

Executive Order on Management and Control of Banks etc.¹⁾

Executive Order no. 1325 of 1 December 2010

The following shall be laid down pursuant to section 65(2), section 70(5), section 71(2), section 152(4) and section 373(4) of the Financial Business Act, cf. Consolidating Act no. 1125 of 23 September 2010 as amended by Act no. 579 of 1 June 2010, as well as section 21 and section 39(3) of the Mortgage-Credit Loans and Mortgage-Credit Bonds etc. Act, cf. Consolidating Act no. 1261 of 15 November 2010:

Part 1

Scope

1.-(1) This Executive Order shall apply to the following undertakings, cf. however, subsection (2):

- 1) Banks.
- 2) Mortgage-credit institutions.
- 3) Danish Ship Finance A/S.
- 4) Investment companies, cf. however, section 23.
- 5) Investment management companies, however not management by investment management companies of investment associations, special-purpose associations, hedge associations, approved restricted associations and professional associations.
- 6) Branches in Denmark of credit institutions, investment firms and management companies, which have been granted a licence in a country outside the European Union with which the Union has not entered into an agreement for the financial area, with the exceptions made necessary by the circumstances of the branch, or laid down in, or pursuant to, international agreements.

(2) Undertakings covered by subsection (1), which only have a licence to carry out certain specified services, shall comply with the regulations of this Executive Order for the area for which the undertaking has a licence.

(3) If the board of directors and board of management can confirm that provisions in this Executive Order are either not relevant for the undertaking as a whole or for the risk areas affected, or that the undertaking or the risk area, despite a derogation, can continue appropriate operation, the undertaking may derogate from the provisions of this Executive Order unless otherwise stated elsewhere. Derogation may, for example, be as a consequence of

- 1) low or straightforward activity in one or more activity or risk areas,
- 2) the size of the undertaking,

¹⁾ This Executive Order contains provisions implementing parts of Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions (recast) and Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 amending Directives 2006/48/EC, 2006/49/EC and 2007/64/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management.

- 3) the structure of the undertaking, or
- 4) the structure of any group of which the undertaking may be part.

(4) For undertakings with extensive or very complex activities in one or more risk areas, the board of directors and board of management of the undertaking shall assess regularly whether it is necessary to supplement the requirements of this Executive Order with further initiatives.

Part 2

Tasks and responsibilities of the board of directors

2. As part of the overall and strategic management of the undertaking, the board of directors shall

- 1) decide the business model of the undertaking,
- 2) assess whether the risk profile and policies of the undertaking, cf. section 5, and guidelines for the board of management, cf. sections 6 and 7, are appropriate in relation to the business activities, organisation and resources of the undertaking as well as market conditions under which the activities of the undertaking are performed,
- 3) assess and decide the budgets, capital, liquidity, material transactions, special risks and overall insurance situation of the undertaking,
- 4) monitor that the board of management performs its duties appropriately and in accordance with the risk profile, policies and guidelines laid down for the board of management,
- 5) ensure that reporting and information from the board of management to the board of directors is complete for the work of the board of directors,
- 6) monitor that the undertaking has effective forms of corporate governance, and
- 7) when required and no less than once a year decide the individual solvency need of the undertaking, cf. sections 124(4) and 125(7) of the Financial Business Act.

3. The board of directors shall regularly assess whether its members collectively possess the necessary knowledge and experience regarding the risks of the undertaking to ensure appropriate operation of the undertaking. This applies in particular with respect to the undertaking's use of models for risk calculations when introducing new products, cf. section 28, and other initiatives which could involve an increased risk for the undertaking or which could significantly influence the way in which risks are calculated and reported in the undertaking.

4.-(1) When the situation of the undertaking, the market situation, or other relevant factors so dictate, and no less than once a year, the board of directors shall carry out an assessment of the risks of the undertaking.

(2) Such an assessment shall be carried out on the basis of a report on the risks of the undertaking prepared by the board of management. As a minimum, the report shall include a description of:

- 1) the types of risk to which the undertaking is exposed, including an assessment of the influence of the business model on the risks and risk levels,
- 2) to which activities the relevant risks are linked,
- 3) the scope of the individual types of risk, and
- 4) how the types of risk affect each other, if relevant.

(3) If some of the conditions mentioned in section 1(3) and (4) exist, which give grounds for the undertaking to derogate from or supplement the provisions of this Executive Order, the report pursuant to subsection (2) shall contain a description of current or future derogations or supplementary initiatives as well as the reason for the derogation or the supplementary initia-

tives. The minute book of the board of directors shall state that the board of directors has taken a position on the derogation or the supplementary initiatives described in the report.

(4) The report pursuant to subsection (2) shall also contain a basis for the assessment by the board of directors of whether the undertaking has appropriate staff resources, both competences and numbers, appropriate IT systems and support, including in connection with risk management, as well as whether the undertaking has appropriate procedures for rapid and effective communication across the undertaking.

5.-(1) On the basis of the risk assessment carried out in pursuance of section 4(1), the board of directors shall adopt the relevant policies and contingency plans etc. including:

- 1) Credit policy, including for possible participation by the undertaking in securitisation activities, cf. Annex 1.
- 2) Market risk policy, cf. Annex 2.
- 3) Policies to manage operational risk, cf. Annex 3.
- 4) Policies for covering risks by insurance.
- 5) Liquidity policies, including a contingency plan in the event of inadequate or non-existent liquidity, cf. Annex 4.
- 6) IT security policy, cf. Annex 5, including an IT contingency plan.
- 7) Contingency plans for other serious operational problems.

(2) The content of the policies shall be determined according to the nature of the undertaking, its size and business model, the complexity of business activities, the interplay between the individual risk areas, the undertaking's overall willingness to take risks and capital position, legislation and market conditions. The policies shall contain the overall strategy goals of the undertaking for the relevant risk area and instructions on how these goals are to be achieved in the form of statements of methodology or means. Finally, the policies etc. shall contain provisions on how often and in what manner the board of directors is to be informed of non-compliance with the individual conditions and strategic goals in the individual policies.

(3) The policies etc. prepared pursuant to subsection (1) nos. 1-2 and 4-6 shall, as a minimum, contain provisions on the risk profile of the undertaking and the desired level of risk for the individual risk area, cf. section 2(1), no. 2.

(4) The board of directors shall adapt the policies adopted to material changes in the premises on which these are based. The board of directors shall no less than once a year, however, assess and update the policies adopted.

6.-(1) On the basis of the risk assessment carried out in pursuance of section 4(1), and the policies adopted in pursuance of section 5, the board of directors shall provide the board of management with written guidelines.

(2) The guidelines pursuant to subsection (1) shall state which transactions the board of management may carry out as part of its position, which decisions the board of management may take followed by a briefing of the board of directors, and which transactions require a decision by the board of directors.

(3) The board of directors may not delegate to the board of management authority which belongs to the overall management duties of the board of directors or which is otherwise of an unusual nature or of material significance for the undertaking, cf. section 117(1) of the Companies Act. For an undertaking subject to this Executive Order, the following authorities shall not be delegated to the board of management:

- 1) Decisions on outsourcing significant areas of activity.

- 2) Authorising unusual or significant exposures, cf. however, section 117(1), 4th and 5th clauses of the Companies Act and exposures covered by section 78 of the Financial Business Act.
- 3) The annual review of large assets and liabilities, cf. the principles of section 115, no. 1 of the Companies Act.
- 4) Employment of the board of management and the chief internal auditor.
- 5) Decisions on principles for calculating risks, cf. section 7(1), no. 4, including use of internal models which are not covered by no. 6.
- 6) Decisions on applications for approval of internal models to calculate the solvency of the undertaking, including:
 - a) VaR models, cf. section 40 of the Executive Order on Capital Adequacy.
 - b) AMA models, cf. section 57 of the Executive Order on Capital Adequacy.
 - c) EPE models, cf. section 49 of the Executive Order on Capital Adequacy.
 - d) Application of the IRB method, cf. section 19 of the Executive Order on Capital Adequacy.
- 7) Decisions on the individual solvency need of the undertaking, cf. sections 124(4) and 125(7) of the Financial Business Act.

7.-(1) Guidelines pursuant to section 6(1) and (2) shall

- 1) be in accordance with the policies and risk profile adopted by the board of directors for the individual risk areas,
- 2) observe the limits set in legislation,
- 3) contain controllable limits for the size of the risks the board of management is authorised to take on behalf of the undertaking,
- 4) lay down principles for how utilisation of the limits for each type of risk is calculated, including how the risk originating from financial instruments and funds which are managed on behalf of the undertaking by external portfolio managers is incorporated in the overall risk calculations,
- 5) determine the extent to which, and to whom the board of management may delegate the authorities granted in the guidelines, and
- 6) stipulate how often and in which form the board of directors wishes to receive reports pursuant to subsection (6).

(2) The limits in the guidelines shall state unambiguously the size of the individual limit stipulated for risk, for example as absolute figures or by relating the risk to the own funds or capital base of the undertaking.

(3) Only in exceptional circumstances may the guidelines allow for the board of management to manage risks of a size outside those that are stipulated in the risk profile and the limits in the guidelines, and only if the preconditions for this are stated in the guidelines. If these preconditions cannot be stipulated, prior authority to exceed the limits in the guidelines may not be granted to the board of management.

(4) In their formulation of the guidelines for the board of management, the board of directors shall ensure that the chief executive officer or the board of management collectively possess the knowledge and experience necessary to use authority stated in the guidelines in a manner appropriate for the undertaking.

(5) If the policies etc. pursuant to section 5 and the guidelines pursuant to subsection (1) are contained in the same document, it shall be clear which provisions relate to the policy for a risk area and which provisions relate to the guidelines for the board of management.

(6) The guidelines shall state that reports for the board of directors shall cover all the areas for which the board of directors has stipulated limits for the board of management or for which limits have been laid down in legislation. Reports shall state therefore whether limits laid down

in legislation have been observed. The reports shall state the extent to which the limits for risk stipulated by the board of directors have been utilised both at the reporting date and over time, including whether the limits have been exceeded. Finally, if relevant, the reports shall include a basis for assessment by the board of directors of the reliability of the models used. Decisions by the board of directors on the reports received shall be recorded in the minute book.

(7) Reports pursuant to subsection (6) shall also include funds, and risks originating from funds, which are managed by external portfolio managers, as it is still the responsibility of the board of directors, cf. section 2(2), final clause of the Executive Order on outsourcing significant areas of activity, that funds managed by external portfolio managers, as well as other funds, are together placed within the guidelines stipulated by the board of directors and are in accordance with legislation.

Organisation of work by the board of directors

8. The board of directors shall organise its work in accordance with the legislation such that sound and prudent management of the undertaking is ensured, cf. Annex 6.

Part 3

Tasks and responsibilities of the board of management

9.-(1) The board of management shall be responsible for the day-to-day management of the undertaking in accordance with provisions in legislation, including the Companies Act and the Financial Business Act, the policies etc. adopted by the board of directors, cf. section 5, the guidelines issued by the board of directors, cf. sections 6 and 7, and any other oral or written instructions from the board of directors.

