measures is not considered satisfactory, improvement measures are implemented. Measures that reduce probability shall take precedence over measures that reduce consequences.

Capital allocation: Return on economic capital is one of the most important strategic result measurements for the internal control of SpareBank 1 SR-Bank. This implies that capital is allocated to business areas in accordance with the calculated risk of the operation and the return on capital is monitored continuously.

Financial projections and stress tests: Projections of expected financial development are made for the next 5 years, based on the strategic targets and the business plan. In addition, projections are made of a situation involving a serious economic recession.

To assess the consequences of an economic downturn, the Group largely focuses on those areas of the economy that affect financial development. This is primarily the development in the demand for credit, the stock market, interest rate market and the development of credit risk. In addition to having an impact on the yield of the underlying assets, an economic recession will also have an impact on customer savings habits. The purpose of these projections is to calculate how the financial development in activities and the macroeconomic situation will impact the Group's financial development, including the return on equity, the funding situation and capital adequacy.

Evaluation and measures: The analyses provide the executive management team and the Board with sufficient understanding of the risk so that they can assess whether the Group has an acceptable risk profile and ensure that the Group is adequately capitalised in light of the risk profile and strategic targets.

SpareBank 1 SR-Bank prepares capital plans in order to achieve long-term and effective capital management and ensure that the Group's capital adequacy is acceptable taking into account the risk exposure. The capital plan takes into account both expected developments and a situation with a serious economic downturn over a number of years. SpareBank 1 SR-Bank has also prepared contingency plans for such critical situations.

Reporting and follow-up: The Group's overall risk exposure and risk trends are monitored via periodic risk reports for the executive management team and Board. General risk monitoring and reporting is performed by the Risk Management and Compliance Department which is independent of the business units.

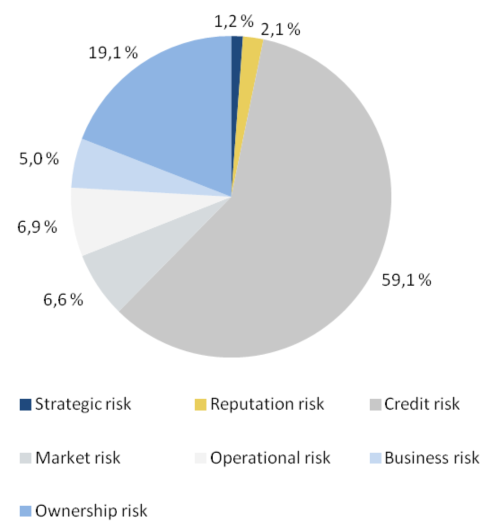
Organisation and organisational culture: SpareBank 1 and SR-Bank aim to maintain a strong organisational culture characterised by a high level of awareness of risk management. The organisational culture comprises management philosophy and the people in the organisation with their personal attributes, such as integrity, core values and ethics. It is difficult to compensate for an inadequate organisational culture by using other control and management measures. SpareBank 1 SR-Bank has therefore established a clearly defined value base and ethical guidelines which have been clearly communicated and presented throughout the organisation.

Overall risk exposure

Risk-adjusted capital describes how much capital the Group believes it needs to cover the real risk that the Group has assumed. Since it is impossible to fully protect against all losses, the Group has stipulated that the risk-adjusted capital shall cover 99.97 per cent of the potential unexpected losses.

The graph below illustrates risk-adjusted capital distributed by the type of risk at the end of 2012.

Figure 3: Risk-adjusted capital distributed by type of risk



Credit risk represents 59 per cent of the overall risk picture as measured by the risk-adjusted capital. After credit risk, ownership risk represents the largest risk category, at 19 per cent.

Capital adequacy rules and regulations

Introduction to current capital adequacy rules and regulations – Basel II

The EU's capital adequacy directive was introduced in Norway on 1 January 2007. The regulations are based on a standard for capital adequacy calculations from the Bank for International Settlements (BIS). The object of the capital adequacy requirements is to strengthen stability on the financial market by means of:

- More risk-sensitive capital requirements
- Improved risk management and control
- Closer supervision
- More information to the market

The new capital adequacy requirements are based on three pillars:

Pillar I: Minimum regulatory capital requirements

Pillar II: The bank's internal risk and capital adequacy assessment and individual supervisory follow-up.

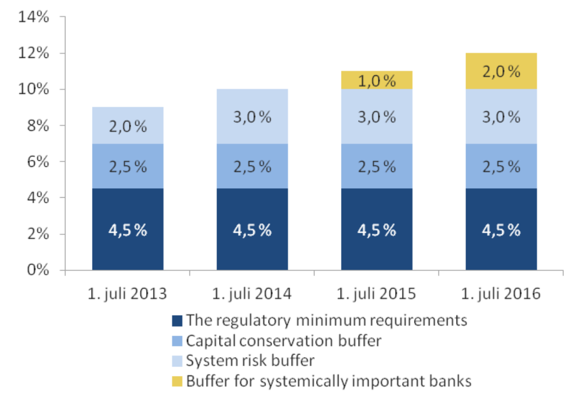
Pillar 3: Disclosure of information

Introduction to the new regulations – Basel III

On 16 December 2010 the Basel Committee presented the new minimum requirements for capital adequacy and liquidity for the banking industry (Basel III). The EU will implement these regulations in the Capital Requirements Directive CRD IV and the Capital Requirements Regulations CRR. These regulations will enter into force from January 2014.

On 22 March 2013 the Ministry of Finance proposed the introduction of the new capital requirements somewhat earlier than the implementation deadline for the international regulations. The figure below illustrates the new proposed statutory capital requirements for Norway.

Figure 4: Planned phasing in of the new requirements in Norway



The regulatory minimum requirements, capital conservation buffer and system risk buffer will apply to all the banks, while the buffer for systemically important banks will apply to banks that are particularly important to the economy.

In addition, a countercyclical buffer[1] of 0 to 2.5 per cent of the pure core capital is proposed. The level will be adapted to the economic situation.

Including the countercyclical buffer, the new minimum level for the pure core capital adequacy ratio will be up to 14.5 per cent.

For a transitional period, the current IRB banks will not have minimum capital requirements based on the current capital adequacy rules and regulations (Basel II) that are lower than 80 per cent of the minimum capital requirements based on the old capital adequacy rules and regulations (Basel I). The Norwegian authorities have decided that the "IRB floor" will be maintained for the time being, but that it will in principle cease upon the introduction of Basel III.

Other new capital and liquidity requirements pursuant to Basel III include:

- New hybrid capital and subordinated loan requirements
- New deduction rules for core and regulatory capital
- Change in the capital consolidation rules for the SpareBank 1 Group[2]

[1] During periods with high credit growth.

[2] In the current regulations, the book value of the companies is deducted by 50 per cent in the pure core capital and 50 percent in the supplementary capital, respectively. In the proposed new regulations, the book value of the companies in excess of 10 per

- Requirements for the unweighted equity ratio (leverage ratio)
- Quantitative liquidity requirements – Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR).
- Introduction of higher capital requirements for derivative positions (Credit Valuation Adjustment – CVA)

The aforementioned changes will be introduced during the period from 2014 to 2019, with certain transitional rules.

In addition to the aforementioned changes, the Ministry of Finance published a consultation memorandum concerning stricter risk-weighting for home mortgage loans. The four proposals presented could replace the transitional rules.

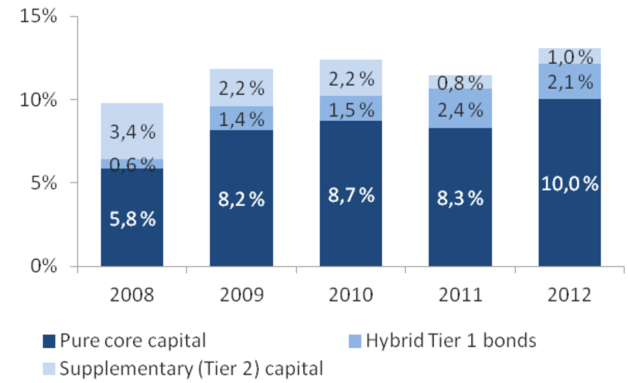
- Capital requirements as under the standard method (35 per cent risk-weighting for home mortgage loans)
- Increase the LGD floor[3] from 10 to 20 per cent
- Risk weight multiplier of 2, i.e. a doubling of the current risk weights
- Minimum requirement of 25 per cent for home mortgage loan risk weights

Capital adequacy – SpareBank 1 SR-Bank

During the period from 2008 to 2012, SpareBank 1 SR-Bank increased its pure core capital by NOK 6 billion, which more than doubled its core (Tier 1) capital. At the end of 2012, SpareBank 1 SR-Bank had a pure core capital adequacy of 10.0 per cent and capital adequacy of 13.1 per cent, compared with 8.3 per cent and 11.4 per cent at the end of 2011. These calculations observe the transitional rule, which stipulates that the capital requirements when using internal methods cannot be less than 80 per cent of the capital requirements given in Basel I ("the Basel I floor").

The figure below illustrates the change in capital adequacy during the period from 2008 to 2012.

Figure 5: Capital adequacy



SpareBank 1 SR-Bank has prepared a capitalisation strategy to achieve its future capital targets. SpareBank 1 SR-Bank is well-equipped to meet uncertainty regarding the performance of the economy and higher capitalisation requirements from the authorities and the market.

cent of the pure core capital in SpareBank 1 SR-Bank will be deducted from the pure core capital.

[3] *Loss Given Default (LGD)*

Minimum regulatory capital requirements

In Pillar 1 different methods the banks can choose from when calculating capital requirements are described. The various methods are illustrated in the figure below:

Table 1: Alternative methods for calculating the minimum regulatory capital requirements

Credit risk	Market risk	Operational risk
Standard method	Standard method	Basic method
Foundation IRB Approach*	Internal measurement approach*	Standardised approach
Advanced IRB Approach*		AMA approach*

* The methods require permisson by the Financial Supervisory Authority of Norway

The minimum requirements for regulatory capital amount to 8 per cent of the weighted balance (calculation basis). In principle, there are two different approaches to the calculation of the minimum regulatory capital requirements according to the capital adequacy rules and regulations. One approach is based on standardised approach rules, while the other is based on the application of internal ratings. In the internal ratings based (IRB) approach, the minimum regulatory capital requirements will be based on the banks' internal risk assessments. Consequently, the statutory minimum capital adequacy requirement is more risk sensitive, so that the capital requirement corresponds more closely to the risk in the underlying portfolios or activities. Use of internal models must be approved in advance by the supervisory authorities.

The table below shows the main methods that SpareBank 1 SR-Bank uses for calculation of its capital requirements for credit, market and operational risk, respectively.

Table 2: SpareBank 1 SR-Bank's methods for calculating the minimum regulatory capital requirements

Type of risk	Portfolio	Regulatory method
Credit risk	States – parent bank	Standard method
	Institutions – parent bank	Standard method
	Housing cooperatives, clubs and associations – parent bank	Standard method
	Enterprises – parent bank	IRB – Basic
	Mass market – parent bank	IRB – mass market (advanced)
	SpareBank 1 SR-Finans AS – subsidiary	Standard method
	SpareBank 1 SR-Investering AS – subsidiary	Standard method
	SpareBank 1 SR-Forvaltning AS – subsidiary	Standard method
	Mass market – SpareBank 1 Boligkreditt AS	IRB – mass market (advanced)
	Enterprises – SpareBank 1 Næringskreditt AS	Standard method
	Enterprises – BN Bank AS	Standard method
	Mass market – BN Bank AS	Standard method
Market risk	Equity risk – parent bank	Standard method
	Debt risk – parent bank	Standard method
	Currency risk – parent bank	Standard method
	Subsidiaries and part-owned companies	Standard method
Operational risk	SpareBank 1 SR-Bank including subsidiaries	Standardised approach
	Other part-owned companies	Standard method

For the subsidiary SpareBank 1 SR-Finans AS, plans have been prepared for a transition to the IRB approach, but the portfolio reports will be based on the standard method for the time being. The company's principal activities are lease funding and secured car loans.

