

# 2017

PILLAR 3



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# 1 Introduction

Pillar 3 is a regulatory requirement for the publication of information about capital and risk conditions. This document provides a description of SpareBank 1 Østlandet's risk and capital management and in order to satisfy the requirements for the public disclosure of financial information as stipulated in the Part IX of the Capital Adequacy Regulation.

Work is taking place internationally to standardise the disclosure of information by using standardised templates, as well as clarifying requirements for qualitative descriptions. The Basel Committee and the European Banking Authority, hereinafter referred to as the EBA, updated their pillar 3 framework in March 2017 and December 2016 respectively. Until the new regulations have been implemented in the EU, SpareBank 1 Østlandet has supplemented the requirements of the capital adequacy regulation with the guidelines from the EBA of December 2016 in the publication. The standardised templates follow as attachments to the Pillar 3 document.

This document is updated annually. If, however, there are significant changes that have an impact on the assessment of the Group's financial situation, then this document will be updated with new information. Standardised forms in attachments are updated at the recommended frequency for each form. Periodic information on capital adequacy and the minimum own funds requirements is available in the Group's quarterly reports. All figures are stated in NOK million unless otherwise described.

Beyond the information available in this document with appendices, we refer to About us/investor on SpareBank 1 Østlandet's website **<https://www.sparebank1.no/nb/ostlandet>**.

This document is printed in both a Norwegian and an English version. In case of any differences between the two versions the Norwegian version overrides the English version.

## 1.1 Capital adequacy regulations

The capital adequacy regulations are based on a standard for calculating capital adequacy where the purpose is to reinforce the stability of the financial system through the following measures:

- Risk sensitive capital requirements.
- Regulatory requirements for risk management and control.
- Supervisory review and evaluation.
- Information to the market

The regulations are intended to ensure there is an alignment between how the authorities stipulate capital adequacy requirements for financial institutions and the approaches the financial institutions use to calculate and assess their capital requirements. The capital adequacy rules and regulations are based on the following three pillars:

- **Pillar 1:** Minimum primary capital requirements.
- **Pillar 2:** Evaluation of the overall capital requirements and supervisory review and evaluation.
- **Pillar 3:** Public disclosure of information.

### 1.1.1 Pillar 1 – Minimum own funds requirements

Pillar 1 concerns the minimum own funds requirements for credit risk, operational risk and market risk, for which the minimum capital adequacy requirement has been set at 8 per cent. In addition to this comes a total buffer requirement of 7.5 per cent as at 31.12.2017.

SpareBank 1 Østlandet has not been defined as a nationally systemic important bank.

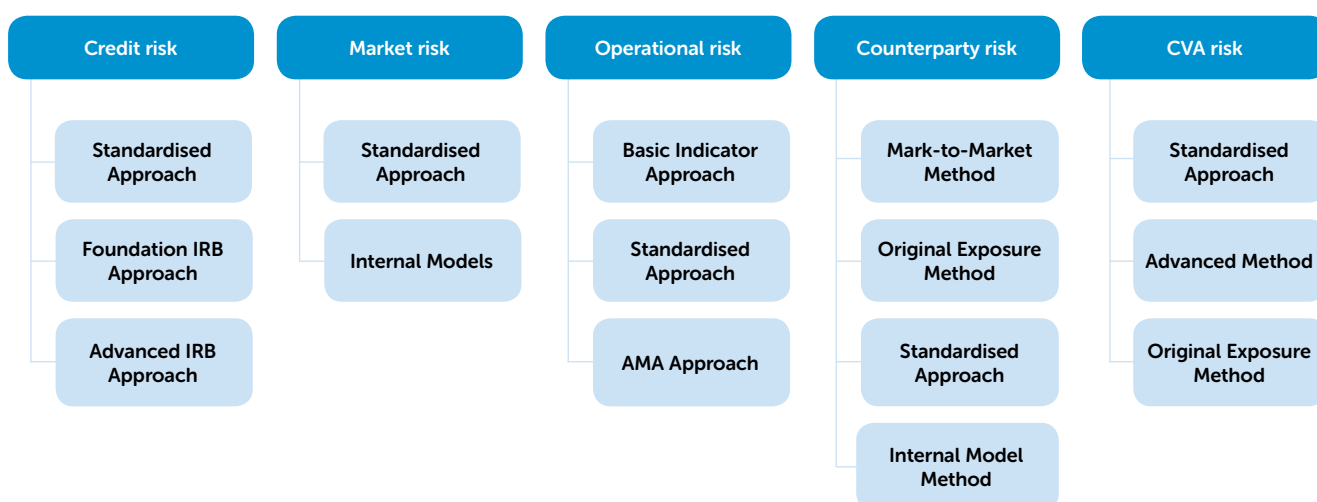
Capital adequacy is defined as the relationship between the bank's total own funds and its risk-weighted assets.

Figure 1.1: Capital adequacy ratio

$$\frac{\text{Core equity tier 1 capital} + \text{other tier 1 capital} + \text{supplementary capital}}{\text{Credit risk} + \text{market risk} + \text{operational risk}} \geq \text{minimum requirement} + \text{buffer requirement}$$

The capital adequacy regulations contain various approaches for calculating capital requirements. The various approaches are illustrated in the figure below.

Figure 1.2: Approaches for calculating capital requirements



For enterprises that have permission to use an internal measurement approach, hereinafter called IRB approaches, where IRB is an abbreviation of Internal Rating Based Approach, the statutory minimum capital requirement for credit risk will be based on the enterprise's risk models. The use of IRB approaches will make the minimum capital requirement more risk sensitive and means that capital requirements, to a greater degree than when using the standardised approach based on

regulatory risk weights, will correlate more with the risk inherent in the underlying portfolios. The regulations for the IRB banks, however, include a requirement that the total capital requirement may not be lower than 80 percent of a capital requirement calculated by the standardised method under Basel I. As a result of this Basel I floor, the regulatory capital requirement will therefore not always be determined by the risk sensitivity of the IRB models.

### 1.1.2 Pillar 2 – evaluation of the own funds requirements and individual supervisory review and evaluation

Pillar 2 sets requirements for the enterprise's capital assessment process, hereinafter referred to as the ICAAP process, where ICAAP is an abbreviation of Internal Capital Adequacy Assessment Process. The purpose of this process is to implement a structured and documented assessment process for the Group's risk profile in order to ensure that the Group has adequate capital to cover the risk associated with its operations. In addition, financial institutions must have a strategy for maintaining an adequate level of capital.

In autumn 2016, the Financial Supervisory Authority of Norway published circular 12/2016 "The Financial Supervisory Authority of Norway's practices for assessing risk and capital requirements". The Group has adapted its ICAAP process to comply with this circular.

Based on the above-mentioned circular, the Group calculates its Pillar 2 supplementary capital requirement in a process involving the parent bank, subsidiaries and the stakes in associated companies/joint ventures. The process is based on an assessment of exposure and quality in management and control, where the capital requirements are mainly based on the approach described in the aforementioned circular.

The Financial Supervisory Authority of Norway is required to monitor and evaluate the Group's internal assessments of capital requirements and associated strategies, as well as the Group's ability to ensure compliance with the authorities' capital requirements. The Financial Supervisory Authority of Norway has the authority to implement suitable supervisory measures if the Financial Supervisory Authority is not satisfied with the results of this process.

### 1.1.3 Pillar 3 – Public disclosure of information

The purpose of Pillar 3 is to help increase market discipline and to make it easier to compare financial institution. The financial institution shall publish information that gives the market participants the opportunity to assess the financial institutions risk profile, capitalisation and control of risk. The information shall be provided in an understandable way that makes it

possible compare different enterprises. The information shall mainly be published at least annually, with the financial statements, but the financial institution shall assess whether some requirements are to be made public more frequently.

## 1.2 The Group's capital adequacy targets

The Group's overarching strategic targets are set on the basis that they should underpin a moderate to low risk profile, where the Group shall be among Norway's financially strongest and profitable regional financial groups.

The Group's financial strength is expressed through its regulatory capital adequacy. The following conditions shall be taken into account when setting the level of capital:

- The authorities' capital adequacy requirements.
- Need for freedom of action.
- Level of ambition in the strategic targets.
- Commercial framework conditions.
- Desired risk profile.

The level of capital set should ensure that the Group has adequate capital to satisfy regulatory requirements for capital adequacy.

The Group has the following capital targets:

- Core equity tier 1 ratio of 16.0 per cent.
- Total capital adequacy ratio of 17.8 per cent.
- Leverage ratio of 6.0 per cent.

## 1.3 Adapting to the Capital Adequacy Regulation

As at 31.12.2017, the parent bank, SpareBank 1 Østlandet, uses the advanced IRB approach for calculating minimum requirements for primary capital for credit risk in the loan portfolio. The figure below provides an overview of the approaches the Group uses for calculating capital requirements.

Figure 1.3: Approaches for calculating capital requirements in the Group

Area	SpareBank 1 Østlandet (parent bank)	SpareBank 1 Finans Østlandet
<b>Credit risk</b>		
- Governments	Standardised Approach	Standardised Approach
- Institutions	Standardised Approach	Standardised Approach
- Enterprises	Advanced IRB Approach	Standardised Approach
- Retail	IRB approach	Standardised Approach
- Equity positions	Standardised Approach	N/A
<b>Market risk</b>	N/A	N/A
<b>Operational risk</b>	Standardised Approach	Standardised Approach
<b>Counterparty risk</b>	Mark-to-Market	N/A
<b>CVA risk</b>	Standardised Approach	N/A

## 2 Regulatory capital

At the year end 2017, the group is subject to a core equity tier 1 capital requirement of 12 percent under Pillar 1. In addition, the additional capital requirement under Pillar 2, as at 31.12.2017 has been set by the Financial Supervisory Authority of Norway at 1.7 percent. With effect from 31.03.2018, the Pillar 2 requirement increases to 1.8 percent.

The purpose of the Pillar 2 requirement is to cover capital requirements associated with risks that are not, or are only partially, covered by the capital requirements in Pillar 1. The Group is subject to a minimum own funds requirement under Pillar 1 of 15.5 per cent as at 31.12.2017.

### 2.1 Regulatory capital adequacy

The following table shows the Group's capital adequacy calculation under Pillar 1 as at 31.12.2017.

Table 2.1: Calculation of capital adequacy

SpareBank 1 Finans		ØstlandetAS		Parent Bank	Group
	1 055		6 078	Paid-up equity	6 078
	177		5 928	Earned equity capital	6 791
			400	Hybridcapital	400
				Minority interests	62
	<b>1 231</b>		<b>12 406</b>	<b>Total equity carried</b>	<b>13 332</b>
				<b>Common equity tier 1 capital</b>	
	-118		-629	Results for the accounting year not included	-629
			-400	Share of equity not included in core capital	-462
				Minority interests that can be included in core capital	42
			93	Cumulative gains and losses due to changes in own credit risk on fair valued liabilities	93
				Cash flow hedge reserve	8
	-12		-103	Goodwill and other intangible assets	-380
			-189	Positive value of expected losses under the IRB approach	-231
				CET 1 instruments of financial sector entities where the institution does have a significant investement	-154
			-28	Value adjustments due to the requirements for prudent valuation (AVA)	-35
	<b>1 101</b>		<b>11 150</b>	<b>Common equity tier 1 capital</b>	<b>11 583</b>
				<b>Additional Tier 1 capital</b>	
			400	Hybrid capital	616
			<b>400</b>	<b>Tier 1 capital</b>	<b>616</b>
				<b>Supplementary capital in excess of Tier 1 capital</b>	
			1 700	Subordinated loan capital	2 068
			-130	T2 instruments of financial sector where the institution does have a significant investement	-130
			<b>1 570</b>	<b>Total supplementary capital</b>	<b>1 939</b>
	<b>1 101</b>		<b>13 120</b>	<b>Total eligible capital</b>	<b>14 138</b>
			5 154	Corporates - SME	5 154
			9 776	Corporates - Specialised Lending	9 776
			633	Corporates - Other	633
			1 020	SME exposure	1 203
			14 507	Retail mortgage exposure	21 840
			1 701	Other retail exposure	1 723
			<b>32 792</b>	<b>Risk-weighted assets credit risk IRB</b>	<b>40 330</b>
	5 769		11 004	Exposures calculated using the standardised approach	15 438
				Market risk	
			72	CVA	765
	341		3 343	Operational risk	4 503
			2 577	Basel I floor	7 884
	<b>6 110</b>		<b>49 787</b>	<b>Risk-weighted assets</b>	<b>68 920</b>
	<b>489</b>		<b>3 983</b>	<b>Capital requirements (8%)</b>	<b>5 514</b>
			<b>846</b>	<b>Pillar 2 (1.7%)</b>	<b>1 172</b>

SpareBank 1 Finans Østlandet AS		Parent Bank	Group
		Buffer requirements	
	1 245	Capital conservation buffer (2.5%)	1 723
	996	Countercyclical capital buffer (2%, 1.5% in previous period)	1 378
	1 494	Systemic risk buffer (3%)	2 068
	<b>3 734</b>	<b>Total buffer requirements for common equity (7.5%)</b>	<b>5 169</b>
<b>1 101</b>	<b>4 329</b>	<b>Available common equity (12%)</b>	<b>2 141</b>
<b>Capital ratios</b>			
<b>18.0%</b>	<b>22.4%</b>	CET 1 capital ratio	<b>16.8%</b>
<b>18.0%</b>	<b>23.6%</b>	CET 1 capital ratio (excluding Basel 1-floor)	<b>19.0%</b>
<b>18.0%</b>	<b>23.2%</b>	Tier 1 Capital ratio	<b>17.7%</b>
<b>18.0%</b>	<b>26.4%</b>	Capital adequacy ratio	<b>20.5%</b>

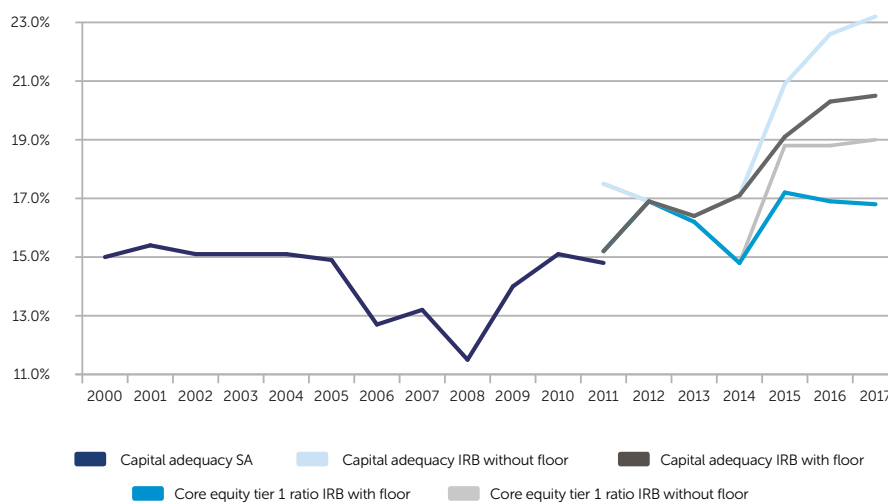
The following table shows the Group's minimum own funds requirement (8 per cent) as at 31.12.2017.

Table 2.2: Minimum own funds requirements

Minimum own funds requirement	SpareBank 1 Finans Østlandet AS	Parent Bank	Group
IRB Exposures			
Corporates - SME		412	412
Corporates - Specialised Lending		782	782
Corporates - Other		51	51
Retail - Secured by real estate SME		82	96
Retail - Secured by real estate non-SME		1 161	1 747
Retail - Other		136	138
Equity IRB			
<b>Minimum requirement IRB</b>		<b>2 623</b>	<b>3 226</b>
Standardised Approach exposures			
Central governments or central banks		0	0
Regional governments or local authorities		8	8
Public sector entities	3		3
Institutions	0	145	70
Corporates	89	57	167
Retail	359	5	421
Secured by mortgages on immovable property		2	58
Exposures in default	3		3
Covered bonds		46	103
Collective investments undertakings (CIU)			
Equity		519	272
Other items	7	98	128
<b>Minimum requirement SA</b>	<b>462</b>	<b>880</b>	<b>1 235</b>
Operational risk	27	267	360
CVA		6	61
Added for Basel I-floor		206	631
<b>Total own funds requirement</b>	<b>489</b>	<b>3 983</b>	<b>5 514</b>

The figure below shows the development of the Group's capital adequacy.

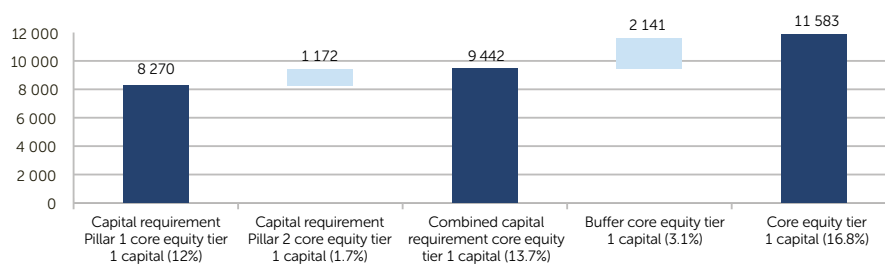
Figure 2.1. Development of capital adequacy



## 2.2 Regulatory core equity tier 1 ratio

The figure below provides a graphic representation of the Group's capital situation with a focus on core equity tier 1 capital as at 31.12.2017.

Figure 2.2: Core equity tier 1 ratio





## 2.3 Leverage ratio

The leverage ratio is calculated as the Group's Tier 1 capital as a percentage of the Group's exposure measure. The exposure measure is defined as the sum of the accounting value of the assets plus the off-balance sheet items drawing

rights, guarantees and unutilised credit facilities. As at 31.12.2017 the Group is subject to a minimum requirement for leverage ratio of 5 percent. The following table shows the leverage ratio as at 31.12.2017

Table 2.3: Leverage ratio

<b>On-balance sheet exposures (excluding derivatives and SFTs)</b>	
On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	160 545
(Asset amounts deducted in determining Tier 1 capital)	-699
<b>Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets)</b>	<b>159 846</b>
<b>Leverage ratio common disclosure</b>	
Replacement cost associated with all derivatives transactions (ie net of eligible cash variation margin)	6 374
Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	1 380
(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	-5 200
(Exempted CCP leg of client-cleared trade exposures)	-219
<b>Total derivatives exposures</b>	<b>2 335</b>
<b>SFT exposures</b>	
Gross SFT assets (with no recognition of netting), after adjusting for reverse repurchase transactions	
(Netted amounts of cash payables and cash receivables of gross SFT assets)	
Counterparty credit risk exposure for SFT assets	
<b>Total securities financing transaction exposures</b>	
<b>Other off-balance sheet exposures</b>	
Off-balance sheet exposures at gross notional amount	30 476
(Adjustments for conversion to credit equivalent amounts)	-19 864
<b>Other off-balance sheet exposures (sum of lines 17 and 18)</b>	<b>10 613</b>
<b>Capital and total exposure measure</b>	
Tier 1 capital	12 199
*Leverage ratio total exposure measure (sum of lines 3, 11, 16, 19, EU-19a and EU-19b) *	172 794
Leverage ratio	7.1%

## 3 Regulatory framework implementation

### 3.1 Consolidation for capital adequacy purposes

Consolidation of capital adequacy follows the rules set out in Chapter 18 of the Financial Enterprises Act on "Activities in financial groups, consolidation etc.". The most significant differences from ordinary consolidation according to IFRS are due to the proportional consolidation of financial enterprises where participant interest is above 20 percent.

