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 31 March 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.

Over the course of 2014 the systemic risk buffer requirement will increase by a further 1 percentage point, bringing the overall CET1 requirement as of 30 June 2014 to 10 per cent. As of 1 July 2015, a countercyclical buffer requirement of 1 percentage point will be applicable.

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 31 March 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	31 Mar 2013	31 Mar 2014	(NOKm)	31 Mar 2014	31 Mar 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	-	Other equity and minority interest	1,419	1,402	1,421
-	231	450	Net profit	500	321	-
9,811	**8,700**	**9,909**	**Total book equity**	**11,389**	**10,170**	**11,242**
-447	-447	-447	Deferred taxes, goodwill and other intangible assets	-613	-531	-582
-	-	-	Part of reserve for unrealised gains, associated companies	98	57	98
-352	-	-	Deduction for allocated dividends and gifts	-4	-6	-361
-401	-448	-413	50 % deduction for subordinated capital in other financial institutions	-120	-2	-106
-240	-178	-275	50 % deduction for expected losses on IRB, net of write-downs	-259	-193	-214
-	-	-	50 % capital adequacy reserve	-623	-734	-595
-109	-109	-80	Surplus financing of pension obligations	-78	-107	-107
-	-231	-450	Net profit	-500	-321	-
-	169	329	Year-to-date profit included in core capital (73% pre tax)	365	234	-
8,262	**7,455**	**8,574**	**Total common equity Tier one**	**9,655**	**8,568**	**9,374**
1,431	932	1,433	Hybrid capital, core capital	1,647	1,118	1,615
9,693	**8,387**	**10,007**	**Total core capital**	**11,303**	**9,686**	**10,989**
			Supplementary capital in excess of core capital			
-	-	-	State Finance Fund, supplementary capital	-	31	31
304	308	304	Perpetual subordinated capital	362	308	363
1,569	1,610	1,570	Non-perpetual subordinated capital	2,230	1,875	1,950
-401	-448	-413	50 % deduction for subordinated capital in other financial institutions	-120	-2	-106
-240	-178	-275	50 % deduction for expected losses on IRB, net of write-downs	-259	-193	-214
-	-	-	50 % capital adequacy reserve	-623	-734	-595
1,231	**1,292**	**1,187**	**Total supplementary capital**	**1,591**	**1,285**	**1,428**
10,924	**9,679**	**11,194**	**Net subordinated capital**	**12,893**	**10,971**	**12,417**
			Minimum requirements subordinated capital, Basel II			
1,573	1,661	1,508	Involvement with spesialised enterprises	1,508	1,661	1,573
1,478	1,505	1,380	Other corporations exposure	1,381	1,505	1,479
70	52	136	SME exposure	145	56	74
363	326	703	Retail morgage exposure	1,153	583	628
28	26	37	Other retail exposure	43	28	33
1,157	1,108	1,225	Equity investments	-	-	-
4,669	**4,678**	**4,989**	**Total credit risk IRB**	**4,229**	**3,833**	**3,787**
224	257	281	Debt risk	281	257	224
8	14	-	Equity risk	3	15	10
-	-	-	Currency risk	-	-	-
297	337	292	Operational risk	416	438	398
560	545	579	Exposures calculated using the standardised approach	2,186	2,086	2,151
-67	-75	-69	Deductions	-126	-125	-119
-	-	-	Transitional arrangements	-	102	316
5,690	**5,756**	**6,072**	**Minimum requirements subordinated capital**	**6,989**	**6,606**	**6,767**
71,130	71,951	75,900	Risk weigheted assets (RWA)	87,361	82,578	84,591
			Capital adequacy			
11.6 %	10.4 %	11.3 %	Common equity Tier one ratio	11.1 %	10.4 %	11.1 %
13.6 %	11.7 %	13.2 %	Core capital ratio	12.9 %	11.7 %	13.0 %
15.4 %	13.5 %	14.7 %	Capital adequacy ratio	14.8 %	13.3 %	14.7 %