SpareBank 1 SR-Bank owns 29.9 per cent of SpareBank 1 Boligkreditt AS, 28.3 per cent of SpareBank 1 Næringskreditt AS and 23.5 per cent of BN Bank ASA as at the 4th quarter of 2012. SpareBank 1 SR-Bank's share of the capital requirements for these companies are consolidated in SpareBank 1 SR-Bank's capital adequacy reporting based on the Group's ownership interest.

SpareBank 1 SR-Bank owns 19.5 per cent of the SpareBank 1 Gruppen AS and 19.5 per cent of Bank 1 Oslo Akershus AS as at the 4th quarter of 2012[4]. The part of the investment in the SpareBank 1 Group's book value that exceeds 2 per cent of the SpareBank 1 Group's regulatory capital is deducted from the regulatory capital and calculation basis in SpareBank 1 SR-Bank.

SpareBank 1 SR-Bank has received permission from the Financial Supervisory Authority of Norway to make use of internal ratings based (IRB) measurement methods for credit risk. The bank has received permission for the use of the Foundation IRB for enterprises (hereinafter referred to as the corporate market) and IRB (Retail IRB) for the mass market (hereinafter referred to as the retail market). This means that the statutory minimum capital adequacy requirement for credit risk will be based on the Group's internal risk models.

When calculating the capital requirements according to the Foundation IRB approach for the corporate market, the probability of default (PD) risk parameter is estimated on the basis of internal ratings. The risk parameters conversion factor (CF) used in determining the exposure at default (EAD) and the loss given default (LGD) are determined based on the standardised approach rules in the Capital Requirements Regulations. SpareBank 1 SR-Bank will submit an application to the Financial Supervisory Authority of Norway in the 2nd quarter of 2013 to use Advanced IRB for corporate exposure.

When calculating the capital requirements according to the IRB approach for the retail market, internal models are used for calculation of the risk parameters probability of default (PD), conversion factor (CF) used in determining the exposure at default and loss given default (LGD).

[4] In the 1st quarter of 2013, SpareBank 1 SR-Bank reduced its ownership interest from 19.5 to 4.8 per cent.

Detailed capital adequacy information

Consolidation

Method of consolidation is the same for accounting purposes and capital adequacy purposes.

Table 3: Consolidation basis (amounts in NOK 1,000)

Subsidiaries **As at 31/12/2012**	**No. of shares**	**Book value**	**Voting rights**	**Consolidation method**
Wholly consolidated companies				
SpareBank 1 SR-Finans AS	334,000	485,566	100%	Acquisition method
EiendomsMegler 1 SR-Eiendom AS	150	97,205	100%	Acquisition method
Westbroker Finans AS	100	0	100%	Acquisition method
SR-Investering AS	3,500	178,191	100%	Acquisition method
SR-Forvaltning AS	6,000	29,019	100%	Acquisition method
SR-Forretningsservice AS	1,000	125	100%	Acquisition method
Kvinnherad Sparebank Eigedom	3,000	15,061	100%	Acquisition method
Rygir Industrier AS Group	69,938,739	3,238	100%	Acquisition method
Etis Eiendom AS	10,000	115	100%	Acquisition method
Total		**808,520**		

As at 31/12/2011				
Wholly consolidated companies				
SpareBank 1 SR-Finans AS	334,000	439,566	100%	Acquisition method
EiendomsMegler 1 SR-Eiendom AS	150	56,885	100%	Acquisition method
Westbroker Finans AS	100	0	100%	Acquisition method
SR-Investering AS	3,500	175,527	100%	Acquisition method
SR-Forvaltning AS	6,000	29,019	100%	Acquisition method
SR-Forretningsservice AS	1,000	125	100%	Acquisition method
Kvinnherad Sparebank Eigedom	3,000	15,061	100%	Acquisition method
Total		716,183		

Table 4: Subsidiaries that report based on the standard method (amounts in NOK million)

SR-Finans AS	**31/12/2012**	31/12/2011
Net regulatory capital	**596**	542
Minimum regulatory capital requirements	**431**	392
Capital adequacy %	**11.07**	11.06

Investments in associated companies

Investments in associated companies are accounted for according to the equity method in the Group and according to the acquisition method in the parent bank. Investments will be treated the same as for capital adequacy purposes except for the Group's investments in SpareBank 1 Boligkreditt AS and SpareBank 1 Næringskreditt AS. Proportionate consolidation is carried out for the Group's capital adequacy.

Investments in joint ventures

Investments in joint ventures are accounted for in accordance with the equity in the Group. For the Group's capital adequacy, the book value of investments in SpareBank 1 Gruppen AS and Bank 1 Oslo Akershus AS is deducted from the regulatory capital and the calculation basis. With regard to the investment in BN Bank ASA, proportionate consolidation is carried out for the Group's capital adequacy. In SpareBank 1 SR-Bank, the investments are recognised according to the acquisition method. The portion of the book value of the investments in SpareBank 1 Gruppen AS and Bank 1 Oslo Akershus AS that exceeds 2 per cent of the regulatory capital of the SpareBank 1 Group and Bank 1 Oslo Akershus is deducted from the regulatory capital and calculation basis.

Table 5: Investments in associated companies and joint ventures

Amounts in NOK 1000	Ownership percentage 31/12/2012	Capital requirements [1] 31/12/2012	Capital adequacy percentage 31/12/2012	Ownership percentage 31/12/2011	Capital requirements [1] 31/12/2011	Capital adequacy percentage 31/12/2011
SpareBank 1 Boligkreditt	29.9	1,713	10.46	34.4	1,553	9.83
SpareBank 1 Næringskreditt AS	27.8	235	12.32	30.7	212	13.67
BN Bank ASA	23.5	581	15.08	23.5	624	13.70

1) SpareBank 1 SR-Bank's share

SpareBank 1 Boligkreditt AS uses the IRB approach in its capital adequacy reporting. The other companies use the standard approach for reporting capital adequacy.

Table 6: Regulatory capital in other financial institutions

Amounts in NOK million	Book value 31/12/2012	Book value 31/12/2011
SR-Pensjonskasse	35	35
Sandnes Sparebank	48	62
Other financial institutions	46	45
Total	**129**	142

SpareBank 1 SR-Bank places an emphasis on maintaining adequate capitalisation at all times for all business units within the Group. The Group's governing bodies have not imposed any limitations on the Board of Directors' authorisation to transfer capital between the parent bank and its subsidiaries and from subsidiary to subsidiary with the exception of regulatory and other statutory limitations.

In addition, there are no provisions in the Articles of Association that impose any such restrictions.

For the same reason, the bank and its subsidiaries do not enter into agreements that impose limitations on the Board of Directors' right to transfer capital as mentioned above. This applies to funding loan agreements and agreements with suppliers and customers.

Accordingly, no restrictions have been placed on the Board's opportunity to transfer capital between the various business units in the parent bank either. Moreover, the transfer of capital between the companies will be regulated by ordinary legislation for these companies and for the financial group as a whole.

As for investment in subsidiaries, the Group has a strategic interest in supporting the activities of SpareBank 1 Boligkreditt AS and SpareBank 1 Gruppen AS. In this connection the Group is concerned about no agreements being entered into or decisions etc. made that entail a restriction of the owner banks' opportunity to transfer capital to these companies if this should be necessary in order to achieve satisfactory capital adequacy or financial strength. The Group is not aware of any such constraints with the exception of those imposed by legislation and the regulation. The Group assumes that the transfer of capital from these two companies to the owner banks will not be practical, with the exception of ordinary dividend payments, and it has based the Group's own risk profile on this assumption. As far as the Group knows, there are no private law impediments that restrict dividend distributions from these companies.

Regulatory capital

The equity value of non-perpetual subordinated loan capital is reduced by 20 per cent every year during the last 5 years before maturity. To the extent the Group has regulatory capital in other financial institutions, this is directly deducted from the Group's own regulatory capital for that part which exceeds 2 per cent of the receiving financial institution's regulatory capital.

If the Group has regulatory capital in other financial institutions that constitutes less than 2 % of the individual financial institution's regulatory capital, the total of such capital is deducted from the Group's regulatory capital for that part which exceeds 10 % of the Group's regulatory capital. If the Group has been instructed to maintain a 100 % capital adequacy reserve for specific assets, an amount corresponding to the assets' book value must be deducted from the regulatory capital and in the basis for calculation. The basis for calculation is weighted according to risk.

Table 7: Regulatory capital

Group (amounts in NOK million)	**31/12/2012**	31/12/2011
Share capital	**6,394**	3,183
– Own shares	**-9**	-3
Share premium reserve	**1,587**	625
Allocated dividend	**384**	299
Fund for unrealised gains	**72**	43
Other equity	**4,209**	1,183
Dividend equalisation fund	**–**	1,448
Primary capital	**–**	2,631
Compensation fund	**–**	55
Endowment fund	**–**	293
Total recorded equity	**12,637**	9,757
Core (Tier 1) capital		
Deferred tax, goodwill and other intangible assets	**-56**	-71
Fund for unrealised gains, available for sale	**-1**	-2
Deduction for allocated dividend	**-384**	-299
50% deduction for regulatory capital in other financial institutions	**-17**	-21
50% deduction in expected losses IRB less loss provisions	**-319**	-255
50% capital adequacy reserve	**-727**	-665
Hybrid Tier 1 bonds 1)	**2,374**	2,402
Total core (Tier 1) capital	**13,507**	10,846
Supplementary (Tier 2) capital in excess of core (Tier 1) capital		
Non-perpetual subordinated capital	**2,124**	1,776
50% deduction for regulatory capital in other financial institutions	**-17**	-21
50% deduction in expected losses IRB less loss provisions	**-319**	-255
50% capital adequacy reserve	**-727**	-665
Total supplementary (Tier 2) capital	**1,061**	835
Net regulatory capital	**14,568**	11,681

[1)] Terms and conditions are presented in table "Subordinated loan capital and Hybrid Tier 1 Perpetual Capital"

Minimum regulatory capital requirements	**31/12/2012**	31/12/2011
Credit risk	**7,072**	6,421
Market risk	**470**	477
Operational risk	**447**	408
Capital adequacy requirement related to transitional arrangements	**908**	861
Minimum regulatory capital requirements	**8,897**	8,167
Capital adequacy	**13.10%**	11.44%
Of which core capital	**12.15%**	10.62%
Of which supplementary capital	**0.95%**	0.82%
Pure core capital adequacy ratio	**10.01%**	8.27%

Minimum regulatory capital requirements – credit risk

Table 8: Minimum regulatory capital requirements for credit risk divided into commitment categories and subcategories (amounts in NOK million)

		Commitments **31/12/2012**	**Commitments EAD** **31/12/2012**	**Minimum regulatory capital requirements Consolidated** **31/12/2012**	Minimum regulatory capital requirements Consolidated 31/12/2011
Enterprises	Specialised enterprises	33,939	31,825	2,328	2,060
	Other enterprises	32,418	29,496	2,346	2,104
Mass market	Mass market SME	5,276	5,268	39	37
	Commitments with mortgage on real estate	105,409	105,400	796	758
	Other mass market commitments	2,088	2,083	58	78
Minimum requirement credit risk IRB		**179,130**	**174,072**	**5,567**	5,037
Governments		883		3	4
Institutions		4,185		86	69
Enterprises		2,318		166	113
Mass market		812		23	19
Consolidated companies		21,675		1,187	1,193
Other assets		1,987		159	96
Minimum requirement, standard method		**31,860**		**1,624**	1,494
Deductions				-119	-110
Total minimum regulatory capital requirements related to credit risk				**7,072**	6,421

Minimum regulatory capital requirements – market risk

Table 9: Minimum regulatory capital requirements for market risk, including position, receipt, party, currency and commodity risk (amounts in NOK million)

	Consolidated **31/12/2012**	Consolidated 31/12/2011
Position risk	**350**	363
– Of which equity instruments	**44**	47
– Of which equity instruments, excluding IRB	**157**	140
– Of which commercial paper and bonds at fair value	**103**	94
– Of which commercial paper and bonds at amortised cost	**46**	82
Counterparty risk (derivatives in trading portfolio)	**120**	114
– Of which derivatives in trading portfolio	**56**	63
– Of which derivatives outside trading portfolio	**64**	51
Currency risk	**0**	0
Total	**470**	477

Minimum regulatory capital requirements – operational risk

Table 10: Minimum regulatory capital requirements for operational risk according to the standardised approach (amounts in NOK million):

2012	**Consolidated**	**Eiendoms-megler 1**	**SR-Finans**	**SR-Forvaltning**
Banking services for mass market customers	241	44	0	6
Bank services for corporate customers	182	0	27	0
Payment and settlement services	24	0	0	0
Total	**447**	**44**	**27**	**6**

2011				
Banking services for mass market customers	228	36	0	7
Bank services for corporate customers	171	0	26	0
Payment and settlement services	9	0	0	0
Total	408	36	26	7

The minimum regulatory capital requirements for operational risk are calculated as a percentage of average earnings for each business unit for the last three years. Banking services for the mass market 12 per cent, banking services for the corporate market 15 per cent and for other services 18 per cent.