(2) The board of management shall also ensure that the undertaking operates in accordance with the requirements of this Executive Order.

(3) The board of management shall ensure that the policies and guidelines adopted by the board of directors are implemented in the day-to-day operations of the undertaking.

(4) The board of management shall forward all relevant information to the board of directors.

(5) The board of directors has day-to-day management responsibility for ensuring that the undertaking only accepts risks, the consequences of which the management and employees may assess to the extent necessary.

(6) The board of management shall approve the procedures of the undertaking or appoint one or more persons or organisational entities with the necessary specialist knowledge to do this, cf. section 17. If approval of the procedures of the undertaking is carried out by several persons or organisational entities, the board of management or one of the persons or organisation entities appointed by the board of management shall be responsible for ensuring that all relevant activities are described in the procedures, cf. section 18.

(7) The board of management shall lay down a policy for the initiatives to be implemented in the event of key employees leaving the undertaking.

(8) The board of management shall approve the guidelines of the undertaking for development and approval of new products which may impose material risks on the undertaking, counterparties or customers, including changes to existing products by which the risk profile of the product is changed significantly, cf. section 28.

Part 4

Organisation and allocation of responsibilities

Tasks and resources

10.-(1) The undertaking shall be organised in organisational entities with clearly defined tasks and all employees shall have clear authority, responsibilities and lines of reference.

(2) Each organisational entity shall be staffed by employees with relevant competences at a suitable level. The number of employees, together with their competences, shall ensure that the entity can carry out its tasks adequately.

(3) If, because of the size of the undertaking or area of responsibility, organisational entities cannot have an adequate number of employees to carry out tasks in the event of ordinary or extraordinary absenteeism, tasks may be carried out by employees in other organisational entities. As far as possible, procedures, descriptions of processes, or similar for the organisational entities involved shall state which employees, groups of employees or other organisational entities are to carry out which tasks for the relevant entity and under which conditions this is to be.

Information for the board of directors and other management levels etc.

11. The undertaking shall be organised so that all relevant information reaches the board of directors and the board of management at other organisational levels within time schedules and in a form which ensures that the measures necessary can be initiated without undue delay.

Segregation of duties

12. The undertaking shall be organised so that responsible entities do not refer to a manager who is responsible for entities which carry out settlement, return and risk calculations, internal control or reporting.

13.-(1) The organisation of the undertaking shall be such that there are clearly defined reporting lines.

(2) Settlement, preparation of return and risk calculations, internal control or reporting may be carried out in the same entity unless, in the specific case, this cannot be regarded as appropriate, for example because of the nature of the other tasks of the entity.

14. In undertakings in which segregation of duties is not maintained in accordance with sections 12 and 13, cf. section 1(3), adequate compensatory measures shall be introduced which ensure that the undertaking is not imposed unnecessary risks or losses.

Part 5

Administrative and accounting practices

Administrative practices

15.-(1) The undertaking shall be organised such that individual entities and employees have at their disposal the procedures, descriptions of processes, contingency plans, systems and other tools necessary to carry out their duties, cf. sections 17 and 18.

(2) The following shall be clear:

- 1) what tasks are to be carried out,
- 2) how the tasks are to be carried out,
- 3) the extent to which completed tasks are to be documented,
- 4) the form of such documentation,
- 5) where such documentation is to be stored,
- 6) how long such documentation is to be stored,
- 7) to whom documentation is to be forwarded, if relevant, and
- 8) where previous documentation can be found.

(3) Work in the individual entity shall be planned so as to ensure that time limits are complied with, whether these be internal or consequential upon the regulations to which the undertaking is subject.

Accounting practices

16. The undertaking shall have good accounting practices. This includes,

- 1) that the undertaking can document that published annual and interim reports, including all individual items and notes, have been prepared in accordance with the regulations applicable for the relevant reports, and
- 2) that the undertaking obtains necessary information for use in the preparation of annual and interim reports, including all relevant information necessary to determine items based on accounting estimates.

Part 6

Procedures

17. The undertaking shall have procedures or descriptions of processes etc. for all significant areas of activity, which have been approved in accordance with section 9(6). Activities relating to the undertaking in its capacity as a financial undertaking, shall, as a general rule, be regarded as significant.

18.-(1) Procedures, descriptions of processes etc. shall as a minimum:

- 1) be accessible and clear,
- 2) describe satisfactorily the activities to be carried out, including ensuring that legislation and other relevant regulation as well as policies and guidelines decided by the management of the undertaking are complied with and followed,
- 3) state which organisational entity, persons or groups of persons are to carry out the individual tasks and sub-tasks,
- 4) if relevant, state a time limit within which tasks are to be carried out,
- 5) contain provisions on what aspects are to be reported and to whom,
- 6) contain provisions on how employees are to act in the event of an employee becoming aware of risks associated with his work or other areas of activity which have not been described,
- 7) contain provisions on how employees are to act in the event of operational problems, including systems break-down,
- 8) refer to relevant manuals or more detailed descriptions of processes.
- 9) state who is responsible for preparing and updating procedures,
- 10) be updated regularly for changes in internal conditions or in relevant regulation, and
- 11) be dated.

(2) The procedures shall, to a relevant extent, reflect the policies adopted by the board of directors, cf. section 5(1).

(3) Notwithstanding the structure of the procedures, it shall be ensured that all relevant conditions are described and that it is clear who is responsible for carrying out the individual tasks correctly. Therefore, a procedure may relate to tasks in an individual organisational entity, cover all tasks in connection with one or several products, or relate to inter-departmental tasks which require the involvement of more than one organisational entity.

(4) Procedures may be stored electronically. If this is the case, it shall be ensured that employees have access to adequate information and procedures, including contingency plans, to carry out the tasks necessary in the event that the electronic procedures are not accessible.

Part 7

Risk management and compliance

Chief risk officer and risk management function

19.-(1) The board of management shall appoint a chief risk officer who shall be responsible for ensuring that risk management in the undertaking is carried out appropriately, including that an overview is established of the risks of the undertaking and the overall risk profile. The chief risk officer shall refer directly to the board of management. If the chief risk officer is dismissed, the board of directors shall be informed about the dismissal and the reasons for it. In smaller undertakings the chief risk officer may be a member of the board of management.

(2) If the board of management of the undertaking deems that the size, organisation or nature of activities of the undertaking make it unreasonable or unnecessary to appoint an employee without other areas of responsibility than risk management and thereby establish an independent risk management function, an employee responsible for internal control of one or more risk areas may be appointed as the chief risk officer. The board of management shall inform the board of directors and give reasons for a decision not to appoint an independent risk management function and it shall be able to document that risk management in the undertaking can take place appropriately.

(3) In the circumstances mentioned in subsection (2) it shall be clear, for example from the function description and procedures, which tasks fall within the chief risk officer's function as chief risk officer.

20.-(1) The area of responsibility of the chief risk officer shall include the activities of the undertaking involving risk across risk areas and organisational entities as well as the risks originating from outsourced functions.

(2) The chief risk officer shall have adequate knowledge and independence to be able to assess the risks of the undertaking.

(3) The chief risk officer shall have opportunity to make a statement on the risk associated with intended large and unusual transactions. If the chief risk officer advises against a transaction, the chief risk officer shall inform the board of management of this immediately and in writing.

(4) If the board of management wishes to carry out a transaction notwithstanding the assessment of the chief risk officer, the board of management shall inform the board of directors

immediately about the statement by the chief risk officer so that the board of directors may take a position, unless it is not possible to await the decision by the board of directors without significant detriment to the undertaking. In this case, the board of directors shall be informed of the transaction and the assessment of the chief risk officer as soon as possible.

(5) The chief risk officer shall, as a minimum, have opportunity to make a statement in connection with preparation of the basis for decisions by the board of directors on the risk profile etc. of the undertaking mentioned in section 4(2).

21.-(1) The chief risk officer shall have at his disposal a sufficient number of people with relevant competences and authority to make it possible for the chief risk officer to identify, assess, follow up, and make a decision on the undertaking's risk profile, principles for calculating risks, models applied as well as the risk exposure overall and in the individual risk areas.

(2) If the undertaking decides to have risk management for individual risk areas placed in organisational entities outside the risk management function, the board of management shall ensure that the undertaking has procedures and internal controls etc. to ensure that all relevant information on the risk area is forwarded to the risk management function or, in the situations mentioned in section 19(2), the chief risk officer, for use in their assessment and follow-up of the overall risks of the undertaking. Function descriptions and procedures etc. shall also clearly define which tasks are the responsibility of the risk management function, and which fall within risk management of the individual activity or risk area.

Compliance

22.-(1) The undertaking shall have methods and procedures which are suitable to identify and reduce the risk that the undertaking is imposed sanctions, suffers detrimental impact on its reputation, or that the undertaking or the undertaking's customers suffer material financial loss as a consequence of non-compliance with the current legislation, market standards or internal regulations for the undertaking (compliance risks). When complying with the 1st clause the undertaking may take account of the nature, scope and composition of its activities.

(2) The undertaking shall have a compliance function which acts independently and which shall check and assess whether the methods and procedures pursuant to subsection (1), 1st clause and the measures taken to correct any deficiencies are effective.

(3) In undertakings which are securities dealers and which are not covered by section 23, the compliance function shall, for that part of the activities associated with securities trading, carry out compliance and provide guidance and assistance for the persons who are responsible for providing investment services and carrying out investment activities pursuant to section 4(1)-(3) of the Executive Order on the organisational requirements and terms for operating as securities dealers.

(4) In order to ensure that the compliance function can manage its areas of responsibility correctly and independently, the undertaking shall ensure that the following conditions are met:

- 1) the compliance function shall have the necessary resources, the necessary competences and expertise as well as access to all relevant information.
- 2) An employee shall be responsible for the compliance function and reporting to the board of directors and board of management no less than once a year on the conditions dealt with in this provision.
- 3) Employees who are involved in the compliance function may not participate in providing services or performing activities they control.
- 4) The method of setting remuneration for employees in the compliance function shall not jeopardise their independence.

(5) The provisions of subsection (4), nos. 3 and 4 shall not apply, if it can be documented that these requirements are not reasonable in relation to the nature, scope and composition of the activities of the undertaking.

(6) In small undertakings or undertakings with straightforward activities, the same person may be the chief risk officer, cf. section 19(1) and responsible for the compliance function. It shall also be ensured, however, that employees are not involved in performance of the tasks they control as part of their compliance tasks.

23. The provisions of sections 19-22 shall not apply to undertakings which only have a licence as investment companies.

Delegation of authority

24.-(1) If the board of management delegates authority in accordance with the guidelines received from the board of directors, cf. sections 6 and 7, this shall be either in writing or electronically.

(2) If the authority delegated by the board of management so allows, the recipient of the authority from the board of management may also delegate this authority, in full or in part, in writing or electronically.