#### 3.1.1 Cooperative Group

The Group also forms part of a cooperative group according to Chapter 17 part III of the Financial Enterprises Act "Cooperation outside the group structure." Jointly owned

financial enterprises such as SpareBank 1 Boligkreditt AS, SpareBank 1 Næringskreditt AS and SpareBank 1 Kredittkort AS are therefore proportionally consolidated for capital adequacy purposes. The inclusion of these companies' balance sheets represents the greater part of the difference between the accounting balance sheet and the capital adequacy exposure measure.

The table below provides an overview of companies in the Group and the treatment according to IFRS consolidation and capital adequacy.

Table 3.1: Basis for consolidation

Name	Method of accounting consolidation	Method of regulatory consolidation	Description of the entity
SpareBank 1 Østlandet	Full consolidation	Full consolidation	Parent bank
SpareBank 1 Finans Østlandet AS	Full consolidation	Full consolidation	Financing company
EiendomsMegler 1 Hedmark Eiendom AS	Full consolidation	Full consolidation	Real estate broker
SpareBank 1 Regnskapshuset Østlandet AS	Full consolidation	Full consolidation	Accounting and bookkeeping
EiendomsMegler 1 Oslo Akershus AS	Full consolidation	Full consolidation	Real estate broker
Youngstorget 5	Full consolidation	Full consolidation	Renting of real estate
AS Vato	Full consolidation	Full consolidation	Renting of real estate
Torggt 22 AS	Proportional consolidation	Proportional consolidation	Renting of real estate
SpareBank 1 Boligkreditt AS	Equity Method	Proportional consolidation	Covered bond issuer
SpareBank 1 Næringskreditt AS	Equity Method	Proportional consolidation	Covered bond issuer
SpareBank 1 Kredittkort AS	Equity Method	Proportional consolidation	Financing company
Proaware AS	Equity Method	Equity Method	Software development
SMB Lab AS	Equity Method	Equity Method	Advisory services
KOMM-IN AS	Equity Method	Equity Method	Office services
SpareBank 1 Gruppen AS	Equity Method	Equity Method	Financial holding company
SpareBank 1 Betaling AS	Equity Method	Equity Method	Financial holding company
SpareBank 1 Banksamarbeidet	Equity Method	Equity Method	Software development and marketing

The Group attaches importance to maintaining adequate capitalisation for all the companies within the Group at all times. The Group's governing bodies have not imposed any restrictions on the board's ability to transfer capital between

the parent bank and the subsidiaries beyond what follows from law. In addition, there are no provisions in the Articles of Association that impose any such restrictions.

### 3.2 Relevant framework for calculating risk-weighted assets

The bank uses the framework for credit risk in the Capital Adequacy Regulation parts II and III for the substantial part of the balance sheet. Financial derivatives and secured financing transactions, such as reverse repurchase agreements, are treated by the counterparty risk framework defined further in parts IV, V and VI in the same regulation. In determining the amount of commitment the bank uses the market value approach according to chapter 21 of the aforementioned directive. Assets that are deducted from own funds in the calculation of capital adequacy according to the Calculation Regulations are also deducted in the calculation of risk-weighted assets. This includes, among other things, deductions for investments in financial institutions.

The bank does not have a trading portfolio according to capital requirements rules and does not therefore use the framework for market risk. The group had no positions which were processed by the framework for securitisations at the end of the period.

The following tables provide additional information on the use of various risk frameworks. Shown here is a comparison between the balance sheet according to the accounts and capital adequacy, as well as comparison from the bank's balance sheet to exposure which is used in the calculation of risk-weighted assets

Table 3.2: Differences between financial and regulatory consolidation and comparison of accounting and regulatory risk categories

	Carrying values as reported in published financial statements	Carrying values under scope of regulatory consolidation	Subject to the credit risk framework	Subject to the CCR framework	Not subject to capital requirements or subject to deduction from capital
Cash and deposits with central banks	673	673	673		
Loans to and receivables from credit institutions	1 808	738	738		
Loans to and receivables from customers	90 098	130 658	130 658		
Certificates, bonds and fixed-income funds	8 883	20 466	20 466		
Financial derivatives	582	6 377		6 377	
Shares, units and other equity interests	495	495	495		
Investments in associates and joint ventures	3 929	1 070	1 070		-132
Investments in subsidiaries					
Property, plant and equipment	578	579	579		
Investment property					
Assets held for sale					
Goodwill and other intangible assets	366	441	441		-441
Deferred tax asset		2	2		-2
Other assets	910	886	886		
<b>Assets</b>	<b>108 321</b>	<b>162 385</b>	<b>156 008</b>	<b>6 377</b>	<b>-726</b>
Deposits from and liabilities to credit institutions	2 286	3 169			3 169
Deposits from and liabilities to customers	65 985	65 051			65 051
Liabilities arising from issuance of securities	23 686	71 922			71 922
Financial derivatives	307	507			507
Current tax liabilities	358	360			360
Deferred tax liabilities	122	153			153
Other debt and liabilities recognised in the balance sheet	541	5 546			5 546
Hybrid capital		270			270
<i>of which hybrid capital eligible as T1 capital</i>		616			616
Subordinated loan capital	1 706	2 075			2 075
<i>of which hybrid capital eligible as T2 capital</i>	1 570	1 939			1 939
<b>Total liabilities</b>	<b>94 990</b>	<b>149 053</b>			<b>149 053</b>
Issued equity	5 359	5 359			5 359
Premium fund	547	547			547
Hybrid capital	400	400			400
<i>of which hybrid capital eligible as T1 capital</i>	400	400			400
Minority interests	62	62			62
Other equity	6 963	6 964			6 964
<b>Total equity capital</b>	<b>13 331</b>	<b>13 332</b>			<b>13 332</b>
<b>Total equity capital and liabilities</b>	<b>108 321</b>	<b>162 385</b>			<b>162 385</b>

Table 3.3: Discrepancies between regulatory exposure and accounting exposure

	Total	Subject to the credit risk framework	Subject to the CCR framework
Assets carrying value amount under the scope of regulatory consolidation	162 385	156 008	6 377
Liabilities carrying value amount under the regulatory scope of consolidation	162 385		
Total net amount under the regulatory scope of consolidation	156 559		
Off-balance-sheet amounts	17 333	17 333	
Differences in valuations	1 153		1 153
Differences due to different netting rules	-5 826		-5 826
Differences due to consideration of provisions			
Differences due to prudential filters	-726	-726	
Other	57	57	
<b>Exposure amounts considered for regulatory purposes</b>	<b>174 376</b>	<b>172 673</b>	<b>1 704</b>

### 3.3 Encumbered assets

Encumbrance of assets occurs mainly through four types of transactions:

- Deposit of securities in Norges Bank for borrowing.
- Offsetting and cash collateral in conjunction with derivatives contracts.
- The bank does not participate in repurchase agreements, but receives securities in conjunction with reverse repurchase agreements.
- Pledging as security of loans in conjunction with the issue of covered bonds, hereinafter called OMF.

The majority of the bank's encumbrance of assets occurs via Sparebank 1 Boligkreditt AS and Sparebank 1 Næringskreditt AS which issue OMFs. The bonds are collateralised by loans with residential property as collateral

and loans with commercial properties as collateral respectively. These companies are consolidated proportionally within the group, which is done in conjunction with capital adequacy calculation, but are consolidated in accordance with the equity for financial reporting purposes.

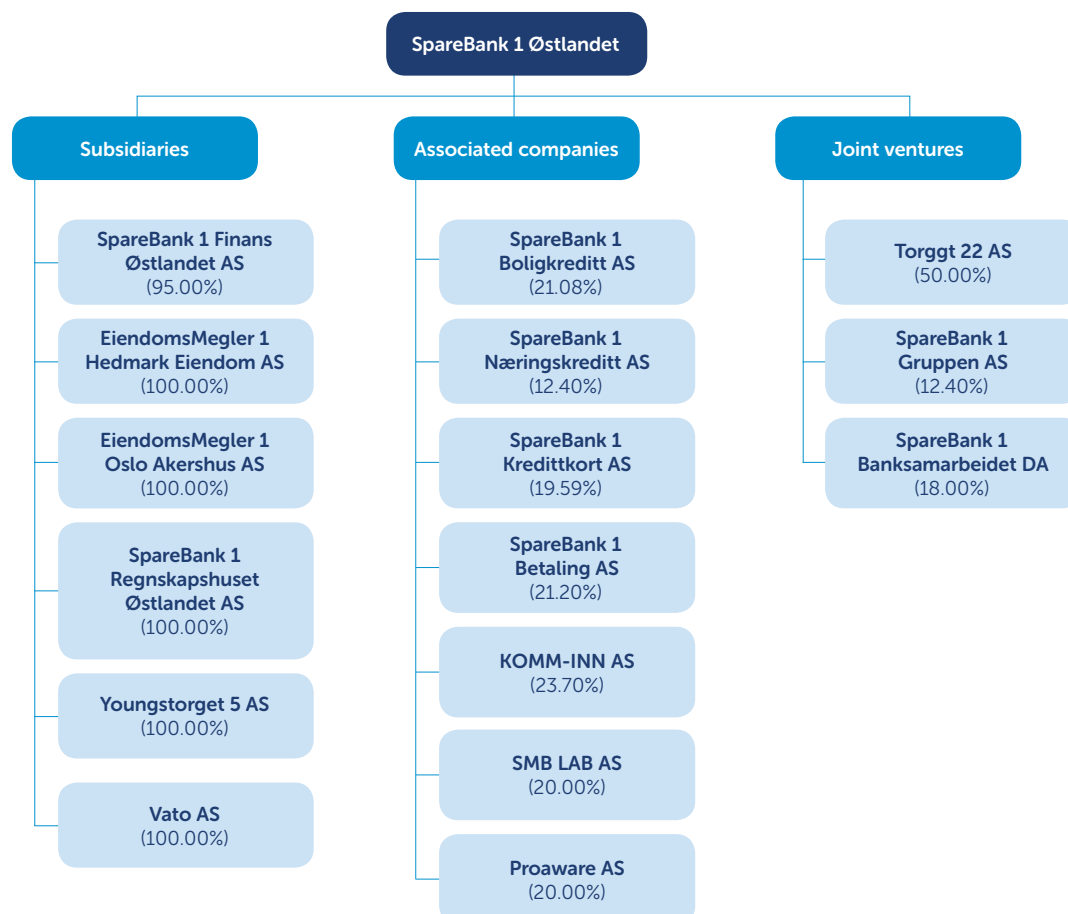
Encumbered assets, including collateral received equals 26 per cent of the sum of assets and received collaterals is used in the calculation of the total capital adequacy ratio. The equivalent key ratio for the parent bank is 1 per cent. Please refer to the enclosures for more information about encumbered assets. For more information on OMF issues, see the covered bond companies' financial reports.

## 4 The group

### 4.1 Group structure

The companies included in the SpareBank 1 Østlandet Group are shown in the figure below.

Figure 4.1: Group structure



**SpareBank 1 Østlandet** is the parent bank of the group and is the leading supplier of financial services to individuals, businesses and the public sector in Hedmark, as well as a contender within the same service spectrum in Oslo and Akershus. The bank has also established offices in Gjøvik and Lillehammer.

**SpareBank 1 Finans Østlandet AS** sells leasing products and secured financing, with all of Eastern Norway as its primary market area. The Parent Bank, SpareBank 1 Ringerike-Hadeland through its ownership position and capital goods suppliers are, in addition to the Internet, the company's most important distribution channels.

**EiendomsMegler 1 Hedmark Eiendom AS** is Hedmark's leading real estate agent and it is represented in the most central locations in the county, as well as at Gjøvik in Oppland.

**EiendomsMegler 1 Oslo Akershus AS** is the group's real estate agent operation in Oslo and Akershus.

**SpareBank 1 Regnskapshuset Østlandet AS** is part of SpareBank 1 Regnskapshuset's endeavour to become one of Norway's leading actors in the accounting industry. The SpareBank 1 banks intend, in line with the Alliance's strong traditions, to build up a national accounting operation based on regional ownership and proximity to the market.

**Youngstorget 5 AS** owns the parent bank's office building at Youngstorget in Oslo.

**Vato AS** owns some of the group's office buildings in Hedmark.

**SpareBank 1 Boligkreditt AS** is the alliance banks' covered

bond company for the retail segment.

**SpareBank 1 Næringskreditt AS** is the alliance banks' covered bond company for the corporate segment.

**SpareBank 1 Kredittkort AS** is the alliance banks' joint credit card company.

**SpareBank 1 Betaling AS** is the alliance banks' joint company for mobile phone payment solutions, which is part owner of Vipps.

**Comm-Inn AS** is an investment and commercialisation company based in industry in the Inland Region.

**SMB LAB AS** develops and provides financial services to small and medium-sized businesses and is owned by the banks of the SpareBank 1 Alliance.

**Proaware AS** develops IT solutions within governance, risk and compliance and is owned by most banks in the SpareBank 1 Alliance, as well as the SpareBank 1 group.

**TORGGT 22 AS** owns an office building in Hamar.

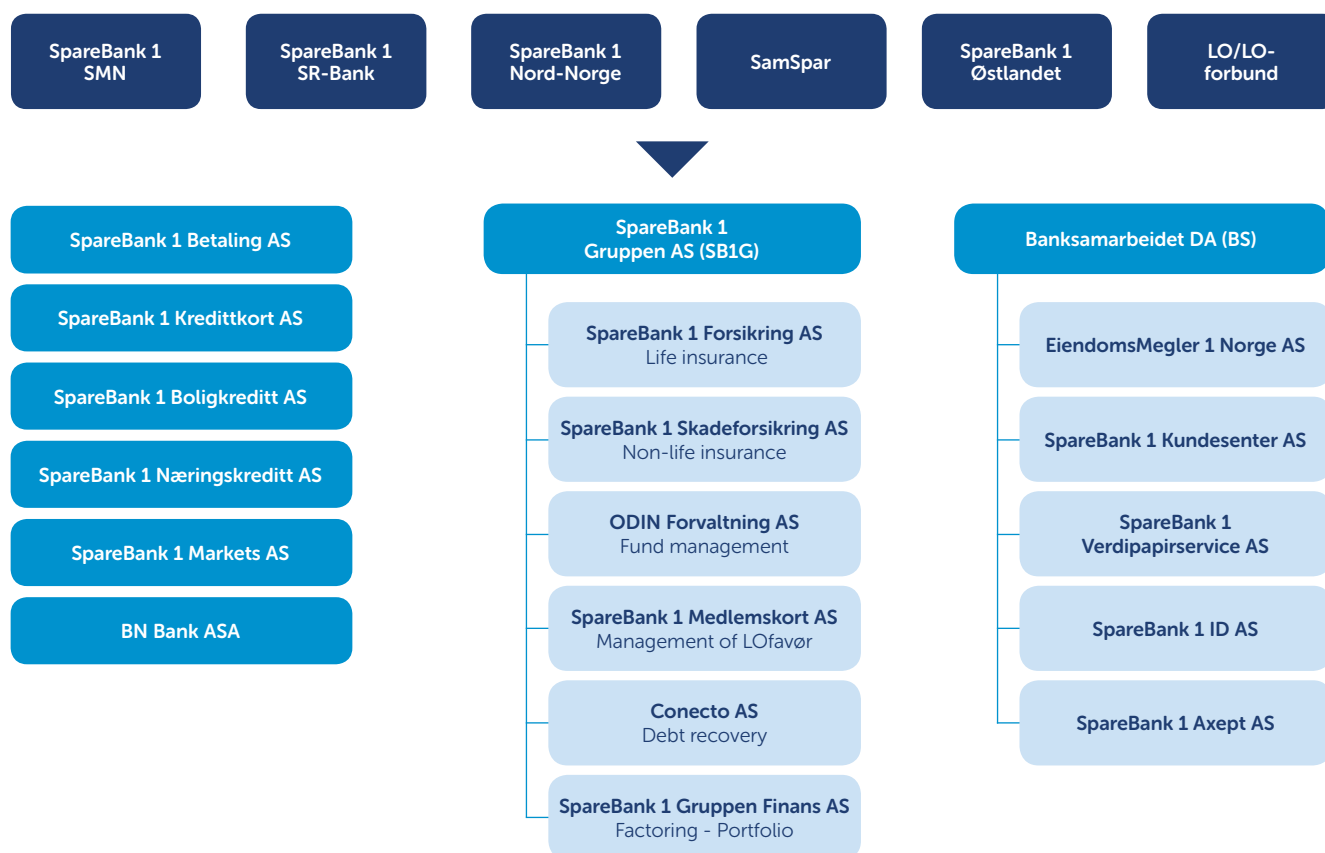
### SpareBank 1 Gruppen AS and SpareBank 1 Banksamarbeidet DA

The purpose of the SpareBank 1 Alliance is to acquire and provide competitive financial products and services, taking advantage of economies of scale in the form of lower costs and/or higher quality. The Alliance contributes accordingly to private individuals and corporate customers experiencing local roots, competence and an easier way of having their various requirements met. In addition, the Alliance shall contribute to ensuring the creation of value by the Bank for the benefit of our own region.

The SpareBank 1 banks run the Alliance, as well as develop and manage products via SpareBank 1 Utvikling DA and SpareBank 1 Gruppen AS. While SpareBank 1 Gruppen is a product provider primarily within insurance, SpareBank 1 Banksamarbeidet is responsible for the cooperation processes in the SpareBank 1 Alliance, where technology, brand names, competence, joint processes/best practices, and purchasing are all key factors.

The SpareBank 1 banks work together extensively on development.

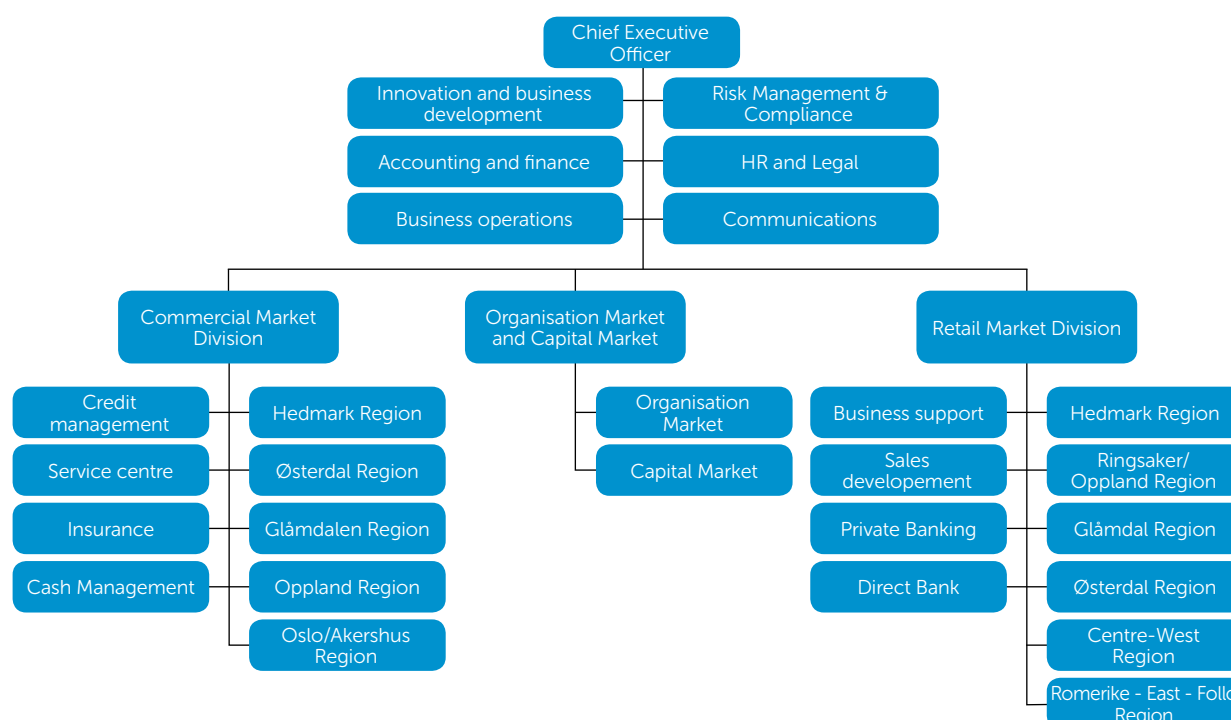
Figure 4.2: SpareBank 1 Alliance



## 4.2 Organisational chart

The parent bank SpareBank 1 Østlandet is organised as shown in the figure below as at 31.12.2017.

