

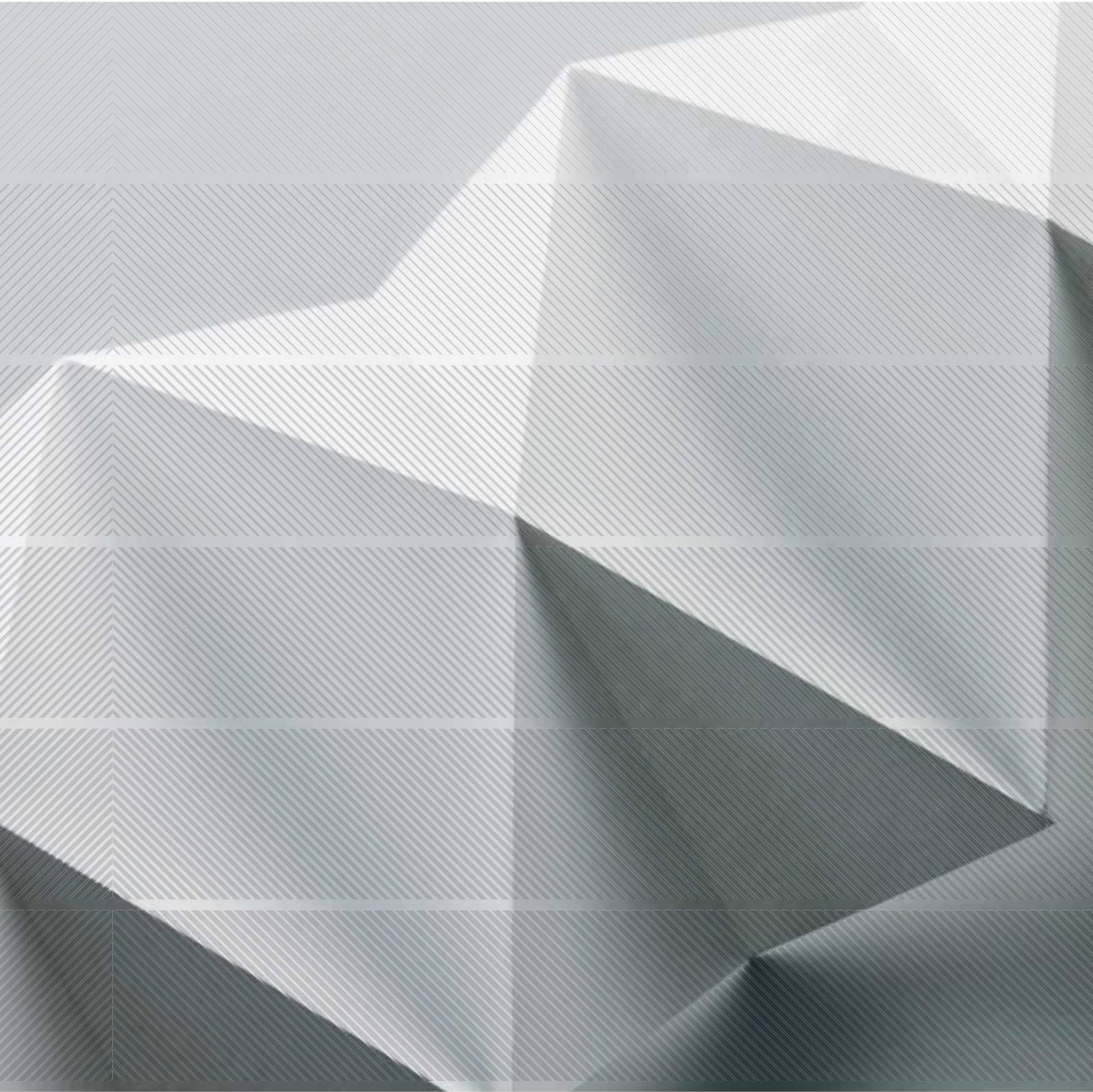


FINANSTILSYNET

THE FINANCIAL SUPERVISORY
AUTHORITY OF NORWAY

ANNUAL REPORT

2010



FINANSTILSYNET'S ORGANISATION

The Board
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Endre Skjørestad

Director General
Bjørn Skogstad Aamo

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COMMUNICATIONS DIRECTOR Kjetil Karsrud
HEAD OF INTERNATIONAL RELATIONS Lisbeth Strand
CONSUMER COORDINATOR Anders N. Kvam
SPECIAL ADVISER/CONTROLLER Rune Grundekjøn
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BOARD SECRETARY Anne Kari Østmo

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Dag Anders Brunstad

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HEAD OF SECTION
Lone Tudborg Lakhan

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Analysis and Reporting
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HEAD OF SECTION
Kjersti Elvestad

Capital Markets Supervision
DEPUTY DIRECTOR GENERAL
Eirik Bunæs

Staff

Securities Institutions
HEAD OF SECTION
Britt Hjellegjerde

Securities Supervision
HEAD OF SECTION
Geir Holen

Estate Agencies and Brokers, Debt Collection Firms
HEAD OF SECTION
Wilhelm Mohn Grøstad

Finanstilsynet is responsible for the supervision of banks, finance companies, mortgage companies, e-money institutions, payment institutions, insurance companies, pension funds, insurance intermediaries, investment firms, securities fund management, stock exchanges and other regulated markets, clearing houses and securities depositories, real estate agencies, debt collection agencies, external accountants and auditors. Finanstilsynet also oversees prospectuses, listed companies' financial reporting and conduct in the securities market.

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For analyses of financial market trends, see the report
Risk Outlook 2011: The Financial Market in Norway.

"Finanstilsynet shall ensure that the institutions it supervises operate in an appropriate and proper manner in accordance with law and provisions issued pursuant to law and with the intentions underlying the establishment of the institution, its purpose and articles of association."
(Financial Supervision Act, section 3)

PREFACE

Norway has emerged from the international financial crisis in a better position than most other countries. In 2010, as previously, the crisis led to no serious problems for Norwegian financial institutions. The banking crisis at the start of the 1990s had taught important lessons with regard to banks' credit practices and supervisory methodology and legislation. As a result the financial industry and the economy were hit less hard by the crisis than was the case in other countries. Solid government finances and a favourable industry structure have also played an important part.

In many countries the financial crisis triggered a need for substantial injections of government capital to banks. This exacerbated government debt problems which in the next instance are creating major uncertainty for economies ahead. If states are unable to service their debt, private banks and other investors that have extended loans to them will be hit. Norway's financial industry and economy stand to be affected both by higher costs of international funding and by new setbacks in the international economy.

The international crisis has led to agreement on new, stricter requirements on banks' capital and liquidity. Thanks to strict Norwegian rules, Finanstilsynet's scrutiny of the individual bank's risk and capital need (Pillar 2) and the banks' own efforts, Norwegian banks are well equipped to meet the new capital requirements. Both the challenges in the market and the need for adequate buffers in relation to the minimum requirements make it necessary for banks, for 2010 as previously, to devote a substantial part of their profits to continued strengthening of their equity capital.

Norwegian banks are dependent on international borrowing for their liquidity supply, and are therefore vulnerable to turbulence in international markets. It is important that both the banks themselves and the authorities work systematically to make the banks more robust in this area.

After a broad-based process, which included canvassing the views of the users of financial services, Finanstilsynet's executive board adopted on 24 November a new strategy for the FSA for the period 2010 to 2014. The strategy builds further on the main objectives of

securing financial stability and well-functioning markets. These are followed up through eight intermediate goals, which are listed on pages 6 to 9.

The goal of "Financially sound and liquid financial institutions" has been at centre stage of Finanstilsynet's work. The intermediate goal of "Good monitoring of risk in the economy and markets" builds on a project which started in 1994 when Kredittilsynet set up a programme for macroeconomic monitoring of risk in the financial system. An important observation made during the Norwegian banking crisis is that no sharp distinction exists between macro and micro risk. The individual bank faces risks which are both specific and are influenced by economic developments. On this basis Finanstilsynet has each six months prepared risk overviews which also take macroeconomic conditions into account. The reports are sent to the Ministry of Finance and Norges Bank. Since 2002 the assessments have been published as part of a yearly report on the state of the financial market. To better reflect the fact that the report is forward looking, it is now named *Risk Outlook*. As from 2010 Finanstilsynet also issues a half-yearly report, *Financial Trends*, each autumn.

The analyses and regular surveys of lending to commercial property and dwellings have provided the basis for Finanstilsynet's oversight of individual institutions in the form of systematic thematic inspections.

Norwegian households are more heavily indebted than ever before. The debt is mainly related to dwellings, where prices are at an unprecedented level. To bring about more robust home financing, Finanstilsynet issued in 2010 guidelines for good practice with regard to lending for housing purposes. Checking compliance with these guidelines, in the first instance by way of systematic inspections, but also if necessary through other policy instruments, is an important task in 2011.

The international financial crisis showed a strong need to strengthen the monitoring of risk in the economy and markets. The new regulatory framework, Basel III, contains instruments specifically designed to counteract the build-up of bubbles in the market that may trigger crises. In Norway it is natural for general macro supervision and

use of special instruments to build on the collaboration established between the Ministry of Finance, Norges Bank and Finanstilsynet. It will be important both to utilise the analyses carried out by the central bank and to ensure that the instruments applied to institutions are properly coordinated with the Ministry of Finance's other work.

The need to protect consumer interests underlies large parts of the legislation administered by Finanstilsynet. Supervision of estate agency and debt collection has in the first instance a consumer perspective. Secure banks and insurance companies are also crucially important to consumers. The intermediate goal "Consumer protection through good information and advice" reflects the fact that the interests of consumers, not least as savers and investors, has now been given a more central place in Finanstilsynet's strategy and activities than previously. The annual report gives a close account of the wide-ranging thematic inspections that were carried out, directed particularly at sales of and advice on savings products at investment firms and banks in 2010. A new set of EU rules requiring uniform information on savings products in various areas (PRIPs) will provide a better basis for this supervision and will also include insurance products.

The new European framework for insurance, Solvency II, entails particular challenges for Norwegian life insurers which may require adjustments to the Norwegian conduct of business rules. Financial institutions' use of ICT has made follow-up of operational risk in these areas an important task. Attacks by criminals, for example in the form of skimming, and the risk associated with outsourcing, are among the challenges being followed up. Compliance with the legislation designed to prevent money laundering and financing of terrorism is also being actively followed up.

Structural changes in European securities markets continued in 2010. The volume of share trading taking place outside the traditional stock exchanges is steadily increasing. This has increased the need for regulation of transaction reporting and for better insight into activities on the various trading platforms. Changes to the MiFID directive, designed in part to attend to these needs, are under preparation in the EU.

A joint European system for settlement of securities transactions, the Target 2 Securities System (T2S), is being prepared. A system in which central banks and central securities depositories participate in an integrated European settlement process is planned. Norges Bank, the Central Securities Depository (VPS) and Finanstilsynet collaborated actively in 2010 to facilitate Norwegian participation in T2S. A binding agreement on Norwegian participation may be signed in 2011.