(3) Delegation of authority may only be to employees who have the necessary knowledge, insight and experience to exercise the authority received appropriately, cf. section 10(2).

(4) If authority is surrendered electronically by using electronic media, the surrenderer and recipient, the time and date, and the scope of the surrender as well as receipt of the authority shall be documented. The procedure shall be described in the procedures.

(5) Delegated authority shall, as a minimum, state:

- 1) the nature and scope of the authority delegated,
- 2) the principles for determining utilisation of authority,
- 3) which products or transactions the authority covers,
- 4) any supplementary limits for the risk as well as principles for determining the authorities that meet the requirements of section 7(1), nos. 3 and 4, and
- 5) how, how often and by which person or organisational entity reporting is to be carried out to the surrenderer of the authority and if relevant, others.

(6) No one may delegate authority which exceeds the authority the person in question himself has received. Furthermore, total authority delegated, including authority given to groups of employees, may not exceed the authority contained in the guidelines of board of directors to the board of management.

(7) If there are supplementary risk targets in connection with delegated authority, the person who surrenders the authorities shall ensure that application of the supplementary risk targets is such that it ensures that the other authorities allocated are not exceeded.

Controls

25.-(1) The undertaking shall control all material risk-associated tasks, including:

- 1) Compliance with all limits laid down by the board of directors in the guidelines given to the board of management pursuant to section 7(1), no. 3 and limits in legislation.
- 2) Compliance with delegated authority.

- 3) Transactions, where the undertaking acts under a power of attorney from a customer or counterparties and where the undertaking has undertaken to comply with limits for risks, including placement limits.
- 4) Transactions, where the undertaking has undertaken to comply with limits for risks agreed with counterparties, for example in framework contracts on trading in financial instruments.
- 5) Other tasks, which for some other reason may involve material financial risks or other material risks for the undertaking, including management of the accounts of the undertaking and tasks in connection with establishing or preparing the basis for financial statements and determining the individual solvency need of the undertaking.

(2) Control shall be carried out by another unit than that which has carried out the task, cf. section 12. Section 12 shall not apply, however, for controls such as reconciliation, monitoring compliance with procedures, error detection or similar. Such controls may therefore be carried out by persons in the same organisational unit, unless this is not appropriate in the specific situation.

(3) Controls covered by subsections (1) and (2) shall be carried out at suitable intervals, depending on the size of the undertaking, the significance and size of the individual risk in relation to the undertaking's business model and area of activities, the complexity of the relevant risks and the capital position of the undertaking. The controls shall include intra-day compliance with limits when transactions regularly take place over more than one day. Intra-day controls may be on a sample basis, when this is appropriate.

(4) The undertaking shall have suitable monitoring that administrative tasks are carried out in an appropriate and uniform manner, and that procedures, descriptions of processes etc. are complied with.

Reporting

26.-(1) Regular written reports shall be issued at all relevant management levels on compliance and utilisation of all limits for risk assumption contained in the guidelines pursuant to section 6 or in the authority transferred. Reports shall also be issued on compliance with the limits laid down in legislation for risk in the area, where this is relevant for the undertaking. Reporting shall also cover risks managed on behalf of the undertaking by portfolio managers.

(2) Reports shall be clear and concise and provide the board of directors, board of management and other employees who have transferred authority, cf. section 24, information on both the current utilisation of the limits laid down and on utilisation over time.

(3) In the event that the undertaking utilises internal models to calculate risks, reporting shall also include relevant back tests as documentation of the reliability of the models.

(4) Reporting to the board of directors shall be at the intervals stated in the guidelines, cf. however, Annex 1, point 25. Furthermore, as a minimum, transgressions shall be reported at each meeting of the board of directors, and reports shall be issued, if the conditions on which the individual limits for risks are based are changed significantly for example as a consequence of market unrest, extraordinary losses, changed capital position etc.

(5) Reporting on delegated authority, including incidents when these are exceeded, shall be to the person who has allocated the authority, at intervals which reflect the surrenderer's involvement in the daily transactions and which are stated in the authority. Incidents of exceeding authority shall normally be reported no later than the day after the incident was ascertained.

27.-(1) Reports shall be issued on other significant aspects which are not covered by the authority stipulated in the guidelines or in the delegated authority, cf. subsection (2). For example, this may be reporting regarding reconciliation errors, irregularities, losses arising from operational conditions, accounting or budgeting errors, resignation of key persons etc.

(2) The procedures of the undertaking shall, as far as possible, contain instructions on what shall or should be reported and to whom, including whether, in exceptional circumstances, reporting may or shall be to other persons than the immediate manager of the person in question or the manager's manager.

New products

28. The guidelines approved by the board of management for development and approval of new services and products, including changes to existing services and products whereby the risk profile of the services and products is changed significantly, see section 9(8), shall as a minimum,

- 1) specify as far as possible when a product or service is "new".
- 2) state which organisational entitie(s), committee(s) or ad hoc committee(s) are to manage the development process, possibly divided by risk area.
- 3) contain guidelines for whom, as a minimum, is to be involved in the development process in order to ensure that all relevant aspects are described.
- 4) contain guidelines for what general conditions are to be analysed and documented, including the nature, size and calculation of risks for the undertaking, effects on the costs and revenues of the undertaking, the possibilities of the undertaking to operate in new markets, the effects on the solvency of the undertaking, accounting treatment, and
- 5) contain requirements that the analysis shall confirm that the undertaking has sufficient expertise, systems, capital and resources otherwise to manage the new product or service adequately.
- 6) contain provisions on guidelines which establish that new products and services, which may involve significant new risks for the undertaking or customers, shall be submitted to the board of directors for their decision on whether utilisation of the new product implies changes to the policies adopted pursuant to section 5 or the guidelines issued pursuant to sections 6 and 7, including establishment of special principles for calculation of the risks associated with the product.

29.-(1) The chief risk officer shall participate, or as a minimum be consulted, in connection with development and approval of new products. The chief risk officer shall be informed regularly about the progress of the approval process.

(2) The chief risk officer shall be consulted in connection with the decision on whether the scope of a change in existing products means that the change shall be subject to the requirements for development and approval of new products. The chief risk officer shall at all times be able to demand that a change to an existing product be treated as a new product.

Part 8

Penalty provisions

30.-(1) Violation of sections 2-8; section 9(3) and (4), (6), 1st clause and (7) and (8); section 10(1) and (2), and (3), 2nd clause; sections 12-16; section 17, 1st clause; section 18(1) and (2), (3), 1st clause, and (4), 2nd clause; section 19(1), 1st-3rd clauses, (2), 2nd clause, and (3); section 20(2)-(5); section 21; section 22(1), 1st clause, (2)-(4), and (6), 2nd clause; section 24(1) and (3)-(7); section 25(1), (2), 1st clause, (3), 1st and 2nd clauses, and (4); section 26; section 27(1), 1st clause and (2); section 28 and section 29 shall be subject to a fine.

(2) Companies, etc. (legal persons) may incur criminal liability under the rules of Chapter 5 of the Criminal Code.

Part 9

Entry into force and transitional provisions

31.-(1) This Executive Order shall enter into force on 1 January 2011, cf. however, subsection (3).

(2) At the same time Guidelines no. 10114 of 22 December 2006 for banks pursuant to section 71(1), nos. 1-8 of the Financial Business Act, Guidelines no. 10118 of 22 December 2006 for mortgage-credit institutions pursuant to section 71(1), nos. 1-8 of the Financial Business Act, Guidelines no. 10117 of 22 December 2006 for investment companies pursuant to section 71(1), nos. 1-8 of the Financial Business Act and guidelines no. 10115 of 22 December 2006 for investment management companies pursuant to section 71(1), nos. 1-8 of the Financial Business Act shall be repealed.

(3) Section 5(1), no. 3, sections 19-22 and Annex 3 shall enter into force on 1 July 2011. The Danish FSA may give undertakings covered by this Executive Order a deadline up to 1 July 2011 to submit documentation that the requirements of this Executive Order have been fulfilled.

Danish Financial Supervisory Authority, 1 December 2010

Ulrik Nødgaard
Director General

/Stig Nielsen

Credit area

Tasks and responsibilities of the board of directors

Credit policy

- 1) On the basis of a prudence principle, the board of directors shall adopt a credit policy, cf. section 5(1), no. 1. Depending on the type and size of the financial undertaking, as well as the complexity of the undertaking's activities subject to credit risk, the credit policy shall contain the decision on what credit-risk profile the board of directors want the undertaking to have.
- 2) The credit policy shall contain principles for the size, type and scope of credit risks, including principles for:
 - a) Types of customers (e.g. corporate customers, private customers, wealthy customers, full customers etc.).
 - b) The types of products that the undertaking wants to offer, including interest-rate and repayment profiles wanted by the undertaking.
 - c) The extent to which and under what circumstances the undertaking wants large exposures that for instance exceed 5% or 10% of the capital base.
 - d) The extent of concentration risk within the corporate and private segments, including maximum exposures within different sectors and other similar types of risk, where the risk concentration of the undertaking is significant.
 - e) Geographical exposure, including the undertaking's maximum exposure within selected geographical areas.
 - f) The undertaking's maximum exposure based on selected types of collateral.
 - g) The financial undertaking's earnings in relation to the chosen risk profile, including product pricing etc.
 - h) Any leasing activities, including which main categories of assets the undertaking intends to lease out, terms and the maximum residual values.
 - i) Any exposures within securitisation activities.
 - j) Any intra-group granting of credit, if the undertaking is part of a group.
- 3) The credit policy shall also contain principles for management and control of credit risks, including principles for:
 - a) The decision basis and risk analyses before a credit facility is approved.
 - b) The customer's financial situation, including earnings capacity and capital position.
 - c) The size of any own share of financing by the borrower.
 - d) Collateralisation, including valuation and the marketability of the collateral.
 - e) Consolidation of exposures to connected clients.
 - f) Loan-financed investment products, including for surplus coverage, stop-loss clauses, marketability of the securities, terms and risk diversification.
 - g) Staff loans, including for collateralisation, if these deviate from the general credit-policy principles.
 - h) Classification of the customers of the undertaking, including any use of models for this purpose.
 - i) Management of exposures with particularly high risk as well as exposures in distress.
 - j) Identification of exposures showing signs of weakness, including stipulating a strategy for the onward process.
 - k) The impartiality of the employees.
 - l) The internal control system for the credit area.
- 4) In connection with its review, cf. section 6(3), no. 3, the board of directors shall review the most important exposures of the undertaking. Amongst other things, during its review the board of directors shall assess the risk and the strategy for the individual exposure, includ-

ing decision on the need for follow-up. During the review the board of directors shall also assess the accounting treatment of the exposure.

The guidelines from the board of directors to the board of management for the credit area

- 5) The guidelines for the board of management for the credit area pursuant to sections 6-7 shall, in addition to the general requirements of sections 6-7, realise the credit policy in specific guidelines for the board of management and shall contain provisions on:
- a) The size of the exposures the board of management can approve without participation by the board of directors.
 - b) How exposures are calculated according to the limits in the guidelines.
 - c) The authority of the board of management to approve exposures in urgent cases.
 - d) The authority to approve debt reduction/respice, 0-interest rate, write-offs, release of collateral and assessment of impairment losses on loans, and provisions on guarantees.
 - e) The limit for exposures which the board of management may approve, but which shall be submitted to the board of directors for their information.