Figur 4.3: Organisational chart



## 4.3 Risk and capital management

### 4.3.1 Objective

The group's risk and capital management shall support the group's strategic development and fulfilment of objectives, and contribute to the maintenance of the desired risk profile. Risk and capital management shall also help to ensure financial stability and satisfactory asset management. This shall be achieved by:

- A clear corporate culture characterised by a high awareness of risk and capital management.
- A good understanding of the risks driving earnings.
- Striving towards a good application of capital within the adopted business strategy.
- Avoiding unexpected negative events seriously harming the Group's financial status

The Group aims for a moderate to low risk profile. The framework for determining the group's risk profile shall provide a holistic and balanced overview of the risk that the business is exposed to and consists of statements that define the group's risk appetite within significant risk areas. Risk appetite is defined as the desired risk exposure/profile from an earnings and loss perspective.

Based on the statements defining the group's risk appetite, the risk profile is quantified through the determination of measurement indicators for the group's risk appetite and risk capacity. Risk capacity is defined as maximum risk exposure before the group breaches regulatory requirements or is forced to take undesired measures, including undesired changes in strategy or business model.

The targeted risk profile shall be reflected in other parts of the risk management framework, including, for example, the

determination of authorisations and frameworks for operational management.

### 4.3.2 Management and supervision structure

Management and supervision comprise all the processes and control measures that have been introduced and implemented by the Bank's management to ensure efficient operations and the implementation of the Group's strategies.

In the process for risk management, corporate culture is the foundation that the other elements build on. Corporate culture encompasses management philosophy, management style, governing principles and the people in the organisation with their individual characteristics such as integrity, core values and ethical attitudes. A good corporate culture is important because without it, it can be difficult to compensate with other control and management measures.

We have therefore established clearly defined core values and code of conduct, which have been clearly communicated and presented throughout the organisation. These guidelines provide information about the expectations of individual employees in terms of integrity, ethical behavior and competence.

The recruitment of new employees considers as a prerequisite professional and personal suitability in relation to the position.

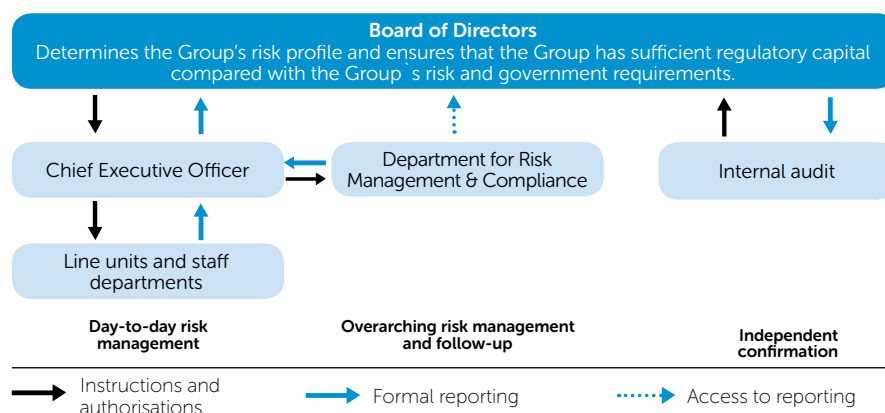
All the group's business areas and staff functions are represented in group management. For all key areas of the group there shall be clearly established responsibilities.

### 4.3.3 Key roles and areas of responsibility

The Group attaches importance to having a supervisory and management structure that promotes targeted and independent

management and control. Responsibility for risk management has therefore been divided between different roles in accordance with the figure below.

Figure 4.4: Responsibilities and roles in the risk management process



**The Board** is responsible for ensuring that the Group has adequate primary capital based on the strategic objectives, adopted risk profile and regulatory requirements. The Board stipulates the overall objectives with respect to the risk profile and return. The Board also stipulates the overall limits, authorisations and guidelines for risk and capital management in the Group, as well as the ethical guidelines that shall contribute to a high ethical standard. Furthermore, the Board shall ensure that management provides an appropriate and effective risk management process in accordance with the laws, regulations, statutes and principles outlined in this document, as well as determining contingency and continuity plans to ensure that operations can continue and losses are limited in the event of significant unforeseen incidents.

The Board's tasks are set out in an annual plan, which is revised annually. This ensures that the Board of Directors has adequate time to focus on its key duties.

**The Board** has its own committees for risk management, audits and remuneration. The Risk Committee is a preparatory body for the Board in cases involving the Group's risk management and internal control, while the Audit Committee prepares cases that involve financial information and internal control associated with this. The committees consist of the same three members of the Board, although the committees do not have the same chair. The Remuneration Committee shall correspondingly assist the Board with matters concerning the CEO's terms of employment, as well as matters concerning the general principles and strategy for the remuneration of the senior executive personnel in the Group. The Remuneration Committee consists of three board members.

**The CEO** is responsible for overall risk management. This means that the CEO is responsible for the implementation of efficient risk management systems in the Group and the monitoring of the risk exposure.

The CEO is also responsible for delegating authority and reporting to the Board of Directors.

**The business divisions and staff units** are responsible for risk management within their areas of responsibility. This means that the managers should make sure that proper risk management is established and executed, and that it is performed in accordance with the management documents, authorisations, routines and instructions.

**The Risk Management and Compliance Department** is organised independently of the line and staff units and reports directly to the CEO. The department is also able to report directly to the board. The department is responsible for independent monitoring and reporting of the risk situation and for ensuring that the Group complies with the applicable laws and regulations. The department is divided into sections for risk management and compliance. The risk management department is responsible for further development of the risk management framework, including risk models and risk management systems, while the compliance department is responsible for further development of the compliance framework.

In the subsidiaries, a person shall be appointed to cooperate with the risk management and compliance department, and to handle responsibility in the respective subsidiary.

**The internal audit** is the Board's instrument for ensuring that risk management is targeted, effective, and functioning as assumed.

### 4.3.4 Decision-making structures

The following committees have been established in the risk management area to assist the CEO with decision-making data and follow-up:

- Risk and balance sheet management committee
- Credit committee for the corporate market division.



The risk and balance sheet management is an advisory body to the CEO and is broadly formulated with key managers from the risk management and compliance department, the finance department and the business areas. Internal audit can act as observer when processing the annual report for validation. The risk and balance sheet management committee is chaired by the CEO.

The risk and balance sheet management committee shall assess the consequence of various scenarios' effects on profitability, solvency, financing and liquidity, as the basis for strategic discussions on the growth targets for deposits and loans, dividend strategies etc. The risk and balance management committee shall also:

- Follow up the Group's risk profile and capital adequacy situation and propose corrective action if necessary.
- Manage and recommend changes to risk based governing documents.
- Manage and recommend changes in the ownership and capital management framework, capital targets and capital plan.
- Manage circumstances of significance to the group's balance sheet management.
- Validate the risk management systems.
- Consider and recommend new risk models.

The credit committee for the corporate market division is an advisory body to the CEO for credit decisions under managing Director's authority and shall:

- Consider loan applications in accordance with current governing documents, appropriation rules and credit management routines.

- Identify risk in each application, including an independent assessment of credit risk.

The credit committee is made up of the CEO, the group director for the corporate market, the credit manager for the corporate market and assistant bank manager credit management for the corporate market. Regional bank manager and case officers participate in the handling of their cases.

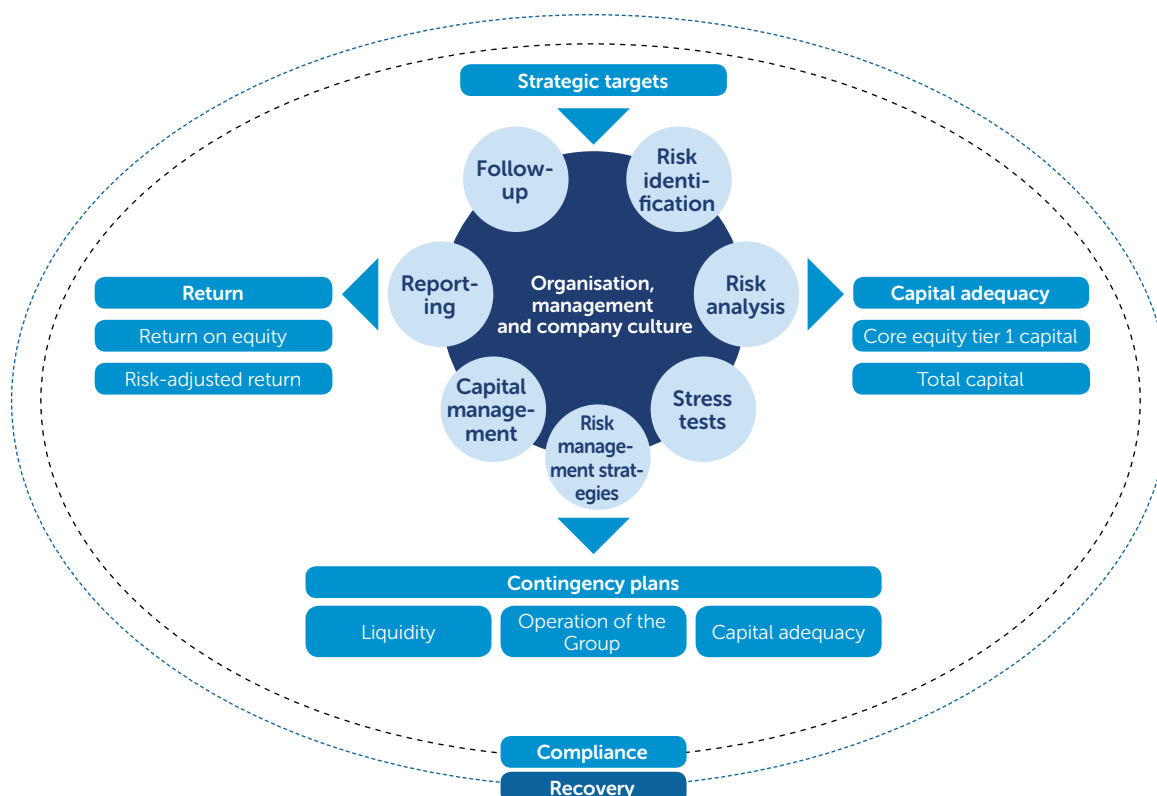
#### 4.3.5 Framework for risk and capital management

In order to ensure an effective and appropriate process for risk and capital management, the framework is based on the following elements, which reflect the way in which Group is managed by its Board of Directors and the bank's senior management:

- Strategic targets.
- Organisation and corporate culture.
- Risk review.
- Risk analysis.
- Stress tests.
- Risk strategies.
- Capital management, including targets for returns and solvency.
- Reporting.
- Follow-up.
- Contingency plans.
- Compliance.
- Recovery plans.

The correlation between the individual elements can be summed up as in the figure below.

Figure 4.5: Framework for risk and capital management



#### 4.3.5.1 Strategic objective and desired risk profile

Risk and capital management shall be based on the group's strategic objectives expressed in the group strategy and the desired risk profile, as this profile is determined in the Group's overall risk strategy and policy for risk and capital management.

#### 4.3.5.2 Risk identification

In order to realise the strategic objective and desired risk profile, the Board and management shall be familiar with the risk pattern. The risk identification process shall be forward looking and an integral part of the strategy process. The process shall cover all the significant risks the Group faces and shall be conducted at least once per year or more often if special conditions requires that

#### 4.3.5.3 Risk analysis

The risk analysis shall form the basis for how the group understands and controls the risks. Among other things, this means that:

- Significant risks shall to the maximum extent possible be quantified, where methods and models of quantification are based on proven methods for measuring risk.
- A review and documentation shall be undertaken of the control measures established and whether these measures are properly safeguarded.
- For significant risks a risk profile shall be defined and quantified to the greatest extent possible.

#### 4.3.5.4 Stress tests

Stress tests are essential tools for showing how negative events affect profit, the balance sheet, capital adequacy and liquidity. Stress tests shall be included as an important element in the Group's projection of financial development, including also projections related to a serious but not unlikely financial setback. Stress tests shall be carried out at least annually and used in the capital assessment process and maintenance of the Group's recovery plan.

#### 4.3.5.5 Risk strategies

There shall be a superordinate risk strategy and risk strategies associated with all major risk areas, as well as a corresponding superordinate policy for risk and capital management and policies relating to all significant areas of risk.

The main risk strategy is the Board's tool for defining and managing the Group's risk profile. With a fixed risk profile, risk indicators are defined for the individual risks, with limits for the Group's risk appetite and capability. The superordinate risk strategy shall be based on the objectives of the business strategy, but also provide guidance for this. The document is issued by the Board and revised as required, and at least once a year.

The policy for risk and capital management is the Group's internal framework for management and control. This policy provides guidelines for the Group's overall attitudes and principles for risk management and should ensure that the Group establishes and maintains an effective and

appropriate risk management process. In addition, the document should ensure that the framework satisfies the external requirements and expectations for good risk management. The document is issued by the Board and revised as required, and at least once a year.

The underlying risk strategies and policies are the Board's instruments for determining the desired risk profile in different areas of risk and ensuring that the risks are managed. The various risk strategies shall reflect overall targets and strategies given by the main risk strategy and the group's business strategy, and shall be compatible with the group's risk capacity and appetite.

The underlying risk strategies and policies are determined by the Board and are revised as needed, as a minimum annually.

#### 4.3.5.6 Capital management

The Group's capital management shall contribute to:

- Effective capital raising and use of capital in relation to strategic targets and adopted business strategy.
- A satisfactory return on equity.
- A satisfactory core equity tier 1 ratio in relation to the desired risk profile as required by the authorities.
- Competitive terms and good long-term access to funding from capital markets.
- Utilisation of growth opportunities in defined market areas at any given time.

On the basis of the strategic objective and the results of the capital assessment process, a capital plan shall be prepared annually. As a minimum, two different projections of the Group's financial development for the next three years shall be used. These projections shall take into account expected developments in the period, as well as a situation with a serious but not unlikely economic downturn.

On the basis of the projections, the Board and management shall make an overall assessment of whether the capital level is sufficient and adapted to the Group's risk profile and strategic objective.

The Group's objectives for core equity tier 1 ratio and total capital adequacy ratio shall ensure sufficient capital to comply with the capital requirements imposed by the authorities and safeguard the group's creditors.

#### 4.3.5.7 Reporting

The purpose of risk reporting is to ensure that all levels of the organisation have access to adequate and reliable risk reporting. This shall ensure an overview of current risk exposure and any weaknesses in the risk management process. The reporting shall form the basis for the further follow up and monitoring of risk exposure and the risk management process within the Group.

#### 4.3.5.8 Follow up and monitoring

The ongoing risk exposure shall be monitored. All managers are responsible for the day-to-day risk management in their own areas of responsibility and thus

the use of capital in their own areas of responsibility and they shall ensure that the risk exposure is within the defined limits.

The overall risk exposure and risk development are followed up through periodic risk reports to the Board and management. Overall risk monitoring and reporting are undertaken by the risk management department. The purpose of the follow-up is to assess the effectiveness of the risk management process over time and ensure that necessary actions or changes are carried out.

The Group has established indicators with limits for follow-up and monitoring. In this way, timely assessments of the need for escalation are ensured from negative development in one or more indicators.

#### 4.3.5.9 Compliance

There shall be processes that ensure compliance with the applicable laws and regulations, so that the Group is not subject to sanctions or other financial loss resulting from breach of these. This shall be achieved by:

- Clearly defined core values and code of conduct, which have been clearly communicated and understood throughout the organisation.
- Guidelines and routines to detect, communicate and implement amendments to laws and regulations.
- Guidelines and routines to follow up and report compliance with laws and regulations

#### 4.3.5.10 Contingency plans

The Group's core business entails the acceptance of risk. Over time this may inflict large unexpected losses on the bank, in spite of good risk management systems and processes. Such a situation may entail serious pressure on capital adequacy, funding and operations. The Group must, therefore, have contingency plans for the aforementioned areas.

#### 4.3.5.11 Recovery plan

In addition to ordinary contingency plans, there must be a separate recovery plan that specifies concrete, practical measures for managing financial crisis situations. The recovery plan shall not predict financial crises; rather it shall identify and assess the Group's opportunities to restore financial strength and viability in situations where the Group is under hard financial pressure.

## 4.4 Remuneration schemes

SpareBank 1 Østlandet's remuneration for executive personnel complies with the rules and guidelines laid down in the "Regulation on Remuneration Arrangements in Financial Institutions, Investment Firms and Management Companies".

Executive personnel and others covered by the regulation's definition receive remuneration in the form of a fixed salary. They are members of the Bank's ordinary defined contribution pension scheme. Those who were members of the defined benefit pension scheme at the time the members were moved to a defined contribution pension scheme receive compensation for the transition from a defined benefit pension to a defined contribution pension in line with the same rules that apply to other employees.

No schemes involving variable pay elements or other special administrative schemes have been established for this group of employees. However, executive personnel can receive a one-time supplement limited to one month's pay, based on the same criteria and within the same limits as other employees.

In 2017, a one-time supplement of between NOK 20,000 to NOK 144,000 was paid to twelve employees categorised as "executive personnel", as defined in relation to the remuneration regulations, due to the especially large workload over a long time in connection with the merger process. The average amount of the one-time supplement for employees in this group was approximately NOK 63,000 and in all cases within the limit of one month's pay.

The company has no form of bonus scheme or any obligations concerning bonuses for the chief executive or chairman of the board.

There are no incentive schemes or obligations concerning share value based remuneration for the benefit of employees or elected officers.

In connection with the IPO for the Bank's equity certificates on the Oslo Stock Exchange, executive personnel took part in the offer made to all employees who were given a chance to purchase equity certificates for a nominal value of up to NOK 125,000 with a 20 per cent discount and lock-in period of 2 years.

The pay conditions are assessed via annual processes at the end of the year and any changes normally come into effect on 1 January the following year. The assessments are based on the Bank's remuneration system and described processes.

The chief executive's assessments and proposals on limits and conditions for changes in the compensation for the members of the Bank's executive management team are presented to the Remuneration Committee to get any input and comments they may have before the chief executive makes a decision.