Through its supervision of securities markets, accounting standards and auditors, Finanstilsynet has responsibility for many factors of importance for a well-functioning market, such as good financial information and a level playing field for all participants. As from 1 May 2010 Finanstilsynet took over operative control of prospectuses for transferable securities. The transfer of responsibility has met the requirements made, but requires continued vigilance and adequate resources. Prospectuses are published on an ongoing basis on Finanstilsynet's website. A well-functioning Norwegian securities market depends on a sound regulatory framework, in line with that applying to competing marketplaces. In 2010 the Norwegian stock market showed a favourable trend with regard to share values, liquidity, new issues and the many new admissions to listing.

Finanstilsynet's wide-ranging and multifarious tasks call for priorities to be set and a continuous effort to secure effective and efficient use of resources. This is also an important aspect of the strategy for the years immediately ahead.

Oslo, 26 January 2011



Endre Skjørestad
Board chair



Bjørn Skogstad Aamo
Director General



FINANSTILSYNET'S STRATEGY 2010–2014

Extracts from Finanstilsynet's strategy, which was adopted by Finanstilsynet's Board of Directors on 24 November 2010. The strategy identifies the following priorities:

- supervision of institutions and areas of greatest significance to financial stability and well-functioning markets
- macroeconomic surveillance and macroprudential supervision
- ensuring that international requirements on institutions and supervision are implemented and complied with
- promoting investor and consumer protection and ensuring a broad public awareness of Finanstilsynet's requirements and supervisory activities

The strategy also describes measures and priorities in the respective areas of supervision.



MAIN GOAL

Finanstilsynet's main goal is to promote financial stability and well-functioning markets.

INTERMEDIATE GOALS

1. Financially sound and liquid financial institutions
2. Good monitoring of risk in the economy and markets
3. Consumer protection through good information and advice
4. Fit and proper management and satisfactory governance at institutions
5. Robust infrastructure ensuring satisfactory payments, trade and settlement
6. Adequate and reliable financial information
7. Good market conduct
8. Effective crisis management

MAIN GOAL

Finanstilsynet's main goal is to promote financial stability and well-functioning markets. Behind this goal lie important economic considerations. Financial stability and well-functioning markets are key to assuring confidence in the financial system and stable economic growth and to protecting the users of financial services.

The financial system promotes efficient distribution of society's resources and contributes to economic growth. Financial stability enables the financial system to absorb disturbances and unexpected shocks and to discharge its functions, thereby avoiding major, negative consequences for the wider economy. Well-functioning markets promote efficient distribution and pricing of capital and risk. There is a close link between financial stability and well-functioning markets. Without financial stability, markets cannot distribute capital and risk in an efficient manner. If capital is not distributed efficiently, and risk is wrongly priced, the upshot may be financial instability.

Financial stability

Financial institutions, financial markets and the financial infrastructure together make up the financial system. Stability problems can originate in any one of these, but will often unfold and intensify through an interplay of parts of the system. Problems in individual institutions, especially larger financial institutions, can spark contagion effects to other institutions.

Finanstilsynet has long experience of macroprudential supervision and of dealing with financial stability issues. It is important to coordinate instruments building on macroprudential supervision with instruments used in the supervision of individual institutions.

Given the financial system's large significance for the real economy, institutions are subject to a comprehensive body of rules. Regulation and supervision of institutions' capital adequacy, liquidity, risk management and deposit insurance schemes also give consumers security with regard to their bank deposits, insurance claims and pensions.

Well-functioning markets

Competition and information are basic to markets' efficient functioning. In a well-functioning market, prices and interest rates reflect the underlying economic realities, uncertainties in the economy and market actors' risk tolerance.

A well-functioning market is predicated on good liquidity, sufficient size and low transaction costs. This is true for the banking, insurance, real estate, securities and commodity markets. In a well-functioning capital market, risk is distributed so that actors best equipped to bear various types of risk do so, while actors not wishing to assume a particular type of risk can hedge against that risk. Timely and precise information and advice enable actors to make decisions in keeping with their wealth position, employment and income situation, and risk tolerance.

Active inspection of actors' compliance with laws and regulations and effective enforcement of sanctions against rule breakers are important for achieving well-functioning markets. Consumers such as savers, borrowers and insurance policy holders need protection due to the complexity of the products, and because the financial consequences of their investments may be substantial and difficult to gauge.

INTERMEDIATE GOALS

1. Financially sound and liquid financial institutions

Finanstilsynet is required to see to it that financial institutions and investment firms have sufficient capital to withstand unforeseen setbacks. Sufficient capital has to be accumulated in good times to absorb losses and value falls in deep economic downturns. This capital must be ample enough to maintain confidence in the institutions, enabling them to raise fresh capital and refinance their operations in a downturn. Finanstilsynet seeks to ensure that financial institutions have the liquidity and the robust funding needed to maintain normal lending in periods of poorly functioning money and capital markets. In view of the major financial groups' importance to financial stability, particular weight is given to their solidity and liquidity. Finanstilsynet is expected to play an active part in international supervisory cooperation addressed to border-crossing financial institutions of significance for Norwegian financial markets.

2. Good monitoring of risk in the economy and markets

Finanstilsynet analyses and assesses potential stability problems in Norway's financial industry against the background of developments in the Norwegian and international economy, and uses this information in its ongoing oversight of individual institutions. Macroprudential supervision requires alertness to possible imbalances, bubble tendencies and corrections in markets and the economy that may threaten financial stability. Potential stability problems resulting from contagion effects between institutions and markets are also assessed. Finanstilsynet will combine and utilise information from its supervision of individual institutions with information from its macroprudential supervision. The Authority will further develop and actively use instruments to mitigate systemic risk. As part of its macroprudential supervision Finanstilsynet will exchange information and collaborate with the Ministry of Finance and Norges Bank to find appropriate risk-mitigating measures.

3. Consumer protection through good information and advice

Through its supervision of advisers and product providers Finanstilsynet will seek to ensure that product sales and advice are

sound and suited to the individual customer. Sales and advice must be based on customers' ability to understand what investments, loans, insurance and pension products entail. As part of its consumer protection effort Finanstilsynet will introduce new European requirements for information on savings and investment options with regard to banking, insurance and securities products. Finanstilsynet's checks on real estate agents' market conduct and their compliance with due care requirements are also important for consumer protection.

4. Fit and proper management and satisfactory governance at institutions

Finanstilsynet will ensure that entities under supervision have good governance, are properly run and conduct their business in accordance with applicable rules. Finanstilsynet will critically assess whether business activities are based on a sound business model and will see to it that firms actively monitor and control all important risks. It is important for financial stability that firms have in place good risk management systems as a basis for ensuring sufficient capital and liquidity. Firms' risk management must also be sufficiently robust and sound to deal with operational risk. Fit and proper management, satisfactory risk management and internal control will help to ensure that firms comply with the conduct of business rules, which are important for markets' proper functioning.

5. Robust infrastructure ensuring satisfactory payments, trade and settlement

Finanstilsynet will contribute to a robust infrastructure featuring secure and stable information and communication systems. Finanstilsynet must ensure that payment services systems – including online banking and card facilities – are efficient, effective and secure. It is important that integrated technological systems function satisfactorily and that the risk of criminal acts arising in connection with internet-based solutions is under control.

Finanstilsynet will seek to ensure that marketplaces function in such a way that investors can be certain that prices of securities and other financial instruments are based on updated and relevant information. Finanstilsynet will see to it that settlement systems

are secure and efficient, enabling the market to function efficiently and attract investors. Finanstilsynet will work to ensure that settlement and depository functions are organised in accordance with international standards and the objective of an integrated European securities settlement system.

6. Adequate and reliable financial information

Finanstilsynet will ensure that ongoing and periodic information from listed companies is sufficient, reliable and timely. The same applies to the quality of information published by institutions under supervision and their reporting to the authorities. Finanstilsynet will ensure that prospectuses, financial information and other reporting are in conformity with applicable rules, and that the audit of companies fulfils its purpose and is of satisfactory quality. Through its supervision of external accountants and auditors, Finanstilsynet will help to ensure that annual accounts data from the business sector in general is of satisfactory quality. This is highly important for banks and other lenders.

7. Good market conduct

Finanstilsynet will ensure that the markets are characterised by appropriate rules of conduct, effective supervision and general good conduct on the part of the actors. A prerequisite for well-functioning markets and adequate investor and consumer protection is that all actors comply with laws, regulations and good practice. To achieve this, Finanstilsynet will in all areas of supervision contribute to a high detection rate and a rapid and effective response in the case of rule breaches. Effective and rapid enforcement of the conduct of business rules, which include the prohibition of insider trading and price manipulation, promotes investor and consumer confidence in the markets.

8. Effective crisis management

Finanstilsynet will maintain preparedness to deal with critical situations and avoid harmful knock-on effects and lasting problems for the financial sector and financial services users. A preparedness must be in place to meet unforeseen problems in individual institutions, markets and infrastructure, and wider-scale crises in the

financial system. The close collaboration with the Norwegian Banks' Guarantee Fund will continue.

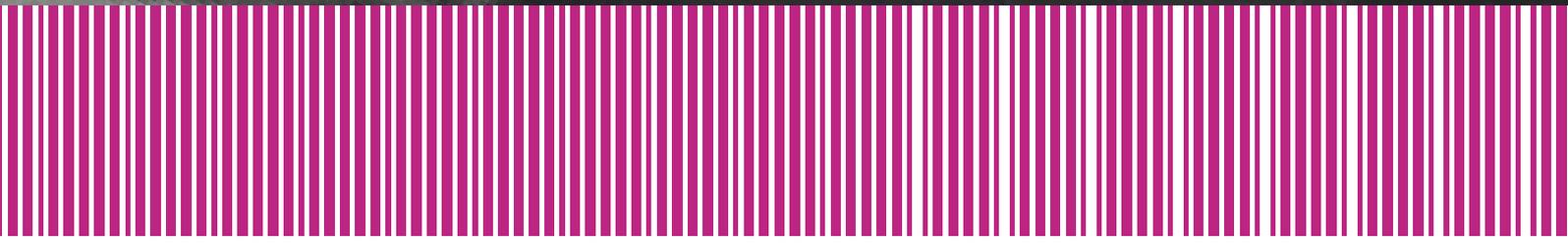
Finanstilsynet will hold regular national crisis drills, ensure good collaboration with other affected national authorities, and participate in international crisis exercises and in international supervisory collaboration for cross-border institutions. Finanstilsynet will play its part in ensuring that the guarantee schemes, including the deposit guarantee, function as intended and are practised in such a way as to minimise inconveniences to the individual customer. Further, Finanstilsynet will discharge its responsibility related to the Financial Infrastructure Crisis Preparedness Committee so that any crisis in this area can be handled in a satisfactory manner.

Instruments

Finanstilsynet's activity is wide-ranging and requires active use of various instruments, on their own or in combination; in the supervisory effort, risk and materiality are given priority.

To achieve its goals, Finanstilsynet makes use of the following instruments:

- supervision and monitoring
- licensing
- regulatory development
- information and communication



IMPORTANT EVENTS IN 2010



SUPERVISION AND MONITORING

Close follow-up of banks in 2010 as previously

At on-site inspections Finanstilsynet looks at banks' risk exposure and their governance and controls with particular emphasis on financial strength and liquidity. In 2010 70 inspections were carried out at banks in Norway, more than ever before. These included thematic inspections of investment advice, compliance with the money laundering legislation, capital adequacy reporting and IT inspections. In addition to close follow-up of banks through on-site inspections, Finanstilsynet evaluated, and gave written responses to, banks' assessments of own risk and capital needs (ICAAP).