Tasks and responsibilities of the board of management for the credit area

- 6) The report which the board of management shall prepare pursuant to section 4(2) shall contain an account of how the credit policy is realised in the credit risks accepted by the undertaking. In the report, the board of management shall also make a reasoned assessment of whether the credit risks of the undertaking have been calculated fully and prudently, including whether the methods applied for classification are capable of ranking customers correctly. The report shall include a review of the internal controls carried out as well as the results of these. In addition the report shall include the results of the annual review of exposures which are not covered by the review by the board of directors pursuant to section 6(3), no. 3.
- 7) The board of management shall ensure that, on the introduction of new products with credit risks and on significant changes in existing products which increase the credit risks of the undertaking, cf. section 28, these are properly included in the undertaking's organisation, including in the procedures of the undertaking, its risk management, reporting and internal controls.
- 8) The board of management of undertakings, which administer revolving securitisation transactions subject to an early amortization provision, shall ensure that the relevant organisational entities prepare liquidity plans in order to take account of the effects of both repayment at maturity and repayment before maturity.

Organisation and allocation of responsibilities for the credit area

Segregation of duties

- 9) For the credit area, segregation of duties shall be established, cf. sections 12-14, between persons, groups of persons and organisational entities responsible for approving and establishing credit facilities on the one hand, and persons, groups of persons and organisational entities responsible for control and reporting on the other hand.

Procedures for the credit area

Procedures for approving exposures

- 10) A bank shall have procedures for approving exposures, which for foreign activities of the bank shall take account of the local market conditions and which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain principles for:
- a) The basis for decisions for approvals regarding:
 - Assessment of the borrower's creditworthiness, including ability and willingness to meet obligations in the event of deterioration in the borrower's financial situation.
 - Information about the borrower's current and future earnings and capital position.
 - For corporate customers, also information on relevant group connections, including financial information about groups and group companies.

- An overall risk assessment of every type of project, e.g. the risk in managing, controlling, financing, performance and completion.
- For private customers also information included in the calculation of the borrower's actual wealth debt ratio/leverage as well as expendable income calculated under the assumption of traditional fixed-interest financing.
- For private customers who purchase real property, also information about the customer's financial position after the purchase.
- Description and assessment of collateral provided.
- Information about the guarantors' current and future earnings and capital position.
- Information about the main shareholders'/owners' current and future earnings and capital position.
- Information on how the exposure is to be repaid and interest is accrued.
- Analysis of the possibilities of the borrower to make earlier repayment and pay a higher interest rate.
- Other information relevant to the undertaking's assessment of the risk and repayment of the exposure.
- The undertaking's risk analysis, including a calculation of the risk of losses on the exposure and an estimate of the risk the exposure will become distressed.
- The overall assessment of the undertaking as well as a decision on whether the expected earnings are appropriate in relation to the risk the undertaking is accepting with the approval.
 - b) The board of management's approvals in urgent cases, including that the number of these should be limited as far as possible.
 - c) Documentation of each approval of a credit facility in the form of a decision basis, cf. item a).
 - d) In which circumstances the undertaking requires collateralisation, including the types of collateralisation the undertaking requires, e.g. mortgage collateral when financing assets and guarantees from primary shareholder.
 - e) How collateral is to be valued, including that these shall be valued prudently taking into account current market conditions.
 - f) How stop-loss clauses are to be set when approving exposures which contain collateralisation in securities or positions in derivatives.
 - g) Regular reassessment of the principles for valuation of the collateral.
 - h) Building loans, including requirements for a qualified building inspection and how payment of instalments is to be made as construction is completed.
 - i) Financing property-development projects, including on own financing, and selling or letting a specific percentage before the project commences.
 - j) To what extent utilisation of rating or credit scoring can reduce the requirements for the remaining decision basis in situations where the undertaking uses ratings or credit-score models in connection with the assessment of borrowers.
 - k) How exposures are calculated, including in particular:
 - How exposures are calculated pursuant to section 145 of the Financial Business Act and the Executive Order on Large Exposures.
 - How exposures with market risks are included in the exposure.
 - How counterparty risk from derivatives is included in the exposure.
- 11) A mortgage-credit institution shall have procedures for approving exposures which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain provisions on:
 - a) That for each approval of credit facilities there shall be documentation in the form of a decision basis.
 - b) That real property be valued in accordance with relevant legislation.
 - c) The board of management's approvals in urgent cases, including that the number of these should be limited as far as possible.
 - d) Use of rating and credit scoring, where relevant.
 - e) How exposures are calculated, including in particular:

- How exposures are calculated pursuant to section 145 of the Financial Business Act and the Executive Order on Large Exposures.
- How exposures with market risks are included in the exposure.
- How counterparty risk from derivatives is included in the exposure.

Procedures for continuous monitoring of exposures and credit risks in general

- 12) A bank shall have procedures for regular monitoring of exposures which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain principles for:
- a) Treatment of overdrafts and arrears on exposures.
 - b) Annual prolongation of the undertaking's larger exposures.
 - c) Follow-up of individual exposures, including review of accounting material, annual tax returns and budgets etc. from the borrowers and guarantors etc.
 - d) Regular complete, updated and prudent valuation of collateral.
 - e) Monitoring of customers' positions in securities and derivatives, including compliance with stop-loss clauses.
 - f) Monitoring of building loans, including on a qualified building inspection and payment of building instalments as construction is completed.
 - g) Monitoring of property-development projects.
 - h) The regular valuation of pledged mortgage deeds, including adjustments for defaulted mortgage deeds, monitoring the specified loan to value ratio relevant for the exposure, as well as the diversification in the mortgage deeds, order of priority, structuring, other contents, and marketability of the mortgage deeds and on the administration of the pledged mortgage deeds.
 - i) Correct, regular classification of exposures, including prompt and correct identification of the undertaking's weak exposures.
 - j) Identification and management of exposures with higher risks which involve special requirements for systematic and prompt follow-up.
 - k) Identification and management of weak and distressed exposures as well as exposures with impairment losses and provisions which involve special requirements for systematic and prompt follow-up.
 - l) Identification and management of large exposures.
 - m) Follow-up on the undertaking's concentration risks, including concentrations within specific sectors, concentrations within specific types of collateral and concentrations within large exposures.
- 13) A bank, which has a licence to issue covered bonds, shall also have procedures with provisions on regular monitoring of LTV and on calculating and providing supplementary collateral pursuant to legislation.
- 14) A mortgage-credit institution shall have procedures for regular monitoring of exposures which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain provisions on:
- a) Treatment of arrears on exposures.
 - b) How follow-up of individual exposures is to be carried out, including review of accounting material, annual tax returns and budgets etc. from the borrowers and guarantors etc.
 - c) Regular monitoring of LTV.
 - d) Calculation and establishment of supplementary collateral pursuant to legislation.
 - e) Correct, regular classification/rating of exposures, including provisions which promptly and correctly identify the undertaking's weak exposures.
 - f) Identification and management of exposures with higher risks which involve special requirements for systematic and prompt follow-up.
 - g) Identification and management of weak and distressed exposures as well as exposures with impairment losses and provisions which involve special requirements for systematic and prompt follow-up.
 - h) Identification and management of large exposures.

- i) Follow-up on the undertaking's concentration risks, including concentrations within specific sectors, concentrations within specific types of mortgaged property and concentrations within large exposures.
- 15) An undertaking shall have procedures which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain:
- a) Descriptions of the undertaking's internal control system for the credit area.
 - b) Which internal controls are to be carried out, including the scope and frequency of the internal controls.
 - c) What reporting is to be carried out for individual exposures and at portfolio level, including the scope and frequency of reporting for all levels of the undertaking.
 - d) How the annual review of exposures, which are not covered by the review by the board of directors pursuant to section 6(3), no. 3, are to be carried out, including at what levels of the organisation the review is to take place and how reporting of the result is to be made.

Procedures for risk classification of customers

- 16) An undertaking shall have procedures for risk classification of the undertaking's customers by using models or in some other way. The procedures for portfolios, which are not covered by an IRB licence from the Danish FSA, in addition to the general requirements of sections 17-18 shall, as a minimum, contain:
- a) Provisions on the factors which characterise a customer with high risk, and which factors characterise a customer with normal and low risk, respectively, for the undertakings which do not use models to classify customers.
 - b) Precise descriptions of both models and regulations adopted, including what scales that describe the customer's classification for the undertakings which use models to classify customers.
 - c) Provisions ensuring that the classification of customers by the undertaking does not give an overly positive view of the risk.
 - d) Provisions ensuring that the ongoing control and regular tests by the undertaking of the classification are thorough and well documented.

Particularly on procedures in connection with mortgaging real property

- 17) A bank shall have procedures for mortgaging real property, including pledging mortgage deeds, which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain principles for:
- a) Prudent valuation of mortgages in real property, including regular reassessment of the valuation taking into account current market conditions.
 - b) How the prudent valuation of mortgages in real property is calculated and what current information shall, as a minimum, be available in the undertaking and be included in the assessment, including regarding:
 - The address, post code and property category of the property, including a brief description of the property (possibly Danish Building and Housing Register information).
 - The size of the property (office, warehouse, shop etc.).
 - Operation of rented property, including gross rent, net rent, required yield, risk of reductions in rent, risk of further vacant property, current and future operating expenses.
 - Costs of necessary investments.
 - Most recent purchase date and transaction price.
 - Current and realisable market price, if the property must be sold within six months.
 - Estimated sales costs.
 - Primary preferential claims in terms of actual remaining debt and lending terms.
 - c) The types of costs to be deducted in connection with realisation of collateral in real property.
 - d) Regular monitoring of the loan to value ratio for pledging mortgage deeds in real property, requirements for the diversification, order of priority, structure, other contents and marketability of the mortgage deeds as well as provisions on appropriate administration of the pledged mortgage deeds.

Particularly on procedures for securitisation activities

- 18) An undertaking with securitisation activities shall have procedures for this which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain:
- a) provisions on how the undertaking is to assess and reduce risks from securitisation transactions, if these are organised or financed by the financial undertaking, including reputational risks which may arise in connection with complex structures or products from securitisation transactions in which the financial undertaking is an investor.
 - b) Provisions ensuring that risk assessment and management decisions provide a fair presentation of the financial content of the transaction.
 - c) Provisions ensuring that undertakings, which organise revolving securitisation transactions subject to a provision on early amortisation, prepare liquidity plans in order to take account of the effects of both repayment at maturity and repayment before maturity.