Subordinated loan capital and perpetual capital security

Tablel 11: Subordinated loan capital and hybrid Tier 1 bonds (amounts in NOK million)

Principal	**Terms**	**Maturity**	**First maturity date**	**2012**	2011
Non-perpetual					
NOK 750	3 month Libor + margin	2021	2016	**744**	658
JPY 13,000	3-month Libor + margin	2012	2012	**–**	1,014
NOK 500	3 month Nibor + margin	2018	2013	**232**	469
NOK 450	3 month Nibor + margin	2017	2012	**–**	362
NOK 75	3 month Nibor + margin	2019	2014	**82**	84
NOK 825	3 month Nibor + margin	2022	2016	**825**	
Total non-perpetual				**1,883**	2,587
Hybrid Tier 1 bonds					
NOK 1,000	3 month Nibor + margin			**992**	992
USD 75	3-month Libor + margin			**428**	485
NOK 684	3 month Nibor + margin			**741**	719
NOK 116	3 month Nibor + margin			**115**	115
NOK 40	3 month Nibor + margin			**40**	40
Total hybrids				**2,316**	2,351
Accrued interest				**24**	37
Total subordinated loan capital				**4,223**	4,975

Subordinated loan capital and hybrid Tier 1 bonds (hybrids) in foreign currencies are included in the Group's total currency position so that there is no currency risk associated with the loans. Of a total of NOK 4 223 million in subordinated loan capital, NOK 2 242 million counts as core (Tier 1) capital and NOK 1 876 million as non-perpetual subordinated capital. Capitalised costs associated with borrowing are reflected in the calculation of amortised cost. Hybrid Tier 1 bonds can account for a maximum of 15 per cent of the combined core (Tier 1) capital for bonds with a fixed term and 35 per cent for hybrid Tier 1 bonds without a fixed term. Any excess qualifies as perpetual subordinated capital.

Credit risk

Credit risk is the risk of loss resulting from the customer's or counterparty's inability or unwillingness to fulfil his obligations

SpareBank 1 SR-Bank is exposed primarily to credit risk through its loan portfolios in the retail and corporate markets. In addition, the Group is exposed to credit risk through the liquidity reserve portfolio. This portfolio consists mainly of low risk commercial paper and bonds that qualify for loans from Norges Bank. The Group is also exposed to credit risk through the portfolio in SpareBank 1 SR-Finans AS, which principally consists of leasing and car loans.

Management of credit risk

Credit risk is managed through the limits for granting credit, follow-up of commitments and portfolio management. The main elements of the limits for granting credit include:

1) Credit strategy The general credit strategy stipulates that the Group shall have a moderate risk profile where no single event shall be capable of seriously harming the Group's financial position. In addition, the Group's credit strategy consists of general credit strategy limits for ensuring a diversified portfolio and a satisfactory risk profile.

This limits the probability of default, expected losses, risk-adjusted capital and how high the total loan exposure can be in the corporate market.

2) Credit policy guidelines The Group's credit policy guidelines stipulate minimum requirements that apply to all types of financing, except commitments granted as part of the exercise of special credit hedging authorities. In addition to the general credit policy guidelines, a set of more specific credit policy guidelines related to sectors or segments that can entail a special risk have been prepared.

3) Credit authority regulations The Board is responsible for the Group's granting of loans and credit, but delegates the responsibility to the CEO, within certain limits. The CEO then delegates these within his own authority. Delegated credit authority is linked to a commitment's expected losses and the probability of default.

The authority is personal. This means that the credit committees do not have decision-making authority, but make recommendations to the authority holder. If there is no credit committee, then the authorisation limits will be reduced. In general the authority is ample if a commitment's expected loss and probability of default indicates a low risk, but the authority will be restricted progressively with increasing risk.

4) Credit review routines The credit review routines regulate in detail all factors related to the granting of credit by the Group and follow-up of commitments. The credit granting process provides a more detailed description of the customer and the purpose of the loan application, in addition to evaluations of:

- Whether the customer will have adequate earnings to service the current obligations, interest and instalments
- For how long and in what manner the customer can meet the current obligations, interest and instalments if the earnings fail
- Whether there is adequate management capability and capacity to meet the current requirements and future challenges
- Collateral and overall risk assessment

Measurement of credit risk

After the commitments have been granted, continuous commitment and portfolio monitoring is carried out. The credit risk is followed up in general by means of the Group's portfolio management systems, systems for early notification of key development trends (early warning) and systems for monitoring the quality of the actual credit granting process.

The portfolio management system contains information on the risk at both the aggregate and detailed levels. This is made possible by efficient monitoring and management of the risk performance of the portfolio. All the portfolio information is updated monthly, including updates of the customers' probability of default. The development of risk in the portfolios is followed up with special emphasis on the development of the risk classification (migration), expected losses, risk-adjusted capital and risk-adjusted return.

SpareBank 1 SR-Bank uses risk-adjusted capital as a measurement parameter, since the risk-adjusted capital reflects the actual risk exposure significantly better than what the traditional focus on lending volume does. Commitments with a high risk require significantly more risk-adjusted capital than commitments with low risk. This means that significantly less money can be loaned to customers with high risk than customers with low risk.

Risk classification system

The Group utilises credit models for risk classification, risk pricing and portfolio management. The risk classification system is based on the following risk parameters:

1) Exposure at Default (EAD)

The conversion factor (CF) defines to what extent the unutilised credit limit is anticipated drawn up at default. For guarantees and allocated, but not drawn up limits for corporate market customers a drawing of 75 per cent (0.75 per cent). For allocated, but not drawn up limits for corporate market customers there is a drawing of 100 per cent (1).

2) Probability of Default (PD)

The customers are classified into default classes based on the probability of default over a 12-month period, based on a long-term outcome.

The probability of default is calculated on the basis of historical series of data for financial key figures related to earnings and deterioration, as well as the basis of non-financial criteria such as conduct and age. Nine default classes (A – I) are used to classify the customers according to the probability of default. Definitions of the individual default classes are shown in the table below.

Table 12: Definition of default classes

Default class	Lower limit for default	Upper limit for default
A	–	0.10%
B	0.10%	0.25%
C	0.25%	0.50%
D	0.50%	0.75%
E	0.75%	1.25%
F	1.25%	2.50%
G	2.50%	5.00%
H	5.00%	10.00%
I	10.00%	99.99%

The Group has two additional default classes (J and K) for customers with defaulted and/or written-down commitments.

3) Loss Given Default (LGD)

The loss given default describes how much the Group potentially can lose if the customer defaults on his obligations. The valuation takes in account the value of underlying securities and the costs the Group has in recovering defaulted commitments. The Group sets realisation values on collateral security lodged based on its own experience over time, and such that these, based on a conservative assessment reflect the expected realisation value in a period of recession.

Seven different classes are used (1 – 7) for classifying commitments in relation to loss given default. Definitions of these classes for corporate market commitments are illustrated in the table below. Retail market customers have somewhat higher estimated recovery levels on defaulted commitments, and similar loss given defaults for these will therefore be somewhat lower than for corporate market customers within the same collateral class.

Table 13: Definition of loss given default (collateral class)

Class	Loss given default lower limit	Loss given default upper limit
1	–	0.08%
2	–	0.08%
3	0.08%	13.62%
4	13.62%	27.23%
5	27.23%	40.85%
6	40.85%	54.46%
7	54.46%	68.08%

4) Expected Losses (EL)

Expected losses describe the loss the Group can statistically expect to lose on the loan portfolio during a 12-month period (long-term outcome). Expected losses are calculated by multiplying the probability of default, exposure at default and loss given default, respectively.

A commitment is assigned a risk group from the lowest to the highest risk group based on the commitment's expected loss. The risk groups are defined as illustrated in the table below.

Table 14: Definition of risk groups

Risk group	Expected losses lower limit	Expected losses upper limit
Lowest	0%	0.0125%
Low	0.0125%	0.50%
Average	0.50%	2.00%
High	2.00%	2.40%
Highest	2.40%	99.99%

5) Unexpected Losses (UL)

There are many factors that affect the Group's losses on loans and credits. The expected loss is based on the amounts that are uncertain. The uncertainty is to a great extent related to the properties of the commitments. There is relatively little uncertainty connected to well-secured commitments for borrowers with a good capacity to service loans, while there is relatively great uncertainty connected with secured commitments and with customers with an unstable capacity to service loans

To take these factors into account an unexpected loss on all commitments is calculated. By totalling the unexpected losses among all the commitments we get an estimate of how much the Group can lose beyond the expected loss. This estimate takes into account that all the customers do not generate losses at the same time.

In other words, risk-adjusted capital describes how much capital the Group finds it requires to cover the actual risk the Group believes it requires to cover the actual risk assumed. Since it is impossible to fully protect against all losses, the Group has stipulated that the risk-adjusted capital shall cover all possible unexpected losses based on a stipulated confidence level of 99.97 per cent.

6) Risk pricing – RORAC (Return On Risk Adjusted Capital)

SpareBank 1 SR-Bank is concerned about pricing risk correctly. This means that commitments with a high risk are priced higher than commitments with low risk. The general level of risk pricing will, however, also depend on the Group's general return targets and the consideration to the competition situation.

SpareBank 1 SR-Bank therefore uses models that calculate the correct risk price that should be taken into consideration when pricing the expected losses and return on risk-adjusted capital. The risk pricing model uses the same main components as in the Group's risk classification system as the basis. The model is based on a standard "RARORAC" model (Risk Adjusted Return On Risk Adjusted Capital) for measuring risk-adjusted return.

The pricing model is primarily used for granting and renewing credit and also to calculate the customer's price and to measure and follow up profitability.

Collateral

SpareBank 1 SR-Bank takes into account the main types of collateral as illustrated in the table below:

Table 15: Main types of collateral

Type of collateral	Retail market	Corporate market
Real property	X	X
Motor vehicles	X	X
Leisure boats	X	
Securities	X	X
Guarantees	X	X
Machinery and plant		X
Vessels		X
Construction equipment		X
Inventories		X
Agricultural chattels		X
Trade receivables		X
Deposits		X

Deposits are not permitted as collateral for retail market customers that are encompassed by the consumer definition in the Financial Contracts Act.

In the retail market the market value of real estate is stipulated either by utilising a broker valuation/appraisal, value estimates from Eiendomsverdi (applies only to residential properties) or by self-assessment in exceptional cases. Eiendomsverdi is an information and analysis tool that gives access to an estimated market value for properties in Norway. Value estimates from Eiendomsverdi may be utilised in accordance with internal procedures if the property is located in a well-functioning residential market and if there is little uncertainty with regard to the value estimate. A self-assessment can only be used if the terms for this have been met, but a person other than the customer manager must approve the valuation that is used as the basis.

The realisation value for real property is stipulated by using the market value as the basis, and reducing this by 20 per cent for residential properties and 40 per cent for land and recreational properties, respectively. In the retail market, assets other than real property are used as collateral to a limited extent.

In the corporate market the lease value method is the primary method for calculating the collateral value of commercial properties. The market value is calculated by multiplying the net rental income by an interest rate that reflects risk-free investment + a general risk premium. On the basis of the calculated market value the realisation value is stipulated at between 60 and 80 per cent, dependent on the building's condition and what it is used for. Specialised industrial buildings with limited alternative application possibilities are given a realisation value of 25 per cent of the market value as a maximum.

Other security values are assessed in accordance with stipulated internal routines. The realisation value of the provided securities is stipulated by using the market value as the basis, and this is reduced by a factor that varies with the security object's properties and amounts to a minimum of 20 per cent. Securities in the form of negative mortgage and unlisted securities are not given any security-related realisation value, while guarantees can only be given a realisation value if certain terms are fulfilled.