Guidelines for prudent lending practices for bank lending for housing purposes

In March 2010 Finanstilsynet published new guidelines for prudent home mortgage lending practices. The guidelines require banks to apply a thoroughgoing process when assessing borrowers' ability to pay and to ensure that as a rule a mortgage loan does not exceed 90 per cent of property value. Finanstilsynet's survey in autumn 2010 showed that the largest banks had revised their procedures as a result of the new guidelines. Finanstilsynet continued to check compliance with the new guidelines, including in the home loan survey in autumn 2010. In 2011 Finanstilsynet will conduct thematic inspections focusing on compliance with the guidelines.

Assessment of financial stability – half-yearly publishing of analyses

Macroprudential supervision has acquired a more prominent role internationally. Finanstilsynet has carried on macroeconomic monitoring since 1994, and has each spring since 2002 published the report *The Financial Market in Norway*. Finanstilsynet decided in 2010 to publish reports analysing financial stability on a twice-yearly basis. As from 2011 *Risk Outlook* is to be published in the spring and *Financial Trends* in the autumn.

Thematic inspections of sales of structured savings products

In 2010 Finanstilsynet surveyed sales of savings products in 2009 and 2010 at almost 30 banks, including all the largest ones. The surveys were followed by on-site inspections at eight banks in 2010. With one exception, no bank had sold complex savings products or granted any loan directly connected with the savings product in question in the period. The survey showed that advisers' remuneration was product-neutral at seven of the eight inspected banks. Finanstilsynet's observation is that banks can do more to sell lower-priced funds, and that many savers would be well served by including index funds and bond funds in their portfolio.

Criticisms levelled at several large investment firms after inspection

Finanstilsynet conducted on-site inspections at several large investment firms in 2010. It focused in particular on firms' compliance function, their information handling and handling of conflicts of interest. Finanstilsynet also examined the quality of firms' periodic reporting, and in several cases brought to light seriously flawed reports. A number of firms received sharp criticism. Finanstilsynet checks firms to verify that they come into line with the supervisory comments made.

Banks' compliance with new money laundering legislation

In the first half of 2010 Finanstilsynet conducted on-site inspections at a selection of financial institutions to verify their compliance with the Act relating to measures to combat money laundering and the financing of terrorism etc (Money Laundering Act). The inspections showed that Norwegian banks and financial institutions are not satisfactorily in compliance with the new legislation, and triggered improvements at the institutions.

Outsourcing of banks' ICT functions

In May 2010 Finanstilsynet issued a circular to financial institutions warning of the risk associated with outsourcing banks' central ICT functions to high-risk areas. The risk associated with relocating operating functions connected to banks' ledger and payment systems to high-risk countries is too high to be acceptable.

Norwegian financial institutions have little exposure to countries with government debt problems

In early summer 2010 Finanstilsynet conducted a detailed survey of Norwegian financial institutions' exposure to Portugal, Italy, Ireland, Greece and Spain. The survey was based on the institutions' ordinary reports to Finanstilsynet. Overall exposure to these countries was small, and no institution had significant exposure to Greece.

Establishment of a central counterparty (CCP) for clearing equity instruments

In April 2010 Oslo Clearing ASA was granted a licence to operate as a clearing house for equity instruments. Finanstilsynet closely followed the start-up of the clearing business. Thus far experiences with clearing equity instruments appear good.

Lack of market data in valuation of investment property

In 2010 Finanstilsynet examined some issuers' valuation of investment property. The survey showed that valuing investment property poses challenges, and that the market for commercial property in Norway is illiquid and non-transparent. Greater openness in the market would enable valuations based on discounted cash flows to a greater degree to reflect market conditions on the balance sheet date. The survey results are published in a separate report. The survey is being followed up on a case-by-case basis.

Thematic inspections directed at auditors' obligations when considering assignments

In spring 2010 Finanstilsynet conducted a round of thematic inspections focused on auditors' obligations when considering whether to accept and/or continue an assignment, including change of auditor. Compliance with the Auditors Act's provisions in this regard is an important contribution to preventing the continuation of business that is not run in compliance with the applicable rules. Contact between the former and the new auditor will ensure that the new auditor has a particular focus on circumstances that need to be rectified. The synoptic report prepared after the round of inspections, along with preceding years' thematic inspections, will be published on Finanstilsynet's website.

LICENSING

Gjensidige Forsikring converted to a public limited company

In May 2010 Finanstilsynet recommended the Ministry of Finance to approve Gjensidige Forsikring BA's application for permission to convert to a public limited company and to convert Gjensidigestiftelsen ('Gjensidige Foundation') to a 'financial foundation'. The Ministry of Finance authorised Gjensidige to carry out the conversion in June 2010.

Guaranteed interest rate lowered in life insurance

Finanstilsynet decided to lower the maximum guaranteed interest rate in life insurance to 2.5 per cent for all life insurance contracts

written after 1 January 2011. Accordingly the highest permissible guaranteed interest rate that Norwegian life insurance and pension funds can employ when computing premiums and technical provisions in respect of new pension benefits earned under collective annuity and pension insurances must as from 1 January 2012 not exceed 2.5 per cent.

New rules on hedge funds and venture funds

The provisions of the Securities Funds Act dealing with hedge funds and venture funds and provisions on such funds in regulations to the same act entered into force on 1 July 2010. Hedge funds and pension funds can feature very differing levels of risk and protection, and may involve high risk taking. The Ministry of Finance intends that hedge funds and venture funds should be neither marketed nor sold to non-professional customers, and that this shall apply regardless of whether the initiative comes from the customer or the firm. In 2010 Finanstilsynet issued three licences to establish Norwegian hedge funds and venture funds and six licences to market foreign hedge funds and venture funds in Norway.

REGULATORY DEVELOPMENT

New, stricter capital and liquidity requirements on banks

Against the background of the international financial crisis the Basel Committee on Banking Supervision presented in December 2010 new capital and liquidity standards for the banking industry, Basel III, to be introduced step-by-step in the period 2013–2019. These standards will be incorporated as amendments to the EU capital adequacy directive, CRD IV, due to be adopted in the course of 2011 and transposed into Norwegian legislation by the turn of 2012. Previous regulatory tightening, in the shape of CRD II and III, was carried through in Norwegian law at the turn of 2011. A number of the provisions will not enter into force until 31 December 2011.

Proposed new legislation on securities funds

Finanstilsynet has headed a working group drawing representatives from authorities and the industry which has proposed a new securities trading act with regulations. The working group's proposal was sent to the Ministry of Finance in June before being circulated for comment and returned to the ministry for further consideration. The working group's proposal for regulations was sent to the ministry in January 2011. A new body of rules is expected to apply as from July 2011.

New asset management rules for insurance

Upon Finanstilsynet's proposal, new regulations on asset management for insurance were laid down by the Ministry of Finance in December 2010. The changes give life insurance and pension funds greater scope to invest in unlisted securities and in shares issued by companies that operate or own infrastructure. The changes will facilitate longer-term asset management.

Proposed regulations on remuneration at financial institutions forwarded to the Ministry of Finance

Measures to discourage remuneration schemes that heighten risk in the financial market are an important aspect of the international regulatory effort. Finanstilsynet's proposal with regard to remuneration will ensure openness and sound processes at all financial institutions and investment firms and will encourage continued moderate practices at banks.

Guidelines for stress testing and guidelines for concentration risk

The Committee of European Banking Supervisors (CEBS) published on 26 August revised guidelines for stress testing and revised guidelines for concentration risk. Both sets of guidelines were put into effect on 31 December 2010. Finanstilsynet expects financial institutions to start their work on implementing the guidelines by this date and to pay due regard to the guidelines in their continuing work on stress testing and assessment of concentration risk. Finanstilsynet will incorporate the new guidelines in its supervisory methodology.

Investment firms' remuneration systems and compensation from parties other than the customer

The Ministry of Finance and Finanstilsynet have examined the requirements made of investment firms' remuneration systems by the rules governing conflicts of interest, and conclude that a remuneration system for investment advisers that directly links remuneration to the customer's investments is in conflict with the Securities Trading Act. When conducting their business, investment firms must ensure that the customer's interests are protected in the best possible manner.

Amendments to the estate agency legislation

With effect from 1 July 2010 amendments were adopted in some provisions of the Estate Agency Act. The amendments relate to rules on winding up estate agency firms, own-account trading and estate agent in charge. EEA obligations under Directive 2005/36/EC on Recognition of Professional Qualifications regarding EEA nationals' right of temporary establishment were also implemented.

NEW TASKS

Finanstilsynet takes over prospectus control as from 1 May 2010

Responsibility for operative prospectus control for transferable securities, which previously rested with Oslo Børs, was transferred to Finanstilsynet with effect from 1 May 2010. This is part of the adjustment to common European rules in the securities area.

Finanstilsynet takes over the management of and secretariat function for the Financial Infrastructure Preparedness Committee

As from 1 June 2010 Finanstilsynet took over management and secretariat functions for the Financial Infrastructure Preparedness Committee. These functions have hitherto rested with Norges Bank.



Finanstilsynet's Board of Directors has by law the overarching responsibility for the agency's activities and handles important matters in relation to regulations and licences, budgets and action plans. The Board has five members. Members and alternates are appointed by the Ministry of Finance for a four-year period.

ORGANISATIONAL SET-UP AND RESOURCE USE



BOARD OF DIRECTORS

The present Board comprises:

Endre Skjørestad, lawyer, chair

Vivi Lassen, assistant director, deputy chair

Hilde C. Bjørnland, professor, board member

Mette Bjørndal, professor, board member

Harald Indresøvdde, former bank manager, board member

Beate Sjøfjell, associate professor, first alternate

Jostein Skaar, department director, second alternate

Birger Vikøren, director at Norges Bank, attends as observer.

Arild J. Lund, director, is his alternate.

A new Board was appointed at Finanstilsynet on 1 March 2010, and the new chair, **Endre Skjørestad**, was appointed as from 15 April 2010. The previous chairman, **Finn Hvistendahl**, acted as chairman until the new chairman took over. Former bank manager **Harald Indresøvdde** was appointed as a new board member as from 26 March 2010. **Birger Vikøren**, Norges Bank's observer to the Board, was on leave until 15 April 2010. **Arild J. Lund**, director at Norge

Bank, was observer up to that date and **Sindre Weme**, assistant director at Norges Bank, was alternate observer during this period.

Two members elected by and from among the employees supplement the Board when administrative matters are dealt with. As from February 2009 the employee representatives were:

Marit Sletta, senior adviser

Knut Godager, special adviser

Their alternates were senior adviser **Øyvind Jenssen**, head of international relations, **Nina Moss** and head of section **Lone Tudborg Lakhan**.