Risk management for the credit area

Chief risk officer and risk management function

- 19) The chief risk officer shall, in addition to the general requirements of sections 19-21, ensure that appropriate management of credit risk takes place in the undertaking, including that:
- a) Approval of exposures is carried out in an appropriate manner.
 - b) There is a regular assessment of whether the undertaking has adequate resources and knowledge for appropriate follow-up and management of the credit risks of the undertaking.
 - c) Correct calculation of the undertaking's large exposures is regularly carried out.
 - d) There is prompt identification of weak and distressed exposures, and that action plans are prepared for these exposures.
 - e) There is prompt and correct classification of the exposures of the undertaking, including a test no less than once every year of whether the undertaking is able to rank its customers correctly.
 - f) Appropriate follow-up on individual exposures is regularly carried out, including in particular (where relevant), that there is:
 - Prompt treatment of overdrafts and arrears.
 - Prompt follow-up on the undertaking's exposures for investment purposes.
 - Regular assessment of the risk of losses of an exposure and the probability that an exposure (or portfolios of exposures) will become distressed.
 - Regular follow-up of the valuation of the collateral provided.
 - Regular monitoring of property development projects and financing of construction loans.
 - Regular monitoring of the developments in pledged mortgage deeds.
 - g) There is regular assessment of whether pricing of credit risks is sound in relation to the credit risks accepted.
 - h) There is regular assessment and decision on the concentration risks of the undertaking.
- 20) The chief risk officer shall, in addition to the general requirements of sections 19-21, also ensure:
- a) That the necessary control procedures for the credit area are implemented in the undertaking, cf. section 25 and nos. 22-24 of this Annex.
 - b) That the reporting prepared by the undertaking provides a fair and sound view of the undertaking's credit risks and activities in the credit area.
 - c) That there is an annual review by the undertaking of exposures which are not covered by the review by the board of directors pursuant to section 6(3), no. 3.

Delegation of lending authorities

- 21) Delegated lending authorities shall, in addition to the general requirements of section 24, as a minimum, contain:

- a) Specific limits for the size of exposures and what types of products the recipient of the authority may approve.
- b) How exposures are calculated according to the limits of the authority.
- c) What customer categories are covered by the lending authority.
- d) Specific limits for authority to release collaterals, approve debt reduction/respice, 0-interest rate, write-offs, assessment of impairment losses on loans and provisions on guarantees.
- e) Regulations for approval of exposures with signs of weakness, including loans with impairment losses and guarantees with provisions.
- f) Specific limits for which of the approved exposures shall be reported to the delegator of the lending authority.

Controls for the credit area

- 22) The undertaking shall establish independent internal controls of all material activities in the credit area, cf. section 25. As a minimum, there shall be regular internal control that:
- a) The credit policy is complied with by the employees of the undertaking.
 - b) Lending authorities are observed.
 - c) The basis for approval, cf. nos. 10-11, is present when approving credit risk.
 - d) Exposures are established correctly, including with correct documents, observance of security perfection etc.
 - e) Exposures are calculated correctly pursuant to section 145 of the Financial Business Act.
 - f) There is the necessary follow-up on overdrafts and arrears.
 - g) There is the necessary identification of and follow-up on weak and distressed exposures.
 - h) Risk classification of customers is updated.
 - i) There is correct accounting treatment of the exposures.
 - j) Reporting within the undertaking is correct.
 - k) Other procedures for the credit area are complied with by the undertaking's employees.
- 23) The undertaking's internal controls for the credit area may be through sample reviews, if such reviews give adequate certainty that the activities in the controlled areas are appropriate.
- 24) The undertaking shall document internal controls carried out.

Reporting for the credit area

- 25) The board of directors of the undertaking shall, at least every quarter, receive reports best possibly illustrating the undertaking's observance of credit policies, cf. section 5. Reporting shall be at portfolio and sub-portfolio levels and shall, as a minimum, contain information about:
- a) The largest exposures of the undertaking.
 - b) The undertaking's exposures with higher or special risks.
 - c) The undertaking's exposures with:
 - Overdrafts.
 - Arrears.
 - Objective evidence of impairment (OEI).
 - Impairment losses on loans.
 - Provisions for losses on guarantees.
 - Write-offs.
 - d) Break-down of exposures by
 - Size.
 - Sector.
 - Type of loan.
 - Risk groups (classification/rating).
 - Geographical area.

- e) Analyses/or stress tests as well as assessment of the developments in the risk of portfolios.

Accounting practices

- 26) An undertaking which, pursuant to accounting principles is obliged to recognise amounts under »impairment losses on loans and receivables etc.« in the undertaking's annual or interim report, shall, as a minimum, always be able to document the items below. The requirements basically apply for loans valued at amortised cost, but they shall also apply correspondingly, with the necessary adjustments, for loans valued at fair value.
- a) For individually assessed loans:
- Overview of all loans of material size which, on the basis of this criterion, are assessed individually in order to identify whether there is objective evidence of impairment.
 - Overview of any loans which the undertaking assesses cannot be placed in a group and which, on the basis of this criterion, are assessed individually in order to identify whether there is objective evidence of impairment.
 - Overview of other loans which are assessed individually.
 - Overview of all loans for which the undertaking assesses there is objective evidence of impairment. For each of these loans, there shall be documentation that there is evidence.
 - Overview of all weak loans for which the undertaking assesses there is no objective evidence of impairment. For each of these loans, there shall be documentation that there is no evidence.
 - For each of the loans for which the undertaking assesses there is objective evidence of impairment, there shall be calculations of the present value of the expected future cash flows from the loan and calculations of any need for the recognition of an impairment loss.
 - For each loan for which an impairment loss is partly reversed in relation to the last financial statements, there shall be calculations of the present value of the expected future cash flows, which demonstrate that there is no longer the same need for the recognition of an impairment loss.
 - For each loan for which an impairment loss is fully reversed in relation to the last financial statements, the undertaking shall be able to demonstrate that the relevant evidence is no longer present or that one or more events have otherwise taken place which have a positive effect on the expected future cash flows.
- b) For collectively assessed loans:
- Documentation that the board of directors and the board of management have examined the results calculated using the models used for collectively assessed impairments losses. This shall include documentation that the board of directors and the board of management have corrected the model-based collectively assessed impairment losses, if it is deemed that the model has not or has not entirely taken account of all relevant aspects in relation to the accounting regulations.
 - Documentation that the group allocation of loans is carried out such that the individual group has uniform characteristics with regard to credit risks.
 - Estimates of the cash flows expected from the individual groups. The estimates and the basis for these shall be documented.
 - Description of the factors on which the undertaking's models for estimating collective impairment losses are built, including the relationships between changes in specific observable data and the need for recognition of impairment losses.
 - Overview of groups on which impairment losses have been recognised. For each of these groups, there shall be documentation that there is evidence of impairment at portfolio level as well as a calculation of the impairment losses.
 - For each group of loans for which a collectively estimated impairment loss is partly reversed in relation to the last financial statements, there shall be calculations of the present value of the group's expected future cash flows, which demonstrate that there is no longer the same need for recognising an impairment loss.
 - For each group of loans for which a collectively estimated impairment loss is fully reversed in relation to the last financial statements, the undertaking shall either document that the

relevant evidence is no longer present or that one or more events have otherwise taken place which have a positive effect on the group's expected future cash flows.

- Documentation that a back test has been performed of the models used and the calculated collective impairments, as well as the results of these tests.
 - c) For guarantees:
 - Overview of all guarantees with statement of which guarantees have been recognised as liabilities and which have not been recognised.
 - For all recognised guarantees, there shall be documentation that it is likely that the guarantee will be effective. For collectively assessed guarantees, the undertaking shall document the estimates of losses using relevant material based on experience. For individual assessment the undertaking shall document the basis for the specific qualified estimate.
 - The requirements, which appear in the two sub-points above to item c, shall not apply for the guarantees which are recognised solely because of the requirement to recognise the minimum liability. For these guarantees the undertaking shall be able to document that there is a numerical relationship between the premiums and provisions etc. received and the liabilities recognised.
 - For reversals of guarantee liabilities, the undertaking shall be able to document that it is no longer likely that the guarantee will be made effective. However, this does not apply for the guarantees which were originally recognised, because of the requirement to recognise the minimum liability. For reversals (write-offs) of these liabilities, the undertaking shall be able to document that there is a numerical relationship between the length of the period and the size of the reversal.
- 27) An undertaking's assessment of whether an impairment/value adjustment on a loan to a borrower is to be recognised in an annual or interim report shall be based on the most recent information available about the financial situation of the relevant borrower at the reporting date. This means that, if it is practicable, the undertaking shall obtain updated and audited material about the borrower (e.g. an annual report). Furthermore, the undertaking shall in other ways seek to update its knowledge about the borrower for use in its assessment at the reporting date, including budget follow-ups, interim financial statements, other accounts, minutes of meetings or telephone conversations.

Market risk

Scope and definitions

- 1) "Market risks" means risks on interest rates, currency, shares, and commodities, including related risks linked with derivative financial instruments, e.g. risks on options. Interest-rate risks include interest-rate risks on all balance-sheet and off-balance-sheet items, including on fixed-interest deposits and lending and fixed-interest funding. Interest-rate risks also include interest-structure risks.

Tasks and responsibilities of the board of directors

Market risk policy

- 2) The board of directors shall adopt a policy for which market risks the undertaking may undertake.
- 3) The policy for the market risk area shall, in addition to the general requirements contained in section 5(1), contain relevant overall instructions on the following:
 - a) what risks the undertaking includes under market risk,
 - b) the desired or acceptable level of risk overall and for the individual types of market risk, for example by stating whether the risk can be low, medium or high,
 - c) under what circumstances, for example unrest on the financial markets, the board of management shall secure a decision by the board of directors on whether the financial undertaking is to maintain the levels of risk in the market risk policy as well as the procedure for this,
 - d) any limitations with respect to which types of market risk the individual business area may accept and to what extent,
 - e) principles for the organisational division of responsibilities in the market-risk area, including for risk taking, risk management, control and reporting,
 - f) any special types of risk which the financial undertaking specifically does not want to accept, for example commodities risks, risks on spread trading or risks originating from certain structured products,
 - g) overall requirements for employee skills in the market-risk area, as well as
 - h) procedures for informing the board of directors on the market-risk policy, cf. section 5(2), final clause.

Guidelines from the board of directors to the board of management for the market-risk area

- 4) For the market-risk area, the guidelines shall meet the general requirements of section 7 and, where relevant for the financial undertaking, contain
 - a) limits for the financial undertaking's total risk on interest rates, currency, shares and commodities,
 - b) how the individual risks are calculated and how the individual instruments are included in the calculation,
 - c) limits for the particular risks linked to complex or unusual products, including risks on structured products, or to the undertaking's activities in the market-risk area otherwise, such as risks on options, interest-rate curves, spread, etc., unless these risks are of exceptional size,
 - d) statement of the purposes for which securities, currency and derivative financial instruments may be traded, e.g. risk hedging, active risk assumption or trading for customers,
 - e) which currencies or groups of currencies may be traded or taken positions in, and for what purpose such trading and positions may be,
 - f) which types of derivative financial instruments may be traded or taken positions in,
 - g) which other types of products, including structured products may be traded or taken positions in, and

- h) provisions for on what markets or trading platforms as well as in which countries or groups of countries trading may be carried out.
- 5) For mortgage-credit institutions and banks with a licence to issue covered bonds, the policy and guidelines for the market-risk area shall be drawn up under observance of the relevant provisions in the Executive Order on bond issuance, the balance principle and risk management.