Commitments in default

A commitment is considered to be in default if:

1) A claim has been due for more than 90 days and the amount is over NOK 1,000, or

2) The bank has reason to assume that the debtor is not able to repay (in full) in accordance with his obligations:

- The bank makes write-downs due to impaired creditworthiness.
- The bank sells a claim at a discount as a result of impaired creditworthiness.
- As a result of payment problems by the counterparty the bank grants a postponement of payment or new credit until payment of the instalment, or agrees on changes to the interest rate or other terms and conditions of the agreement.
- The counterparty is subject to debt settlement, bankruptcy or public administration proceedings, or voluntary debt negotiations have been initiated.
- The bank assumes due to other reasons that the obligation will not be fulfilled.

Validation

The Group continuously develops and tests the risk management system and the credit granting process to ensure that it is of high quality over time. This validation work can be divided into two main areas:

Quantitative validation: Quantitative validation is intended to ensure that the estimates used for the probability of default, exposure at default and loss given default are always of adequately good quality. Analyses are performed to assess the capacity of the rating models to rank customers according to risk (discrimination capacity) and the ability to establish the correct level of risk parameters. In addition, the stability of the models' estimates and the models' cyclical sensitivity are analysed. The quantitative validation will be supplemented by more qualitative assessments in some cases.

Application: The verification will show whether the system for management and measurement of credit risk is well integrated in the organisation, and that it represents a key part of the Group's risk management and decision making. Validation shows that the system for management and measurement of credit risk is well integrated in the organisation, and that it represents a key part of Group's risk management and decision making.

Credit exposure summary

The following tables present a summary of the bank's commitments in relation to credit risk based on regulatory calculations.

Commitments by geographic area

Table 16: Commitment amount for each type of commitment, broken down into geographic areas before deductions for write-downs (amounts in NOK million)

2012	**Gross lending to customers**	**Unutilised credit**	**Guarantees**	**Total**
Rogaland	**76,872**	**8,699**	**9,370**	**94,941**
Agder counties	**9,650**	**1,084**	**1,167**	**11,901**
Hordaland	**14,029**	**1,576**	**1,697**	**17,302**
Other	**8,962**	**941**	**1,014**	**10,917**
Total gross commitments, customers	**109,513**	**12,300**	**13,248**	**135,061**

2011				
Rogaland	71,256	8,121	6,942	86,319
Agder counties	8,872	942	800	10,614
Hordaland	12,660	1,359	1,153	15,172
Other	8,580	1,028	873	10,481
Total gross commitments, customers	101,368	11,450	9,768	122,586

Commitments by type of commitment

Table 17: The total commitment amount, defined as gross lending to customers + guarantees + non-utilised credit in the Group, after any write-down and without taking account of any securities and the average size of the commitments during the period, divided by type of commitment (amounts in NOK million)

2012	**Commitment amount as at 31/12/2012**	**Average commitment amount in 2012**
Enterprises	**78,635**	**75,136**
Mass market	**56,426**	**53,688**
Gross commitments, customers	**135,061**	**128,824**
Individual write-downs	**-423**	**-421**
Write-downs for groups of loans	**-332**	**-347**
Write-down of guarantees	**-1**	**-2**
Net commitment, customers	**134,305**	**128,055**
Governments (Norges Bank)	**1,007**	**505**
Institutions	**1,087**	**905**
Total commitment amount	**136,399**	**129,465**

2011	**Commitment amount as at 31/12/2011**	**Average commitment amount in 2011**
Enterprises	71,637	68,045
Mass market	50,949	56,357
Gross commitments, customers	122,586	124,402
Individual write-downs	-418	-410
Write-downs for groups of loans	-362	-360
Write-down of guarantees	-2	-3
Net commitments, customers	121,804	123,630
Governments (Norges Bank)	3	513
Institutions	723	998
Total commitment amount	122,530	125,141

Commitments by customer groups

Table 18: Commitment amount for each type of commitment, broken down into sectors before deductions for write-downs

	2012			2011		
	Gross loans	**Unutilised credit and guarantees**	**Total**	Gross loans	Unutilised credit and guarantees	Total
Agriculture/forestry	**4,141**	**1,659**	**5,800**	3,773	729	4,502
Fisheries/fish farming	**597**	**204**	**801**	416	199	615
Mining operations and extraction	**2,351**	**977**	**3,328**	2,728	81	2,809
Industry	**2,135**	**597**	**2,732**	1,686	1,224	2,910
Power and water supply/building and construction	**3,804**	**1,260**	**5,064**	4,022	2,518	6,540
Wholesale and retail trade, hotels and restaurants	**2,975**	**1,052**	**4,027**	2,487	1,086	3,573
Overseas shipping, pipeline transport and other transport	**6,451**	**2,527**	**8,978**	6,553	4,481	11,034
Property management	**24,306**	**10,302**	**34,608**	23,749	3,111	26,860
Service sector	**7,650**	**2,671**	**10,321**	6,827	2,376	9,203
Public sector and financial services	**1,949**	**1,027**	**2,976**	1,068	2,523	3,591
Not allocated (added value fixed interest lending)	**585**	**-585**	**0**	466	-466	0
Total for enterprises	**56,944**	**21,691**	**78,635**	53,775	17,862	71,637
Mass market	**52,569**	**3,857**	**56,426**	47,593	3,356	50,949
Total gross commitments, customers	**109,513**	**25,548**	**135,061**	101,368	21,218	122,586

Commitment amount by remaining maturity

Table 19: Commitment amount for each type of commitment, broken down by the remaining term (amounts in NOK million)

2012	**Upon request**	**< 1 year**	**1–5 years**	**Over 5 years**	**Total**
Gross lending – customers	33,309	4,708	18,200	53,296	109,513
Unutilised credit	12,300				12,300
Guarantees		10,020	1,561	1,667	13,248
Total gross commitments, customers	**45,609**	**14,728**	**19,761**	**54,963**	**135,061**
Governments (Norges Bank)	**1,007**	–	–	–	**1,007**
Institutions	**1,087**	–	–	–	**1,087**
2011					
Gross lending – customers	33,216	3,871	15,161	49,120	101,368
Unutilised credit	11,450				11,450
Guarantees		7,096	859	1,813	9,768
Total gross commitments, customers	45,472	10,967	16,020	50,933	122,586
Governments (Norges Bank)	3	–	–	–	3
Institutions	723	–	–	–	723

Defaulted and doubtful commitments by customer group

Table 20: Defaulted and doubtful commitments by customer group (amounts in NOK million)

	Total commitment amount			
2012	**Doubtful**	**In default**	**Individual write-downs**	**Value changes recognised during the period**
Agriculture/forestry	7	8	6	1
Fisheries/fish farming	0	0	0	0
Mining operations and extraction	0	0	7	-1
Industry	59	3	21	-2
Power and water supply/building and construction	27	13	20	9
Wholesale and retail trade, hotels and restaurants	50	13	22	11
International shipping, pipe transport, other transport	59	30	58	1
Property management	227	161	122	42
Service sector	202	13	77	103
Public sector and financial services	0	0	0	0
Total for enterprises	**631**	**241**	**333**	**164**
Transferred from write-downs on groups of loans				-30
Mass market	156	219	90	3
Total	**787**	**460**	**423**	**137**
2011				
Agriculture/forestry	17	9	10	-1
Fisheries/fish farming	–	–	–	-1
Mining operations and extraction	11	–	8	–
Industry	70	6	31	4
Power and water supply/building and construction	42	26	21	6
Wholesale and retail trade, hotels and restaurants	26	6	19	4
Overseas shipping, pipeline transport and other transport	105	38	50	15
Property management	224	123	128	30
Service sector	64	30	57	31
Public sector and financial services	–	–	–	–
Total for enterprises	**559**	**238**	**324**	**88**
Transferred from write-down on groups of loans				5
Mass market	137	177	96	46
Total	**696**	**415**	**420**	**139**

Table 21: Actual losses by default class for the period (amounts in NOK million)

	2012	2011
A (0.00–0.10%)	**0**	0
B (0.10–0.25%)	**0**	0
C (0.25–0.50%)	**0**	0
D (0.50–0.75%)	**0**	0
E (0.75–1.25%)	**0**	0
F (1.25–2.50%)	**0**	0
G (2.50–5.00%)	**0**	0
H (5.00–10.00%)	**0**	0
I (10.00–)	**0**	0
J	**0**	0
C	**137**	139
Total	**137**	139

Defaulted and doubtful commitments by geographic area

Table 22: Separate specification of the total commitment amount with impairment and defaulted commitments divided into geographic areas, including total changes in value and write-downs (amounts in NOK million)

	Total commitment amount		Individual write-downs
2012	**Doubtful**	**In default**	
Rogaland	437	194	276
Agder counties	124	120	76
Hordaland	150	115	51
Other	76	31	20
Total	**787**	**460**	**423**
2011			
Rogaland	342	170	229
Agder counties	203	118	116
Hordaland	146	94	71
Other	5	32	4
Total	**696**	**415**	**420**

Write-downs on loans

Tabel 23: Reconciliation of changes in value changes and write-downs respectively for commitments on impairment

2012	**Opening balance**	**Write-down amount recognised**	**Amount set aside for or reversed from estimated losses**	**Closing balance**
Individual write-downs	418	194	199	423
Write-downs on groups of loans	362		-30	332
Specified loss provisions guarantees	2		-1	1
Total	**782**	**194**	**168**	**756**

2011				
Individual write-downs	402	174	190	418
Write-downs on groups of loans	357		5	362
Specified loss provisions guarantees	3		-1	2
Total	**762**	**174**	**194**	**782**

Exposure of portfolios in which the IRB approach is used

Table 24: Distribution by risk classes in which the IRB approach is used(amounts in NOK million)

2012 **Commitment category**	**Default class**	**Total EAD**	**Total unutilised facility**	**Average risk weight**	**Average loss given default**	**Average conversion factor**
Enterprises	A	69	19	28.9%	45.0%	99.0%
	B	1,019	483	40.9%	45.0%	87.6%
	C	7,931	3,330	58.3%	45.0%	87.8%
	D	10,945	3,168	68.5%	45.0%	91.2%
	E	6,056	1,103	77.8%	45.0%	94.6%
	F	14,708	3,874	100.5%	45.0%	92.0%
	G	14,458	2,348	118.0%	45.0%	94.9%
	H	2,351	490	164.1%	45.0%	93.5%
	I	2,934	380	185.7%	45.0%	95.9%
	J	161	12	0.0%	45.0%	97.7%
	C	690	18	0.0%	45.0%	99.2%
Total for enterprises		**61,322**	**15,225**	**95.3%**		**92.4%**
Commitments with mortgage on real estate	A	12,346	3,247	1.6%	9.3%	100.0%
	B	11,358	1,119	4.3%	9.6%	100.0%
	C	32,449	2,564	6.6%	10.0%	100.0%
	D	18,432	1,016	9.6%	10.1%	100.0%
	E	21,272	916	13.2%	10.2%	100.0%
	F	6,569	169	19.9%	11.0%	100.0%
	G	1,033	23	30.0%	10.6%	100.0%
	H	843	17	45.1%	10.8%	100.0%
	I	902	7	61.5%	11.2%	100.0%
	J	91	2	1.9%	9.5%	99.9%
	C	106	0	11.7%	25.8%	100.0%
Total mass market, real estate		**105,400**	**9,080**	**9.4%**	**10.0%**	**100.0%**
Other mass market	A	909	375	3.4%	17.7%	99.7%
	B	2,108	421	5.6%	14.1%	99.8%
	C	1,926	202	15.2%	24.1%	99.8%
	D	830	63	23.7%	27.3%	99.9%
	E	787	42	31.0%	28.1%	99.9%
	F	333	14	34.8%	24.0%	99.9%
	G	146	5	42.4%	21.1%	99.9%
	H	103	2	57.5%	24.2%	99.8%
	I	121	3	75.1%	26.2%	99.7%
	J	8	0	0.4%	36.0%	99.8%
	C	79	0	8.2%	74.1%	17.3%
Total other mass market		**7,351**	**1,127**	**16.6%**	**21.8%**	**99.8%**