Eleven ordinary board meetings were held in 2010. The Board dealt with a total of 46 administrative matters and 57 supervisory matters requiring decisions. The Board received information on a further 54 administrative matters and 68 supervisory matters, bringing total items received to 225. In addition, the Board is given a verbal briefing at each meeting on relevant matters that have been or are being dealt with by the administration.



The Board of Directors of Finanstilsynet

Endre Skjørestad, Vivi Lassen, Hilde C. Bjørnland, Mette Bjørndal, Harald Indresøvdde, Beate Sjøfjell, Jostein Skaar, Birger Vikøren, Marit Sletta and Knut Godager
Photo: CF-Wesenberg@kolonihaven.no



Finanstilsynets Management Team

Bjørn Skogstad Aamo, Emil Steffensen, Eirik Bunæs, Anne Merethe Bellamy, Cecilie Ask, Gun Margareth Moy and Kjetil Karsrud
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ACCOMPLISHMENT OF PRIORITIES IN 2010

Finanstilsynet's supervisory activities start out from the tasks imposed on it by law, the Ministry of Finance's annual letter of allocation (which is based on the budget adopted by the Storting, the Norwegian Parliament), and Finanstilsynet's strategy. Based on the priorities set out in Proposition no. 1 to the Storting (2009–2010), which are acted upon in the letter of allocation, the Board of Directors of Finanstilsynet resolved that the following tasks should have highest priority in 2010.

The points below give an overview of the execution of the tasks with highest priority in 2010, as elaborated in Finanstilsynet's business plan for 2010.

1. In 2010, there were no serious problems for Norwegian financial institutions as a result of the financial crisis. Through close contact with possible buyers, problems at one smaller insurance company were resolved without problems for policyholders.
2. Finanstilsynet drafted amendments to regulations to implement CRD II and CRD III, the EU's initial legislative response to the financial crisis. Steps were taken in cooperation with other Nordic supervisory authorities to prepare the implementation of the new regulatory framework developed after the financial crisis (Basel III). Finanstilsynet played an active part in discussions with European supervisory bodies and in the deliberations of Norway's Financial Crisis Commission.
3. Finanstilsynet conducted a record number of 337 on-site inspections in 2010. Of these, 70 were in banking and finance, 12 at insurance companies and 24 at investment firms. Particular emphasis is placed on sound capital positions with respect to risk, adequate liquidity and good control of risk arising from the use of ICT systems.
4. Finanstilsynet kept a close watch on developments in institutions and markets. A risk report on the state of the financial market was prepared at the start of 2010, and a report on financial trends was prepared in October 2010. Special guidelines for good home mortgage lending practice were implemented in light of developments in home mortgage lending.
5. Preparation of new solvency regulations for insurance companies (Solvency II) is well under way, and a comprehensive survey of possible impacts (QIS5) has been carried out.
6. Operational prospectus control was taken over from the Oslo Stock Exchange as from 1 May, and has worked well under Finanstilsynet's auspices.
7. A central counterparty (CCP) solution was established in the securities settlement system. The continuous reporting by investment firms, including TRS reports, is followed closely.
8. The supervision of auditors and audit firms that audit public interest companies was prioritised, inter alia by conducting more audit firm inspections. Work on changes to the auditor register continued, including the allocation of auditor numbers to statutory auditors.
9. A series of on-site inspections was carried out at investment firms and banks to ensure good business practice and good advisory services with a view to protecting consumers and investors.
10. 31 new staff members were appointed, and staff turnover was low (9 per cent). 66 staff have more than five years' experience in areas under supervision. A new survey of the work environment was carried out, prompting further strengthening of the work environment with regard to internal communication.
11. Following user surveys among entities under supervision, industry organisations and collaborating authorities, a new strategy for Finanstilsynet was developed and adopted.
12. The change of name to Finanstilsynet and relocation to new premises was completed, providing a sound basis for further developing in-house corporate culture and good relations with partner bodies.

ADMINISTRATION, STAFF AND GENDER EQUALITY

Finanstilsynet's Director General is appointed by the King in Council for a six-year term. **Bjørn Skogstad Aamo** was appointed for a new six-year term in February 2005, with effect from April 2005.

The Director General's salary at the end of 2010 totalled NOK 1,194,000. The Chairman of the Board's remuneration was NOK 195,000, the Deputy Chair's remuneration was NOK 135,000, remuneration for board members was NOK 115,000, and remuneration for alternates was NOK 35,000. Remuneration per meeting attended was NOK 7,000.

Fifty-two vacancies were advertised in 2010 compared with 44 in 2009. Sixteen of these were in-house, compared with ten in 2009. Applicants totalled 938 in 2010 compared with 976 in 2009.

At the end of 2010, Finanstilsynet had 261 full-time staff, compared with 246 at the end of 2009. Fifty-two per cent of full-time staff are women. Eighty-nine per cent of staff hold a university degree or the equivalent.

Women made up 43 per cent of Finanstilsynet's management team in 2010, and 46 per cent of all staff with managerial responsibilities. Women employees' pay measured 85.9 per cent of men's pay in 2010, compared with 87.7 per cent in 2009.

The gender equality effort is anchored in the work-environment and gender-equality committee whose meetings are attended by a gender equality representative on a regular basis. The committee routinely reviews pay statistics for each job category, and for Finanstilsynet as a whole, to keep abreast of developments in pay equality, which is a priority area of the in-house pay policy. The committee also reviews other equality-related issues. Finanstilsynet's action plan for equality, adopted in February 2007, was developed on the basis of a broad understanding of the concept of equality, and thus also covers ethnic origin, disability and age.

Key to Finanstilsynet's pay and personnel policy are measures to recruit, develop and retain staff with a high level of competence in areas under supervision. Through its active use of instruments,

Finanstilsynet has assured that it has the competence needed to execute its tasks in a sound, effective manner.

At the end of 2010, 66 members of staff had solid experience (generally more than five years) from industries under supervision. Staff turnover in 2010 was 9 per cent, compared with 6 per cent in 2009. Finanstilsynet has thus proven successful at retaining staff with long supervisory experience and staff who have developed a high level of expertise during their career with Finanstilsynet. A flexible pay and personnel policy is needed to achieve this.

Finanstilsynet conducted a work environment survey in spring 2010. The survey showed improved results compared with the previous survey in 2008. Feedback from the survey reveals good employee-manager relations and a strong professional commitment and positive corporate culture. The survey also pointed to challenges facing the organisation in terms of in-house communication and knowledge sharing. Remedial initiatives have been developed, and Finanstilsynet will address both organisational culture and technical solutions with a view to enhancing employee satisfaction in these areas.

Chart 1: Staff educational background as at 31.12.2010



Inclusive workplace

With its espousal of the Government-sponsored "IA Agreement" designed to promote inclusive employment, Finanstilsynet attaches much importance to preventing and following up sickness absence. Achieving this requires close cooperation with the corporate health service and the Norwegian Labour and Welfare Administration (NAV). The work environment committee follows up sickness absences and recommends measures when necessary. The work environment and gender equality committee monitors sickness absence and the advisability of initiating measures. Sickness absence fell from 4.8 per cent in 2009 to 3.4 per cent in 2010.

The IA Agreement is designed to prevent discrimination of job applicants with functional impairments and to raise the de facto retirement age. Finanstilsynet stresses its aspiration for diversity with respect to ethnic background, functional capacity, gender and age in job vacancy advertisements, and at least one applicant from an

under-represented group is invariably called in for interview provided the qualification requirements are met.

Cases and case processing time

In keeping with Finanstilsynet's strategy, specific targets are set for the time spent on a selection of administrative cases and for supervisory reports and resulting observations. The aim is to process 90 per cent of administrative cases within 30 days. A longer period is allowed for some types of complex cases. The deadline for supervisory reports and ensuing observations varies from one area of supervision to the next.

In 2010, an improvement was registered in all areas compared with 2009 apart from supervisory observations. Results nevertheless fell short of targets in 2010, and case processing time needs to be reduced. Target attainment was poorest for licence applications with a processing deadline longer than 30 days. The main contributor here is excessive time spent on approval of articles of association in the securities area.

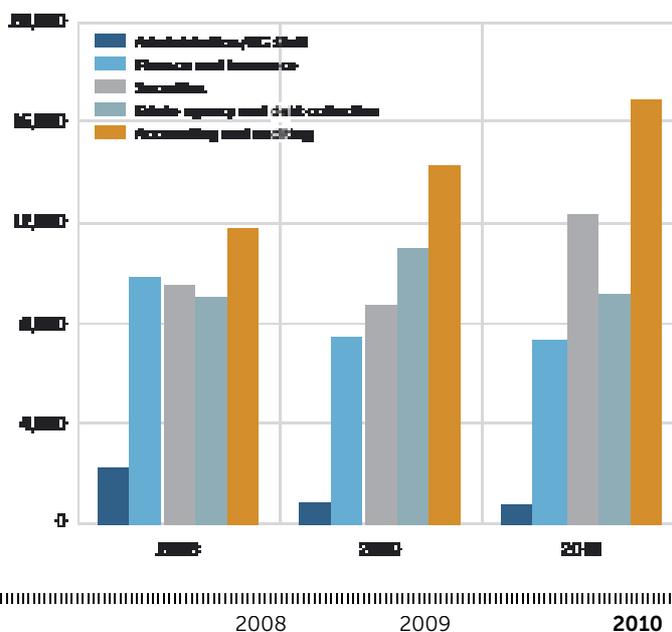
Table 1: Case processing time at Finanstilsynet in 2010

	2009		2010	
	No. of cases	Target attainment	No. of cases	Target attainment
Total no. of cases with processing time target	4,049	65%	3,546	78%
- Cases with 30-day deadline	3,174	78%	3,425	79%
- Cases with deadline longer than 30 days	875 *	19% **	121	53%
Supervisory reports	194	81%	222	81%
Supervisory observations	181	78%	189	72%

* 769 of these cases are appeals against the Register of Company Accounts' refusal to waive late filing penalties.

** The appeals were placed in abeyance pending designation of a new appeal body. The Norwegian National Collection Agency took over this task on 1 January 2010.

Chart 2: Registered case documents – by sector*



	2008	2009	2010
Total number of cases	42,300	42,241	46,470

* Cases in the finance and securities sector are often more complex than cases in other sectors.

The number of incoming and outgoing documents registered in 2010 was about 4,200 higher than in 2009, partly because Finanstilsynet took over operative responsibility for prospectus control from the Oslo Stock Exchange on 1 May 2010. For real estate, the number of case documents fell in 2010 after an increase in 2009 due to the renewal of all licences by year-end.

Efficiency improvements

Developing new, and further developing existing, technical solutions has been an important contributor to improving the efficiency and quality of the basis for supervisory work. It has been necessary to adjust internal routines and modes of collaboration. A three-year data warehouse project was completed in January 2011. The project aimed to devise better solutions for reporting and analysis by collating data from various sources, in addition to optimising reporting. Improved solutions make it easier to see relationships both within and between institutions. Entities under supervision are increasingly using the Altinn internet portal to file reports, making for gains in both efficiency and quality. Preparations have also been made for the introduction of Altinn II. In the administrative sphere Finanstilsynet

has installed a public electronic mail journal and established an electronic management handbook.