The Remuneration Committee is similarly informed on the assessment concerning the remunerations of the managing directors of the Bank's subsidiaries and thereby has an opportunity to present any comments before decisions are made by the subsidiaries' boards. The chief

executive's terms are set by the Board based on the recommendations of the Remuneration Committee. The chief executive has an agreement on possible early retirement from the age of 62. If the Board decides to exercise the option of early retirement, the company will pay an annual early retirement pension that amounts to 70 per cent of the applicable fixed salary on the retirement date. Should the chief executive wish to retire between the ages of 62 to 67, the company will pay an annual early retirement pension that amounts to 60 per cent of the applicable fixed salary on the retirement date.

## 4.5 Key risk groups

The Group is exposed to a variety of risks where the main risk groups are:

- **Credit risk** is the risk of losses resulting from a customer's or other counterparty's inability or unwillingness to fulfil its obligations.
- **Concentration risk** is the risk of loss resulting from accumulation of exposures to customer, industry and/or geographical areas.
- **Market risk** is the risk of losses due to changes in observable market prices, such as interest rates, share prices or currency rates.
- **Operational risk** is the risk of losses due to weak or inadequate internal processes or systems, human error or external incidents.
- **Liquidity risk** is the risk of being unable to fulfil obligations or finance assets, including desired growth, without significant extra costs.
- **Ownership risk** is risk that the Group will suffer negative results from stakes in strategically owned companies and/or the need to inject fresh capital into these companies.
- **Business risk** is the risk associated with unexpected income and cost fluctuations due to factors other than credit risk, market risk, and operational risk.
- **Reputation risk** is the risk of a failure in earnings and access to capital due to failing confidence in the market, i.e. customers, counterparties, stock market and authorities.
- **Strategic risk** is the risk of losses resulting from unsuccessful strategic investments.
- **Compliance risk** is the risk that the Group will incur public sanctions/penalties, financial losses or a damaged reputation as a result of a failure to comply with laws, regulations or guidelines from the authorities.
- **Risk of unjustifiable debt build-up** is the risk that the Group's financial strength will be disproportionately reduced due to a high proportion of external funding and excessive debt build-up.

## 5 Credit risk

Credit risk is the risk of losses resulting from a customer's or other counterparty's inability or unwillingness to fulfil its obligations. The bank is subject to credit risks mainly through loans to personal and corporate market customers, but also through other assets that the bank holds capital for. In the latter group are guarantees, unused drawing rights, interest-bearing securities, equity positions and interbank investments. Credit risk also includes concentrations arising from large exposures to individual customers, single industries, geographical areas and growth.

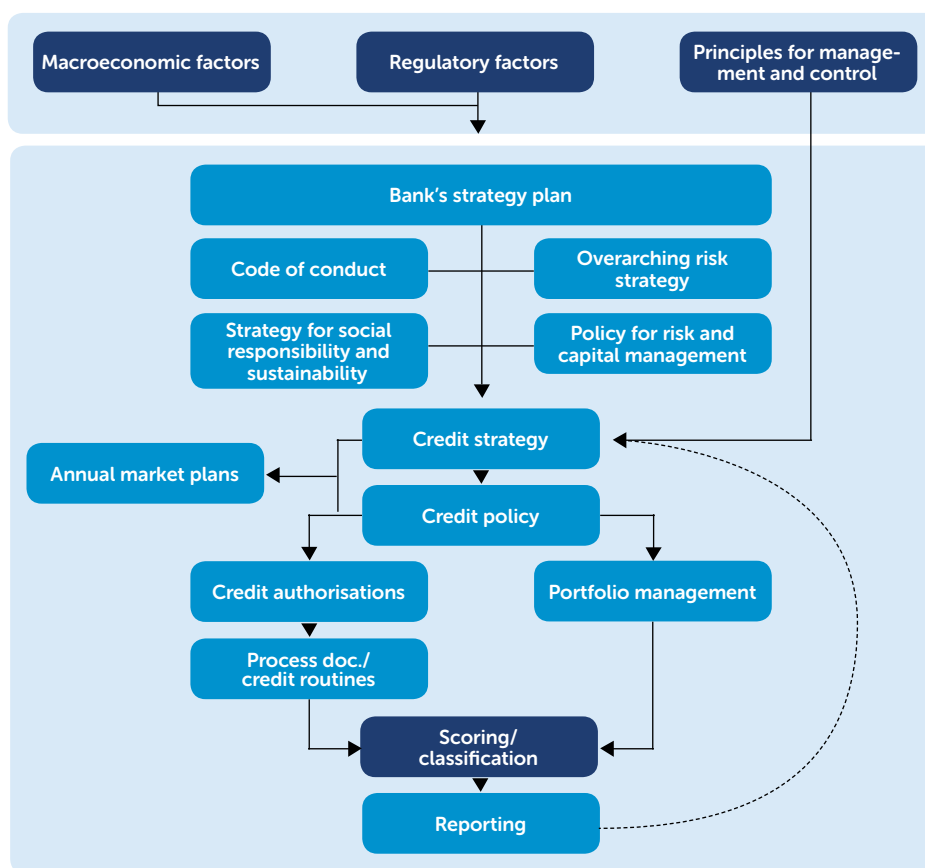
### 5.1 Management and control

Credit risk in the Group shall be managed in accordance with the requirements and recommendations in the:

- Financial Enterprises Act.
- CRR-/CRD IV Regulation.
- Capital Requirements Directive.
- The Financial Supervisory Authority of Norway's methodology for risk-based supervision.

The group shall have a quality in credit handling and the loan portfolio that contributes to a low credit loss over time. The following figure shows strategies and procedures that are the basis of the Group's management and control of credit risks in loan portfolios.

Figure 5.1: Framework for managing credit risk



### 5.1.1 The Group's strategy

The strategy describes the market-related goals for the credit business and defines the bank's market area. The strategy document represents an important foundation for other management and plan documents in the area.

### 5.1.2 Code of conduct

The code of conduct functions as a guide for the Group's activities by defining the ethical requirements that are set internally and how we shall relate to other stakeholders.

### 5.1.3 Strategy for social responsibility and sustainability

The corporate social responsibility and sustainability strategy describes the Group's opportunities and challenges in relation to corporate social responsibility and sustainability and how this issue is managed.

### 5.1.4 Main risk strategy

The superordinate risk strategy is, as previously described, the Board's tool for defining and managing the Group's risk profile.

### 5.1.5 Policy for risk and capital management

The policy for risk and capital management is, as previously described, the Group's internal framework for management and control.

### 5.1.6 Credit strategy

The credit strategy specifies the overall principles for granting credit and the risk appetite for the portfolio. The desired credit risk profile is defined through establishing risk based limits related to portfolios, subportfolios and individual customers. The credit strategy forms the basis for reporting and monitoring the ongoing risk exposure. The document is issued by the Board and revised as required, and at least once a year.

### 5.1.7 Credit policy

The credit policy describes the distribution of responsibilities and roles and determines more detailed criteria for the credit operations. The policy describes what is acceptable within the given credit assessment areas. The purpose is to ensure that the Bank acts in a uniform manner and in accordance with the external regulatory framework, including laws and regulations, and risk level stipulated internally. The document is issued by the Board and revised as required, and at least once a year. Separate policy documents exist for the retail market and the corporate market respectively.

### 5.1.8 Annual market and activity plans

The annual market and activity plans describe what activities are to be carried out for the individual year. These plans should help ensure that the market, earnings and risk related goals in accordance with the Bank's strategy plan and risk strategies are achieved. Annual market and activity plans are issued administratively.

### 5.1.9 Rules and regulations for granting credit/credit authorities

The Board delegates credit authority to the CEO and determines the Bank's rules and regulations for granting credit.

The credit authorities are personal and should reflect the competence of the individual. Credit authorities are differentiated by volume and risk. The rules and regulations for granting credit are revised as required and at least once a year.

### 5.1.10 Process documentation/credit routines

The documentation regulates various matters related to the ongoing granting of credit and follow-up of commitments, including routines for following up defaulted commitments, assessment of the need for impairment etc. The documentation is prepared by the credit managers in consultation with the business divisions. The documents are revised on an ongoing basis.

### 5.1.11 Risk pricing

The Group strives to achieve the right pricing of credit risk and has established price models and customer profitability models based on the risk classification system.

### 5.1.12 Validation

The purpose of the validation process is to verify the credit risk models and the Group's IRB system to ensure that both the quality of the models and the compliance with and application of the IRB system are satisfactory over time. The process and preparation of the necessary reports are carried out by the Risk Management Department. Validation reports are reviewed by the Risk and Balance Sheet Management Committee before the CEO makes decisions relating to matters addressed in the report. The Board is kept informed about the validation work and the decisions that are made.

### 5.1.13 Stress testing

Regular stress tests of the credit portfolio are performed in which developments in credit portfolios are stressed as a result of large, but not improbable, negative events. The purpose of the result of such analyses is to indicate the extent to which the portfolio or parts of the portfolio can withstand an abnormal and powerful weakening of the assumptions, and thus how this affects the bank's risk pattern and solvency.

The stress tests that are carried out have different starting points and methodical approaches. The various stress tests provide the group with different angles and views on how the Group can take into account losses in the bank's projections, planning and capital requirement.

### 5.1.14 Follow-up of credit risk/risk reporting

Risk exposure within the credit area is followed up using a portfolio management system. Importance is attached to following up the portfolio risk distribution and its development based on movements between the risk classes probability of default, capital requirements, concentration risk and risk-adjusted return.

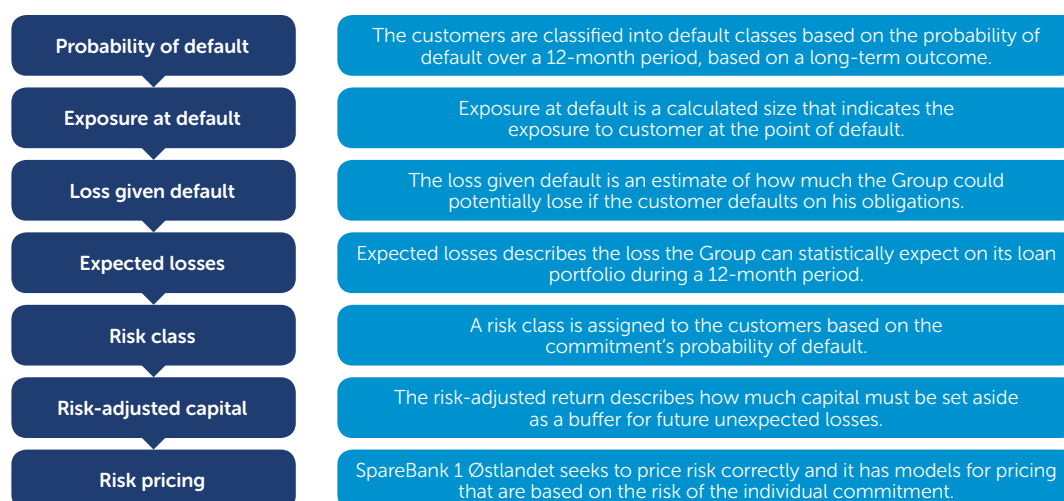
The Risk Management Department follows up the risk in the credit portfolio and reports quarterly to the Board and the Bank's management team. In addition, the divisions prepare a monthly risk report to the bank's management.

## 5.2 Credit risk models and risk classification

SpareBank 1 Østlandet and SpareBank 1 Finans Østlandet use common models for calculating credit risk at the portfolio level and in the granting process together with the other banks and financing companies in the SpareBank 1 Alliance. The models are based on statistical calculations, and are

under continuous validation and development. The parent bank uses the model both in internal reporting and in capital adequacy calculations based on the advanced IRB approach. The models are based primarily on the components in the figure below.

Figure 5.2: Risk classification system



### 5.2.1 The IRB system

SpareBank 1 Østlandet has permission to use the advanced IRB approach for calculating the capital requirements for credit risk for the exposure classes corporates and retail. The former Sparebanken Hedmark and Bank 1 Oslo Akershus received permission to use the foundation IRB approach in February 2012 and May 2008 respectively, and permission to use the advanced IRB approach for enterprises in February 2015.

This means that the risk parameters probability of default and conversion factor used to determine exposure to default and loss given default are calculated using their own models.

Probability of default is hereinafter abbreviated to PD. Conversion factor is hereinafter abbreviated to CF. Exposure at default is hereinafter abbreviated to EAD. Loss given default is hereinafter abbreviated to LGD. Some portfolios are exempt from the IRB approach and use the standardised approach, which means that standardised risk weightings are used. The exceptions apply to states/municipalities and institutions, where permanent exceptions are given, as well as housing cooperatives and associations/clubs, where the Group uses the standardised approach.

The following table describes the Group's methods for estimating the minimum primary capital requirement for the different exposure classes and portfolios.

Table 5.1: Approved methods for calculating the minimum own fund requirement

Company	Portfolio	Regulatory approach
SpareBank 1 Østlandet - parent bank	States/municipalities	Standardised Approach
SpareBank 1 Østlandet - parent bank	Institutions	Standardised Approach
SpareBank 1 Østlandet - parent bank	Cooperatives, clubs and associations	Standardised Approach
SpareBank 1 Østlandet - parent bank	Corporates	IRB Advanced
SpareBank 1 Østlandet - parent bank	Retail	IRB
SpareBank 1 Finans Østlandet AS	Leasing and sale security	Standardised Approach
SpareBank 1 Kredittkort AS	Credit card	Standardised Approach
SpareBank 1 Boligkreditt AS	Retail	IRB
SpareBank 1 Næringskreditt AS	Enterprises	Standardised Approach



### 5.2.2 Models used in regulatory IRB reporting

The table below shows which models the bank uses in regulatory IRB reporting as at 31.12.2017. The models are divided into retail market customers and corporate market

customers, where the customer is categorised according to whether it is registered by corporate registration number or personal ID number.

Table 5.2: Models used in regulatory IRB reporting

Engagement category	Customer segment	PD model	Scorecard	EAD model	LGD model
<b>Retail– security in homes and property (SME and non SME)</b>	All retail market customers	PD model for Retail Market	Scorecard residential property	EAD Retail Market	LGD Retail Market
	All self-employed who are registered in the bank with personal ID number				
<b>Other retail customers (SME and non SME)</b>	All retail market customers		Scorecard other	EAD Retail Market	LGD Retail Market
	All self-employed who are registered in the bank with personal ID number				
<b>Corporates</b>	All enterprises except the following segments	PD model for Corporate Market	Subdivision in industry groups and scorecard	EAD Corporate Market	LGD Corporate Market
	-Institutions and states		Standardised approach		
	- Housing cooperatives				
	- Associations, clubs and organisations				

In addition, there is also a cash flow model for calculating PD for corporate market customers in the rental of commercial property sector. The model is also used to calculate its own value estimates of the objects to be financed. During the year, the Group will apply to the Financial Supervisory Authority of Norway for permission to use this model for regulatory purposes.

- Overdrafts or arrears over 90 days, where arrears/overdrafts have exceeded NOK 1,000.
- Debt settlement, compulsory enforcement, opening of debt negotiations or public scheme of arrangement notification.
- Bankruptcy, opening of bankruptcy or notice of bankruptcy.
- Confirmed loss or individual impairment/loan loss impairment.

#### 5.2.2.1 The PD model

PD is an expression of how probable it is that a customer will default within the next 12 months. The bank's definition of default is based on the Capital Adequacy Regulation section 10-1 where default exists when one or more of the following criteria occur:

The bank uses the PD models when granting credit and in monthly reclassifications of the customers. The PD model is also used in pricing, ongoing reporting and follow-up of commitments. Based on the PD estimate, each customer is assigned a risk class according to the scale in the following table.

Table 5.3: Risk classes

PD	Risk class
0 – 0.10%	A
0.1 – 0.25%	B
0.25 – 0.5%	C
0.5 – 0.75%	D
0.75 – 1.25%	E
1.25 – 2.5%	F
2.5 – 5%	G
5 – 10%	H
10% –	I
Defaulted	J
Impaired	K



The following table shows how the PD model is built up.

Table 5.4: Build-up of the PD model

Commitment category	Explanation variables	Method	History and calibration	Regulatory requirements
Corporates	Accounting Payment history and other behavioural information Industry Age	The bank uses a scorecard model based on regression analysis, where historical observations are used to predict probability of default. Score cards are divided into nine industry variants to take into account that explanation variables have different significance for different industries. The level is also calibrated differently in these variants to take into account different historical default levels.	Data basis for estimation and validation: > 10 years  When calibrating a level, a method is used that is similar to that determined by the authorities for mortgages, but with other parameter values. In this way, the bank takes into account the actual historical default level when predicting future defaults. The bank uses up to 7 years of history when calibrating the level, as well as including the assumed default rate in a severe economic downturn. The model has a ceiling for PD for healthy customers, set at 30%.	No customers can be assigned a PD lower than 0.03%.
Retail	Assessment Information Liquidity and liabilities Payment history and other behavioural information Age	The bank uses a scorecard model based on regression analysis, where historical observations are used to predict probability of default. Score cards have two versions: mortgages and other loans, of which the former portfolio is the dominant.  The explanation variables are weighted differently in the two versions. The level is also calibrated differently in these versions to take into account different historical default levels.	Data basis for estimation and validation: > 10 years  When calibrating a level, a method determined by the authorities is used that takes into account the actual default rate at the bank and an assumed default rate in a severe economic downturn. The model has a ceiling for PD for healthy customers, set at 40%.	No mortgage customers can be assigned a PD lower than 0.2%.

### 5.2.2.2 The EAD model

The EAD model estimates the customer's exposure to default. EAD is the exposure on the balance with the addition of exposure outside the balance multiplied by a CF factor. For credits, the CF factor specifies how much of the available credit frame is assumed to be withdrawn by default. For

guarantees, the CF factor specifies the proportion of the guarantee that is assumed to be paid out on default. The bank uses the EAD model when granting credit and in monthly reclassifications of the customers. The EAD model is also used in pricing, ongoing reporting and follow-up of commitments. The following table shows how the EAD model is built up.

Table 5.5: Build-up of the EAD model

Commitment category	Method and explanation variables	History and calibration	Regulatory requirements
Corporates	Model that assigns conversion factor by account type (guarantee or credit), score type, and probability of default.	Data basis for estimation and validation: > 10 years	The level of the conversion factor should be set so as to provide an estimate of withdrawals in an economic downturn  The guarantee conversion factor has a parameter determined by the authorities of 100% for loan guarantees and 50% for contract and other guarantees.
Retail	Model that assigns conversion factor by account type (guarantee or credit)	Data basis for estimation and validation: > 10 years	The level of the conversion factor should be set so as to provide an estimate of withdrawals in an economic downturn.  The guarantee conversion factor has a parameter determined by the authorities of 100% for loan guarantees and 50% for contract and other guarantees.

### 5.2.2.3 The LGD model

LGD indicates the proportion of the bank's exposure to a customer that is expected to be lost if the customer defaults. The bank uses the LGD model when granting credit and in monthly reclassifications of the customers. The LGD model is also used in pricing, ongoing reporting and follow-up of commitments.

Security is the dominant explanation variable in the LGD model. Therefore, having good estimates of the value of

security is crucial to the quality of the LGD model's estimates. Also, the LGD estimate shall take into account a future powerful recession, which means that the value of the security is adjusted down by a reduction factor.

As well as security, estimates of recovery probability, recovery of unsecured commitments and collection costs are used to estimate LGD.

