SpareBank 1 SMN

Note 13 - Capital adequacy

SpareBank 1 SMN has used IRB (Internal Rating Approach – Foundation) to calculate charges for credit risk since January 2007. Using IRB imposes wide-ranging requirements on the bank's organisation, competence, risk models and risk management systems. In June 2013 the bank applied for permission to switch to Advanced IRB for enterprise portfolios currently reported using the foundation approach. The effect of the risk weights under IRB is limited due to transitional rules set out in regulations issued by Finanstilsynet.

As from Q2 2013 the measurement method for operational risk was changed from the basic approach to the standardised approach at the Parent Bank. At the Group level, subsidiaries are still measured using the basic approach.

As from 1 July 2013 new buffer requirements have been introduced; see the Financial Institutions Act section 2-9e. As of 30 June 2014 the capital conservation buffer requirement is 2.5 per cent and the systemic risk buffer requirement is 2 per cent. These requirements are in addition to the requirement that own funds should constitute at least 4.5 per cent common equity tier 1 (CET1) capital, bringing the overall minimum CET1 requirement to 9 per cent. The systemic risk buffer requirement will increase by a further 1 percentage point from 1 July, bringing the overall CET1 to 10 per cent. As of 30 June 2015, a countercyclical buffer requirement of 1 percentage point will be applicable.

BN Bank received approval for use of the advanced IRB approach for its corporate portfolio in April 2014.

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 characterised by moderate repayment incentives is approved as an element of tier 1 capital up to limit of 15 per cent of aggregate tier 1 capital. If, on the other hand, hybrid capital has no fixed term to maturity and has no repayment incentives, it may be included as an element of core capital up to limit of 35 per cent of aggregate core 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 8 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 recognised as other long-term debt at amortised cost.

In connection with change requirements regarding the conditions for hybrid capital, hybrid capital that does not satisfy the new requirements over time will not be eligible for inclusion in other core capital. Such hybrid capital will be reduced by 20 per cent in 2014 and 10 per cent thereafter. As of 30 June 2014, SpareBank 1 SMN held NOK 450m in hybrid capital which will be subject to reduction.

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.

For detailed information regarding subordinated detbt and hybrid captial, see note 38 in the banks's annual report.

Parent Bank				Group		
31 Dec 2013	30 Jun 2013	30 Jun 2014	(NOKm)	30 Jun 2014	30 Jun 2013	31 Dec 2013
2,597	2,597	2,597	Equity capital certificates	2,597	2,597	2,597
-0	-0	-0	- Own holding of ECCs	-0	-0	-0
895	895	895	Premium fund	895	895	895
2,496	1,889	2,496	Dividend equalisation fund	2,496	1,889	2,496
3,276	2,944	3,276	Savings bank's reserve	3,276	2,944	3,276
227	-	-	Recommended dividends	-	-	227
124	-	-	Provision for gifts	-	-	124
195	106	195	Unrealised gains reserve	206	123	206
-	38	-65	Other equity and minority interest	1,347	1,386	1,421
-	830	942	Net profit	963	606	-
9,811	**9,299**	**10,337**	**Total book equity**	**11,780**	**10,439**	**11,242**
-447	-447	-454	Deferred taxes, goodwill and other intangible assets	-620	-531	-582
-	-	-	Part of reserve for unrealised gains, associated companies	98	57	98
-352	-	-	Deduction for allocated dividends and gifts	-	-	-361
-401	-381	-442	50 % deduction for subordinated capital in other financial institutions	-101	-93	-106
-240	-203	-251	50 % deduction for expected losses on IRB, net of write-downs	-246	-219	-214
-	-	-	50 % capital adequacy reserve	-685	-500	-595
-109	-109	-28	Surplus financing of pension obligations	-21	-107	-107
-	-830	-942	Net profit	-963	-606	-
-	606	688	Year-to-date profit included in core capital (73% pre tax)	703	442	-
8,262	**7,935**	**8,908**	**Total common equity Tier one**	**9,945**	**8,882**	**9,374**
1,431	1,441	1,439	Hybrid capital, core capital	1,690	1,625	1,615
9,693	**9,376**	**10,347**	**Total core capital**	**11,635**	**10,508**	**10,989**
			Supplementary capital in excess of core capital			
-	-	-	State Finance Fund, supplementary capital	-	31	31
304	307	306	Perpetual subordinated capital	306	307	363
1,569	1,598	1,593	Non-perpetual subordinated capital	2,254	1,861	1,950
-401	-381	-442	50 % deduction for subordinated capital in other financial institutions	-101	-93	-106
-240	-203	-251	50 % deduction for expected losses on IRB, net of write-downs	-246	-219	-214
-	-	-	50 % capital adequacy reserve	-685	-500	-595
1,231	**1,320**	**1,206**	**Total supplementary capital**	**1,529**	**1,386**	**1,428**
10,924	**10,696**	**11,553**	**Net subordinated capital**	**13,164**	**11,894**	**12,417**
			Minimum requirements subordinated capital, Basel II			
1,573	1,672	1,576	Involvement with spesialised enterprises	1,863	1,672	1,573
1,478	1,504	1,394	Other corporations exposure	1,472	1,504	1,479
70	63	138	SME exposure	146	68	74
363	348	765	Retail morgage exposure	1,170	613	628
28	32	41	Other retail exposure	43	37	33
1,157	1,139	1,241	Equity investments	27	-	-
4,669	**4,758**	**5,155**	**Total credit risk IRB**	**4,722**	**3,895**	**3,787**
224	255	307	Debt risk	308	255	224
8	12	-	Equity risk	1	13	10
-	-	-	Currency risk	-	-	-
297	297	292	Operational risk	416	398	398
560	544	617	Exposures calculated using the standardised approach	1,682	2,106	2,151
-67	-64	-73	Deductions	-130	-102	-119
-	-	-	Transitional arrangements	-	322	316
5,690	**5,803**	**6,297**	**Minimum requirements subordinated capital**	**6,998**	**6,886**	**6,767**
71,130	72,536	78,712	Risk weighteted assets (RWA)	87,477	86,079	84,591
			Capital adequacy			
11.6 %	10.9 %	11.3 %	Common equity Tier one ratio	11.4 %	10.3 %	11.1 %
13.6 %	12.9 %	13.1 %	Core capital ratio	13.3 %	12.2 %	13.0 %
15.4 %	14.7 %	14.7 %	Capital adequacy ratio	15.0 %	13.8 %	14.7 %