Security and crisis preparedness

Finanstilsynet aspires to being a confidence-inspiring and reliable agency, and acknowledges its security responsibilities towards entities under its supervision, its staff and central authorities. The agency accordingly works continuously on security and preparedness both in its core area of operation and within its own organisation. Finanstilsynet adheres to Norges Bank’s security regulations, which cover physical security and preparedness with respect to office premises. Finanstilsynet has specific security and crisis preparedness plans in place for the various areas under supervision in the financial market, including technical infrastructure. Finanstilsynet has ethical guidelines for its employees, and internal routines for its activities, including routines for secure case handling. Separate security rules apply to internal ICT solutions and the technical infrastructure. Safety tests are regularly conducted in the area of ICT. A secondary site of operation has been established in preparedness for crisis situations. Regular tests and exercises are carried out.

FINANCES

Expenditure

The Storting determines Finanstilsynet's budget as part of the government budget. The budget for 2010 originally totalled NOK 286.9 million. An additional appropriation of NOK 4.5 million was made as compensation for the public sector wage settlement. Including NOK 5.2 million carried forward from 2009, the budget came to NOK 296.6 million. Finanstilsynet received an additional NOK 4.4 million in refunds of parental and sickness benefits. The aggregate disposable budget accordingly came to NOK 301.0 million, while aggregate expenditure came to NOK 293.0 million, an increase of 9.9 per cent. Total salary expenditure rose by 15.3 per cent, and expenditure on goods and services decreased by 0.7 per cent. Finanstilsynet's aggregate expenditure was NOK 8.0 million less than disposable revenues. Unutilised revenues are carried forward to 2011.

As in the case of other government agencies included in the central government accounts, Finanstilsynet's accounts are prepared on a cash basis and, in contrast to private businesses, not an accruals basis. The accounts are prepared with a basis in the central government chart of accounts, which employs natural classification of revenues and expenses. Based on this chart, Finanstilsynet has classified expenditures by function. The main classification by function is shown in Table 2.

The closing letter dated 28 May 2010 from the Office of the Auditor General on the accounts for 2009 had no adverse comments about the accounts or Finanstilsynet's implementation of the budget.

Table 2: Accounts

	2008	2009	2010
Salaries	154,593	175,516	202,491
Of which:			
Salaries and social costs (all positions)	150,756	169,745	197,486
Stand-ins/Substitutes	3,144	4,975	4,002
Other emoluments (directors, consultants, other fees)	693	796	1,003
Goods and services	81,607	91,220	90,553
Of which:			
Operating expenses	35,558	43,957	38,780
Information	2,930	2,728	2,154
Travel and meeting attendance, subscriptions	7,173	7,863	8,355
Inspections and other supervisory work	3,795	3,754	3,467
Organisation development, management and competence development	4,671	4,318	5,657
ICT expenditure	27,480	28,600	32,140
Total expenditure	236,200	266,736	293,044

Figures in NOK 1000s
(Preliminary accounts for 2010)

Comments

The salaries bill, in particular, was considerably higher in 2010. The increase, of NOK 27 million, is explained by staff increases and the general increase in pay. The reduction in operating expenses was NOK 0.7 million. The increase in ICT expenses should be viewed in light of larger requirements on electronic systems for reporting, analysis and work processes.

Revenues

Under section 9 of the Financial Supervision Act, Finanstilsynet's expenses are covered by the institutions under its supervision at the start of the financial year. The Storting therefore adopts a revenue appropriation equal to the expenditure appropriation. The Act requires the expenses to be apportioned among the various institutional groups based on the extent of supervision, and expenses

are therefore paid in arrears. Contributions are also claimed from branches of companies from other EEA states.

The total amount levied for 2009 and due for payment in 2010 was NOK 247.1 million. The levy was smaller than actual expenses because a) the levy is based on the budget appropriation, b) any amount carried forward from the previous year is deducted and c) part of the expenses are covered by the National Insurance Scheme Fund through refunds of parental and sickness benefit outlays. The levy proposed by Finanstilsynet for 2009 was approved by the Ministry of Finance on 3 June 2010 after prior consultation with the trade organisations concerned. Supervised entities liable to pay the amount levied for 2009 numbered 12,575, of which 75 were foreign branches. The largest category of supervised entities is accountants, numbering 8,780. The overall figure in 2008 was 12,003 entities.

Chart 3: Levy distributed on supervised groups

Percentage of total levy

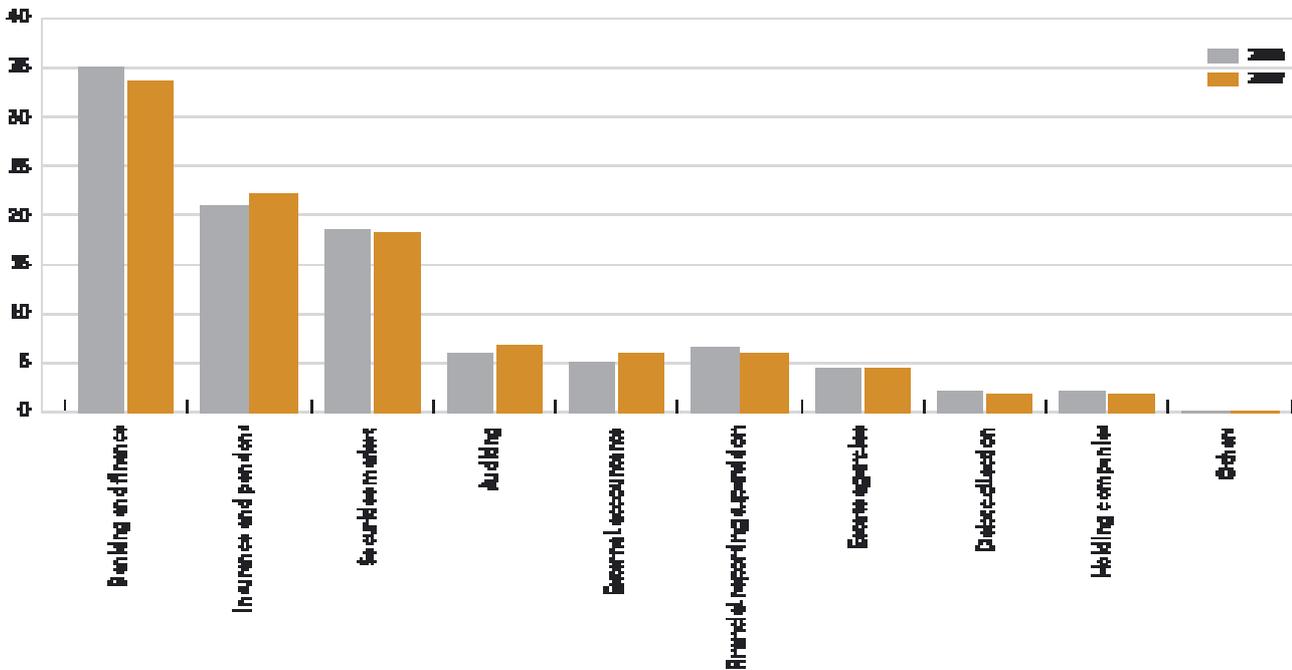


Table 3: Total levy as a percentage of the calculation base

Supervised groups	Calculation base	Percentage of calculation base	
		2008	2009
Credit institutions	Total assets	0.0021	0.0018
Insurance	Premium income	0.0314	0.0360
Investment firms	Income from investment and ancillary services	0.1858	0.1929
Management companies	Assets under management	0.0025	0.0023
Estate agency	Commission income	0.2525	0.2361
Debt collection	Debt collection proceeds	0.1894	0.1631
Auditors	Turnover	0.2481	0.2676

Table 3 shows the size of the levy as a percentage of the calculation base for various groups of supervised entities. External accountants are omitted from the table since they pay an identical annual levy irrespective of turnover (NOK 1,606 at the assessment for 2009). Expenditure on financial reporting supervision is in principle covered by Oslo Børs, which then recovers its costs from the listed companies. Finanstilsynet is taking over this task as from the assessment for 2010.

Resource input by area of supervision

Table 4 shows an increase in resource input from 2009 to 2010 equivalent to 14 full-time positions. A new area for 2010 is prospectus control, accounting for an increase equivalent to 6.5 full-time positions. The table shows resource input in the various areas.

ORGANISATIONAL SET-UP AND RESOURCE USE

Table 4: Resource input by area of supervision

	2008		2009		2010	
	FTEs	%	FTEs	%	FTEs	%
Banks	44.7	21.7	47.6	21.1	49.8	20.8
Finance companies	2.3	1.1	2.3	1.0	2.3	1.0
Mortgage companies	2.7	1.3	3.1	1.4	3.2	1.3
Insurers	25.4	12.3	31.0	13.8	33.6	14.1
Holding companies	3.2	1.6	3.1	1.4	3.4	1.4
Pension funds	7.0	3.4	6.3	2.8	7.6	3.2
Securities market	32.8	15.9	36.3	16.1	37.3	15.6
Prospectus control					6.5	2.7
Estate agents	8.2	4.0	8.7	3.9	7.8	3.3
Debt collection	3.4	1.6	2.9	1.3	2.8	1.2
Auditors	8.8	4.3	12.1	5.4	13.1	5.5
Accounting rules et al.	0.1	0.0	0.2	0.1	0.4	0.2
Financial reporting	9.5	4.6	8.9	3.9	7.9	3.3
External accountants	8.6	4.2	9.2	4.1	10.1	4.2
Miscellaneous	3.3	1.6	4.2	1.9	2.7	1.1
Undistributed	46.3	22.4	49.0	21.8	50.5	21.1
Total	206.3	100	225	100	239	100

KEY FIGURES AND DATA ON SUPERVISORY ACTIVITIES

Table 5: Figures for supervised entities as at 31.12.2010

	2006	2007	2008	2009	2010
Banks and financial institutions					
Savings banks	124	123	121	118	113
Commercial banks	15	16	18	20	20
Finance companies and mortgage companies	41	41	46	59	57
Foreign branches of Norwegian banks and other credit institutions	16	16	13	16	17
Norwegian branches of foreign banks and credit institutions	29	32	46	44	35
E-money institutions					
E-money institutions	4	3	3	3	3
Insurance					
Life insurers	9	10	11	12	12
Non-life insurers	44	44	45	45	44
Local marine insurance associations	13	13	13	13	13
Local fire insurance associations	20	20	20	20	20
Norwegian insurers' foreign branches ¹			9	11	5
Norwegian branches of foreign insurers	41	46	44	41	43
Insurance intermediaries ²	73	91	103	97	98
Private pension funds	91	86	81	76	66
Municipal pension funds	28	29	30	31	31
Pension schemes	19	17	15	9	8
Holding companies					
Holding companies	9	12	12	11	11
Securities institutions					
Investment firms ³	85	132	154	150	154
Norwegian branches of foreign investment firms	9	10	13	17	17
Fund management companies	23	23	22	26	27
Clearing houses	3	3	3	3	2
The Norwegian Central Securities Depository	1	1	1	1	1
Regulated markets, incl. stock exchanges	3	6	5	6	5
Auditors					
Auditors	5,567	5,670	5,777	5,943	6,210
Audit firms	730	789	825	820	776
External accountants					
External accountants	7,472	7,966	8,340	8,780	9,260
External accounting firms	2,652	2,691	2,676	2,693	2,691
Estate agency					
Estate agency firms	682	717	611	516	550
Lawyers' practices incl. estate agencies	1,355	1,324	1,307	1,346	1,294
Cooperative building associations	38	37	24	14	4
Debt collection					
Debt collection agencies	117	112	110	105	102
Debt purchase businesses	6	8	5	6	5

Finanstilsynet also oversees the financial reporting of some 240 listed firms.