2011 Commitment category	Default class	Total EAD	Total unutilised facility	Average risk weight	Average loss given default	Average conversion factor
Enterprises	A	42	14	29.5%	45.0%	98.6%
	B	795	334	42.1%	45.0%	88.8%
	C	6,554	2,484	57.9%	45.0%	88.8%
	D	9,767	2,710	67.1%	45.0%	91.6%
	E	6,980	1,209	80.0%	45.0%	94.6%
	F	13,381	2,649	96.0%	45.0%	93.9%
	G	12,207	1,700	116.1%	45.0%	95.6%
	H	1,134	223	152.2%	45.0%	93.9%
	I	3,992	375	175.9%	45.0%	97.0%
	J	58	15	0.0%	45.0%	92.5%
	C	572	21	0.0%	45.0%	98.8%
Total for enterprises		**55,482**	**11,734**	**93.8%**		**93.5%**
Commitments with mortgage on real estate	A	9,285	2,561	1.6%	9.0%	100.0%
	B	9,377	1,053	4.5%	9.8%	100.0%
	C	27,973	2,462	6.4%	9.7%	100.0%
	D	17,035	1,079	9.7%	10.1%	100.0%
	E	22,035	1,086	13.6%	10.5%	100.0%
	F	6,851	180	19.6%	10.8%	100.0%
	G	915	22	30.3%	10.9%	100.0%
	H	763	11	42.9%	10.3%	100.0%
	I	789	12	61.2%	11.1%	100.0%
	J	85	1	6.0%	10.2%	99.9%
	C	121	0	22.6%	20.7%	100.0%
Total mass market, real estate		**95,229**	**8,468**	**9.9%**	**10.0%**	**100.0%**
Other mass market	A	782	307	3.9%	20.5%	99.7%
	B	2,070	426	5.5%	13.6%	99.9%
	C	2,027	197	17.4%	27.4%	99.8%
	D	841	60	27.6%	31.9%	99.9%
	E	888	57	35.1%	32.2%	99.9%
	F	465	20	41.7%	30.1%	99.9%
	G	171	3	40.5%	19.6%	99.9%
	H	100	2	51.9%	23.0%	99.8%
	I	100	2	78.3%	26.3%	99.8%
	J	8	0	0.3%	50.4%	100.0%
	C	77	0	14.1%	46.0%	100.0%
Total other mass market		**7,528**	**1,075**	**19.1%**	**24.1%**	**99.9%**

Comparison of the risk parameters with the actual outcomes

A commitment is deemed to be in default if a claim is overdue by more than 90 days and the amount exceeds NOK 1,000, or when the bank has reason to assume that it is possible that the debtor is not able to repay in accordance with his obligations to the bank. The table below shows the average estimated and actual default for the portfolio for the last year and for the period from 2006 to 2011. The default percentage is defined as the total number of customers who are, or have been in default within a 12-month period, seen in relation with the total number of customers in the portfolio. This means that a customer in default with a small loan commitment is weighted just as much as a customer in default with a large loan commitment.

Table 25: IRB default level (unweighted)– PD-models

Portfolio	**Estimated defaults 2010 – 2011**	**Actual defaults 2010–2011**	**Estimated defaults 2006 – 2011**	**Actual defaults 2006–2011**
Mass market with mortgage on real estate	0.93%	0.29%	0.91%	0.34%
Other mass market	3.69%	1.91%	3.39%	2.26%
Enterprises	3.74%	2.40%	2.98%	2.24%

Table 26 shows the estimated and actual loss given default for defaulted loans in SpareBank 1 SR-Bank. The Capital Requirements Regulations require that the estimated loss given default shall represent economic downturns. The estimated loss given default for the mass market is estimated for all customers in default one month before default since this is the last estimate of loss given default before the customer was in default. An estimated loss given default of 45 per cent is stipulated by the authorities in the Capital Requirements Regulations for enterprises. The loss data period applies to the period from 2003 to 2011. For enterprises the period is from 2000 to 2010. The estimated loss given default is higher than the actual loss given default since this is a downturn estimate, while the actual loss given default represents realisations carried out in some different economic cycles.

Table 26: Loss given default for defaulted loans (unweighted) – LGD models

Portfolio	**Estimated loss given default**	**Actual loss given default**
Mass market with mortgage on real estate	10.00%	3.40%
Other mass market	15.50%	10.70%
Enterprises	45.00%	28.00%

Total commitment amount and share secured by mortgage (IRB)

Table 27: Total commitment amount (in NOK million) and share secured by mortgage, divided by commitment category (IRB)

	2012		2011	
Commitment category	**Commitment amount**	**Of which secured by mortgage on real estate 1)**	Commitment amount	Of which secured by mortgage on real estate 1)
Mass market – mortgage on real estate	105,409	95%	95,239	94%
Mass market – SME	5,276	89%	4,959	87%
Mass market – other	2,088	3%	2,579	3% 2)
Total	**112,773**		102,777	

1) Percentage of total commitment with such security in relation to total commitment for the relevant commitment category.
2) A commitment for a mass market customer in which the realisation value of the home is deemed to be less than 30 per cent of the customer's commitment is not classified as a commitment with real estate, but as other mass market.

SpareBank 1 SR-Bank has no security that results in a reduced commitment amount. For enterprises the security pledged is not taken into account in the LGD calculation. Instead, LGD factors established by the authorities are applied. The Group therefore does not list this type of commitment in the table above.

Actual value changes

Table 28: The actual changes in value for the individual commitment category and development from previous periods (IRB):

Amounts in NOK million	**Value 31/12/2012**	**Change in value 2012 (%)**	**Value 31/12/2011**	**Change in value 2011 (%)**
Mass market commitments	**112,773**	**9.7%**	102,777	11.8%
– of which mass market SME	**5,276**	**6.4%**	4,959	12.1%
– of which mass market, retail, real estate	**105,409**	**10.7%**	95,239	12.1%
– of which mass market, retail, other	**2,088**	**-19.0%**	2,579	0.6%
Enterprises	**33,939**	**16.2%**	29,215	9.1%
Specialist lending	**32,418**	**7.5%**	30,151	7.6%
Total	**179,130**	**10.5%**	**162,143**	**10.5%**

Bond portfolio

Risk profile and portfolio performance

The Group has two different portfolios consisting of bonds and commercial paper – the liquidity portfolio and trading portfolio, respectively. The respective portfolios are governed by separate management mandates.

Liquidity portfolio (managed by Treasury)

The liquidity portfolio consists of interest-bearing securities that either satisfy the requirements for depositing with Norges Bank, the LCR regulations or uncommitted credit facilities. The size of the portfolio will depend at all times on the Group's balance sheet and thereby the need for liquid assets. At the end of the 4th quarter of 2012 the value of the combined liquidity portfolio, including covered bonds used in the government swap facility, totals NOK 18.2 billion.

In accordance with the Group's internal guidelines, the securities that do not satisfy the aforementioned requirements entail a credit risk governed by special processing rules.

Trading portfolio

The trading portfolio consists of financially oriented investments in interest-bearing securities. The current limit for such investments is NOK 1,000 million. All investments in the trading portfolio that do not satisfy the criteria for uncommitted credit lines stipulated by the Board of Directors shall be subject to ordinary credit processing. At the end of the fourth quarter of 2012 the trading portfolio includes investments in 36 companies valued at NOK 419 million.

The Group has a separate risk model for calculating the risk-adjusted capital associated with the bond portfolios.

The trading portfolio does not have any structured bonds (CDO's etc.) or other types of financial instruments.

The table below provides a summary of SpareBank 1 SR-Bank's exposure to bonds in the different portfolios:

Table 29: Securities exposure, bonds and securities (NOK million)

Risk classes for bonds and commercial paper – total

Risk category	Rating (incl. unofficial)	Market value NOK million	Total per cent
Swap scheme	AAA	7,711	41%
Very low risk	AAA, AA+, AA and AA-	9,890	53%
Low risk	A+, A and A-	505	3%
Moderate risk	BBB+, BBB and BBB-	113	1%
High risk	BB+, BB and BB-	198	1%
Very high risk	B+ and lower	166	1%
Total		**18,582**	**100%**

Risk classes – Treasury

Risk category	Rating (incl. unofficial)	Market value NOK million	Treasury per cent
Swap scheme	AAA	7,711	42%
Very low risk	AAA, AA+, AA and AA-	9,890	54%
Low risk	A+, A and A-	495	3%
Moderate risk	BBB+, BBB and BBB-	68	0%
High risk	BB+, BB and BB-	0	0%
Very high risk	B+ and lower	0	0%
Total		**18,163**	**100%**

Risk classes – Trading / Sales

Risk category	Rating (incl. unofficial)	Market value NOK million	Trading per cent
Very low risk	AAA, AA+, AA and AA-	0	0%
Low risk	A+, A and A-	10	2%
Moderate risk	BBB+, BBB and BBB-	45	11%
High risk	BB+, BB and BB-	198	47%
Very high risk	B+ and lower	166	40%
Total		**419**	**100%**

Market risk

Market risk is a collective term that comprises the risk of loss related to items on and off the balance sheet as a result of changes in the market prices. Securities risk, currency risk, interest rate risk, spread risk, risk associated with own holdings and/or use of equity in syndicates, as well as guarantees for the full subscription of offerings are included in market risk.

Risk profile

The Group's market risk strategy should support the Group's general business plan and strategy in which the tolerance for market risk is defined as moderate.

Interest rate risk

Maximum loss in the event of a 1 percentage point change in the interest rate: NOK 30 million and NOK 45 million for the total balance sheet for Trading and Treasury, respectively. There are no specific limits for the foreign currency balance sheet, but the absolute value of the interest rate risk for Norwegian kroner and foreign currency, respectively, is calculated, and the total balance sheet limit applies.

Table 30: Sub-limits within the different maturity bands

Maturity bands	Trading limit	Treasury limit
0 – 3 months	NOK 20 million	NOK 30 million
3 – 6 months	NOK 20 million	NOK 30 million
6 – 9 months	NOK 10 million	NOK 30 million
9 months – 1 year	NOK 10 million	NOK 30 million
1 year – 18 months	NOK 10 million	NOK 20 million
18 – 24 months	NOK 15 million	NOK 15 million
Each year (1–10)	NOK 30 million	NOK 10 million
10 years or more	NOK 30 million	NOK 10 million

The table below illustrates the development of the total interest rate risk for the last four quarters (without the absolute value).

Table 31: Effect on earnings of a positive parallel shift in the yield curve of one percentage point (NOK million)

Interest rate risk	0–6 months	6–12 months	1–5 years	> 5 years	Total
4th Qtr. 2012	4	12	-4	-5	**7**
3rd Qtr. 2012	-8	8	-7	-18	**-24**
2nd Qtr. 2012	12	7	-7	-1	**11**
1st Qtr. 2012	-7	20	-15	-3	**-5**

Foreign exchange risk

The Group has prepared limits for the net exposure to each individual currency, and limits for the aggregate net currency exposure The overnight price risk for spot trading in foreign currencies shall not exceed NOK 100 million for each individual currency, and NOK 125 million in aggregate.

The table shows the development of the net foreign currency exposure including financial derivatives at the end of the last four quarters.

Table 32: Foreign currency exposure including financial derivatives (NOK million)

Currency	4th Qtr. 2012	3rd Qtr. 2012	2nd Qtr. 2012	1st Qtr. 2012
EUR	-24	17	-23	-31
USD	24	3	61	-1
CHF	2	0	1	2
GBP	0	3	4	-8
Other	5	10	5	2

Securities risk, shares

Shares, units and other equity interests are classified within the categories of fair value and available for sale. Securities that can be measured reliably and are reported internally at fair value are classified as fair value through profit and loss. Other shares are classified as available for sale.

The table below provides a summary of the development of the Group's shareholdings for the last four quarters:

Table 33: The Group's share portfolio at fair value at the end of the year (NOK million)

Balance sheet classification	4th Qtr. 2012	3rd Qtr. 2012	2nd Qtr. 2012	1nd Qtr. 2012
Shares, units etc	**756**	**631**	**708**	**734**
Of which short-term shareholdings	91	114	213	223
Of which long-term shareholdings	481	429	407	423
Available for sale	**184**	**88**	**88**	**88**

Market risk, including spread risk for bonds and securities

The liquidity portfolio's holdings total NOK 21.7 billion, NOK 8.0 billion of which is classified as "held to maturity". These investments are recognised at amortised cost and are therefore not exposed to market risk. The trading portfolio totals NOK 0.3 billion. The table below provides a summary of the portion of the bond portfolio that is exposed to market risk. The portfolio totals NOK 14.0 billion at the end of the 3rd quarter of 2012.

