

Note 5 - Capital adequacy and capital management

New capital adequacy rules were introduced in Norway as from 1 January 2007 (Basel II - the EU's new directive on capital adequacy). SpareBank1 SMN applied to and received permission from Finanstilsynet (Financial Supervisory Authority of Norway) to use internal rating methods (Internal Rating Based Approach - Foundation) to calculate charges for credit risk from 1 January 2007 onwards. This will make the statutory minimum capital adequacy requirement more risk-sensitive, so that it better reflects the risk in the underlying portfolios. Using IRB demands high standards of the Bank's organisation, competence, risk models and risk management systems. Under interim regulations issued by Finanstilsynet, IRB banks are not yet seeing the full effect of the reduced capital requirements. As from 2009, a 20 per cent reduction of the risk-weighted basis of calculation was allowed.

Subordinated debt ranks behind all other liabilities. Dated subordinated loans cannot constitute more than 50 per cent of tier 1 capital for capital adequacy purposes, while perpetual subordinated loans cannot constitute more than 100 per cent of tier 1 capital. Subordinated loans are classified as a liability in the balance sheet and are measured at amortised cost in the same way as other long-term loans.

Hybrid capital denotes bonds with a nominal interest rate, but the bank is not obliged to pay interest in a period where dividends are not paid, and neither is the investor subsequently entitled to interest that has not been paid, i.e. interest does not accumulate. Hybrid capital is approved as an element of tier 1 capital up to limit of 15 per cent of aggregate tier 1 capital. Finanstilsynet (Norway's FSA) can require hybrid capital to be written down in proportion with equity capital should the bank's tier 1 capital adequacy fall below 5 per cent or total capital adequacy falls below 6 per cent. Written-down amounts on hybrid capital must be written up before dividends can be paid to shareholders or before equity capital is written up. Hybrid capital is shown as other long-term debt at amortised cost.

For detailed information regarding subordinated debt and hybrid capital, see note 37 Subordinated debt and hybrid equity issue.

Parent bank			Group	
2011	2012	(NOK million)	2012	2011
2,373	2,597	Equity capital certificates	2,597	2,373
-0	-0	- Own holding of ECCs	-0	-0
183	895	Premium fund	895	183
1,457	1,889	Dividend equalisation fund	1,889	1,457
2,611	2,944	Savings bank's reserve	2,944	2,611
190	195	Recommended dividends	195	190
40	30	Provision for gifts	30	40
70	106	Unrealised gains reserve	123	85
-	0	Other equity and minority interest	1,370	1,409
6,924	8,656	Total book equity	10,042	8,348
-447	-447	Deferred taxes, goodwill and other intangible assets	-674	-692
-	-	Part of reserve for unrealised gains, associated companies	57	64
-230	-225	Deduction for allocated dividends and gifts	-238	-230
-387	-448	50 % deduction for subordinated capital in other financial institutions	-2	-
-137	-165	50 % deduction for expected losses on IRB, net of write-downs	-179	-147
-	-	50 % capital adequacy reserve	-703	-656
-	-55	Surplus financing of pension obligations	-49	-
5,724	7,316	Total common equity Tier one	8,254	6,687
956	918	Hybrid capital, core capital	1,103	1,170
6,680	8,234	Total core capital	9,357	7,856
		Supplementary capital in excess of core capital		
-	-	State Finance Fund, supplementary capital	31	-
326	312	Perpetual subordinated capital	312	328
1,409	1,810	Non-perpetual subordinated capital	2,127	1,674
-387	-448	50 % deduction for subordinated capital in other financial institutions	-2	-
-137	-165	50 % deduction for expected losses on IRB, net of write-downs	-179	-147
-	-	50 % capital adequacy reserve	-703	-656
1,211	1,509	Total supplementary capital	1,586	1,199
7,891	9,742	Net subordinated capital	10,943	9,055

		Minimum requirements subordinated capital, Basel II		
1,456	1,654	Involvement with specialised enterprises	1,654	1,456
1,313	1,470	Other corporations exposure	1,470	1,313
40	39	SME exposure	42	42
324	316	Retail mortgage exposure	560	513
31	28	Other retail exposure	30	33
653	1,118	Equity investments	-	-
3,818	4,625	Total credit risk IRB	3,756	3,358
182	205	Debt risk	205	182
49	14	Equity risk	15	16
-	-	Currency risk	-	-
293	315	Operational risk	420	400
653	553	Exposures calculated using the standardised approach	2,074	2,184
-65	-75	Deductions	-120	-111
-	-	Transitional arrangements	246	-
4,930	5,637	Minimum requirements subordinated capital	6,596	6,027
61,625	70,468	Risk weighted assets (RWA)	82,446	75,338
		Capital adequacy		
9.3 %	10.4 %	Common equity Tier one ratio	10.0 %	8.9 %
10.8 %	11.7 %	Core capital ratio	11.3 %	10.4 %
12.8 %	13.8 %	Capital adequacy ratio	13.3 %	12.0 %