BBS (Banking and Business Solutions) and EDB Business Partner ASA are not under the direct supervision of Finanstilsynet, but are relevant to Finanstilsynet’s supervisory activities as providers of technical solutions to Norwegian financial institutions.

Table 6: Number of on-site inspections by type of institution (incl. IT inspections*)

	2006	2007	2008	2009	2010
Banks/finance	49	49	37	58	70
E-money institutions	1	–	–	–	–
Holding companies	–	–	–	–	–
Insurers	5	6	6	8	12
Insurance intermediaries	5	3	3	7	6
Pension funds	1	2	6	4	8
Investment firms	18	20	19	21	24
Other securities institutions (incl. fund management companies)	7	6	1	3	5
Auditors	52	22	29	47	87
External accountants	46	41	60	49	58
Estate agencies	40	51	66	30	49
Debt collection agencies	5	6	13	12	13
Data processing centres/IT providers	3	4	4	2	4
Other	1	–	–	–	1

* Twenty-six IT inspections were conducted, either singly or in conjunction with ordinary on-site inspections. Finanstilsynet also conducted 31 simplified IT inspections and processed 18 notifications received under the Payment Systems Act after investigating compliance with the requirement to notify any establishment of new, or changes to existing, payment systems.

Table 7: Cases handled after delegation from the Ministry of Finance

	2006	2007	2008	2009	2010
Cases pursuant to the Savings Banks Act (No. 1 of 24 May 1961)	71	53	46	93	50
Cases pursuant to the Commercial Banks Act (No. 2 of 24 May 1961)	27	7	7	18	24
Cases pursuant to the Financial Institutions Act (No. 40 of 10 June 1988)	149	119	140	222	139
Cases pursuant to the Insurance Activity Act (No. 39 of 10 June 1988)	71 ⁴	2	–	–	–
Cases pursuant to Act (No. 44 of 10 June 2005) on Insurers, Pension Trusts and their Activities ⁵	–	58	208 ⁶	108	95
Cases pursuant to the Guarantee Schemes Act (No. 75 of 6 December 1996)	–	–	–	–	–

Notes to the tables:

¹ There is no statistics on this prior to 2008.

² The number of insurance intermediaries has increased since the Act on Insurance Mediation came into force on 1 January 2006. Insurance agent firms that distribute insurances exclusively for Norwegian insurers are not included in this overview, nor are entities engaged in accessory insurance agent business, i.e. entities whose business includes insurance mediation on a part-time basis.

³ The number of investment firms with licences has greatly increased since the new Securities Trading Act came into force on 1 November 2007.

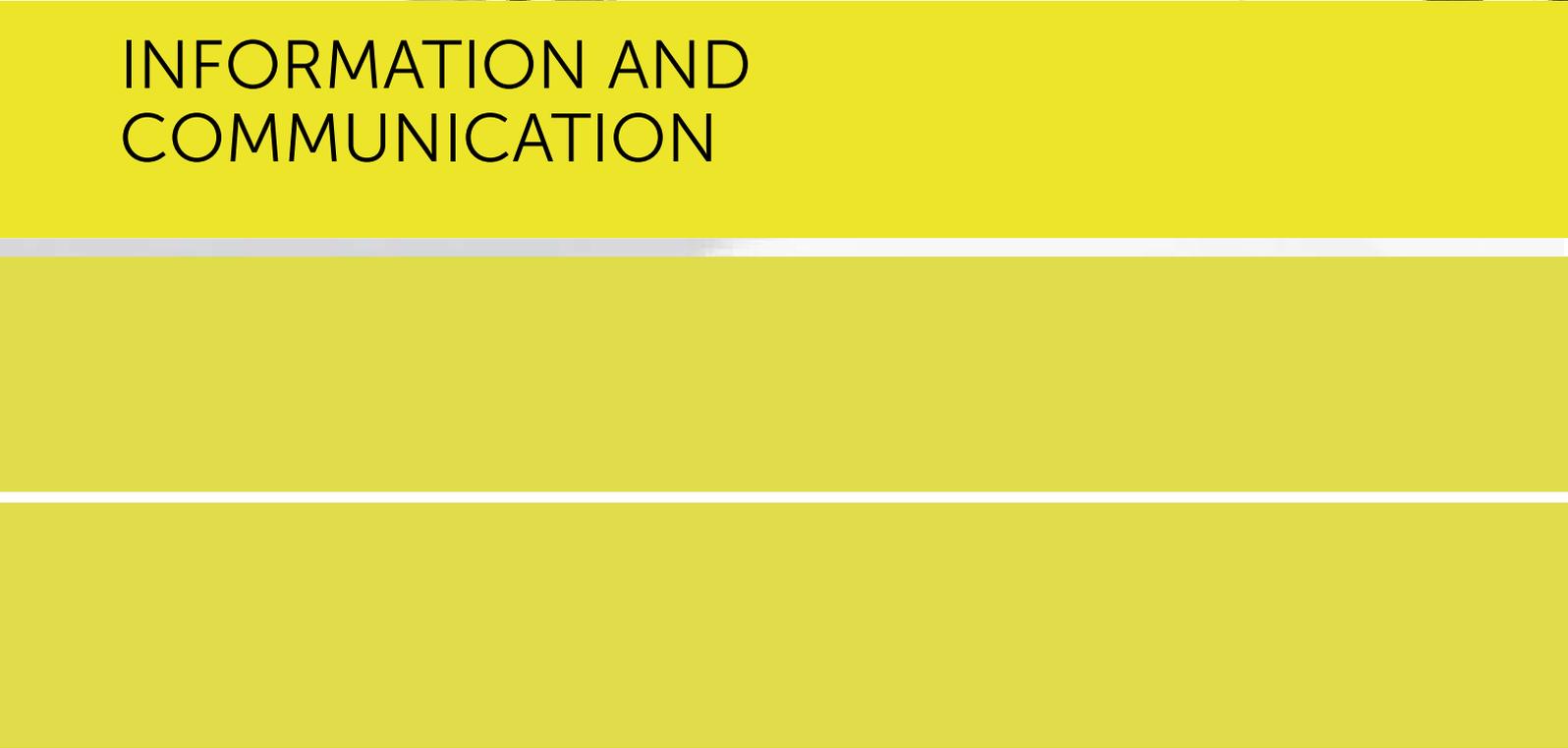
⁴ This figure includes decisions pursuant to both the new and the old Insurance Activity Act.

⁵ This Act came into force on 1 July 2006, but parts of the earlier Insurance Activity Act were in force until 1 January 2008.

⁶ The large number of cases in 2008 is due mainly to the licensing requirement imposed on pension funds by the Insurance Activity Act.



INFORMATION AND COMMUNICATION



INFORMATION

In Finanstilsynet's strategy, *information and communication* comprise one of four strategic instruments of supervision, along with *supervision and monitoring*, *licensing* and *regulatory development*. The information effort is directed in the first instance at institutions and sectors under supervision, and is based on the principles guiding the central government information policy. Finanstilsynet's approach to information and communication is guided by the line principle and the principle of information as a management responsibility. Given Finanstilsynet's many areas of responsibility featuring extensive bodies of rules and complex issues, information and communication are necessarily a management responsibility in the various areas of supervision. The new main strategy and the new communications strategy were drafted with a basis in the central government communications policy adopted in October 2009.

Finanstilsynet has an extensive network of contacts, and meets regularly with collaborating public authorities in Norway and elsewhere and with trade organisations. Collaboration with the Consumer Council is formalised in a special agreement. See also the chart of Finanstilsynet's key relations at the back of this annual report.

Kredittilsynet changed name to Finanstilsynet on 21 December 2009. While the new name is now familiar to other government bodies and the financial sector, general profile surveys show that most people have little knowledge of Finanstilsynet after the name change. On the other hand, surveys among respondents with a knowledge of the organisation show that Finanstilsynet enjoys a good standing. This is confirmed by user surveys carried out in 2010.

USER SURVEYS IN 2010

Finanstilsynet conducts user surveys every few years to obtain input able to improve the organisation's operations. In 2010 Finanstilsynet carried out two user surveys in conjunction with the strategy process. One survey, which was quantitative, was directed at entities under supervision. The other survey was qualitative and directed towards industry organisations, collaborating authorities and some of the largest firms under supervision.

Quantitative user survey

According to the quantitative user survey, which is representative of entities under supervision, firms are generally satisfied with Finanstilsynet's work. The results show improvement compared with equivalent surveys last carried out in 2004 and 2006. The survey also uncovered areas with potential for improvement. In all, 766 entities responded to the survey. This gave a response rate of 64 per cent, which is a great improvement compared with 2004 and 2006.

The survey aimed to gauge users' satisfaction with Finanstilsynet, and to provide Finanstilsynet with a basis for identifying areas for improvement. The survey was conducted by TNS Gallup on behalf of Finanstilsynet in May–June 2010.

A total of 64 quality and service characteristics of Finanstilsynet were evaluated on the basis of users' satisfaction. Users were also asked to rate the importance of the topic concerned. The topics surveyed were:

- Administrative procedures and enforcement of laws and regulations (9 quality indices)
- Inspections (12 quality indices)
- Finanstilsynet's analyses (4 quality indices)
- Reporting (13 quality indices)
- Information from Finanstilsynet (10 quality indices)
- Finanstilsynet's website (4 quality indices)
- Communication with Finanstilsynet (7 quality indices)
- Finanstilsynet's competence within the field (4 quality indices)

Finanstilsynet achieved an average score of 67 on the TRI*M index, indicating a very positive relationship to Finanstilsynet among its users. A score of over 60 is regarded as good, especially since the survey covered opinions about a supervisory authority and not a service organisation.

Compared with the previous surveys from 2004 and 2006, users are consistently more satisfied with Finanstilsynet in 2010.

The analysis shows that Finanstilsynet's *strengths* are first and foremost its competence, inspection activities and the information it provides.

Finanstilsynet's *weaknesses* are first and foremost case processing and enforcement of laws and regulations, and communication with Finanstilsynet.

Finanstilsynet achieved its best score among finance companies (81), savings banks/commercial banks (75) and non-life insurance/local marine insurance associations (73). The next best scores were with insurance brokers and debt collection and agencies (69 in both cases), estate agents (65), and external accountancy firms and life insurers (64 in both cases).

The weakest scores were among investment firms (61), audit firms (60) and fund management companies (49).

Qualitative user survey

The qualitative survey largely confirmed the results from the quantitative survey. Confidence in Finanstilsynet's activities is substantial. However, some larger securities firms and fund management

companies were dissatisfied with Finanstilsynet in some respects, viz. case processing time, supervisory practices and practices with regard to information disclosure and sanctions.