Table 5.6: Build-up of the LGD model

Commitment category	Explanation variables	Method	History and calibration	Regulatory requirements
Corporates	Collateral Customer type Equity proportion EAD	The bank uses a structural/definition model that estimates LGD based on sub-models.  Security is the dominant explanation variable	Data basis for estimation and validation: > 10 years  LGD is calibrated through parameter values in the model	The bank is required to include a safety margin imposed by the authorities in its LGD estimates.
Retail	Collateral Product	The bank uses a structural/definition model that estimates LGD based on sub-models.  Security is the dominant explanation variable.	Data basis for estimation and validation: > 10 years  LGD is calibrated through parameter values in the model	For mortgages there is a floor of 20% for LGD at portfolio level.

### 5.2.3 Validation

Validation of the bank's IRB models is important to ensure that the models' estimates are in line with the actual risk the bank is exposed to. Validation therefore represents an important quality assurance of the bank's IRB system. The IRB system is tested through both quantitative and qualitative validation in accordance with the Capital Adequacy Regulation sections 16-2 and 16-3.

**Quantitative validation** is a process that ensures that the bank's estimates for PD, CF, EAD, and LGD have adequate quality. The quantitative validation process includes an assessment of:

- The data basis that is included in the validation.
- Stability in the model's estimates over time.
- The model's ability to rank customers.
- The model's ability to estimate correct levels.

**Qualitative validation** is a process that ensures that the models are tailored to the bank's portfolios and that they represent a central ingredient of the bank's risk management and decision-making. The IRB system also includes the models, work and decision-making processes, control mechanisms, IT systems and internal guidelines and routines associated with the classification and quantification of credit risks when using the IRB models.

The following table lists the various assessments in the quantitative validation. The above parameters are included in the calculation of expected losses, hereinafter abbreviated to EL, and the bank validates this estimate by looking at the expected loss against actual losses in the period.

Table 5.7: Assessments in the validation

	Suitability and stability	Ranking ability	Level
PD	The validation examines whether the population that the model is applied to is similar to the model's estimation basis. This is safeguarded through statistical tests and qualitative assessments of the data basis.	Tests the model's ability to distinguish between customers that default and customers that do not default. For this, the bank uses both migration matrices and statistical analyses such as AUC	Verifies that the estimated level is robust, measured against actual observations of the default rate. To define what is sufficiently high, a long-term outcome is calculated, based on up to seven years of default history and an assumed default rate in an economic downturn.
EAD (CF)	An assessment is made of whether the model is adapted to the customer base.	Unlike default (PD), the conversion factor (CF) does not have a binary outcome (default or non-default). Therefore, when evaluating the ranking ability of the EAD model, we see whether the model is able to distinguish between customers with high conversion factor and low conversion factor.	By means of validation we check whether the estimated level is robust, measured against actual observations of default.
LGD	An assessment is made of whether the model is adapted to the customer base.	Assessment of the ranking ability of the LGD model has the same approach as the EAD model. We assess whether the LGD model is able to distinguish between default customers with a high level of loss and those with a low level of loss, measured against actual observations	Estimated values are measured against the bank's historically observed values.  Assessment of whether the LGD model's estimates are sufficiently high must take into account that the estimated LGD should be calibrated against an economic downturn.

### 5.2.3.1 Roles in the validation

It is important that the validation of the credit models is done with a sufficient degree of independence. Independence is achieved through the following central roles:

- The unit responsible for developing the credit model.
- The unit responsible for validating the models and their application.
- Internal auditing.

The SpareBank 1 competence centre for credit models, hereinafter called CFK, is carrying out the development of new, and the further development of existing models on behalf of the banks. Development takes place in consultation with the banks in the alliance. Additionally, the CFK contributes with professional input to the quantitative validation.

SpareBank 1 Østlandet, in the area of risk management, is responsible for the qualitative and quantitative validation of the bank. The bank annually prepares a validation report that includes all models, portfolios, and sub-parameters. Here, each model is considered within the areas of suitability, ranking ability and level. Analysis is done on sub-portfolios, such as industries. The report, which also deals with qualitative validation, is handled by the bank's risk and balance sheet management committee before it is presented to the Group's board of directors.

Also, development in estimates and observations is continuously monitored so as to monitor the models' performance. Analyses are performed to give an early warning if a model tends towards a weaker performance, whether this is

due to the model no longer being suited to the portfolio in question, or the ranking ability diminishing or the estimates varying too much from the actual observations.

Internal audits conducts audits to ensure that the IRB system is used and complies with the applicable regulations and the terms of the IRB approval. The internal auditor shall regularly and at least annually revise the system and its use. The purpose of the audit is to give the board and management an independent and neutral assessment of the validation of the IRB system and whether the system is firmly integrated into the bank and forms a central ingredient of the bank's risk management and decision-making process.

### 5.2.3.2 Estimated and observed PD level

The figures below show the rolling, actually observed average default rate, hereinafter abbreviated to DR, each month against the estimated PD at the start of the validation period of 12 months. Categorisation in the retail and corporate markets is done in this context on the basis of the scoring model and not the regulatory categorisation.

The model estimates are a combination of stable and expected estimates. This is because the model uses explanation variables that quickly capture changes in a customer's financial situation, such as payment notes, and other explanation variables that change periodically, such as accounting or assessment information. This results in the actually observed DR often differing from the estimated PD. In addition, the calibration of the estimates plays a part in that the calibration methodology is an element for adjustment against defaults in a serious recession.

Figure 5.3: Estimated regulatory PD against actually observed DR for retail market customers with a mortgage

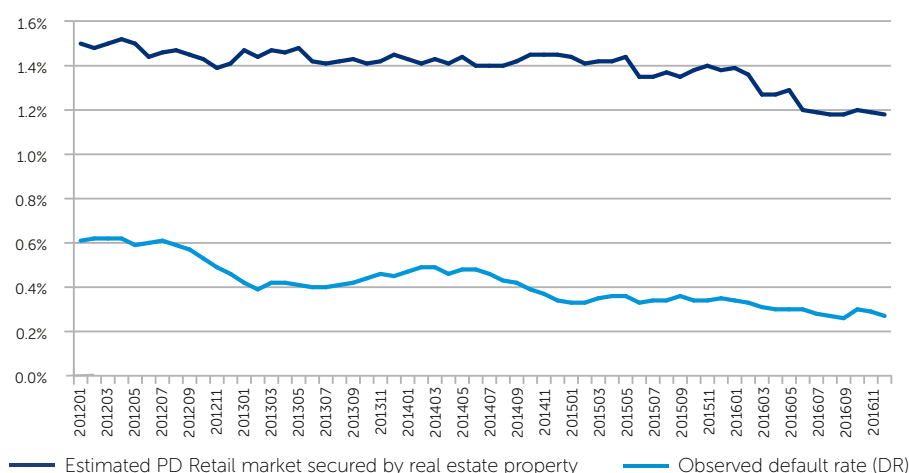


Figure 5.4: Estimated regulatory PD against actually observed DR for retail market customers with a mortgage other

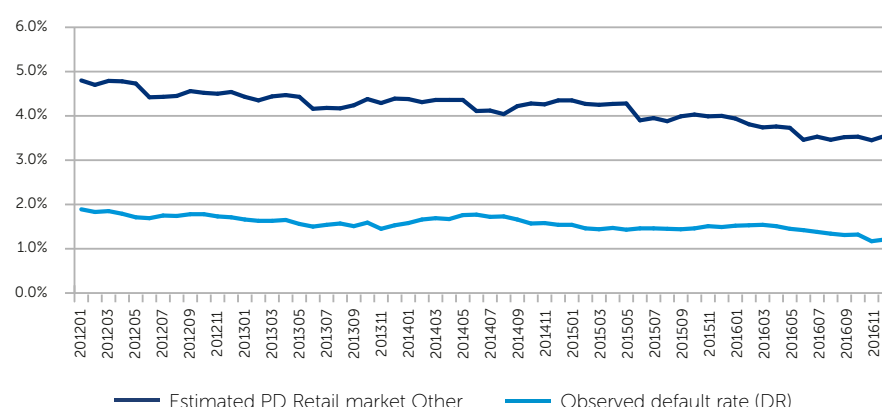
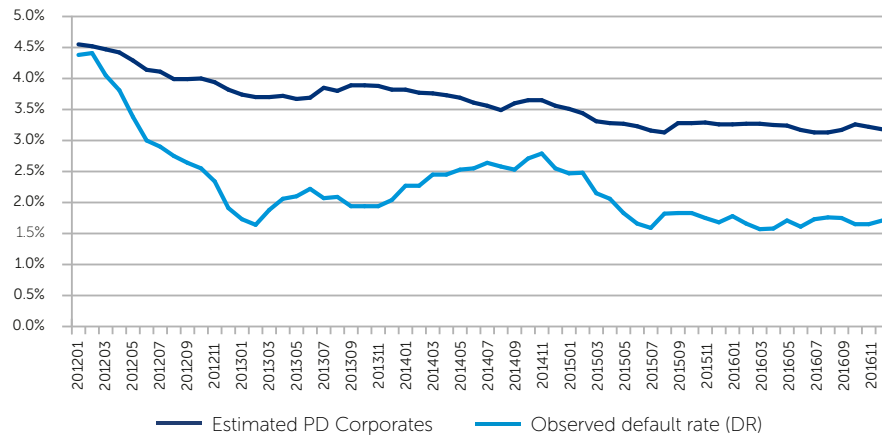


Figure 5.5: Estimated regulatory PD against actually observed DR for corporate market customers



### 5.2.3.3 Estimated and observed EAD level

Unused credit for retail market customers with mortgages has a CF of 1, which means that there is full credit utilisation at default. For corporate market customers, a CF ranging

between 60 and 90 per cent is used, depending on the customer's PD. CF for guaranteed is set by the authorities at 100 per cent for loan guarantees and 50 per cent for contract and other guarantees.

Figure 5.6: Estimated and actually observed conversion factors for retail market customers with credit facilities

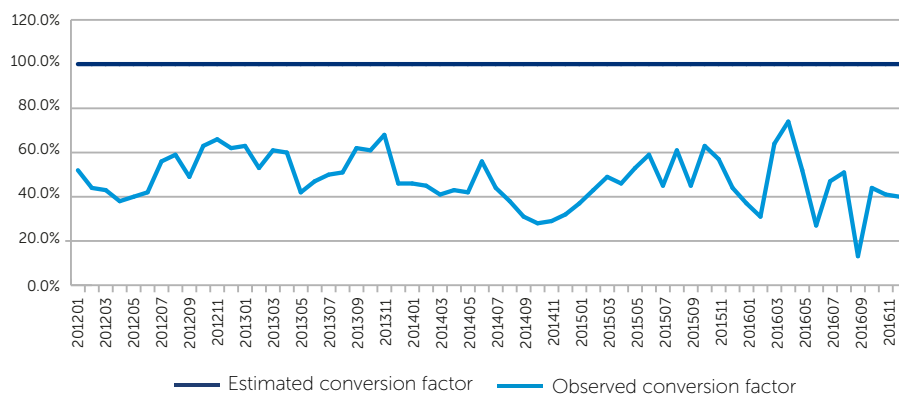
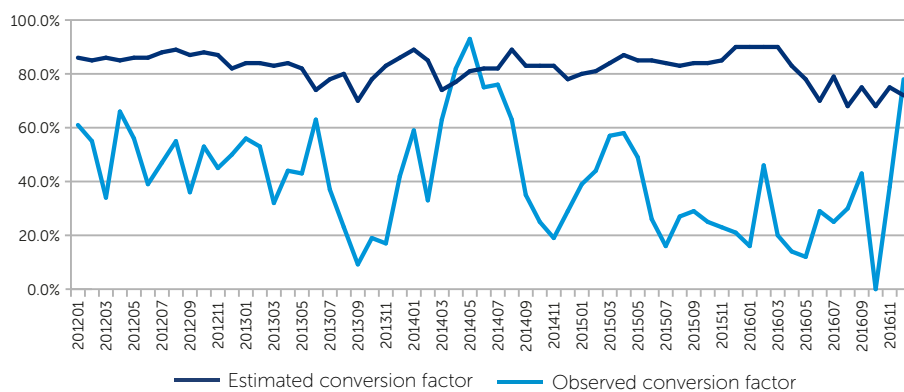


Figure 5.7: Estimated and actually observed conversion factors for corporate market customers with credit facilities



#### 5.2.3.4 Estimated and observed LGD level

The validation is based on the LGD level of defaulted commitments and looks at this level against actually observed losses adjusted for commitments that have become healthy during the period.

The enterprise portfolio utilises the LGD model for corporate market customers. The table below shows that seven classes are used for classifying commitments in accordance with LGD. Class 1 applies to customers with LGD of 10 per cent or lower. These are customers with excellent security coverage after reduction factors. Increasing LGD class corresponds to decreasing security coverage.

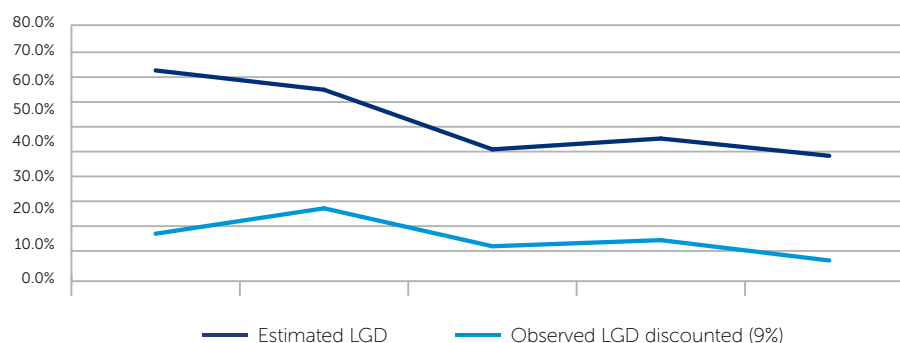
Table 5.8: LGD classes

LGD class	LGD value ranges
1	0-10
2	<10-20
3	<20-30
4	<30-40
5	<40-50
6	<50-60
7	> 60

For the enterprise portfolio, as indicated in the figure below, EAD-weighted estimated and actually observed

LGD levels are noted, where safety margins are included in the LGD estimates.

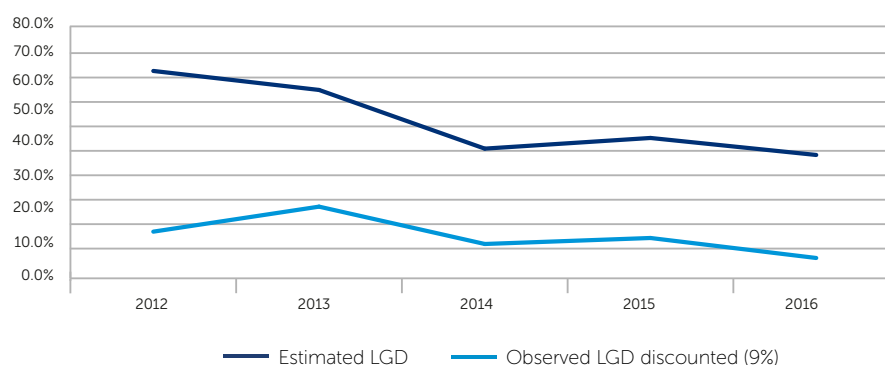
Figure 5.8: Estimated LGD against actually observed LGD for the corporate portfolio



For the retail portfolio, the estimated and actually observed LGD levels are EAD-weighted in the same way. The figure below shows the actually observed and estimated LGD

levels for commitments with mortgages, before adjustment to the Financial Supervisory Authority of Norway's reference model.

Figure 5.9: Estimated LGD against actually observed LGD for the retail portfolio secured by real estate



The figures show that the estimated LGD levels are consistently higher than actually observed LGD throughout the period. The margin between actually observed LGD and estimated LGD is considered robust in terms of taking a strong recession into account.

#### 5.2.3.5 Estimated and observed EL level

The figures below show the EL as a percentage of EAD at the beginning of the year against observed posted losses

as a percentage of EAD at the end of the year. There are large margins between estimated and observed values for EL. This comes from conservative estimates in underlying models. The Group has had low loan losses in recent years – largely due to limited exposure to industries that have been severely hit by the oil downturn, good credit handling and good default follow-up routines for non-performing exposures.

Figure 5.10: Estimated regulatory EL against actually observed losses for the corporate portfolio

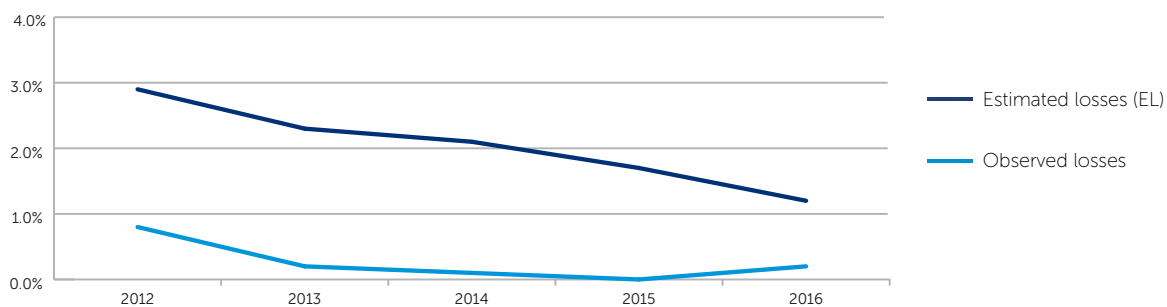
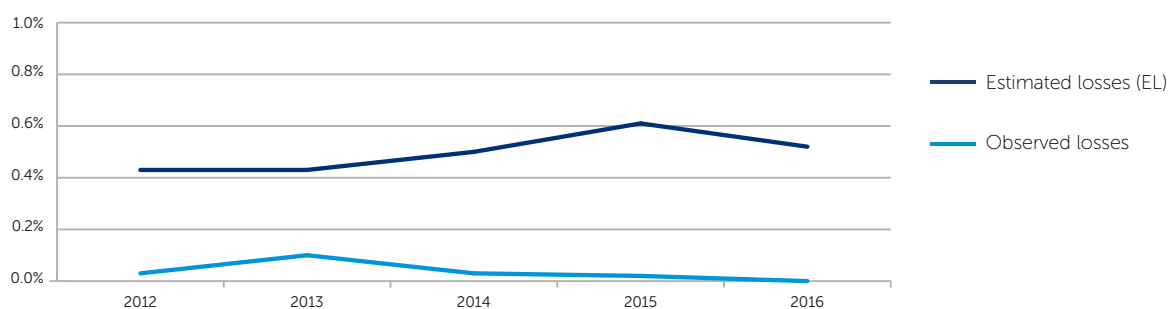


Figure 5.11: Estimated regulatory EL against actually observed losses for the retail portfolio

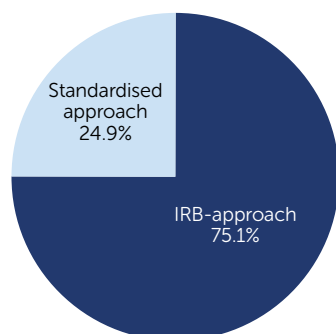


## 5.3 Portfolio information

The figure below shows the distribution of the Group's credit portfolio according to the method used in the capital requirements calculations. The distribution is made

on the basis of net exposure on and outside the balance sheet as at 31.12.2017.