Table 34: Fair value of the bond portfolio that is exposed to market risk (NOK million)

Sub-portfolio	4th Qtr. 2012	3rd Qtr. 2012	2nd Qtr. 2012	1st Qtr. 2012
Treasury	**10,232**	**13,693**	**13,594**	**12,867**
Norwegian state/municipality	10	3,551	4,680	5,381
Covered bonds	6,897	6,877	6,242	5,172
Foreign guarantees	2,945	2,318	1,720	1,435
Norwegian bank/finance	203	809	783	790
Foreign bank/finance	37	37	68	69
Industry/other	140	100	100	20
Trading/sales	**419**	**328**	**756**	**513**
Norwegian bank/finance	59	97	129	160
Foreign bank/finance	1	1	1	1
Industry/other	360	230	626	351

The spread risk is defined as the risk of changes in the market value of bonds as a result of general changes in the credit spreads. The credit spread risk expresses in other words the potential loss in the bond portfolios beyond the bankruptcy risk. Quantification of the risk-adjusted capital for spread risk in the bond portfolios is calculated in accordance with the Financial Supervisory Authority of Norway's model for risk-based supervision of market risk in insurance companies (based primarily on the Solvency II regulations).

Table 35: Risk-adjusted capital for spread risk in the bond portfolios (NOK million)

Sub-portfolio	Market value for risk class	Allocated spread risk
Treasury	10,222	157
Trading/sales	419	58

Market risk – portfolio information – long-term investments

Table 36: Investments (equity positions outside the trading portfolio) broken down by purpose *(amounts in NOK million)*.

	Investments	31/12/2012	31/12/2011
Financial investments at fair value through profit and loss	Progressus	16	16
	Borea Opportunity II	14	10
	Hitec Vision Private Equity IV LP	40	31
	Hitec Vision Asset Solution LP	19	10
	OptiMarin	20	20
	Other financial investments	64	52
Total financial investments at fair value through profit and loss		**173**	139
Strategic investments at fair value through profit and loss	Nordito Property	19	12
	Nets Holding	286	263
Total strategic investments at fair value through profit and loss		**305**	275
Strategic investments available for sale	Other strategic investments	3	4
Total		**481**	418

Shares and other interests are either classified at fair value through profit and loss or as available for sale. Changes in fair value after the opening balance are recognised as revenues from financial investments.

Table 37: Overview of book value and fair value, gains and losses *(amounts in NOK million)*

2012	**Book value**	**Fair value**	**Total realised gain or loss in 2012**	**Unrealised gain or loss in 2012**	**Amount included in core or supplementary capital**
Financial investments at fair value through profit and loss	173	173	3	15	0
Strategic investments at fair value through profit and loss	305	305	0	30	0
Strategic investments available for sale	3	3	0	0	1
Total	**481**	**481**	**3**	**45**	**1**

2011					
Financial investments at fair value through profit and loss	139	139	9	14	0
Strategic investments at fair value through profit and loss	275	275	0	0	0
Strategic investments available for sale	4	4	0	0	1
Total	**418**	**418**	**9**	**14**	**1**

Table 38: Summary of type and value of listed shares, unlisted shares in diversified portfolios and other commitments

Amounts in NOK million	**Value 2012**	Value 2011
Unlisted	**478**	412
Traded on an exchange	**0**	2
Other	**3**	4
Total	**481**	418

Table 39: Summary of counterparty risk for derivatives etc. outside the trading portfolio.

Amounts in NOK million	**Nominal value**	**Credit equivalent**	**Weighted amount**	**Minimum regu-latory capital requirements 2012[1)]**	Minimum regu-latory capital requirements 2011[1)]
Interest rate and currency instruments in trading portfolio	40,059	993	704	56	63
Interest rate and currency instruments for hedging purposes	11,468	2,092	418	33	51
Credit derivatives	–	–	–	–	–
Total financial derivatives	**51,527**	**3,085**	**1,122**	**90**	114

[1)]Minimum regulatory capital requirements are calculated in whole according to the standard method.

Table 40: Sensitivity of net interest expenses before tax (interest rate change of one percentage point) at the end of 2012

Sensitivity of net interest cost	**31/12/2012**	31/12/2011
Currency		
NOK	**6**	-2
EUR	**5**	1
USD	**-4**	-13
CHF	**–**	-2
Other	**–**	-1

Interest rate risk arises because the Group's assets and liabilities may be subject to different fixed rate periods. Interest rate instrument trading must at all times comply with the adopted limits and authorities. The Group's limits define quantitative targets for the maximum potential loss. The commercial risk is quantified and monitored continuously.

The Group's general limits for interest rate risk define the maximum loss from a 1 percentage point change in interest rates. The maximum loss following a 1% change in interest rates totals NOK 75 million with NOK 30 million of the total balance in Trading and NOK 45 million of the total balance in Treasury.

Operational risk

Operational risk is the risk of losses due to weak or inadequate internal processes or systems, human error or external incidents.

Management of operational risks

SpareBank 1 SR-Bank has established a strategy for the management of operational risk specifying that no individual incident caused by operational risk should be able able to severely damage the Group's financial position. The risk management is based on insight into and an understanding of what creates and drives operational risk in the Group, and must, as far as possible, reconcile effective processes with low risk exposure.

It is the responsibility of the individual managers to ensure that the unit for which they are responsible is subject to adequate management and control, and that operational risk is managed in accordance with the strategy and guidelines that have been defined for the Group. The group unit responsible for risk management is, however, responsible for supporting and challenging the risk owners, and it must ensure that the Group has a good framework for the identification, reporting and follow-up of operational risk.

Measurement of operational risk

SpareBank 1 SR-Bank calculates and maintains regulatory capital related to operational risk in accordance with the standardised approach. However, this method is regarded as giving an inadequate indication of the actual exposure to operational risk, since it is only based on historical income and does not take business-specific factors and established controls into account.

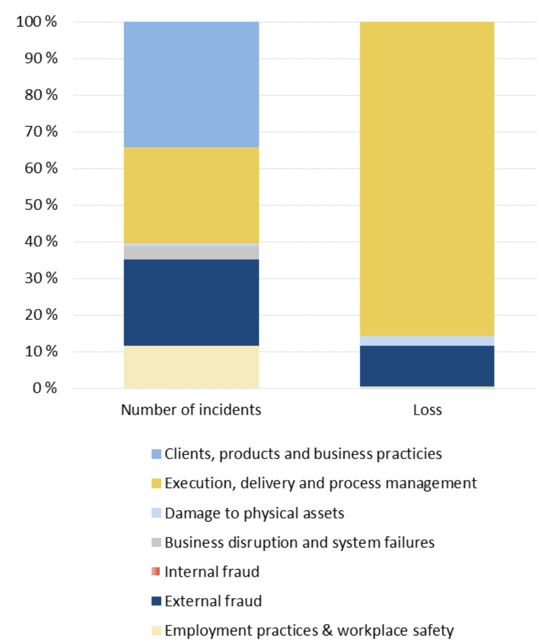
In order to determine the real risk exposure more accurately and to gain insight into what it is that drives operational risk and the Group's business and support processes, a total review of the Group's operational risk exposure is conducted at least annually, in which the potential risk scenarios and the associated probabilities and consequences are surveyed with extensive involvement by the process owners and technical experts. The resultant estimated exposure to operational risk is used in the Group's management accounts in order to calculate the business unit's risk-adjusted return.

With regard to types of operational risk, experience in the industry shows that human error or inadequate qualifications is often a contributing cause of the losses that are incurred in the lending area. For example, inadequate follow-up of the loan terms of negative customer events will entail getting involved too late in the credit protection process, and an incorrect assessment or registration of collateral can lead to large losses in the event of a default. SpareBank 1 SR-Bank therefore systematically evaluates any significant losses from the lending area in order to determine whether portions of the losses can be attributed to operational risk, or if it is possible to improve the work processes in the areas where losses from operational risk arise.

To provide input for risk assessments and form a foundation for continuous operational learning and improvement, other undesired incidents are reported in a special corporate database.

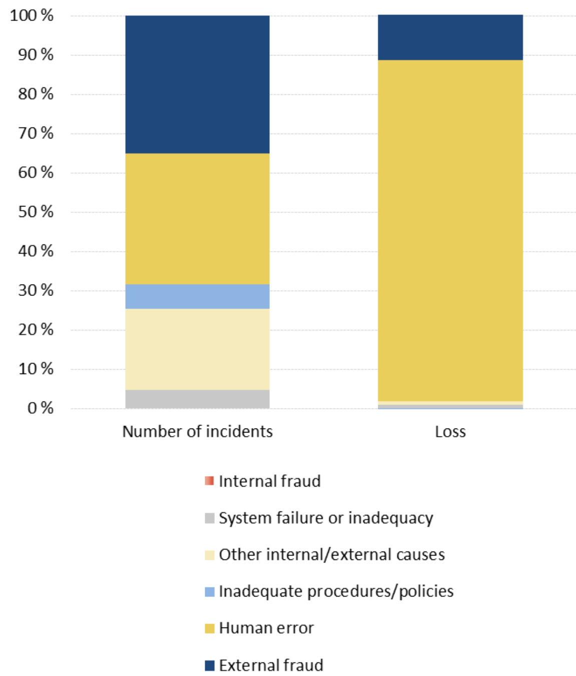
The figure below shows the Group's reported undesired incidents in 2012 by the Basel categories:

Figure 6: Reported undesired incidents in 2012 by the Basel II categories



The same incidents are also broken down by the main cause to which the individual incidents can be attributed. This breakdown is illustrated in the figure below.

Figure 7: Reported undesired incidents in 2012 by main cause



The breakdown for 2012 shows that it is generally incidents related to products and business practices that contribute the most to the absolute losses, and that the cause of the losses arising can generally be attributed to inadequate routines and human error.

Continuous improvement based on the reported incidents should be able to prevent the same types of incidents occurring in the future. An effort is therefore being made to improve the reporting systems and reporting culture even more in order to identify as many incidents as possible.

However, it is not sufficient to prevent recurrence in order to avoid major losses in the future. One of the greatest challenges associated with operational risk is to forecast and calculate credible estimates for rare events with major consequences. For example, it is difficult to estimate the probability of an employee deliberately exceeding his or her authority, and in theory there are no limits to the consequences of this in a worst case scenario.

Extensive scenario models are required in order to identify the complexity related to such scenarios, and SpareBank 1 SR-Bank has collaborated for several years with the risk environment at the University of Stavanger (UiS) to develop such models. The methods developed through this collaboration are increasingly implemented in the Group's ongoing risk management.

SpareBank 1 SR-Bank has high ambitions in the area of operational risk and would like to contribute to making Norway a centre of expertise in Europe for operational risk management and measurement. We are therefore working continuously on developing and improving practical and professional approaches to manage and control operational risk based on insight into real risk drivers and causal relationships. A significant contribution to this work is our cooperation with the University of Stavanger (UIS) which is regarded as one of the world's leading academic risk environments.

Liquidity risk

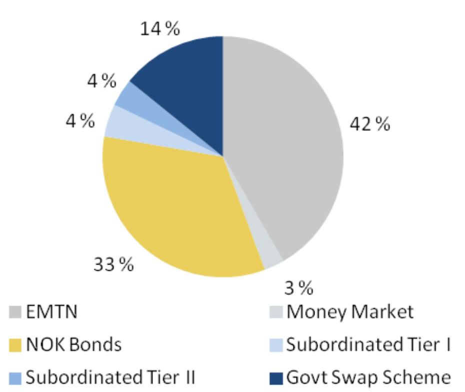
Funding risk is the risk that the Group is not able to refinance its debt or is not able to finance an increase in assets.

Risk profile and management of liquidity risk

The bank's framework for managing liquidity risk shall reflect the bank's conservative risk profile. Liquidity risk shall be low.

