Note 2 - Critical estimates and assessment concerning the use of accounting principles

When it prepares the consolidated accounts the management team makes estimates, discretionary assessments and assumptions which influence the application of accounting principles. This accordingly affects recognised amounts for assets, liabilities, revenues and expenses. Last year's annual accounts give a closer explanation of significant estimates and assumptions in Note 3 Critical estimates and assessments concerning the use of accounting principles.

Pensions

Sparebank1 SMN Group has one pension arrangement; defined contribution plan. For a further description of the pension scheme, see note 25 in the 2020 annual report.

The group's pension liabilities are accounted for under IAS 19R. Estimate variances are therefore directly reflected in equity capital and are presented under other comprehensive income. It was decided to terminate the defined benefit scheme at a board meeting on 21 October 2016. Employees on this scheme transferred to the defined contribution scheme from 1 January 2017, and received a paid-up policy showing rights accumulated under the defined benefit scheme. Paid-up policies are managed by the pension fund, which has been a paid-up pension fund as from 1 January 2017. A framework agreement has been established between SpareBank 1 SMN and the pension fund which covers funding, asset management etc. In view of the responsibility still held by SpareBank 1 SMN, future liabilities will need to be incorporated in the accounts. The board of the pension fund is required to be composed of representatives from the Group and participants in the pension schemes in accordance with the articles of association of the pension fund.

A new calculation of the Group's pension liabilities has not been carried out as per 30 June 2020.

Investment held for sale

SpareBank 1 SMN's strategy is that ownership duse to defaulted exposures should at the outset be of brief duration, normally not longer than one year. Investments are recorded at fair value in the Parent Bank's accounts, and is classified as investment held for sale.

SpareBank 1 Kapitalforvaltning, subsidiary of SpareBank 1 Markets, has been presented as Investment held for sale from second quarter 2021 due to the agreement of sale to SpareBank 1 Forvaltning. The transaction will be carried through in third quarter of 2021. Comparables have been restated.

The company SpareBank 1 Forvaltning is owned by the SpareBank1 banks and will include the subsidiaries Odin Forvaltning, SpareBank 1 Kapitalforvaltning and SpareBank 1 Verdipapirservice.

2021 Q2 (NOKm)	Assets	Liabilities	Revenue	Expenses	Profit	Ownership
Mavi XV AS Group	38	1	3	5	-1	100 %
SpareBank 1 Kapitalforvaltning	71	31	36	26	10	100%
Total Held for sale	**109**	**32**	**40**	**31**	**10**	

Losses on loans and guarantees

For a detailed description of the Bank's model for expected credit losses, refer to note 2 and 3 in the annual accounts for 2020.

In the first quarter 2020 some changes were made in the input in the credit loss model as a result of changed expectations due to the corona situation. The crisis and the significant increase in macroeconomic uncertainty have made the assessments extra demanding. We are in the early stages of the crisis and the consequences for the bank's customers and the industries we are exposed to are difficult to estimate. The regulators have emphasized the importance of focusing on the expected long-term effects of the crisis and this has also been the bank's focus.

In the first quarter 2020 the bank changed the assumptions for the base scenario in a negative direction. This has been continued for the rest of 2020 and in the first quarter of 2021. The bank's exposure to hotels and tourism, including commercial real estate with the income mainly towards this industry, is separated into a separate portfolio with its own assessments of PD and LGD courses as well as special scenarios and weighting of these to reflect this portfolio's exposure to the effects of corona. In addition, this entire portfolio is included in stage 2 or 3.

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The development in the base scenario is prepared using adjustment factors where the development in the business cycle is projected by assumptions about how much the probability of default (PD) or loss of default (LGD) will increase or decrease compared to the base scenario in a five-year period. We expect increased losses related to debtors that have a demanding starting point before the crisis - typically debtors in stage 2. We have therefore chosen to increase the trajectories for PD and LGD as well as reduce expected repayments in the base scenario, especially from year 2 onwards, since this will affect expected losses mainly for debtors in stage 2. To adjust for migration into stage 2, PD and LGD estimates are also increased in the first year. No first year repayments are assumed for all portfolios in the downside scenario.

The applied scenario weighting was changed in the fourth quarter of 2020 to reflect further increased uncertainty. For corporate market including offshore, as well as agriculture, the downside scenario was changed from a weighting with a 10 percent probability, to a weighting of a 20 percent probability. For retail market, the weighting of the downside scenario was changed from 10 to 15 per cent. This has been continued in first half of 2021.

The effect of changes in input assumptions is shown as "Effect of changed assumptions in ECL model" in note 7. The effect is NOK 15 million for the Bank and 7 million for the Group.

Sensitivities

The first part of the table below show total calculated expected credit loss as of 30 June 2021 in each of the three scenarios, distributed in the portfolios retail market (RM) corporate market (CM), and offshore, travel and agriculture which adds up to parent bank. In addition the subsidiary SB 1 Finans Midt-norge is included. ECL for the parent bank and the subsidiary is summed up in th coloumn "Group"

The second part of the table show the ECL distributed by portfolio using the scenario weight applied, in addition to a alternative weighting where worst case have been doubled.

If the downside scenario's probability were doubled at the expense of the baseline scenario at the end of June 2021, this would have entailed an increase in loss provisions of NOK 385 million for the parent bank and NOK 392 million for the group.

Portfolio	Corporate excl offshore/ Agriculture	Retail Market	Offshore	Agriculture	Tourism	Total parent	SB 1 Finans MN	Group
ECL expected scenario	358	91	681	28	48	1,206	52	1,258
ECL downside scenario	1,265	295	1,403	98	96	3,158	114	3,272
ECL upside scenario	291	40	588	14	12	945	39	983
ECL with scenario weights used 80/10/10							57	58
ECL with scenario weights used 65/20/15	529	-	812	40		1,380		1,380
ECL with scenario weights used 60/30/10					59	59		59
ECL with scenario weights used 70/15/15		114				114		114
Total ECL used	**529**	**114**	**812**	**40**	**59**	**1,553**	**57**	**1,611**
ECL alternative scenario weights 70/20/10							63	64
ECL alternative scenario weights 45/40/15	711		956	54		1,720	-	1,720
ECL alternative scenario weights 30/60/10					73	73		73
ECL alternative scenario weights 55/33/15		145				145		145
Total ECL alternative weights (double downside)	**711**	**145**	**956**	**54**		**1,938**	**63**	**2,003**
Change in ECL if alternative weights were used	**182**	**31**	**145**	**14**		**385**	**7**	**392**

The table reflects that there are some significant differences in underlying PD and LGD estimates in the different scenarios and that there are differentiated levels and level differences between the portfolios. At group level, the ECL in the upside scenario, which largely reflects the loss and default picture in recent years, is about 80 per cent of the ECL in the expected scenario. The downside scenario gives more than double the ECL than in the expected scenario. Applied scenario weighting gives about 28 percent higher ECL than in the expected scenario.