Tasks and responsibilities of the board of management

Organisation and allocation of responsibilities for the market-risk area

- 6) The board of management shall ensure that there is the necessary segregation of duties, cf. section 12. Segregation of duties for the market-risk area means that employees involved in establishing trading and risk assumption may not
 - a) assist in the settlement of trading,
 - b) assist in performance of internal controls,
 - c) be responsible for measuring and calculating results and risks, and
 - d) be responsible for preparation of reports.

Accounting practices

- 7) If the undertaking itself calculates risks and gains/losses as well as the values of financial instruments and other items with market risks, the board of management shall ensure that the undertaking has appropriate methods for this, including that it can be controlled and is performed correctly.
- 8) If the undertaking obtains calculations of risks and gains/losses as well as values of financial instruments and other items with market risks from external parties, the undertaking shall ensure that the external parties perform the task appropriately. The undertaking shall also regularly evaluate whether the prices, parameters etc. received from and applied by the external parties are correct and thereby ensure a fair presentation of the risks of the undertaking as well as correctly calculated items as presented in the financial statements.

Procedures for the market-risk area

- 9) The procedures for the market-risk area shall, in addition to the general requirements of sections 17-18, contain provisions on
 - a) entering, control, registration, bookkeeping and settlement of transactions involving securities, currency, derivatives and any other market-risk-bearing activities,
 - b) procedures for regular calculations of risks, gains/losses and values,
 - c) preparation of management reporting on the market-risk area, and
 - d) procedures for introduction of business activities in new financial instruments and other products with market risks.
- 10) For mortgage-credit institutions and banks with a licence to issue covered bonds, the procedures for the market-risk area shall be drawn up under observance of the relevant provisions in the Executive Order on bond issuance, the balance principle and risk management.

Ascertaining whether risks are within authorities

- 11) It must be possible for employees with authority to ascertain whether the transactions they intend to enter into lie within their authorities. This also applies to any collective authorities where several employees together can enter into transactions within a common authority.
- 12) Point 11 shall also apply when employees enter into transactions in accordance with authority received from customers under an agreement on discretionary portfolio management.

Controls for the market-risk area

- 13) The financial undertaking shall be organised such that appropriate, independent controls for the market-risk area are established, cf. section 25. Such controls should, depending on the scope and complexity of the undertaking's market-risk-bearing activities, include control of

- a) whether authorities are observed in that all limits and all persons who have authorities shall be controlled, intra-day control shall, as a minimum, be carried out on a sample basis,
 - b) whether trading, registration, bookkeeping and settlement of transactions takes place in accordance with the procedures for these,
 - c) whether calculation and reporting of positions and risks are correct,
 - d) whether investment limits and portfolio management agreements with customers are complied with,
 - e) whether transactions are entered into at correct rates and prices,
 - f) whether gains/losses on market-risk-bearing transactions for the undertaking or on behalf of customers are calculated correctly,
 - g) reconciliations of holdings of securities, financial instruments and accounts, and
 - h) whether the prices, parameters etc. received from and applied by external parties are correct and thereby ensure a fair presentation of the risks of the undertaking.
- 14) For mortgage-credit institutions and banks with a licence to issue covered bonds, the controls for the market-risk area shall be drawn up so that they ensure observance of the relevant provisions in the Executive Order on bond issuance, the balance principle and risk management.

Reporting for the market-risk area

- 15) For mortgage-credit institutions and banks with a licence to issue covered bonds, the reporting for the market-risk area shall be drawn up so that it also includes the limits stated in the Executive Order on bond issuance, the balance principle and risk management.

Operational risk

Scope and definitions

- 1) "Operational risk" means the risk of losses due to inappropriate or inadequate internal procedures, human errors and system errors or as a consequence of external occurrences, including legal risks. Reputation risk and strategic risks are not considered operational risks in this Executive Order, but when relevant they should be treated according to the same guidelines as operational risk.

Tasks and responsibilities of the board of directors

Policy for operational risk

- 2) The policy for operational risk shall, in addition to the general requirements contained in section 5(1), when relevant include the following:
 - a) decision on what types of incident are to be considered as operational incidents, including as far as possible limits in relation to other risk areas such as credit risk, market risk, strategic risk and reputation risk,
 - b) decision on what methods are to be applied to gather information on incidents which can be considered as relating to the area for operational risk, and the extent to which such incidents are to be recorded and reported,
 - c) decision on the size of losses to be recorded and reported, and
 - d) decision on the principles for reporting to the board of directors itself in order to gather data and with regard to management reporting otherwise.
- 3) The Board of directors shall decide how losses are to be managed, both with regard to incidents which are expected to arise with high probability, but with low losses, and incidents which are expected to arise with low probability but with large losses.
- 4) In identifying the operational risk of the undertaking, the following factors may be included in the assessment:
 - a) special operational risks linked to the undertaking's business model and activities,
 - b) integration, stability and suitability of the undertaking's IT systems,
 - c) manual routines, for example in connection with control and settlement of transactions, controls and non-integrated IT systems,
 - d) dependence on external relationships, including sub-suppliers,
 - e) competences of employees in relation to the complexity of tasks,
 - f) the quality of procedures etc.
 - g) organisation, including the scope of internal controls and any lack of possibilities to establish segregation of duties, and
 - h) physical security.

Guidelines from the board of directors to the board of management for operational risk area

- 5) In its guidelines for the board of management, the board of directors shall include provisions which the board of directors considers necessary to ensure compliance with the policy of the board of directors for operational risk. The board of directors may stipulate
 - a) specific requirements for the organisation and operation of the undertaking or parts of it,
 - b) principles for how operational risk is to be gathered and calculated and who is to do this,
 - c) any financial limits for losses to be gathered and registered
 - d) guidelines for whether, and if so to what extent, incidents which are known and which could have led to losses but did not, are to be registered and assessed, and
 - e) guidelines for reporting operational risk to the board of directors, including limits and time limits for when operational risk and losses (including possible incidents which

could have led to material losses) from operational risk are to be reported to the board of directors.

Tasks and responsibilities of the board of management

- 6) The board of management shall organise the financial undertaking in such a way that operational risk is limited as much as possible within a framework which is in accordance with the policy and strategy of the board of directors for the area as well as ensure that all relevant employees are aware of the undertaking's policy for operational risk.
- 7) The board of management shall ensure that
 - a) incidents are gathered and registered in accordance with the policy of the board of directors for operational risk and/or guidelines,
 - b) there are effective systems and methods to communicate and store information about operational risk,
 - c) IT systems support the day-to-day operations adequately,
 - d) all employees have adequate knowledge about operational risk to carry out their tasks in the area,
 - e) there are procedures for continuous identification of areas, systems and products, which can lead to material operational risks, and that
 - f) there are procedures for gathering, calculating and reporting on losses and any risks of losses arising.
- 8) The board of management shall assess in advance the extent to which decisions can lead to operational risk which are in conflict with the policy and strategy for the area stipulated by the board of directors. This applies both for decisions of principle on business areas, including performance of new services or transactions with new financial instruments, as well as for important decisions on the operation and organisation of the undertaking. This may demand that the board of management involve the person responsible for operational risk, cf. section 19(1) and (2), or in exceptional circumstances external consultants.
- 9) The board of management shall regularly assess whether there are areas in which operational risk should be minimised, and if so establish an action plan for this.
- 10) The report prepared by the board of management pursuant to section 4(2) for operational risk shall be adequate for the board of directors to monitor the size of and changes in the operational risk of the undertaking and make any changes in the policy and guidelines. The report shall contain an assessment of the probability that a given type of incident may arise and how large the direct or indirect loss could be in the worst case. The risk that an incident may arise, like the risk of losses of a specific size, may be stated as a categorisation such as "very high", "high", "medium", "low" and "very low". As a minimum, the report shall
 - a) contain an assessment of the current operational risk based on a review of the situation of the undertaking and loss-giving incidents which have occurred,
 - b) contain a report on the incidents which have led to material losses for the undertaking or, where possible, which could have led to material losses,
 - c) describe intended changes in the undertaking's business model, systems, products etc. which are relevant in relation to operational risk,
 - d) describe developments in relation to the surroundings of the undertaking, and
 - e) describe any areas in which the board of management has established an action plan pursuant to point 9.

Liquidity risk

Tasks and responsibilities of the board of directors

Liquidity policy

- 1) "Liquidity risk" means the risk that
 - a) the costs of the undertaking to obtain liquidity increase disproportionately,
 - b) lack of financing prevents the undertaking from maintaining its current business model and
 - c) the undertaking ultimately cannot fulfil its payment obligations because of lack of financing.
- 2) The board of directors shall adopt a written liquidity policy, cf. section 5(1), no. 5. Depending on the size of the financial undertaking and its composition of legal entities, the overall risk profile and complexity of the undertaking's activities subject to liquidity risk, the liquidity policy shall state what liquidity-risk profile the board of directors wants the undertaking to have.
- 3) The board of directors shall ensure that the liquidity policy is appropriately prudent and that at all times it secures appropriate liquidity, including an appropriate liquidity reserve and an appropriate financing structure.
- 4) The liquidity policy shall, as a minimum, contain principles for the following
 - a) how the undertaking calculates its liquidity risk,
 - b) the financing structure of the undertaking,
 - c) the size and composition of the undertaking's liquidity reserve,
 - d) limits for the liquidity risk of the undertaking, calculated for different time horizons,
 - e) what stress tests the undertaking is to carry out, including choice of methods and scenarios,
 - f) under what circumstances the board of management shall secure a decision by the board of directors on whether the financial undertaking is to maintain the levels of risk as well as the procedure for this,
 - g) a contingency plan for obtaining funding, including possibilities for obtaining liquidity via sale or mortgaging assets and utilising borrowing facilities.
 - h) principles for allocating liquidity costs,
 - i) any legal or other limitations on transfers of assets within the undertaking, including whether the different types of assets are recognised within the regulations for liquidity in the countries in which the undertaking operates,
 - j) overall requirements for employee skills in the liquidity area,
 - k) procedures or following up the liquidity policy, cf. section 5(4), and
 - l) the regular reporting to the board of directors.
- 5) If the undertaking is systematically important in one or several of the countries in which it carries out activities, the board of directors shall also ensure that the liquidity policy takes sufficient account of this.