Liquidity risk is managed and measured by means of several measurement methods, since no one method can be used to quantity this type of risk. The methods include limits for the maximum refunding need for various maturities, key balance sheet figures and survivability targets in a normal situation, assuming the capital markets are closed. In addition, stress tests are conducted to determine the bank's ability to survive under various scenarios, including a serious bank or market specific crisis. The results of the stress tests are included in the information on which the Group's liquidity strategy and contingency plan for a liquidity crisis are based.

Figure 8: Composition of the Group's securities borrowing as at 31 December 2012



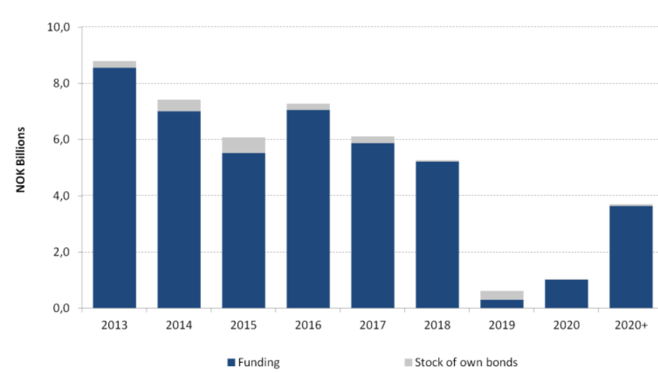
Of the liquidity reserves of NOK 20.7 billion, NOK 8.3 billion represents mortgage loans that have been prepared in the WEB client (loans ready to be transferred to SpareBank 1 Boligkreditt AS). The liquidity reserves without the WEB client are thus NOK 12.4 billion. The liquidity situation is satisfactory for SpareBank 1 SR-Bank, and the liquidity reserves without the WEB client indicate an ability to survive for 17 months (31 months including the WEB client) at the end of September without access to external funding. Treasury has issued bonds for a gross amount of NOK 15.6 billion in 2012. During the same period loans corresponding to approximately NOK 5.7 billion were redeemed. During the next 12 months, debt corresponding to NOK 8.6 billion will be refinanced.

Deposits from customers represent the Group's most important source of funding. For the Group as a whole the volume of deposits increased from NOK 3.6 billion (5.5 per cent) in 2012. During the year, the Group's lending excluding home mortgage and commercial credit increased by NOK 8.1 billion (8.0 per cent). This means that the deposit-to-loan ratio has declined from 63.2 per cent to 61.7 per cent. The deposit-to-loan ratio is able to meet the target with regard to the Group's liquidity strategy guidelines, which specify a target of maintaining a deposit-to-loan ratio of at least 55 per cent.

Home mortgage loans in SpareBank 1 Boligkreditt AS totalled around NOK 48,2 billion at the end of the 4th quarter of 2012, compared with NOK 44.7 billion at the end of 2011. The transferred balance accounts for around 46 per cent of the gross home mortgage loan balance and around 31 per cent of the total gross lending. Loans in SpareBank 1 Næringskreditt AS total approximately NOK 0.5 billion.

The figure below illustrates the maturity structure for the funding portfolio at the end of the 4th quarter of 2012.

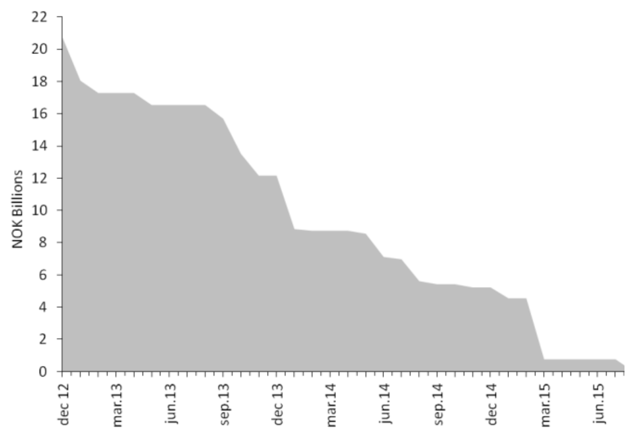
Figure 9: The funding portfolio's maturity structure as at 31 December 2012



The average remaining term to maturity in the portfolio of senior bond funding was 3.1 years at the end of the fourth quarter of 2012.

A sensitivity analysis that measures the Group's ability to survive in the event of closed capital markets is prepared on a monthly basis. The primary objective of the analysis is to measure whether the funding risk is in accordance with the definition of targets for liquidity management, which specify that SpareBank 1 SR-Bank must be able to survive for a minimum 12 months without external access to liquidity in a normal situation. The analysis is based on different scenarios. In the basis scenario the growth in net funding needs is set at zero, i.e. the relationship between deposits and loans are kept constant.

Figure 10: Sensitivity analysis of the funding risk – basis scenario



Since the basis scenario requires that access to external funding is not available, new lending can only be funded by instalments from and the maturity of the existing loan portfolios. In such a situation, the Group's liquidity buffer, which totals NOK 20.7 billion at the end of the 4th quarter of 2012, ensures the ability to survive to the end of July 2015. The liquidity buffer consists of cash, very secure interest-bearing securities and home mortgage loans ready to be transferred to SpareBank 1 Boligkreditt AS.

Ownership risk

Ownership risk is the risk that SpareBank 1 SR-Bank will incur a negative result from ownership interests in strategically owned companies and/or must inject fresh capital into these companies. Owned companies are defined as companies where SpareBank 1 SR-Bank has a significant stake and influence.

The ownership risk varies from company to company depending on the company's operations and the inherent risk, as well as SpareBank 1 SR-Bank's ownership interest. At the end of the 4th quarter of 2012 SpareBank 1 SR-Bank has primarily ownership risk through ownership in the SpareBank 1 Gruppen AS (19.5 per cent), Bank 1 Oslo Akershus AS (19.5 per cent)[5], BN Bank ASA (23.5 per cent) and SpareBank 1 Næringskreditt AS (28.3 per cent).

SpareBank 1 Group is owned by SpareBank 1 SR-Bank (19.5 per cent), SpareBank 1 Nord-Norge (19.5 per cent), SpareBank 1 SMN (19.5 per cent), SpareBank Hedmark (12 per cent), Samarbeidende Sparebanker AS (19.5 per cent), and the Norwegian Federation of Trade Unions (LO) and affiliated unions (10 per cent).

SpareBank 1 Gruppen AS owns 100 per cent of the shares in ODIN Forvaltning AS, SpareBank 1 Livsforsikring AS, SpareBank 1 Skadeforsikring AS, SpareBank 1 Medlemskort AS and SpareBank 1 Gruppen Finans Holding AS, as well as 97.55 per cent of the shares in SpareBank 1 Markets AS. SpareBank 1 Gruppen Finans Holding AS owns SpareBank 1 Factoring AS (100 per cent), Actor Fordringsforvaltning AS (100 per cent) and Actor Portefølje AS (100 per cent). SpareBank 1 Gruppen AS also has an interest in SpareBank 1 Utvikling DA.

The SpareBank 1 Group also has administrative responsibility for all the cooperation processes in the SpareBank 1 Alliance, where technology, brand names, competence, joint processes / application of best practices and purchasing are all key factors. The Alliance also conducts development work at three Centres of Expertise – Training (Tromsø), Payment Services (Trondheim), and Credit Control (Stavanger).

[5] In the 1st quarter of 2013, SpareBank 1 SR-Bank reduced its ownership interest from 19.5 to 4.8 per cent.

Bank 1 Oslo Akershus operates under the marketing name SpareBank 1 Oslo Akershus. The Bank 1 Oslo Akershus Group consists of the parent bank Bank 1 Oslo Akershus AS and the subsidiaries EiendomsMegler 1 Oslo og Akershus AS, Invest 1 AS, Invest 3 AS, Invest 4 AS and Invest 5 AS.

SpareBank 1 SR-Bank's ownership risk consists primarily of the underlying credit risk in this company.

BN Bank ASA is owned by the SpareBank 1 banks and offers a broad range of banking services to businesses and private individuals. The bank's operations are based on traditional banking operations aimed at home mortgage loans in the retail market and commercial property. SpareBank 1 SR-Bank's ownership risk consists primarily of the underlying credit risk in this company.

In SpareBank 1 Næringskreditt AS's portfolio there is only lending to commercial properties with leases in central locations. Lending cannot make up more than 60 per cent of the total market value. SpareBank 1 SR-Bank's ownership risk consists primarily of the underlying credit risk in this company.

At the end of the 4th quarter of 2012, SpareBank 1 SR-Bank owns 29.9 per cent of the shares in SpareBank 1 Boligkreditt AS. The company's operations include the financing of loans to retail customers with security within 75 per cent of the basic value of real estate. At the end of the 4th quarter of 2012 SpareBank 1 SR-Bank had transferred NOK 56.3 billion (EAD) to the company. The ownership risk corresponds primarily to the share of the transferred portfolio, and the risk is thus followed up and reported as credit risk.

Management of ownership risk

SpareBank 1 SR-Bank has a strong focus on management and control in companies in which the bank has full or partial ownership.

In companies that are partially owned, either through direct ownership by SpareBank 1 SR-Bank or indirectly through ownership of 19.5 per cent of SpareBank 1 Group, SpareBank 1 SR-Bank, as the largest bank in the alliance, is represented as a board member in all companies of significant importance.

All follow-up of ownership interests is performed under the Group's Chief Financial Office. All reporting from the individual companies and questions regarding capital increases etc. are reported here. Through active participation in the board of directors of a number of the partially owned companies, a good supply of information is assured, which safeguards SpareBank 1 SR-Bank's ownership interests. In cases that are of importance to SpareBank 1 SR-Bank's other operations, the individual board chairman/member will submit the matter for a plenary discussion by the Group management. With this structure for corporate governance the quality of the management and control is perceived as being well safeguarded.

Risk limits and the allocation of equity to the individual companies is stipulated annually by the Group's Board of Directors. This is based on a framework for the assessment of risk. Seen in connection with the limits for risk identification in the Group's operations on the credit side, the limits are not as well developed on the ownership side, but a continuous effort is being made to develop this further in order to achieve even better management of the risk related to ownership.

The individual areas are closely followed up through the fixed structure at corporate governance meetings in the Group and reporting at level of the Group's Board of Directors. The business areas that are organised as separate subsidiaries have the same structure at board meetings as the rest of the Group. As a result of this, corrective measures can quickly be implemented since the development of important management parameters or circumstances of an external nature require measures to maintain the creation of value and risk management.

Business risk

Business risk is the risk of unexpected fluctuations in revenues and expenses resulting from changes in external circumstances, such as the market situation or government regulation.

Analysis of the Group's income and cost structure in relation to economic cycles shows that the greatest volatility is in the Group's capital gains from equity investments and bonds, earnings from the savings areas and commission income from real estate brokering. A decline in income is compensated for in part by means of cost reductions.

The Group has developed a well-diversified revenue base over a long period of time, and this means that any reduction in the individual product groups or customer segments will not have significant consequences over time.

Over time, the Group has developed cost-effective operations in combination with a continuous development of competence and expansion of the operations with regard to the range of products and geography. SpareBank 1 SR-Bank has systematically focused on the value chain philosophy and development of products and services for several years.

Through its systematic work today, the Group has a great deal of interaction across the divisions and subsidiaries. Nevertheless, this interaction can be improved and the potential is there for realising more business through the value chain.

Reputation risk

Reputation risk is the risk of a failure in earnings and access to capital because of lack of trust and reputation in the market, i.e. customers, counterparties, stock markets and authorities

SpareBank 1 SR-Bank has established a principal communication strategy to ensure communication of information internally and externally in a way which supports the Group’s value base, goals and vision. The main element of the communication strategy is a profile as a “Proper bank”.

SpareBank 1 SR-Bank has also implemented an internal process for identifying and evaluating the Group's overall reputation risk situation. The evaluation is carried out annually. All reputation risks are evaluated in relation to the inherent risk and established control and management measures.

Improvement measures are implemented when required. Through the analyses based on scientific methods and the harmonisation of these, any incorrect evaluations are eliminated. The results of the annual analyses are reviewed, discussed and possibly operationalised after reviews for the different levels in the organisation, including the Board of Directors and group management.