Figure 5.12: The Group's credit portfolio, distributed by the IRB approach and standardised approach



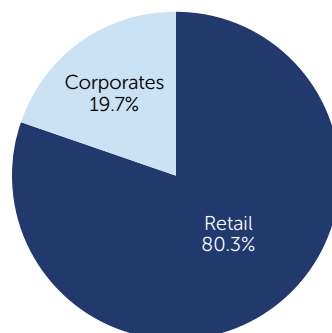
### 5.3.1 The IRB Portfolio

Of the Group's consolidated credit portfolio, the IRB approach is used on 75 percent of the total portfolio with related models previously described.

The Group's IRB portfolio consists of 80 per cent retail customers and 20 per cent corporate customers

measured in net exposure on and outside the balance sheet. SpareBank 1 Boligkreditt AS consolidates proportionally and represents 38.5 per cent of the IRB portfolio retail. The figure below shows the distribution of the IRB portfolio on the retail and enterprises respectively.

Figure 5.13: The Group's IRB portfolio



The following figures show the breakdown within the retail portfolio and the corporate portfolio.

Figure 5.14: Breakdown of retail portfolio

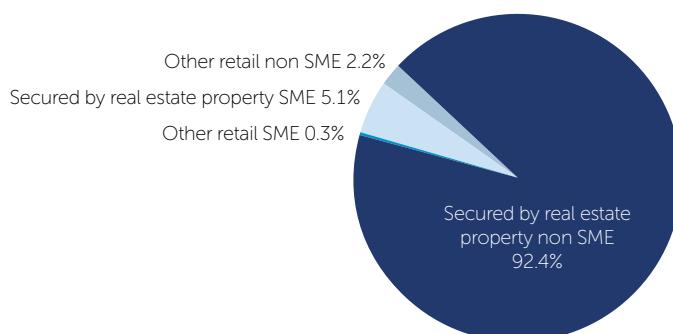
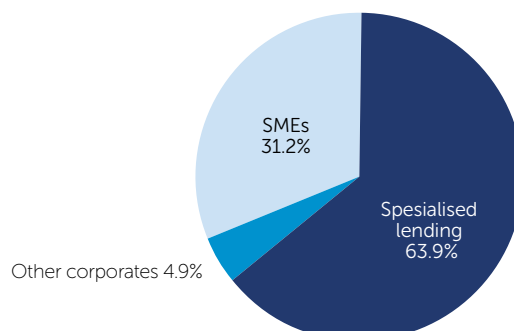


Figure 5.15: Breakdown of corporate portfolio

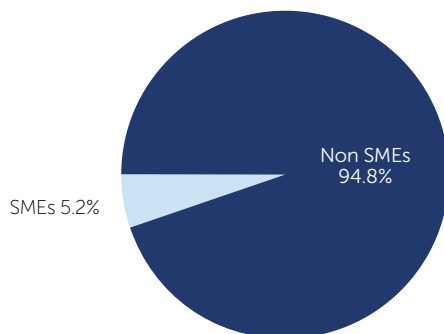


The retail portfolio is mainly exposed to mortgage loans. There is also a proportion categorised as property commitments against small and medium-sized enterprises (SMEs). The corporate portfolio has the largest proportion classified as specialised corporates. This categorisation is mainly made up of customers in commercial property rental, which is the largest single industry the Group is exposed to on the enterprise side; see Figure 5.19.

### 5.3.1.1 Mortgage portfolio

The group's mortgage portfolio accounts for 97.5 per cent of the Group's IRB portfolio for the retail market. The following figure shows the distribution of the mortgage portfolio as SME and non SME.

Figure 5.16: The mortgage portfolio distributed by EAD for the IRB retail

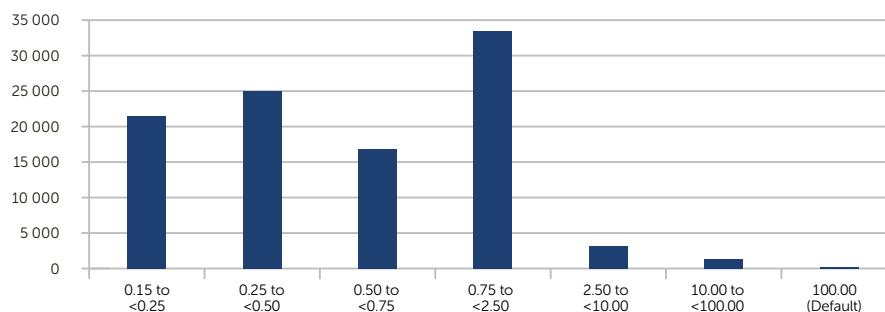


Below, the IRB portfolio in mortgages is distributed in risk groups according to various ranges of PD:

- **Low:** PD 0.00 – 0.75%.
- **Medium:** PD 0.75 – 5%.
- **High:** PD over 5%.
- **Defaulted and impaired:** Defaults and commitments with loss impairments.

The figure below shows that the Group's mortgage portfolio is mainly in the lower risk groups.

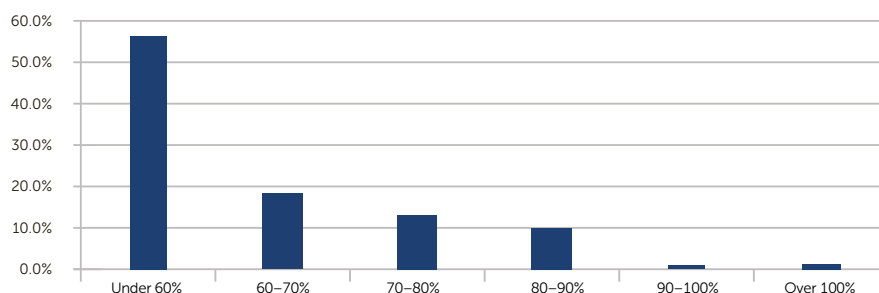
Figure 5.17: The mortgage portfolio distributed by PD range



Low interest rates and a large demand surplus in the market have driven housing prices in the eastern Norway area in recent years. Prices increased particularly sharply in the Oslo area, but the Inland Region has also experienced pressure on house prices in recent years. In 2017, Oslo in particular experienced a correction in prices, while the price level of

the Inland Region has been flat to a greater extent. Loan to value, hereinafter abbreviated to LTV, of the mortgage portfolio shows a weighted average of 56.9 per cent compared to 56.5 per cent in April 2017 when the correction in housing prices started.

Figure 5.18: Loan to value by LTV group





Loan to value is calculated from balance sheet exposure per account, taking into consideration the preceding debt and other loans with security in the same object, and the entire exposure is placed in the LTV group which the exposure falls within. Then each LTV group's proportion of the overall exposure of the portfolio is calculated.

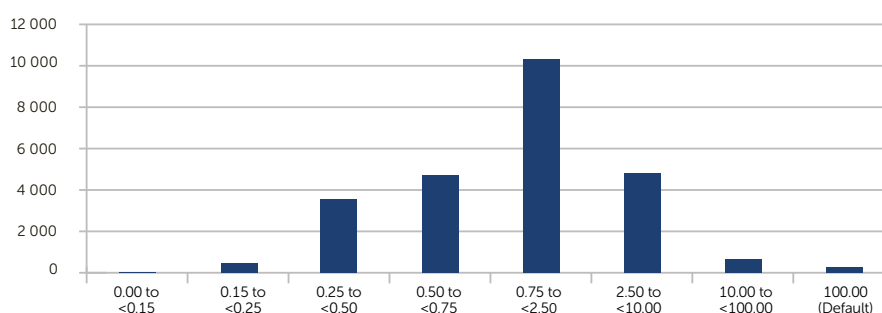
The largest proportion of the group's mortgage portfolio is in the group with under 60 percent loans, see figure 5.17, with a further declining proportion in the higher LTV groups. In 2015, a new mortgage regulation came into effect

governing the requirements for security, debt servicing capacity, debt ratio and size of mortgage payments in Norway. The regulation was further sharpened in 2016 with less room for deviation, especially in the Oslo area. The Group performs regular checks against the regulation's provisions.

### 5.3.1.2 The Corporate portfolio

The figure below shows the enterprise portfolio distributed in the same PD ranges as for mortgages. The portfolio has a low to medium risk profile.

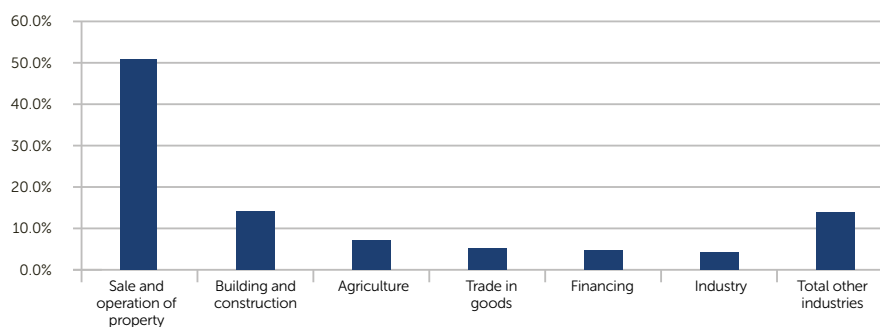
Figure 5.19: The corporate portfolio distributed in regulatory PD range



The largest single industry the enterprise portfolio is exposed to is "sale and operation of property", and exposure to this

industry accounts for about 51 per cent of the enterprise portfolio's overall net exposure.

Figure 5.20: The corporate portfolio distributed by industries



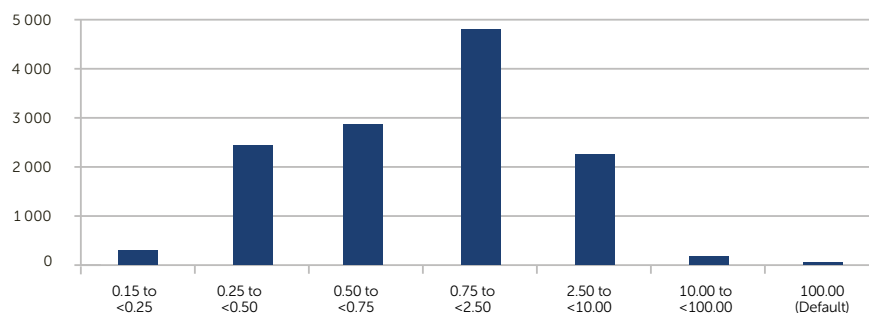
### 5.3.1.3 Commercial property

The Group has a good experience with commercial property in eastern Norway and has had the largest proportion of its exposure in this industry. The Group uses its own cash flow model with associated routines to calculate PD. The model has its own built-in yield matrices, which are viewed together with the properties' net cash flow to put value estimates on the objects to be financed.

The price level of commercial property has shown an increasing trend and low yield levels have also been observed in the Inland Region. This suggests that there has been a demand surplus in the market in the last year and a lower offering in the most central areas is pushing investors farther out of downtown areas. The Group validates its own value estimates against actual transactions, and the Group's estimates are consistently conservative in relation to actual transactions observed in its own market area.

NOK million

Figure 5.21: The commercial property portfolio distributed in regulatory PD range



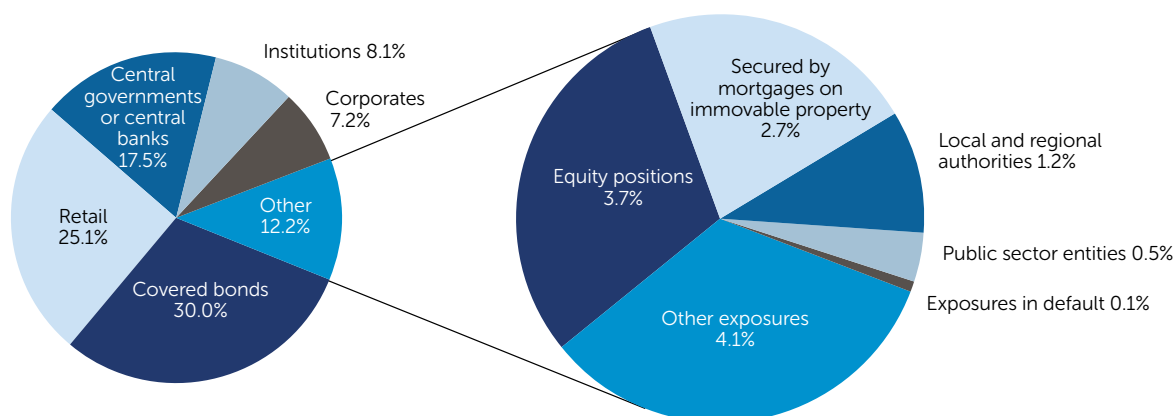
### 5.3.2 The standardised approach portfolio

The credit portfolios that are not covered by the IRB approach are reported according to the standardised approach. Of the Group's consolidated credit portfolio, the standardised portfolio represents 25 per cent. The distribution is made on the basis of net exposure amount on and outside the balance sheet as at 31.12.2017.

The standardised approach portfolio consists of the parent bank's own lending, where the bank has been given permanent or temporary exemption from the use of the IRB approach, while the lending portfolios in the partly-owned companies that use the standardised approach are proportional consolidated.

Interest-bearing securities, equity positions and Interbank investments are also covered by the standardised approach.

Figure 5.22: The group's standardised approach portfolio



### 5.3.3 Collateral

The use of collateral is an important measure to reduce credit risk in the bank's portfolios. When credit is granted, the bank normally requires that the customer furnishes collateral

for the loan commitment. The most common form of collateral is collateral in property, but collateral in inventory and guarantees by individuals, companies, state/municipality, guarantee institutions or banks are also used.

Table 5.9: Most commonly used collateral types

Security type	Retail market	Corporate market
Property	x	x
Undeveloped land	x	x
Securities	x	x
Guarantees	x	x
Plant and machinery		x
Motor vehicles/fixed assets		x
Inventory		x
Accounts receivable		x
Deposits	x	x

#### 5.3.3.1 Valuation of collateral

When valuing collateral, banks in the SpareBank 1 Alliance have a common standard for valuations. The guidelines cover assessment criteria, updating of value and the associated use of reduction factors.

The market value of residential property is determined by the use of purchase price according to contract, estate agent valuation or value estimates from Eiendomsverdi. For commercial property, in most cases the Group uses the present value of an expected net cash flow associated with the property as a basis. The value basis is calculated by taking into account ongoing lease contracts, costs and yield. The latter takes into account location, alternative use potential, duration of lease contract, standard, solvency, regulation and risk-free interest rate.

The estimated market value of residential property is updated at least every other year, while the value of commercial property is updated more frequently. For the enterprise portfolio, the bank performs an assessment of the value base of collateral at least annually, either through an annual commitment review or automatic update of value from the accounts.

The realisation value of pledged collateral is determined from the value basis, which is reduced by a factor that varies with the type of security object. The size of the reduction factors has been determined by the fall in value that could be expected in a powerful economic recession. The reduction factors are validated annually.

### 5.3.4 Impairment and default

#### 5.3.4.1 Individual impairment

Individual impairment for losses on individual exposures is made when there is objective evidence of default that triggers a loss of value for the Group. The Group's definition

of default is therefore central to the process

The Group's definition of default is based on the Capital Adequacy Regulation section 10-1 where default is considered to exist when one or more of the following criteria occur:

- Overdrafts or arrears over 90 days, where arrears/overdrafts have exceeded NOK 1,000.
- Debt settlement, compulsory enforcement, opening of debt negotiations or public scheme of arrangement notification.
- Bankruptcy, opening of bankruptcy or notice of bankruptcy.
- Confirmed loss or individual impairment/loan loss impairment.

Individual write-downs represent the difference between the commitment's book value and the present value of the discounted cash flow based on the effective interest rate at the time of the initial calculation of the individual write-down. A write-down entails that a commitment is given the highest risk class.

Importance is attached to specific project orientation and caution in the estimation of value as basis for the realisation value of collateral. The cash flow is updated at least once a year based on materiality assessments.

Individual impairments reduce the book value of the exposures on the balance sheet, and changes in the assessed value during the period are recognised in the income statement as losses on loans and guarantees.

#### 5.3.4.2 Collective impairment

The approach for Collective impairments up to and including 31.12.2017 encompassed the Group's assessment of the grounds for a loss in value for groups of loans with approximately the same risk characteristics. Loans assessed

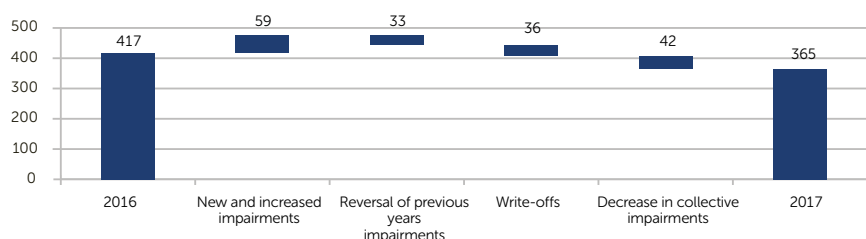
for individual impairment are also subject to collective impairment when the objective evidence for a loss in value has not been proven. All loans are consequently assessed with the exception of those that have been subject to individual impairment. The model for the calculation of collective impairments is based on changes in the expected losses as a result of loan portfolio migration, as well as any additions in the event of major changes in the macro conditions. Collective impairments reduce the book value on the balance sheet, and changes in the assessed value during the period are recognised in the income statement as loan loss provisions.

With effect from 01.01.2018, IFRS 9's rules for loan loss impairments enter into force, and will thus replace the current methodology for collective impairments. This means a significant change compared with the current regulations. The Group has, in cooperation with the SpareBank 1 Alliance, developed a new model for calculating collective impairments based on the guidelines in IFRS 9.

#### 5.3.4.3 Development in defaulted and impaired loans

The figure below shows the developments in the group's accumulated individual and collective impairments.

Figure 5.23: Developments in the group's accumulated individual and collective impairments



The following table shows the Group's loss costs in the last year.

Table 5.10: Recognised changes in value/losses for the period

Net recognised losses in 2017	2017	2016
Change in individual impairments for the period	-8	7
+ Change in collective impairments in the period	-42	22
+ Realised losses on commitments for which earlier impairment provisions has been made	36	40
+ Realised losses on commitments for which no earlier impairment provisions has been made.	13	38
- Recoveries on loans and guarantees previously impaired	19	33
<b>Total losses on loans and guarantees</b>	<b>-20</b>	<b>75</b>

The following figures show the proportional distribution of total impairments on loans and guarantees between retail

and corporate market portfolios as at 31.12.2017.

Figure 5.24: Individual impairments to cover losses on loans and guarantees

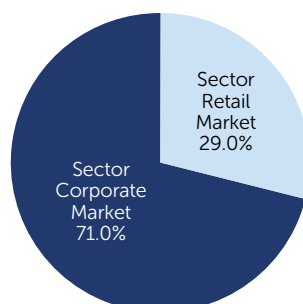
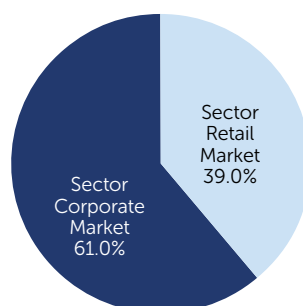


Figure 5.25: Collective impairments to cover losses on loans and guarantees



Individual impairments account for 0.07 per cent of gross lending to the retail market and 0.33 per cent to the corporate market. Collective impairments account for the equivalent of 0.14 per cent for the retail market and 0.43

per cent for the corporate market. The table below shows provisions in relation to net defaulted and doubtful commitments.