Guidelines from the board of directors to the board of management for the liquidity area

- 6) The guidelines for the board of management shall, in addition to the general requirements of sections 6 and 7, realise the liquidity policy in specific guidelines which shall contain provisions on:
 - a) calculation of liquidity according to section 152 of the Financial Business Act. This provision shall not apply, however, for mortgage-credit institutions.
 - b) Methods to calculate liquidity risk and time horizons for the calculations. Calculation of liquidity risk shall include both balance-sheet items and off-balance-sheet items and as a minimum include:
 - the expected payment flows on the basis of expected behaviour one week hence,

- the expected payment flows on the basis of expected behaviour with monthly observations for no less than 12 months, and
- the expected funding need of the undertaking for at least the next three years, if the undertaking funds itself otherwise than through deposits.
 - c) The composition of the undertaking's liquidity reserve, including which assets can be included in the reserve and a break-down of these into very liquid assets and liquid assets, as well as the proportion of the unencumbered assets, which may be used as collateral in the event of unexpected financing needs.
 - d) Limits for the total liquidity risk of the undertaking.
 - e) Limits for the use and concentration of different types of funding.
 - f) Limits for the maturity of funding.
 - g) Limits for currency and geographical concentration, so far as they are relevant.
 - h) Methods to conduct stress tests of liquidity risk. The stress tests shall be conducted monthly as a minimum over 12 months and consist of
 - an undertaking-specific stress scenario,
 - a market-specific stress scenario, and
 - a combination scenario which includes both institution and market-specific stress.
 - i) Requirements for management initiatives and time horizons in the contingency plan for obtaining funding.
 - j) Requirements for when the undertaking is to establish local contingency plans, including as a minimum, if the undertaking has legal entities, where liquidity does not flow freely between the entities.
- 7) For mortgage-credit institutions which finance themselves by issuing bonds in accordance with relevant legislation, in many cases there will be a very narrow payment relationship between the loan and the bonds issued to finance the loan, cf. the Executive Order on bond issuance, the balance principle and risk management. In such cases many of the specific requirements of the Executive Order for guidelines, reports and procedures will be met by explanatory references to this, and the primary liquidity risk will arise from refinancing funding and any requirements for supplementary collateral as a consequence of subsequently exceeding lending limits.
- 8) For banks with a licence to issue covered bonds, the policy, guidelines, procedures, procedures and internal controls and reporting for the liquidity area shall be drawn up under observance of the relevant provisions in the Executive Order on bond issuance, the balance principle and risk management.

Tasks and responsibilities of the board of directors for the liquidity area

- 9) The report which the board of management shall prepare pursuant to section 4(2) shall contain an account of how the liquidity policy is realised in the liquidity risk accepted by the undertaking. In the report, the board of management shall also make a reasoned assessment of whether the liquidity risk of the undertaking has been calculated fully and prudently, including whether the liquidity reserve, financing structure, contingency plan and the selected stress tests are suitable.
- 10) The board of management shall include the report in regular updating of the liquidity policy, internal limits regarding liquidity risk and the contingency plan.
- 11) The board of management shall ensure that, on the introduction of new products with liquidity risk and on significant changes in existing products which increase the liquidity risk of the institution, cf. sections 28-29, these are properly included in the undertaking's organisation, including in the procedures of the undertaking, its risk management, reporting and internal controls.

Procedures for the liquidity area

Procedures for regular calculations of liquidity flows

- 12) An undertaking shall have procedures for continuous identification, measurement, control and monitoring of the undertaking's liquidity flows which, in addition to the general requirements of sections 17-18, as a minimum, contain:

- a) Provisions on the methods chosen by the undertaking to calculate the undertaking's liquidity flows.
- b) Provisions on stipulating the expected time for possible realisation of assets which affect liquidity, and how assets can be realised in accordance with the expectations of the undertaking.
- c) Provisions on assumptions for the time for maturity of assets and liabilities which can be determined by contract and by behaviour.
- d) Provisions on regular reassessment of calculations of the undertaking's liquidity flows, including validation of assumptions on liquidity flows.
- e) Provisions which ensure that, where relevant, the undertaking takes account of legislative, administrative and operational limitations, which affect the possibilities for transferring liquidity and unencumbered assets between entities in different countries.

Procedures for managing intra-day liquidity

- 13) An undertaking shall have procedures for intra-day liquidity which, in addition to the general requirements of sections 17-18, as a minimum, contain provisions which ensure active management of intra-day liquidity so that the undertaking can meet payment and settlement demands promptly in both normal situations and crisis situations.

Procedures for preparation of liquidity stress tests

- 14) An undertaking shall have procedures for liquidity stress tests which, in addition to the general requirements of sections 17-18, as a minimum, contain provisions:
- a) That stress scenarios take account of unlikely but not inconceivable conditions.
 - b) That, when calculating stress tests, if relevant, the undertaking shall include
 - off-balance-sheet items and other contingent liabilities, including securitisation special purpose entities (SSPE) or other entities with a special purpose, for which the undertaking acts as administrator or provides material liquidity support, and
 - conditions which may have a low probability, but a great influence on the undertaking.
 - c) That the stress tests shall apply different time horizons and different degrees of stressed conditions which as a minimum cover two sub-periods
 - an initial period of at least the first week with a serious and acute crisis situation, and
 - a subsequent period of at least three weeks in which the stress situation abates but does not cease.
 - d) That the undertaking's stress test, as a minimum, comprises
 - an undertaking-specific stress scenario, which as a minimum includes that unsecured loans from financial undertakings, except for financial undertakings within the same group, in the initial period, cf. point 14c, first sub-point, fall due by contract and are not extended, and that a certain proportion of deposits from corporate customers and private customers cease.
 - a market-specific stress scenario, which as a minimum, includes that the liquidity reserve can only be realised at a lower value than the current market value and that the undertaking's possibilities for financing itself via the capital markets deteriorate, and
 - a combination scenario which includes both institution and market-specific stress, but which is not merely the sum of the institution-specific and the market-specific stress scenarios.
 - e) That the scenarios are to show the impact on the liquidity of the undertaking.
 - f) That the undertaking is to calculate the effect of the stress tests for a number of sub-periods which, as a minimum, include the time horizons one week, four weeks and monthly over 12 months.

Procedures for the liquidity reserve

- 15) An undertaking shall have procedures for the liquidity reserve which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain:
- a) Provisions on which types of assets can be included in the undertaking's liquidity reserve and on the assumptions of the undertaking for the terms of the assets. Provisions on the types of assets shall, as a minimum, be based on:

- that only liquid assets may be included,
- that cash may only be included, if it is not necessary in order to maintain the commercial activities of the undertaking. For example the undertaking's cash in tellers and cash resources for ATMs may not be included.
 - b) That own listed capital investments may not be included in the liquidity reserve.
 - c) Provisions on the distinction between mortgaged assets and unencumbered assets. For the unencumbered assets, the undertaking shall also distinguish between assets which are available at all times, particularly in emergency situations, and assets which are not available at all times.
 - d) Provisions that the undertaking shall have a liquidity reserve which means that the undertaking shall be able to continue its activities for no less than four weeks in a potential crisis situation, which shall be defined in the undertaking's stress scenarios, cf. point 14. The liquidity reserve shall be divided into at least two sub-periods corresponding to the sub-periods in the stress tests and characterised by the following conditions:
 - In the initial period, cf. point 14c, first sub-point, the liquidity need shall be covered by very liquid assets. These may be deposits at central banks, very liquid government bonds, mortgage-credit bonds or shares.
 - Subsequently, the liquidity need may also be covered by liquid, but not necessarily very liquid assets. Here the undertaking may include other liquid securities admitted to trading on a regulated market and liquid unlisted securities.
 - If the undertaking is able to demonstrate that the assets can be used in a crisis situation, then other types of assets than those mentioned in point 15d, first and second sub-points may also be included to cover the liquidity need after the first sub-period.

Procedures for the contingency plan for obtaining funding.

- 16) An undertaking shall have procedures for the contingency plan for obtaining funding which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain:
- a) Definition of what incidents lead to part or full implementation of the plan. The undertaking shall include stress tests in its considerations.
 - b) Definition of early indications of a potential crisis situation so that the undertaking can secure itself early against any increased liquidity risk. Indicators may be negative publicity in the media, for example, rumours about the undertaking, falls in share prices, unusual falls in deposits or increased costs of financing.
 - c) Guidelines for what is to happen if the undertaking's limits for liquidity risk are exceeded, or if liquidity projections show that they will be exceeded.
 - d) A description of the individual potential initiatives for both the assets side and the liabilities side. These may include selling or mortgaging assets, issuing new debt, or reducing lending.
 - e) Stipulation of the undertaking's priorities for the individual initiatives, including the probability that the initiatives can be implemented, the expected time horizon for implementation of the individual initiative and the expected impact on liquidity.

Procedures for calculation of collateral received and placed

- 17) An undertaking shall have procedures for calculation of collateral received and placed which, in addition to the general requirements of sections 17-18 shall, as a minimum, contain:
- a) Provisions which ensure that the undertaking identifies and estimates current and potential needs for placing collateral and receiving collateral over different time horizons.
 - b) Provisions which stipulate how the undertaking is to calculate the liquidity value of the undertaking's current and potential collateral. The liquidity value is the value which the undertaking can expect to achieve, if collateral is to be sold or mortgaged in a crisis situation. The liquidity value usually does not correspond to the carrying amount.
 - c) Provisions which ensure that the liquidity value is always calculated prudently and that the undertaking takes account of the fact that it can be very difficult to sell or mortgage certain assets within a reasonable time horizon. When calculating the liquidity

value, the undertaking shall apply a relevant deduction in which fluctuations in the market value of the asset are a significant element.

- d) Provisions which ensure that the undertaking takes account of any legal and operational limitations in connection with mortgaging or selling collateral.

Procedures for allocating internal liquidity costs

- 18) An undertaking shall have procedures for allocating liquidity costs. Liquidity costs are both direct costs of obtaining liquidity and indirect costs, for example costs of holding a liquidity reserve or costs of maturity mis-match between the financing chosen and the assets the financing is to support. In addition to the general requirements of sections 17-18 the procedures shall, as a minimum, contain:
 - a) Provisions on principles for allocating liquidity costs between relevant entities in the undertaking.
 - b) Provisions which ensure that all significant factors are included in the undertaking's calculation of liquidity costs.
 - c) Provisions on calculation of liquidity costs. Calculation of liquidity costs shall take account of the direct costs of obtaining liquidity as well as the indirect costs arising from costs related to the liquidity risk that obtaining the relevant liquidity imposes on the undertaking. When calculating liquidity costs the undertaking may, for example, apply the risk-free market interest rate plus an undertaking-specific supplement plus costs linked with the relevant maturity plus costs linked with the liquidity reserve. The purchase price which was current at the date of acquisition for a given financing may usually not be used.
 - d) Provisions which ensure that the undertaking includes the liquidity costs which can arise in a crisis situation, when it is normally more expensive and more difficult to obtain liquidity.
 - e) Provisions which ensure that calculation of liquidity costs takes account of credit commitments in that credit commitments may be exploited and thus burden liquidity.
 - f) Provisions which ensure that the undertaking calculates relevant liquidity costs relating to the undertaking's trading book, which take account of both the expected holding period (maturity) for the trading book and the liquidity value of the trading book, which does not necessarily correspond to the carrying amount.