The Group continuously monitors its reputation. Both through day-to-day monitoring and evaluation of the media, as well as the continuous monitoring of discussions in different social channels. The continuous day-to-day evaluations are carried out as objectively as possible. Members of the group management and other key personnel receive daily media reports.

Strategic risk

Strategic risk is the risk of losses resulting from the wrong strategic decisions.

The Group will give priority to profitable and long-term value creation and balance long and short-term priorities. Our ambition is to have controlled growth in the entire market area, with special emphasis on the areas with a high population density. Growth shall take place organically and through the exploitation of structural opportunities.

The financial sector is experiencing increasing regulatory requirements from the authorities. This provides guidance for the Group's future plans.

Among our retail and corporate customers, our goal is net growth in customers and increased product coverage. The Group's capital markets services and the savings, deposits investments and pensions area should be responsible for a greater share of the Group's overall results. The Group's operations shall be made more efficient through improvement of the processes and systems. Our ambition is that all of this combined shall contribute to maintaining our position as the most attractive supplier of financial services in Southern and Western Norway and that we should be in the top half of the comparable financial groups with regard to earnings.

Management of strategic risk

SpareBank 1 SR-Bank carries out an annual strategy process once a year that involves the Board of Directors, key personnel, departments and subsidiaries. The result of this process is a strategic presentation of goals for the following three years, with an associated business plan and plan of action. The business plan clearly shows the priorities the Group has made for the period based on scenarios and the competition and market situation. The business plan and plan of action is the most detailed for the nearest year.

The group management carries out monthly and four-monthly evaluations of the Group’s achievements and strategic direction. The four-month evaluation also evaluates relevant new initiatives and measures that must be implemented based on changes in assumptions or changes in the market situation. Strategic work is therefore flexible in its approach and can safeguard both short-term and long-term goals.

Compliance risk

Compliance risk is the risk that the Group incurs public sanctions/penalties or financial loss as a result of failure to comply with legislation and regulations.

The compliance function at SpareBank 1 SR-Bank is an independent function that ensures that the laws, regulations, standards and recommendations that regulate our operations, and are laid down by government agencies or other institutions or associations, are implemented and complied with.

Compliance policy

The Group's compliance policy is adopted by the Board and describes the main principles for responsibility and organisation.

The Group stresses the importance of good processes to ensure compliance with the current laws and regulations. Effective tools for achieving this include:

- Clear values that are clearly communicated and understood throughout the organisation
- A process that detects, communicates and implements changes in legislation and regulations
- A process to monitor and report compliance with legislation and regulations

Management of compliance risk

The limits for compliance are based primarily on the EBA's"Guidelines on Internal Governance (GL 44)", Basel Committee on Banking Supervision's "Compliance and the compliance function in banks" and the Financial Supervisory Authority of Norway's "Module for the evaluation of general management and control".

The Group's compliance function is performed by the Risk Management and Compliance Department, which is organised independently of the business units. The department has the overall responsibility for the limits, follow-up and reporting in the area of compliance.

The Group's managers have an operational responsibility for practical implementation and compliance with laws and regulations. All employees are responsible for ensuring that they comply and understand the laws and regulations on a day-to-day basis.

Compliance for investment firm

The Group has a designated compliance manager for the Group's investment firm, who is responsible for ensuring that the bank's activities related to the provision of investment services are carried out at all times in compliance with the regulations for securities trading.

The compliance manager for the investment firm reports directly to the general manager of the securities firm and also reports to the Risk Management and Compliance Department.

Remuneration scheme

SpareBank 1 SR-Bank ASA's remuneration policy

SpareBank 1 SR-bank ASA has established a remuneration scheme that applies to all employees.

The Group's remuneration scheme shall:

- Be consistent with the Group's overall objectives, risk tolerance and long-term interests
- Help to promote and provide incentives for good management and control of the Group's risk, discourage excessive or unwanted risk taking, and help to avoid conflicts of interest
- Comply with the regulations governing remuneration schemes in financial institutions, investment firms and management companies for securities funds of 1 December 2010 (Remuneration Scheme Regulations)

The total remuneration shall be competitive, but not leading. It shall ensure that the Group attracts, develops and retains the most competent employees over time. The scheme will ensure a reward model that is perceived to be fair, predictable and future-oriented and motivating.

Decision process

The Board of SpareBank 1 SR-Bank ASA has established a Remuneration Committee consisting of three board members.

The Remuneration Committee prepares matters for the Board and is mainly responsible for:

- annually reviewing and proposing the total salary and remuneration for the CEO
- annually considering proposals for corporate scorecard (CEO's scorecard)
- annually considering the Group's remuneration scheme, including strategy and guiding principles for variable remuneration
- advising the CEO on matters relating to remuneration and other key benefits and other personnel-related issues for the Group's executive personnel
- ensuring that the practice of the Group's remuneration arrangements are reviewed annually by an independent control function
- preparing a statement on the fixing of salaries and other remuneration to executive personnel (ref. section 6-16a of the Public Limited Liability Companies Act)
- considering other conditions as determined by the Board and/or Remuneration Committee
- reviewing other personnel-related matters concerning the Group's remuneration scheme that are likely to involve significant reputation risk.

Guidelines for the coming financial year
CEO's remuneration

The CEO's salary and other financial benefits shall be fixed annually by the Board based on the recommendation of the Remuneration Committee. Fixed salary is determined on the basis of results achieved, and market trends for similar positions. The CEO's variable remuneration is fixed on the basis of a comprehensive assessment based on the following factors: customer/market perspective, internal processes, organisation and expertise, as well as a financial perspective. Variable compensation can be earned annually, but must be based on goals achieved in the last two years. The CEO can receive group bonuses on a par with other employees. Any variable remuneration, including group bonuses, may amount to up to 25% of fixed salary including holiday pay. No performance-based benefits are paid over and above the said schemes. Variable pay is not included in pensionable salary.

Half of the variable remuneration, with the exception of the group bonus, is paid in the form of shares in SpareBank 1 SR-Bank ASA, where 1/3 can be used in each of the next three years. That part of the variable remuneration that is paid in shares will be reduced if the recalculation basis for calculating the variable remuneration in the qualifying year shows that the calculation basis is considerably lower than the calculation basis that was assumed in the qualifying year.

The CEO may also receive benefits in kind to the extent that the benefits are naturally related to the CEO's function in the Group and are in line with market practice in general. A life-long pension scheme has been entered into for the CEO with the pensionable age being the end of the year in which he reaches the age of 64 years, and then with an annual salary up to the age of 67 representing 67 per cent of pensionable salary. From the age of 67, the CEO will receive a supplementary retirement pension which, together with the SpareBank 1 SR-Bank's pension fund, pension from the National Insurance

Scheme and statutory early retirement pension (AFP) will constitute 67% of pensionable pay, assuming full earning period.

The CEO has no agreement concerning termination benefits if he leaves his post prior to reaching retirement age.

Remuneration of other executive personnel

The CEO fixes the remuneration of executive personnel in accordance with SpareBank 1 SR-Bank's adopted remuneration scheme at any given time. Executive personnel are employees who report to the CEO, i.e. the executive management team.

Salaries are fixed after considering the performance and conditions in the market for the various areas. Salaries should promote good performance and ensure that the Group achieves its strategic goals. Remuneration should not be detrimental to the Group's reputation nor shall the Group be a market leader. Salaries should ensure that the Group has the ability to attract and retain executives with the skills and experience required.

Variable remuneration is fixed on the basis of a comprehensive assessment based on the following factors: customer/market perspective, internal processes, organisation and expertise, as well as financial perspective. Variable compensation can be earned annually, but must be based on goals achieved in the last two years. Executive personnel may receive a group bonus on a par with other employees. Any variable remuneration, including group bonuses, may amount to up to 25% of fixed salary including holiday pay. For the Executive Vice President Capital Market variable pay, including group bonus may be up to 50% of fixed salary including holiday pay. No performance-based benefits are paid over and above the said schemes. Variable pay is not included in pensionable salary. The Executive Vice President, Risk Management and Compliance receives no variable remuneration beyond group bonuses.

Half of the variable remuneration, with the exception of the group bonus, is paid in the form of shares in SpareBank 1 SR-Bank ASA, where 1/3 can be used in each of the next three years. That part of the variable remuneration that is paid in shares will be reduced if the recalculation basis for calculating the variable remuneration in the qualifying year shows that the calculation basis is considerably lower than the calculation basis that was assumed in the qualifying year.

Benefits in kind can be offered to executive personnel to the extent that benefits are naturally linked to each function in the Group and are in line with market practice in general.

The pension schemes should be seen in the context of other remuneration and should provide competitive terms. Members of the executive management team have a retirement age of 62 years, with the exception of the last member to be employed, who has a retirement age of 67. The executive management team are members of the closed defined benefit plan which, with full pension earnings, entitles them to a pension of 70 per cent of pensionable income, including pension from the National Insurance Scheme and AFP from the age of 67. This does not apply to the last member of the executive management team to be employed, for whom the pension is limited to 12G. Members of the executive management team who have a retirement age of 62 years are entitled to a pension equivalent to 70 per cent of pensionable income in the form of service pension, from age 62 to age 67.

No executive personnel have an agreement concerning termination benefits upon leaving his/her post prior to reaching retirement age.

Variable remuneration of other employees

Group bonus

The Group has a bonus scheme which includes all employees. The group bonus is set at an equal percentage of salary, and can, as a maximum, amount to 1.5 times the monthly salary. The Group bonus is determined on the basis of corporate scorecards set by the Board and in relation to financial and non-financial targets that are weighted 70% and 30% respectively. The group bonus is paid entirely in cash.

Team bonus

Team bonuses can be utilised as a tool to promote activities and sales results. Team bonuses can, as a maximum, amount to NOK 50 000 per employees are paid in cash.

Individual bonus

Individual bonuses can be used as a tool for the Group to reward extraordinary achievements, while at the same time they may be a good tool to maintain a reasonable fixed salary development.

Individual bonuses are paid in shares (50 %) and cash (50 %). Individual bonuses can, amount to no more than 25 per cent of the fixed salary, including the group bonus and any team bonus.

Special schemes
The competitive situation and market practice may indicate that it is desirable to establish special arrangements related to variable remuneration in some areas. For employees covered by special schemes, or who can receive individual bonuses, and who should be regarded as executive personnel, employees with duties essential to the enterprise's risk exposure or other employees and representatives with similar remuneration (according to the regulations governing remuneration schemes), the same principles that apply to the executive management team in relation to criteria for the allocation and payment of variable remuneration shall apply. This category of employee may not receive team bonuses.

Employees with control functions cannot receive variable remuneration beyond group bonuses.

Binding guidelines for shares, subscription rights, options, etc. for the coming financial year

The CEO and executive management team are able to participate in private placements for employees on an equal footing with other employees.

Half of all the variable remuneration, with the exception of the group bonus, the CEO and executive management team will earn in 2013 will be paid in the form of shares issued by SpareBank 1 SR-Bank ASA. Up to 1/3 of shares that are allotted as variable remuneration can be traded in each of the following three years.

Report on executive pay policy in the preceding financial year

The Board confirms that the executive pay policy guidelines for 2012 provided in last year's statement have been complied with, except for the fact that the group bonus was paid fully in cash instead of half of the bonus being paid in the form of shares in SpareBank 1 SR-Bank ASA. Employees who received an individual bonus, and who are not covered by the special scheme in the regulations governing remuneration schemes are subject to a 2-year lock in period for bonus shares instead of receiving 1/3 of the shares in each of the following 3 years.

Disclosure of remuneration

For 2012 a total cost of NOK 874 million has been recognised for remuneration, distributed among 1,330 employees. NOK 780 million of this amount represents fixed remuneration, and NOK 94 million represents variable benefits Reference is made to note 22 in the Group's annual report for information on personnel expenses.

The table below discloses the remuneration of employees subject to special remuneration scheme requirements.

Table 41: Disclosure of remuneration

Disclosure of remuneration	Number	Remuneration	Of which variable remuneration
Key executives: CEO, members of the group management team	9	19,073	1,527
Employees and elected representatives with duties of significant importance to the enterprise's risk exposure	6	7,995	562
Other key executives	8	13, 929	3,263
Employees with control functions	7	6,026	337