Table 5.11: Defaulted and impaired commitments

Defaulted (over 90 days) and doubtful commitments	2017	2016
Defaulted commitments (over 90 days)	286 574	233 220
Individual impairments of defaulted commitments	42 161	54 430
Net defaulted commitments	244 413	178 790
<b>Loan loss provision ratio</b>	<b>15.0%</b>	<b>23.0%</b>
Other doubtful commitments	254 452	271 650
Individual impairments in other doubtful	103 587	100 610
Net other doubtful	150 865	171 040
<b>Loan loss provision ratio</b>	<b>41.0%</b>	<b>37.0%</b>
<b>Total loan loss provision ratio</b>	<b>27.0%</b>	<b>31.0%</b>

The extent of the commitments that have defaulted, but not been impaired, appears in the table above with a total loan loss impairment ratio of 15 percent. The remaining defaulted commitments have been assessed, but as at 31.12.2017 there is no objective evidence that they will lead to a loss in value for the group.

Commitments may also be considered as doubtful without the commitment being in default in accordance with the Group's definition of default. Other doubtful commitments are marked with a loss event in which objective conditions indicate a probability of loss of value. For these commitments, the loan loss impairment ratio is 41 percent.

## 6 Counterparty risk

### 6.1 Management and control

The group enters into derivative trades on the basis of customer demand and to hedge positions arising from such activity. Derivatives are also used to hedge currency and interest rate risks arising in connection with borrowing and lending.

Derivatives are traded with several different counterparties, which also do other types of business. Credit risks arising in connection with trading in derivatives is included in the measurement of credit risk in a capital adequacy context. In order to minimise the counterparty risk against single counterparties, there are netting agreements and bilateral collateral agreements.

The bank has signed ISDA agreements with the vast majority of bank counterparties. ISDA is an abbreviation of the International Swaps and Derivatives Association, which is an association of international financial Institutions, and an ISDA

agreement enables offsetting. This means that all counterparties' contracts are seen in context, and contracts with negative market value, as well as any security received, will reduce the group's actual risk and thus capital requirements. However, in order to be able to see collateral received in context, there must be a CSA agreement. CSA is an abbreviation of Credit Support Annex.

### 6.2 Portfolio information

Table 6.1 below provides an overview of the bank's derivative agreements by type of derivative, type of hedging, the contracts' nominal value, credit equivalent taking into account potential future exposure, risk-weighted amounts basis and requirements for core equity tier 1 capital both before and after offsetting as at 31.12.2017. The group has no trading portfolio.

Table 6.1: Derivative agreements

Type of derivative	Nominal value	Credit equivalent (EAD)	Risk Weighted Amount	Core Equity Tier 1 capital requirements
Currency Instruments (financial hedging)	2 461	41	24	3
Interest rate instruments (financial hedging)	14 901	411	212	25
Interest rate instruments (fair value hedging)	8 074	297	59	7
Credit derivatives	-	-	-	-
<b>Gross value before set-off</b>	<b>25 435</b>	<b>749</b>	<b>295</b>	<b>35</b>
Agreements on set-offs	21 494	522	160	19
<b>Net value after set-offs</b>	<b>3 941</b>	<b>227</b>	<b>135</b>	<b>16</b>

\* Requirement for core equity tier 1 capital according to pillar I (12.0%) is calculated in full by the standardised approach.

The banking group has NOK 16.2 million in core equity tier 1 capital for the bank's counterparty risk as at 31.12.2017. In addition, an additional NOK 8.6 million in core equity tier 1 capital is held for the Group's CVA risk. CVA is an abbreviation of Credit Value Adjustment and is the risk of weakened creditworthiness among counterparties. Established offsetting agreements, i.e. ISDA and CSA agreements, combined with close monitoring of security received and given, significantly reduces the CVA risk.

The derivatives are recognised at fair value through profit and loss. Contracts with unrealised gains are recognised as

assets, while contracts with unrealised losses are recognised as debts for all derivatives. Hedges relating to the bank's borrowing activities are generally defined as "fair value hedging" according to IFRS standard IAS 39. Other hedges are defined as financial hedging and are used, in part, for securing interest rate swaps with small amounts which are not naturally hedged on a one-to-one ratio. These derivatives are hedged in bulk, which means securing multiple hedge objects with one hedge instrument and this will therefore not qualify for documented hedge accounting. The group does not use cash flow hedging.

## 7 Market risk

Market risk is the risk of loss due to changes in observable market variables such as interest rates, foreign exchange rates and shares/equity certificates. The risk associated with falls in value in the real estate market is also included in market risk. So is the risk of changes in the market value of bonds, certificates and funds due to general changes in credit spreads.

The group has no trading portfolio and is thus does not calculate capital requirement for market risk under Pillar 1. Under Pillar 2, the group calculates capital requirements for market risk for interest rate risk, equity risk, currency risk, property risk and spread risk.

Shares, units and other equity interests are classified in compliance with IAS 39 as either financial assets held for trading or financial assets available for sale. Equity interests classified as available for sale are assessed at fair value on the basis of listed prices or using different valuation approaches. Unrealised gains and losses on equity interests available for sale are included in other comprehensive income in compliance with IAS 1 as at 31.12.2017. With effect from 2018, gains and losses on the income statement are recognised according to IFRS 9. Realised gains and losses, dividends, and impairments are recognised in the income statement as income from other financial investments.

Purchased certificates and bonds are measured at fair value through profit or loss pursuant to IAS 39. Changes in value after the opening balance are recognised as income from other financial investments.

Also see the notes in the Group's annual financial statements for 2017 for a more detailed description of how financial instruments are accounted for.

### 7.1 Management and control

The management of the Group's market risk is based on risk-based governing documents for the market risk area. The governing documents are adopted by the Board and apply for the strategy period, although they are revised as required and at least once a year. The Group's governance and control of the market risk is considered to be satisfactory to meet the group's risk profile and strategy.

To ensure satisfactory division of work between the departments and the people who take positions on the group's behalf and the departments and persons responsible for settlement, control and reporting, the Group has defined different roles and responsibilities.

The strategy and policy for market risk, both approved by the Board, provide the CEO with guidelines, frameworks and authorisation for the management of market risk. The CEO further delegates this according to area of responsibility.

The finance department is responsible for ongoing control of frameworks. The department for risk management is

responsible for monthly follow-up and reporting of positions in relation to financial strategic frameworks. In the case of a framework breach, the risk management department will immediately report upwards in the organisation. The risk management department submits independent reports to the management group every month and to the Board every quarter.

#### 7.1.1 Interest rate risk

The purpose of the Group's management of interest rate risk is to ensure that the Group has a known interest rate risk exposure and that this concurs with the Group's risk profile and current limits for the area. Management of the interest rate risk should take all the elements of the interest rate risk into account.

The Group measures interest rate risk as the total net income effect on the group's balance sheet and off balance sheet items on shifts in the interest rate. The calculations take into account administrative interest rate risk. That is to say, the effect of the time it takes in practice from when an interest rate change occurs in the market until the Group has adjusted the terms for deposits and loans with adjustable interest rates.

Frameworks have been set for the amount of effect on profit allowed for a 2 percentage point parallel shift and a 2 percentage point distortion of the interest rate curve. Interest rate curve risk is the risk that the interest rate curve shifts differently within the different maturity buckets when the interest rates change. The interest rate risk is also limited through frameworks for the maximum weighted time to maturity and duration in the securities portfolio.

To minimise the group's interest rate risk, interest rate swap agreements are used. Hedging transactions are conducted with reputable Norwegian and foreign banks in order to reduce own risk. Derivative business is linked to ordinary banking and is carried out to reduce risks related to the bank's borrowing in financial markets, and to reveal and reduce risks related to customer activities.

#### 7.1.2 Currency risk

Currency risk arises when differences exist between the Group's assets and liabilities in the individual currency. The currency risk is measured based on the combined net currency position and the net position in the various currencies.

The aim of the group's currency activities is to safeguard customers' need for foreign exchange trading, foreign currency funding and international money-transfer services, and to secure the currency positions that occur within the financing/liquidity and management of securities.

Activities related to currency turnover shall at all times occur within the adopted guidelines, frameworks and authorisations. The Group's frameworks define quantitative targets for maximum currency exposure, measured in NOK. There are frameworks for net positions in each currency, as well as total absolute sum of net positions per currency. The currency risk is quantified and monitored continuously.

### 7.1.3 Property risk

Property risks are market risks associated with exposure in property. This includes ownership positions and shares in commercial property, property companies, property funds as well as direct ownership of properties, including our own bank buildings and property for our own or employee use.

The Group's investments consist mainly of its own bank buildings. The bank also owns a total of eight holiday properties. Beyond this, the bank has strategic interests in Torggata 22 AS og Oslo Kongressenter Folkets Hus BA, but these are recognised in the accounts as shares. In the Pillar 2 assessment, however, this is included as property risk and calculations show that overall there is major excess value in the bank's properties compared to the book values.

### 7.1.4 Equity risk

Equity risks arise in that the group owns shares, equity certificates or other equity instruments that derive the value determined by market developments.

According to the market risk policy, the bank has its own framework for investments in strategic and financial share positions. Strategic share positions mean "investments to contribute to growth and development in the Group's market area" and "strategic stakes in relation to the banking business". Financial share positions are short-term or long-term investments with the goal of providing the best possible returns.

In measuring exposure to the market risk frameworks, the market value of investments is used. Shares in subsidiaries as well as investments in affiliated companies or joint ventures are kept outside as they are essentially consolidated in full or proportionately in the CRD IV group. Non-consolidated companies are included in the assessment of ownership risk according to Pillar 2.

### 7.1.5 Spread risk

Spread risk is risk of loss on a change in the mark-up against the reference rate on the Group's investments. Mark up against the reference index consists of both credit risk and liquidity risk and is part of the group's total market risk assessment.

## 7.2 Portfolio information

As previously mentioned, as at 31.12.2017 the group has no trading portfolio and does not calculate market risk under Pillar 1. Capital requirements for the bank's interest rate portfolio, properties and equity positions are included instead as credit risks in a regulatory context. Credit risks associated with the bank's interest rate portfolio appear in the table below.

Table 7.1: Credit risk in the interest rate portfolio

Bonds and certificates	Book value	Risk Weighted Assets	Capital requirement 8%
States and central banks	2 355	-	-
Local and regional authorities	524	105	8
Institutions*	25	67	5
Enterprises	52	28	2
OMF	5 613	561	45
<b>Total</b>	<b>8 568</b>	<b>761</b>	<b>61</b>

\* Book value has been reduced by NOK 129.5 million due to deduction in additional capital

The market value excluding the amount of interest on the banking group's investment in bonds and certificates as at

31.12.2017 is shown in the following table. Investments included in the CRD IV group are kept outside this summary.

Table 7.2: Bonds and certificates

Rating	Market value
AAA	6 318
AA	1 685
A	49
BBB	25
BB	-
B or lower	2
Non rated Norwegian municipalities	469
Other non rated papers	129
<b>Total</b>	<b>8 679</b>



The Group's positions in equity positions can be divided into five categories. Summary of book value and fair value, gains and losses as at 31.12.2017 is shown in the following table.

Table 7.3: Overview of book value and fair value, gains and losses.

Investment type	Book value	Fair value	Realised gains or losses as at 31 December 2017	Unrealised gains or losses as at 31 December 2017	Amount deducted in core equity tier 1 capital
Financial investments at fair value through profit or loss	-	-	-10	-	-
Financial investments available for sale at fair value against equity	33	33	-	-	-
Strategic investments at fair value through profit or loss	-	-	-	-	-
Strategic investments available for sale at fair value against equity	461	461	-	25	-21
Associated companies and joint ventures	3 892	3 892	-4	-	-132
<b>Total</b>	<b>4 386</b>	<b>4 386</b>	<b>-14</b>	<b>25</b>	<b>-154</b>

The group has, as at 31.12.2017, investments in both substantial and non-substantial equity positions in financial enterprises which, according to applicable rules, will be deducted from the bank group's core equity tier 1 capital at NOK 153.6 million as at 31.12.2017.

The Group's equity positions consist mainly of investments in affiliated companies and joint ventures, as well as other

strategic investments. The Group's investments in SpareBank 1 Boligkreditt AS, SpareBank 1 Kredittkort AS and SpareBank 1 Næringskreditt are consolidated proportionately in the CRD IV group. A detailed overview of the bank's investments by purpose as at 31.12.2017 is given in the following table.

Table 7.4: Investments (equity positions outside the trading portfolio) distributed by purpose

Objective	Investments	Book value
<b>Financial investments available for sale at fair value against equity</b>	NorgesInvestor Proto AS (2013)	22
	NorgesInvestor IV AS A shares	7
	Other financial investments	4
	<b>Total</b>	<b>33</b>
<b>Strategic investments available for sale at fair value against equity</b>	Totens sparebank	189
	Eksportfinans ASA	77
	SpareBank 1 Markets	40
	VISA Inc A shares	52
	VISA Inc. (US)	17
	Other strategic investments	86
	<b>Total</b>	<b>461</b>
<b>Associated companies and joint ventures</b>	SpareBank 1 Boligkreditt AS	2 127
	SpareBank 1 Gruppen AS	1 174
	SpareBank 1 Kredittkort AS	239
	SpareBank 1 Næringskreditt AS	233
	SpareBank 1 Betaling AS	61
	SMB Lab AS	20
	SpareBank 1 Banksamarbeidet DA	19
	Torggata 22 AS	10
	Komm-In AS	6
	ProAware AS	3
	<b>Total</b>	<b>3 892</b>
<b>Sum total</b>		<b>4 386</b>

The following table provides an overview of the book value by type of share investment as at 31.12.2017. Affiliated companies and joint ventures are in this overview defined

as other. The remaining share portfolio is primarily unlisted, except for three papers traded on the stock exchange.

*Table 7.5: Overview of the type and value of listed shares, unlisted shares in diversified portfolios and other commitments*

Type	Book value
Unlisted	236
Traded on stock exchange	258
Others	3 892
<b>Total</b>	<b>4 386</b>

The interest rate risk for all interest rate positions can be expressed by looking at the change in the value of interest rate instruments in the event of a parallel 1 per cent change in interest rates. The following table shows the effect of the aforementioned interest change by assets

and liabilities, time to maturity and currency as at 31.12.2017. These calculations take into account administrative interest rate risk. Where the interest rate risk is negative, this means that the result will be reduced at an increased rate.

*Table 7.6: Interest rate risk*

<b>Interest rate risk, 1 percentage point change</b>	<b>2017</b>
Bonds and certificates	-41
Fixed-rate loans to customers	-97
Fixed-rate deposits to customers	13
Bank and credit borrowing	3
Bond borrowing	447
Other fixed-rate funding and investments	3
Derivatives	-340
Administrative interest rate risk	-6
<b>Total interest rate risk, effect on profit after tax</b>	<b>-18</b>
<b>Yield curve risk, 1 percentage change</b>	<b>2017</b>
0-1 months	0
1-3 months	7
3-6 months	5
6-12 months	12
1-3 years	-11
3-5 years	6
5-10 years	-41
Over 10 years	3
<b>Total interest rate risk, effect on profit after tax</b>	<b>-18</b>
<b>Currency, 1 percentage point change</b>	<b>2017</b>
NOK	-22
EUR	3
Other	0
<b>Total interest rate risk, effect on profit after tax</b>	<b>-18</b>

The table below provides an overview of the Group's net currency exposure as at 31.12.2017. The currency risk is

quantified and monitored continuously. The Group was exposed to limited currency risk both during the year and at year end.

*Table 7.7: Currency exposure*

Currency	Net exposure
GBP	-1
USD	0
DKK	0
JPY	-1
PLN	0
SEK	0
EUR	3
CHF	-2
Other	2
<b>Total</b>	<b>0</b>

## 8 Liquidity risk

Liquidity risk is the risk of being unable to fulfil obligations when they fall due or finance assets, including desired growth, without significant extra costs.

### 8.1 Management and control

The management of the Group's funding risk is based on risk-based steering documents for the area of liquidity. The governing documents are adopted by the Board and apply for the strategy period, although they are revised as required and at least once a year. In connection with the steering documents, a separate contingency plan has been established for managing the funding situation during periods of turbulence in the financial markets, and the funding situation is also a key theme in the Group's recovery plan. The Group's governance and control of liquidity risk is considered to be satisfactory to meet the group's risk profile and strategy.

#### 8.1.1 Strategic objective and management processes

The group aims to ensure that the liquidity risk will be low and the objective is secured through:

- Sufficient liquid reserves.
- Diversification and a long-term approach to financing.
- Identification and control of the on and off balance sheet risk measurement.

Frameworks that support the strategic objective, including minimum requirements for positive liquidity without new funding ("survival targets"), the size and quality of the liquidity reserve and the financing's duration and diversification, are determined in the policy for liquidity risk.

##### 8.1.1.1 Sufficient liquid reserves

Investments in interest-bearing securities are made for the purpose of controlling the liquidity risk. The Group shall have sufficient liquid reserves to support the survival targets. Different assets have different levels of liquidity. The composition and the size of the reserves shall be such as to satisfy all of the group's survival targets. Holding a liquidity reserve has a cost. Total liquidity costs shall be the lowest possible.

##### 8.1.1.2 Diversification and a long-term approach to financing

Deposits from customers represent the most important source of funding. Deposits are considered to be stable funding, so the group shall always have a sufficiently high percentage of balance financing via deposits. Deposits with low liquidity risk shall be prioritised, while the deposits should be from a sufficient number of different types of depositors. Given sufficient diversification, the deposits shall be priced so that the group's profitability is maintained.

The foreign capital market has in recent years taken over a larger proportion of the group's financing. The desired level of refinancing risk shall be achieved through diversification on different geographical markets, types of investor groups

and maturities. There is the opportunity to enter into derivative agreements relating to loan transactions. Borrowing cost shall be minimised, given the requirements for diversification and long-term financing.

Covered bonds, hereinafter called OMF, issued by SpareBank 1 Boligkreditt og SpareBank 1 Næringskreditt shall be actively used to secure the Group stable and long-term financing, contribute to the diversification of financing and reduce financing costs. In order to ensure the greatest possible flexibility in financing opportunities, the Group shall actively work to maintain the facilitation pace of loans that can be transferred to the companies.

The Group's balance of loans in residential and commercial credit companies shall be limited so as to take into account the group's own creditworthiness and general risk considerations. In general, the Group shall follow a conservative policy and not be negatively differentiated compared with other banks' use of the residential and commercial covered bond companies as a funding source.

##### 8.1.1.3 Identification and risk measurement

Different parts of the balance give the Group varying levels of liquidity risk. To better understand different assets' actual liquidity risks, there shall be continuous work to increase knowledge of the assets' inherent risks.

Deposits creates liquidity risk for the Group. Different types of deposits have different risks of being withdrawn. Similarly, unused credits cause the Group risk because the customer may choose to take advantage of free credit. The group does not have full control over this liquidity risk. The group therefore makes stress scenarios that shall seek to describe the various liquidity risks.

Borrowing shall be refinanced on maturity and desired growth shall be financed. Through regularly updated liquidity forecasts, the liquidity risks that occur through borrowing activity are measured.

By combining known liquidity flows with different scenarios, the group's total liquidity risk is measured.