Risk management controls and reporting

Chief risk officer and risk management function

- 19) The chief risk officer shall, in addition to the general requirements of sections 19-21, ensure that appropriate management of liquidity risk takes place in the undertaking, including that:
 - a) The undertaking's liquidity, including intra-day liquidity, is continuously monitored and controlled.
 - b) The contingency plan is tested regularly as far as possible. For example sale of subsidiary undertakings may be exempted from regular tests.
 - c) The institution's assumptions regarding liquidity flows are validated and that validation is documented.
 - d) The limits stipulated are regularly reassessed.

Controls for the liquidity area

- 20) The undertaking shall establish independent internal controls of all material activities in the liquidity area, cf. section 25. As a minimum, there shall be regular internal control that:
 - a) the liquidity policy is complied with by the employees of the undertaking,
 - b) authorities to approve exposures are observed, and
 - c) reporting within the undertaking is correct.
- 21) The undertaking shall document internal controls carried out.

IT security

Scope and definitions

- 1) This Annex contains provisions on the matters dealt with in the Executive Order which particularly relate to the IT area, including IT security management.

Tasks and responsibilities of the board of directors

- 2) The board of directors shall adopt an IT security policy for the undertaking.
- 3) The IT security policy shall, depending on the financial undertaking's desired risk profile for the IT area, as well as the size and complexity of the undertaking's use of IT, contain overall decisions on the following:
 - a) Organisation of IT work, including segregation of duties between
 - system development/maintenance,
 - IT operations, and
 - conduct of the undertaking's business.
 - b) Regular risk assessment.
 - c) Protection of systems, data, hardware and channels of communication.
 - d) System development and maintenance of systems.
 - e) Operations.
 - f) Back-up and security copying.
 - g) Contingency plans, which include objectives and plans for re-establishing normal operation in the event of errors, break-down, loss of data or systems, as well as full or part destruction of buildings, hardware and channels of communication.
 - h) Quality assurance.
 - i) Principles for implementation of the policy in detailed guidelines, procedures and instructions.
 - j) Precautions in the event of breaches of IT security and security regulations.
 - k) Compliance with relevant legislation.
 - l) Reporting, control and follow-up.
 - m) Any exemptions from the IT security policy.
- 4) The board of directors shall regularly, and no less than once a year, assess the IT security policy, including the extent to which the IT security policy is sufficient to ensure that the risks that arise, and can be expected to arise, from utilising IT are at an acceptable level for the undertaking in the future.
- 5) The IT security policy shall, as far as possible, be independent of the technology utilised.

Tasks and responsibilities of the board of management

- 6) The board of management shall ensure compliance with the IT security policy of the undertaking. The board of management shall detail the IT security policy in procedures etc. which support that
 - a) responsibility, including ownership, for IT processes and resources is allocated,
 - b) segregation of duties is monitored,
 - c) maintenance of the desired level of IT security is controlled as well as management of any weaknesses,
 - d) systems and data are classified and prioritised,
 - e) systems (both basic and user systems) and configuration (hardware) as well as changes in these are documented,
 - f) there are security copies of systems and data, including storage of security copies,
 - g) adequate IT resources are procured,
 - h) systems development, configuration and maintenance as well as testing new and changed systems take place appropriately,
 - i) tests and other quality assurance are carried out,
 - j) change management and problem control are carried out,

- k) there is controlled access to systems and data, and
 - l) there is adequate physical security, including physical access control.
- 7) In addition, the board of management shall ensure that an IT contingency plan is prepared which shall be approved by the board of directors. Depending on the circumstances of the undertaking, the plan shall contain
- a) a description of how a contingency organisation is to be established, and
 - b) activity plans in the event of serious system break-down, errors and interruptions in IT use.
- 8) The contingency plan shall be tested regularly and the financial undertaking shall have rules on reporting the result of a tests of the contingency plan.

Organisation of the work of the board of directors

The rules of procedure of the board of directors

Provisions containing the requirements for the rules of procedure of a financial undertaking, taking into account the new wording of requirements in the new Companies Act.

- 1) The board of directors shall lay down more detailed provisions with regard to the performance of its duties by means of rules of procedure, cf. section 65 of the Financial Business Act.
- 2) When wording the rules of procedure pursuant to point 1, the board of directors shall base its work on its statutory obligations as well as the undertaking's complexity, business and activity areas. The rules of procedure shall, however, always contain
 - a) Provisions on the specific offices of the members of the board of directors, including the use of proxies, and requirements for competence to pass resolutions, as well as the intervals at which meetings shall be held.
 - b) Provisions on written and electronic meetings of board of directors, cf. point 18 of this Annex.
 - c) Procedures for stipulating the distribution of responsibilities between the board of directors and board of management, including authorisation, responsibility for procedures and duty of confidentiality.
 - d) Procedures for regular decisions by the board of directors on organisational location and staffing of the risk management function dealt with in section 19(2).
 - e) Procedures for supervision by the board of directors of management by the board of management of the financial undertaking and any subsidiary undertakings, including assessment of whether the board of management carries out its tasks and duties in an appropriate manner and in accordance with the stipulated risk profile, policies and guidelines laid down by the board of directors for the board of management , cf. section 2(1), no. 4.
 - f) Procedures for establishment and keeping of books, lists and registers under companies legislation.
 - g) Procedures for regular decisions by the board of directors on the financial undertaking's business plan, risk profile, organisation and resources.
 - h) Procedures for how the board of directors is to procure the information necessary for performance of its tasks and duties, including the obligations to which the board of directors is subject pursuant to the Financial Business Act, the Securities Trading, etc. Act., the Act on Measures to Prevent Money Laundering and Financing of Terrorism, and other relevant legislation.
 - i) Provisions on regular decisions by the board of directors on reports from the board of management to the board of directors, including decisions on the financial undertaking's individual solvency need, budgets, financial reports, liquidity and capital need, material transactions, special risks and overall insurance position.
 - j) Procedures for decisions and signature by the board of directors on the audit book.
 - k) Procedures for how the board of directors is to secure the necessary basis for the audit, including, if relevant, consideration as to whether there is a requirement for internal audit.
- 3) The board of directors shall regularly, and no less than once a year, review the rules of procedure with a view to ensuring that these reflect the business and activity areas of the financial undertaking.
- 4) The board of directors shall ensure that all members of the board of directors have knowledge about the rules of procedure. The rules of procedure shall therefore be signed by all the members of the board of directors. This may be by new members of the board of directors signing for the receipt of the current rules of procedure.

Meetings of the board of directors and negotiations by the board of directors

- 5) The board of directors shall, cf. section 74(1) of the Financial Business Act, meet when a decision is to be made on matters which are not covered by the authorities given to the board of management by the board of directors. Therefore the board of directors cannot legally delegate its decision-making competence to e.g. an executive committee.
- 6) Point 5 shall not apply for processing standard matters which, pursuant to the articles of association or otherwise shall be processed by the board of directors. Matters of this type may be delegated for processing and decision by a sub-committee under the board of directors, provided the full board of directors has stipulated guidelines in advance for processing the matter. These guidelines, as well as the work of the sub-committee on the relevant matters, should be regularly reassessed by the board of directors. Delegation shall not include the responsibility of the board of directors for processing the case and the decisions made.
- 7) The board of directors may decide that employees of the financial undertaking and members of the board of directors as well as other group companies may take part in a meeting of the board of directors, possibly only for a single item on the agenda.
- 8) The board of directors may also, in exceptional circumstances, decide that there may be other persons present than those mentioned in the 1st clause, e.g. shareholders or advisors, for one or several specific items on the agenda.
- 9) Notwithstanding point 7, no unauthorised persons may be present at meetings of the board of directors or for an item on the agenda of the meeting of the board of directors, if confidential information is being considered that cannot legally be disclosed in accordance with the regulations on disclosure of confidential information in part 9 of the Financial Business Act.
- 10) The minute book kept pursuant to section 74(3) of the Financial Business Act shall reflect the discussions at the meetings, and shall include the important risk assessments and the decisions made as well as the assumptions for these. It shall state which members have been present at a meeting. If other persons than members of the board of directors have been present, this shall also be stated.
- 11) The minute book must be designed so that the risk of subsequent additions, corrections or omissions is as small as possible. If the minute book is kept as a loose-leaf system, this may be done by having the initials of the chairperson or another member of the board of directors on each page. Each page of the minute book shall be numbered consecutively.
- 12) If a separate minute book of loans approved is kept, this must be stated in the minute book. The minute book of loans approved shall clearly state which loans are:
 - a) Approved/refused.
 - b) Approved pursuant to section 78 of the Financial Business Act.
 - c) For reconsideration.
 - d) For confirmation (urgent cases)
 - e) Whether approval has been through written processing or at a meeting of the board of directors held electronically.
- 13) The minute book of loans approved and the minute book respectively shall explicitly state when exposures covered by section 78(1) and (4) of the Financial Business Act are being addressed, and it must be noted that the relevant members of the board of directors and members of the board of management have not been present during consideration of the matter.
- 14) The provision of point 13 shall not prevent a member of the board of directors or a member of the board of management who also participates in the management of a parent company which owns the entire capital of the undertaking or, for a fully-owned fellow subsidiary company or subsidiary, from participating in the processing of issues regarding, or exposures with, this company.
- 15) The provisions of section 78(1) and (4) of the Financial Business Act shall not prevent members of the board of directors elected by employees from otherwise being approved exposures on the same terms as employees of the relevant financial undertaking.

The provision of section 78(3) of the Financial Business Act shall not apply to fully secured exposures or exposures of entirely insignificant size.

- 16) At least once annually, the board of directors shall review the exposures with the persons and companies mentioned in section 78(1) and (4) of the Financial Business Act, e.g. in connection with the annual review of assets. The minute book shall state that such review has been carried out as well as the conclusions of the review.

Written and electronic meetings of board of directors

- 17) The board of directors may hold written and electronic meetings of board of directors pursuant to the relevant regulations of the Companies Act.
- 18) The board of directors shall carefully consider which matters are suitable for processing at a written or electronic meeting of the board of directors. This will primarily be straightforward and routine matters which do not require a new decision of principle by the board of directors or impose material risks on the undertaking, or urgent matters which cannot be postponed without harmful effects for the undertaking.
- 19) The decisions of the board of directors as to which matters are suitable for written or electronic procedure respectively shall be stated in the rules of procedure.
- 20) For written meetings of board of directors the minute book of the board of directors shall state when the meeting was concluded.
- 21) Point 17-20 shall apply correspondingly for written procedures for approval of exposures.
- 22) If a resolution by board of directors is made in writing or electronically, as far as possible there shall be a final statement from the individual members of the board of directors, cf. section 124 of the Companies Act, cf. section 84 (savings banks) and section 88 (cooperative savings banks) of the Financial Business Act. Such statements shall be recorded in the minute book. Omission to react to material submitted shall not be a sufficient statement.