Follow-up of user surveys

The results from the user surveys are used as a basis in the strategy process, and will be closely assessed and will underlie the operations planning process in 2011. Survey feedback items already raised to the strategic level through Finanstilsynet's new strategy include the need to reduce case processing time (especially in the securities area). The strategy also states that supervisory practices and practice regarding information disclosure and sanctions in the securities area constitute a supervisory standard and will remain unchanged.

SEMINARS AND PRESENTATIONS

Finanstilsynet participates widely in seminars for trade organisations and institutions under supervision, and numerous presentations are given on the agency's activities and tasks, as well as on rules and guidelines affecting supervised entities. Representatives from Finanstilsynet give presentations on the agency's activities in teaching programmes organised by education institutions. In

June and December 2010 Finanstilsynet, in cooperation with the Oslo Stock Exchange, organised seminars for investment firms on topical issues in the securities field. There was also extensive contact between Finanstilsynet and the banking and insurance sector regarding new legislation on capital and liquidity requirements and solvency.

CIRCULARS AND PRESS RELEASES ETC

Nineteen circulars were issued in 2010 compared with 20 in 2009, and superseded or obsolete circulars were removed. An overview of removed circulars was published in Circular 1/2011. Firms and other interested parties can register on Finanstilsynet's website to be notified whenever a new circular is published.

Finanstilsynet issued 42 press releases in 2010, compared to 38 in 2009. A press conference was held at the end of February to present the annual report for 2009 and the report *The Financial Market in Norway 2009: Risk Outlook*. A press briefing was held in March to

present the report *Risk and Vulnerability Analysis* which takes up the risk attending use of ICT in the financial sector. In October the *Financial Trends 2010* report, a half-yearly summary of the situation in the financial market, was presented.

Finanstilsynet received good media coverage in 2010. A broad range of Finanstilsynet's supervision activities were highlighted. The home mortgage lending survey and the regulations on remuneration in financial institutions that Finanstilsynet prepared for the Ministry of Finance were news features in early March. Outsourcing of IT systems

to foreign countries was covered in conjunction with the presentation of the risk and vulnerability report. New capital requirements for Norwegian banks, and follow-up of the home mortgage lending survey from spring 2010 also received positive attention in October.

A key channel for communication with the world at large is the letters written and distributed by Finanstilsynet each year. A total of 17,516 letters were sent (outgoing documents) in 2010. A central aim is to write in a style that is clear and understandable to the recipients.

FINANSTILSYNET'S WEBSITE

The website is the main channel for information from Finanstilsynet, and is set up to make it simple for all types of firms to find information on rules, licensing requirements, reporting etc., applying to their particular line of business. The website also features a searchable licence register of all firms and individuals under Finanstilsynet's supervision. The register is the most used service on the website. The website also provides an overview of market warnings against firms

that are not licensed to engage in the business they are pursuing. When Finanstilsynet took over operative control of prospectuses from Oslo Stock Exchange on 1 May, the website was enlarged to provide an overview of controlled prospectuses. In 2010, the Finanstilsynet.no website had 150,000 unique visitors, accounting for 395,000 visits all told. Around 15 per cent of all visits were made by users outside Norway.

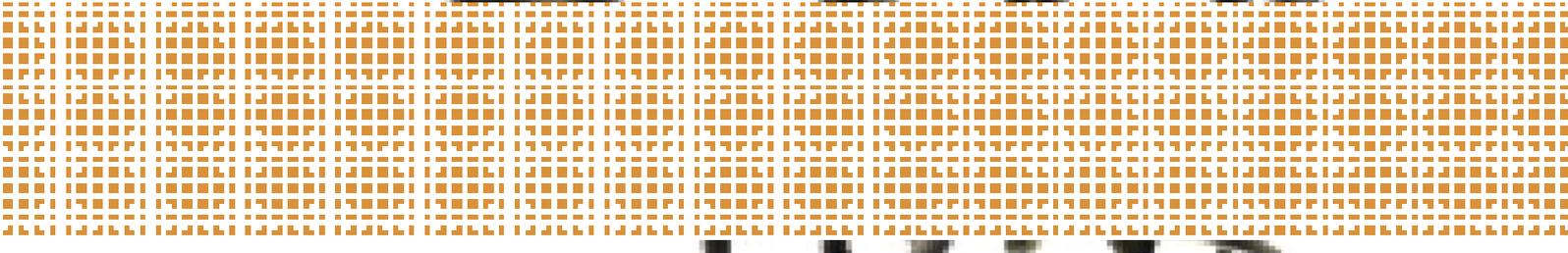
DOCUMENT ACCESS AT FINANSTILSYNET

Finanstilsynet received a total of 652 requests for document access involving orders for 3,531 documents in 2010. Of these, 2,958 were in the public domain, 231 were distributed as public versions, and 342 were not released since their entire content was barred from

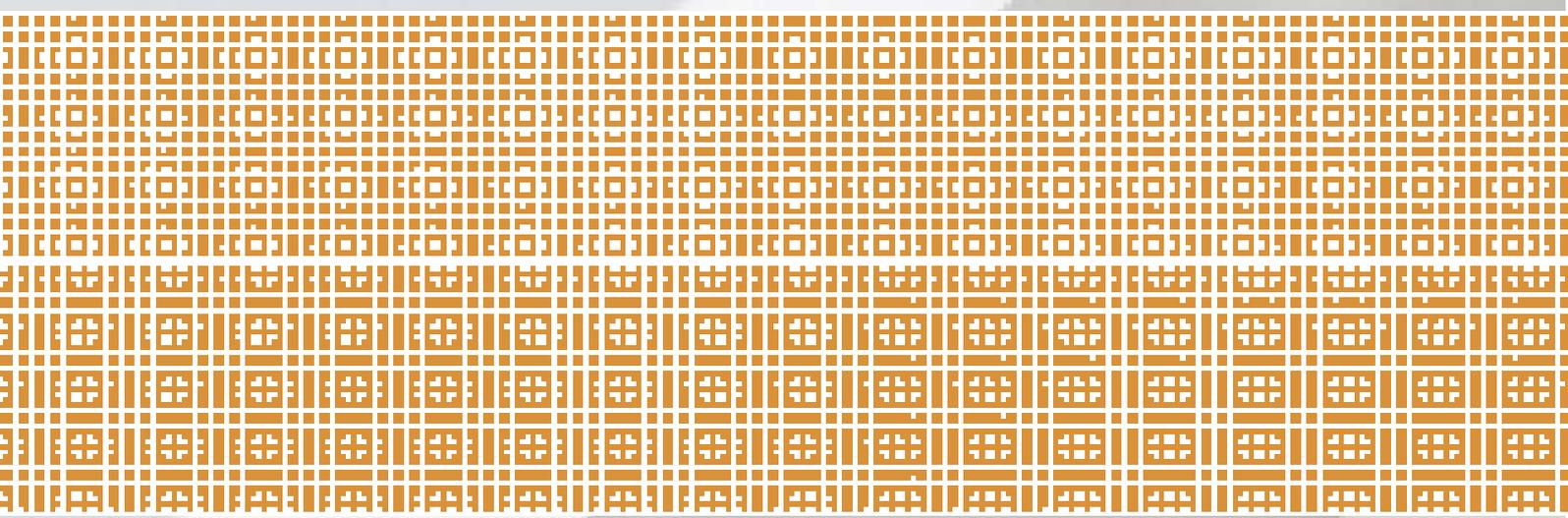
publication. On an annual basis there has been a slight increase in requests for access since Finanstilsynet hooked up to the new public electronic mail journal in July 2010. Most access requests are now received through this portal.

Table 8: Requests for document access

	2008	2009	2010
Orders placed	2,916	3,155	3,531
Not released	429	248	342



CONSUMER PROTECTION



CONSUMER PROTECTION THROUGH SUPERVISION

Important economic considerations and the desire to protect consumers and investors underlie Finanstilsynet's main goal – to promote financial stability and well-functioning markets. Banking crises and securities market crashes can result in heavy economic losses and costs for the consumer. Financial stability and confidence in banks' and insurers' ability to discharge their basic functions are related to the reallocation of capital and risk and are a prerequisite for good consumer protection.

Supervised entities manage capital in important areas on behalf of their customers, for example bank depositors, insurance policyholders and investors in securities markets. Should uncertainty arise about the safety of banks and insurance companies the upshot may be increased costs and higher prices for financial services for the consumer and, at worst, loss of capital. A significant part of consumer protection must therefore be achieved through the regulation and supervision of companies' liquidity and solvency, and through various public guarantee schemes, such as banks' deposit guarantees. Protection of consumer interests in the form of continuing oversight is therefore largely indirect, but also direct through checks on compliance with specific rules and regulations.

Supervision of institutions focuses on financial position and operations and on entities' compliance with the rules governing their activities and general rules of conduct. Continuous supervision of the solvency of financial institutions gives consumers security for their deposits, and ensures that current agreements with the institutions stand firm. Supervision of fund management companies, insurance companies and pension funds also involves a "product check" for the benefit of consumers.

Ministry of Finance clarifies Finanstilsynet's mandate

Consumer protection in the financial sector is gaining ever more attention. Responsibility for consumer protection has been fragmented since tasks have been assigned to various ministries and various directorates and supervisory agencies. This prompted Finanstilsynet to send the Ministry of Finance, in May 2009, a preliminary report entitled *Kredittilsynet's contribution to consumer protection and information*. At the same juncture Finanstilsynet asked the ministry to clarify Finanstilsynet's mandate with regard to consumer protection and information (see also the discussion in Finanstilsynet's Annual Report 2009, page 37).

After the report had been circulated to relevant parties for comment, the Ministry of Finance stated in a letter of 30 July 2010 that consumer protection and information is an important aspect of

Finanstilsynet's mandate, and proposed no change in the distribution of responsibility. The ministry emphasises that it is even more important than before for Finanstilsynet to pay close attention to this area in the period ahead.

"Finanstilsynet's mandate follows directly from the Financial Supervision Act, the annual budget set by the Storting and the annual allocation letter from the Ministry"; according to the ministry's letter. Finanstilsynet oversees financial market participants and ensures compliance with laws and regulations. Collaboration with consumer authorities and industry organisations to ensure that consumers receive objective and reliable information about financial products and attendant risks is as a central priority of the mandate.

From this it follows that a task of Finanstilsynet is to safeguard the aims of the financial legislation. It also requires Finanstilsynet to see to it that institutions at all times comply with rules laid down to protect consumers, for instance in the Financial Contracts Act; that legislation governing businesses is complied with; and that violations of laws and regulations are quickly dealt with.

Given the complexities inherent in today's financial market, and the many new products being marketed, it is, says the Ministry of Finance, more important than ever for Finanstilsynet to spend time on consumer issues and to provide effective supervision in this area, which includes making sure that companies provide relevant and understandable information about financial products.

Finanstilsynet has taken signals from the ministry into account in its new strategy (see the presentation on pages 6–9) and stepped up its work on consumer issues as from autumn 2010.