### 8.1.2 Organisation, roles and responsibility

To ensure satisfactory division of work between the departments and the people who take positions on the group's behalf and the departments and persons responsible for settlement, control and reporting, the Group has established an organisation in which executive and controlling functions are independent of each other.

#### 8.1.2.1 Control of liquidity risk

The Board's adopted liquidity strategy and policy for liquidity risk provide the CEO with guidelines, frameworks and authorisation for the management of liquidity risk. The CEO further delegates this according to area of responsibility. The group director of finance has the overall responsibility for the

liquidity management within the group. The operational responsibility for the liquidity management is delegated to the chief financial officer, who is responsible for:

- Monitoring of the ongoing development in the group's liquidity situation.
- Management of the liquidity reserve.
- The Group's borrowing of foreign capital.
- Correct determination of the internal price.

#### 8.1.2.2 Identification and measurement of liquidity risk

The financial department and risk management department have a shared responsibility for identifying and measuring liquidity risks. The results are used when self-defined stress is defined.

- The finance department is responsible for identifying and measuring the liquidity risk for foreign capital funding, including the use of OMF and the portion of liquid reserves invested in the market.
- The risk management department is responsible for identifying and measuring the liquidity risk of deposits and unused credits.

#### 8.1.2.3 Reporting of liquidity risk

To ensure independent control, the risk management department is responsible for reporting.

- Ongoing framework control and reporting of positions according to the framework determined in the liquidity risk policy and any guidelines from the Financial Supervisory Authority of Norway.
- Independent reporting to the Board and management.
- Risk assessment.
- Monitoring of government reporting within the liquidity area.

#### 8.1.2.4 Ongoing follow up

Operations are responsible for settlement and control at transaction level. The business divisions are responsible for ensuring that liquidity events that are essential for liquidity management are reported to the finance department as soon as they are known.

Before basic new instruments are used, this should be approved by the Group CFO. A risk analysis shall also be drawn up with related risk measures.

Systems for management and control shall be evaluated regularly by the Group's internal auditor.

## 8.2 Portfolio information

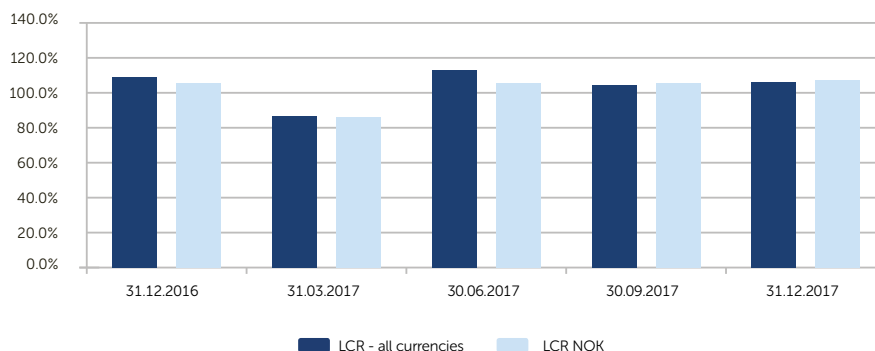
### 8.2.1 Survival targets

In order to realise the objective of low liquidity risk, multiple targets have been established for survival at different time horizons.

#### 8.2.1.1 Survival according to liquidity coverage ratio

Liquidity Coverage Ratio, hereinafter LCR, defines a stress scenario that lasts for 30 days. The development in the last quarters of the Group's consolidated LCR for all currencies and NOK is shown in the figure below. Supplementary information about diversification of financing and the liquidity portfolio's composition can be found in the sections below.

Figure 8.1: LCR

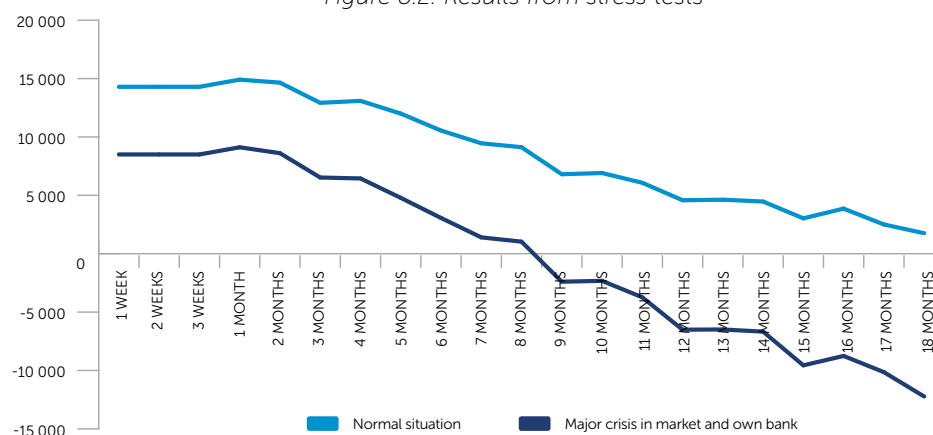


### 8.2.1.2 Survival in a normal situation and in a self-defined stress with a great crisis in the market and our own bank

As at 31.12.2017, the Group could continue its operations for more than 18 months in a normal situation. In a scenario

defined as a major crisis in the market and at our own bank, the Group as at 31.12.2017 had enough liquidity to continue operations for over 8 months in this scenario.

Figure 8.2: Results from stress tests



### 8.2.2 Liquidity reserve

The liquidity reserve shall at all times be large enough to satisfy government requirements and internal survival targets. As at 31.12.2017 the liquidity reserve was NOK 15.6 billion, given the group's internal limitation on transferring loans to SpareBank 1 Boligkreditt.

The liquidity reserve shall consist of liquid assets of good quality. The liquidity reserve at the start of the year contained cash, access to loans from Norges Bank, bonds, loans prepared for sale to residential and commercial covered bond companies and collective investment funds and listed shares. The following figures indicate the composition and quality of the liquidity reserve.

Figure 8.3: The composition of the liquidity portfolio

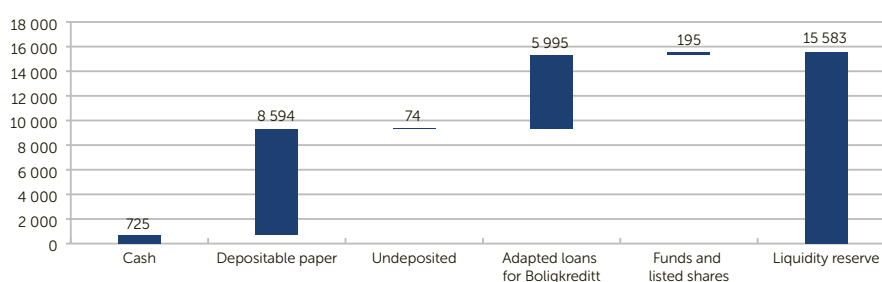
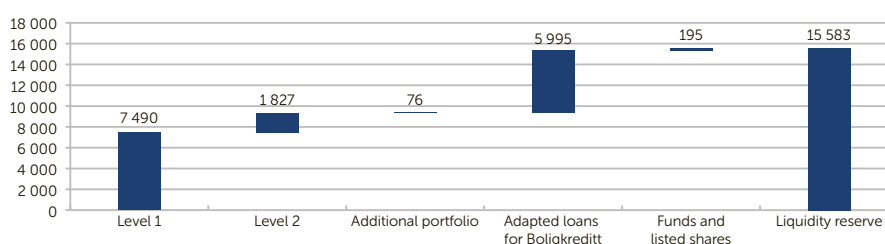


Figure 8.4: The quality of the liquidity portfolio.



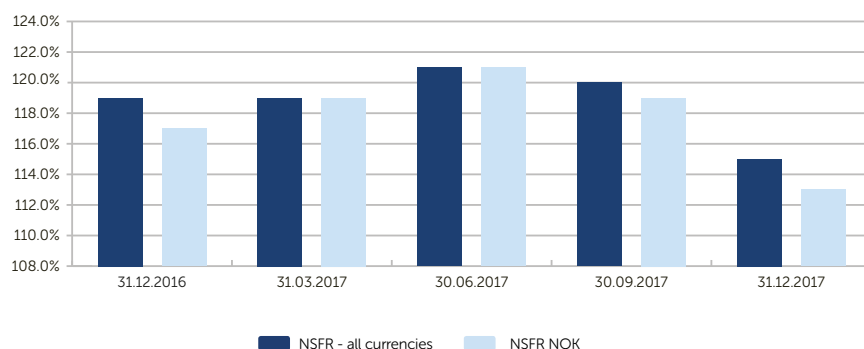
### 8.2.3 Diversification and long-term approach to financing

Liquidity risk is reduced by the diversification of financing over different markets, financing sources, instruments, terms and currencies. Total financing, consisting of equity, customer deposits, loans transferred to residential and commercial credit companies and market financing, was NOK 145.6 billion as at 31.12.2017. The market financing alone on the same date was NOK 27.2 billion.

#### 8.2.3.1 Long-term financing

Net Stable funding Ratio, hereinafter called NSFR, describes the degree to which the group is long-term funded. The development in the last quarters of the Group's consolidated NSFR for all currencies and NOK is shown in the figure below.

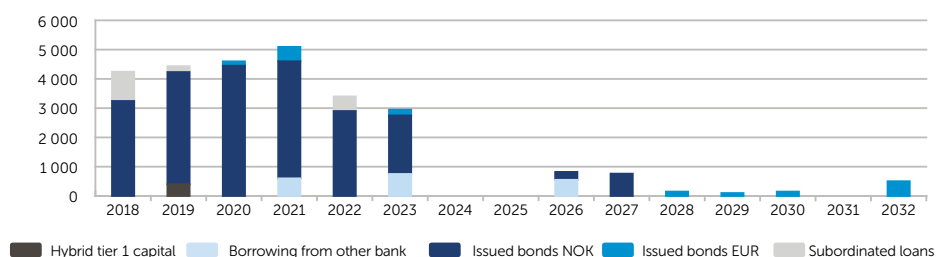
Figure 8.5: NSFR



Of the Group's total funding volume of NOK 27.2 billion, NOK 4.2 billion will be refinanced in 2018. The average term for the Group's market financing was 3.6 years as at

31.12.2017. The figure below shows the maturity structure for the Group's market financing.

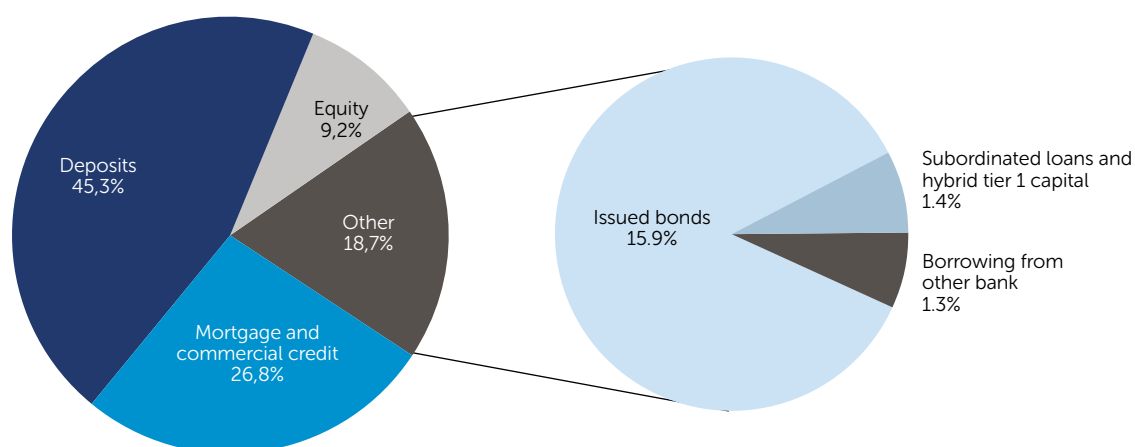
Figure 8.6: Maturity structure



### 8.2.3.2 Diversified financing

The figure below shows the Group's sources of financing as at 31.12.2017.

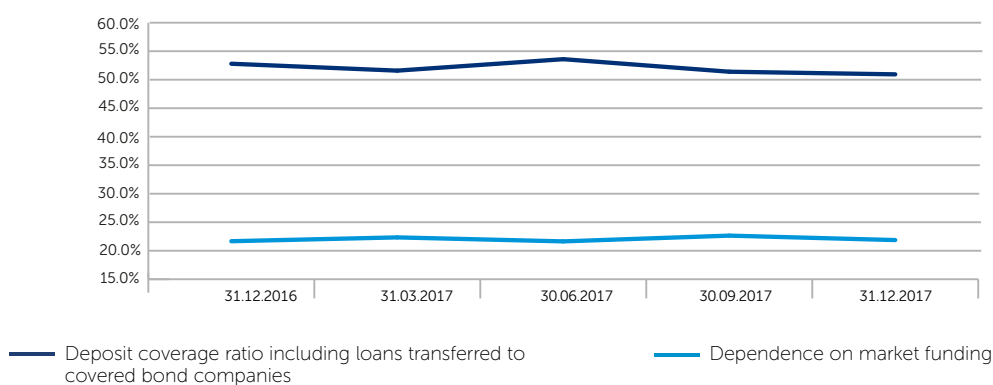
Figure 8.7: The Group's sources of financing



To ensure other diversification of financing than different maturities and funding sources, the Group has established

frameworks for reliance on market funding, use of OMF as a funding source and diversification of deposits.

Figure 8.8: Deposit coverage ratio and reliance on market funding



At the end of the year, the group's funding in EUR represented 6.4 per cent of total market funding and 1.8 per

cent of total liabilities on its own balance sheet.

## 9 Operational risk

Operational risk is the risk of losses due to weak or inadequate internal processes or systems, human error or external incidents. Operational risk also includes legal risk, which is a risk that often arises due to problems with documentation and the interpretation of contracts, as well as varying legal practices where the Group operates.

### 9.1 Management and control

While the Group deliberately accepts market and credit risk, operational risk is a type of risk that banks would like to avoid to the greatest possible extent. The operational risk in the Group shall be characterised by few and minor operational incidents. The practical management of operational risk in the Group is based on the main activities described in the subsections below.

#### 9.1.1 Manager confirmation

All managers of business and support functions are responsible for day-to-day risk management, and for ensuring that a satisfactory internal control is established within their area of responsibility. All managers must report on status and development in annual manager confirmations, as well as assess the risk culture as an element in analyses and reports for their areas. The manager confirmations are intended to provide the CEO and Board with information about whether risk management is being properly addressed, including whether routines, guidelines and Acts/Regulations are being followed. Manager confirmations are an important part of the Group's systematic quality work. The work on manager confirmation is coordinated by the risk management department.

#### 9.1.2 Losses, incidents and customer complaints

The Group must be focused, and capable of, identifying and understanding risks and at the same time learning from adverse incidents. Operational losses and incidents shall be registered in the incident database and handled in accordance with the defined guidelines. Losses and incidents shall be reviewed periodically to identify significant or systematic errors, weaknesses and areas requiring improvement. All employees in the Group have a responsibility to report incidents and customer complaints. The risk management department is

responsible for ensuring that the incidents and complaints are registered in the incidents database in accordance with the defined routines.

The parent bank has a centralised complaint scheme that at any given time seeks to safeguard the parent bank, the parent bank's customers and other contractual partners. The scheme shall satisfy the Financial Supervisory Authority of Norway's guidelines for complaint management. The purpose of this scheme is to ensure that all complaints are given satisfactory treatment in line with the parent bank's principles of complaint processing and contribute to adequate consumer protection in line with the Financial Supervisory Authority of Norway's guidelines. The system shall also ensure that the bank gains a better overview of the operational risk, and can thus analyse the complaints to determine whether they are due to systematic errors. The extent of complaint cases and serious complaint cases are reported quarterly to the Board. In addition, complaints are reported annually to the Financial Supervisory Authority of Norway.

#### 9.1.3 Continuous improvement

The risk management department shall register and follow up material suggestions for improvements based on reports from the internal audit and measures based on experience from the Financial Supervisory Authority of Norway or recommendations from other independent control bodies. All managers with a responsibility to follow up measures shall register regular updates on progress and relevant activities that have been started in the improvements database.

#### 9.1.4 Risk analyses

The risk management department shall facilitate risk analysis and assist with methodology and tools that enable the first line to implement its own risk analyses.

## 9.2 Minimum primary capital requirements

The Group uses the basic approach to calculate the primary capital required to cover operational risk.

Table 9.1: Minimum primary capital requirement for operational risk

	Consolidated	SpareBank 1 Østlandet	SpareBank 1 Finans Østlandet AS
Risk Weighted Assets	4 503	3 343	341
<b>Capital requirement 8%</b>	<b>360</b>	<b>267</b>	<b>27</b>



## 10 Compliance risk

Compliance risk is the risk that the Group will incur public sanctions/penalties, financial losses or a damaged reputation as a result of a failure to comply with laws, regulations or guidelines from the authorities.

### 10.1 Management and control

The compliance department has the overall responsibility for the coordination of compliance work. The Group has a separate person responsible for compliance function related to the provision of investment services, who is responsible for

checking that the activities related to the provision of these services are carried out in accordance with the regulations for securities trading.

The Group's management is responsible for implementation and compliance with laws and regulations, while each individual employee is responsible for day-to-day, ongoing compliance.

Incidents and violations in the compliance area will be registered in the same manner as operational risk is registered and followed up via the Group's incident database.

# 11 Ownership risk

Ownership risk is the risk that the Group will incur negative earnings from ownership interests in strategically owned companies, or that the Group must inject new equity in strategically owned companies, whether it is due to strong growth or to ensure continued operations as a result of large losses.

## 11.1 Exposure

SpareBank 1 Østlandet is as at 31.12.2017 exposed to ownership risk through the following ownership positions:

- SpareBank 1 Gruppen AS, stake 12.4 per cent.
- SpareBank 1 Boligkreditt AS, stake 21.1 per cent.
- SpareBank 1 Næringskreditt AS, stake 12.4 per cent.
- SpareBank 1 Kredittkort AS, stake 19.6 per cent.
- SpareBank 1 Betaling AS, stake 21.2 per cent.

In addition, some smaller stakes are handled, such as affiliated companies and joint ventures with smaller amounts.

## 11.2 Management and control

The SpareBank 1 banks conduct their alliance work through the jointly owned holding company SpareBank 1 Gruppen AS. SpareBank 1 Gruppen is owned by SpareBank 1 Østlandet, SpareBank 1 SR-Bank, SpareBank 1 Nord-Norge, SpareBank 1 SMN, Samarbeidende Sparebanker AS, as well as the Norwegian Confederation of Trade Unions (LO) and trade unions associated with LO. SpareBank 1 Boligkreditt, SpareBank 1 Næringskreditt, SpareBank 1 Kredittkort and SpareBank 1 Betaling are owned by all the banks in the SpareBank 1 Alliance.

The CEOs from the owning banks, SpareBank 1 Østlandet, SpareBank 1 SR-Bank, SpareBank 1 Nord-Norge, SpareBank 1 SMN and the chair of Samarbeidende Sparebanker AS, as well as the Norwegian Confederation of Trade Unions (LO), as owners of the company, sit on the board of SpareBank 1 Gruppen. The finance director of SpareBank 1 Østlandet joins the board meetings of SpareBank 1 Boligkreditt and SpareBank 1 Næringskreditt. SpareBank 1 Østlandet is similarly represented on the boards of SpareBank 1 Kredittkort and SpareBank 1 Betaling.