Besides the continuing supervision that underlies consumer protection, the following measures were taken in 2010 to strengthen consumer interests:

New guidelines for home mortgage loans

In the spring of 2010 Finanstilsynet introduced guidelines for home mortgage lending (see also the discussion in *Banking and finance*, page 39). It did so in the knowledge that both the international financial crisis and previous crises have shown the danger of a sharp increase in debt and house prices. High debt, high loan-to-value ratios, a floating interest rate and low repayments make many Norwegian households vulnerable to interest rate hikes or economic setbacks. In the interest of the consumer and financial stability it is important to contribute to more robust home financing and greater stability in the housing market.

New Securities Fund Act

Investing in securities is a regulated and safe form of saving for consumers with limited knowledge of the securities market. In 2010 Finanstilsynet headed the effort to frame new rules for securities funds.

Follow-up of financial advisory services

Follow-up of financial advisers is central to the protection of consumer interests. The need for consumer and investor protection is substantial because of many products' complexity, because the financial consequences for savers can be far-reaching and difficult to grasp, and because the incentive systems employed by providers of such products are in some cases designed in such a way that insufficient emphasis is given to the customer's goals and capital position.

Finanstilsynet oversees that investment firms licensed to provide investment advisory services related to financial instruments (including banks with such licences) comply with detailed requirements for good business conduct. As a part of its supervision of banks and investment firms, Finanstilsynet surveyed in 2010 savings products sold in 2009 by a selection of 29 banks, including all the largest banks. The survey was followed by on-site inspections at eight banks. The inspections showed that only one bank had sold complex savings products or granted loans that were directly linked to the savings product concerned in this period. At seven of the eight inspected banks, adviser salaries were product neutral. Finanstilsynet notes that banks could do more to sell lower-priced funds, and that many savers would be well served by including index and bond funds in their portfolio.

Finanstilsynet will continue to verify companies' ability to document that the products they have sold are suitable for the customer, and

that the customer has received sufficiently individualised, balanced and accurate information on investment risk.

Finanstilsynet warns against disreputable market actors

Finanstilsynet published 30 warnings against companies that had provided financial services in Norway in 2010 without the requisite licence. A further 338 warnings given by foreign supervisory authorities were published. Very often these firms are engaged in some form of fraud, and individuals who transfer money to such firms must in many cases consider the money lost. Finanstilsynet published market warnings on its website, cited warnings given by foreign supervisory authorities and posted notices in the media to warn consumers against dealing with such firms. Finanstilsynet's website also contains information on investment fraud, advising investors on how to protect themselves against fraudsters. As from November 2010, Finanstilsynet's market warnings are also available at Finansportalen.no.

Payment systems and online banks exposed to crime

Organised internet crime in the form of attacks on technical solutions in the financial sector is a continuing problem. It particularly affects internet banking and internet shopping. After a long period without serious attacks in Norway, in 2010 attacks were again recorded against online banking solutions. Close cooperation between banks, industry organisations and authorities nationally and internationally has a preventive effect and helps to limit the consequences of attacks. In 2010, no direct losses were recorded as a result of this problem.

In the period 2006–2009, there were no serious skimming attacks, i.e. attacks involving the copying of the contents of the magnetic strip on credit cards, on Norwegian ATMs, to Finanstilsynet's knowledge. Criminal attacks using various forms of skimming equipment were however carried out on self-service machines at petrol stations, but not to the same extent as on ATMs. In 2009 point of sale terminals

(EFT/POS) were exposed to serious skimming attacks. Although the number of attacks fell after measures were put in place, they still represented a direct loss to banks. All customer losses were covered.

In 2010 ATMs were exposed to planned attacks using a sophisticated technical solution that evaded the anti-skimming measures that were now in place. Although active collaboration between banks, industry organisations and governments curbed the attacks, banks still suffered direct losses. Effective measures to stop the current attacks are under development and will be introduced step by step. Of the 2,180 ATMs installed in Norway, 42 were registered as being exposed to skimming or attempted skimming attacks in 2010.

Payment services are repeatedly exposed to attack by criminal groups. In 2010 both ATM and internet banking systems in Norway suffered. The heaviest losses arose however from crime targeting the use of debit and credit cards outside the country. To be effective, measures must in the main be based on international cooperation, updated security requirements, enforcement of those requirements along with effective measures to stop skimming and hacking into collection centres for card transactions. Finanstilsynet also considers it important to give card owners guidance on careful card use.

Survey of financial knowledge

In its report *Kredittilsynet's contribution to consumer protection and information* from 2009, Finanstilsynet concluded that all surveys conducted in Norway in recent years show limited knowledge in the population of the various types of financial products and services. With this in mind, Finanstilsynet decided in 2010 to grant researchers Ellen K. Nyhus (University of Agder) and Christian Poppe (SIFO) final funding for the project *Financial knowledge in Norway*. The project aims to gauge financial knowledge in a representative sample of the Norwegian population.

Greater focus on consumer protection in the EU

An increased focus on consumer information and consumer protection is in evidence in the EU in the wake of the financial crisis. When the new European supervisory authorities were established, the EU countries were agreed that they had a clear responsibility towards consumers. The new authorities (one for banking supervision, one for supervision of insurance and occupational pensions, and one for securities and market supervision) will promote a market for financial products that is transparent, simple and fair for consumers by collecting and analysing data on consumer trends, reviewing and coordinating financial literacy and education initiatives by national authorities, developing training standards for the industry and contributing to the development of common disclosure rules.

Estate agency and debt collection

Finanstilsynet's consumer protection tasks are most prominent in the supervision of estate agents and debt collection agencies, where consumer protection is an object of the legislation. Further details of the supervision of these areas in 2010 can be found under *Estate agency*, page 86, and *Debt collection*, page 90.



BANKING AND FINANCE

Banks are key actors in the financial system. Regulation and supervision are important contributors to financial stability and confidence in the financial system. Supervision of the banking and financial sector promotes solid financial institutions with good risk awareness, management and control. Financial service provision must be in compliance with the regulatory framework and in the best interest of society and the users of financial services.

SUPERVISION AND MONITORING

Monitoring and analysis

Monitoring and analysis of developments in the economy and markets and of the situation in the financial sector are prerequisites for the continuing supervision of individual institutions' liquidity and financial strength. Analyses are the basis for Finanstilsynet's assessment of the general state of the financial sector and for the supervision of individual institutions.

As part of the macroeconomic surveillance, half-yearly analyses and assessments are made of possible stability problems in the financial sector. The banks are crucial to financial stability. Quarterly reports on the situation of banks, finance companies and mortgage companies are also produced with emphasis on the trend in results, liquidity and financial position. Press releases in February, May, August and November summarise these analyses, which are also published in *Report for Financial Institutions* on Finanstilsynet's website. Overall assessments of the situation and various risks for Norwegian financial institutions in the light of developments in the economy and markets were published in the spring 2010 report *The Financial Market in Norway 2009: Risk Outlook* and in the autumn 2010 report *Financial Trends*. As from 2011 Finanstilsynet will publish *Risk Outlook* in the spring and *Financial Trends* in the autumn.

Reports submitted by institutions are an important basis for analysis and on-site inspections. A full overview of applicable reporting requirements is available on Finanstilsynet's website.

Finanstilsynet collaborates with Statistics Norway on the form, content and processing of reports submitted by banks, finance companies and mortgage companies through ORBOF (Statistics Norway's database of financial information from banks and finance companies).

Basel II led to a reorganisation of capital adequacy reporting by banks, finance and mortgage companies and holding companies in 2008 when Finanstilsynet introduced a new reporting regime based on EU-wide Guidelines on Common Reporting (COREP). A new technical reporting solution for COREP went into production in 2010. In view of the importance of capital adequacy reporting for supervision purposes, the old and new solutions operated in parallel in the first two quarters of 2010; as from the third quarter the new reporting solution was the only one in use.

Financial strength, liquidity and profitability at Norwegian banks

Knock-on effects of the international financial crisis caused Norwegian banks' aggregate profit in 2008 to fall to the level seen in the previous economic contraction in 2002–2003. In 2009, however,

Norwegian banks posted sound profit performances, and in 2010 a further improvement was noted along with high returns on equity. While the positive development is partly ascribable to one-time gains, the main reason is a favourable loss trend due to continuing corporate profits combined with only a moderate rise in unemployment. The figures also reflect satisfactory risk management and credit practices at most institutions. Banks' net interest revenues remain low due to intense competition for borrowers and depositors as well as to higher funding costs. Credit growth picked up significantly in late autumn 2010 after falling steeply through 2009 and into the first half of 2010. Corporate borrowing, the main factor behind the credit growth, rose through autumn 2010 in light of the improved economic outlook. Retail lending has shown greater stability, supported by low interest rates, increased consumer confidence and rising prices in the housing market.

In Norway bank loans to households account for about 60 per cent of total lending to the non-financial private sector, and 90 per cent of this figure is collateralised by residential property. Norwegian banks therefore have substantial indirect exposure to the housing market. As yet few households have opted to fix their mortgage rate. A high proportion of floating mortgage rates renders the household sector vulnerable to rate hikes. House prices in Norway have risen of late and – viewed in relation to consumer prices, building costs, rentals and households' disposable income – they are high in historical terms. Finanstilsynet's new guidelines for home loans are expected to prompt some tightening of bank lending, which could lead to a more robust situation for borrowers and banks in the event of a fall in house prices. See page 39 for a fuller account of the new guidelines.

According to a survey of banks' practice with regard to home loans, conducted by Finanstilsynet each autumn since 1994, loan-to-value ratios on a substantial proportion of loans granted have been high for a number of years. The autumn 2010 survey showed a decline in 100 per cent financing of house purchases, in particular for younger housebuyers. However, a substantial portion of home loans to the youngest housebuyers still exceed 90 per cent of property value. Due to the time lag between mortgage commitment and mortgage disbursement, it is by no means certain how far last autumn's survey captures banks' compliance with the new guidelines. Finanstilsynet will carry out a thematic on-site inspection in spring 2011 to determine banks' compliance with the guidelines.

In May 2010 Finanstilsynet surveyed Norwegian financial institutions' exposure to countries with government debt problems (Portugal, Italy, Ireland, Greece and Spain). Exposure was low overall, and no bank had significant exposure to Greece.

Banks' assessment of risk and capital needs (ICAAP)

A large number of banks bolstered their financial position in 2009 by raising funds in the market or by turning to the Government Finance Fund.

The main focus of monitoring banks' financial strength in 2010 was on ensuring that institutions do not reduce the minimum levels of core capital set by their board of directors and that actual tier 1 capital adequacy does not fall below the minimum levels.

As part of this effort the 17 largest banks and a selection of other institutions were instructed to submit the outcome of their ICAAP processes. Other banks' capital assessments were also evaluated and commented on by Finanstilsynet in the course of ordinary inspections. A total of 50 institutions received written evaluation from Finanstilsynet in 2010.

Finanstilsynet asked the board of directors of five banks to contemplate either increasing the actual core capital ratio or reducing the level of risk. In addition, the boards of several other institutions were asked to raise their internal core capital ratio *target*.

Liquidity monitoring

Banks' liquidity risk was closely monitored in 2010 by means of their liquidity reports and by on-site inspections.

Liquidity risk refers in the first instance to banks' ongoing refinancing needs in the domestic and international money and bond markets. These markets function well in normal periods, but may collapse entirely in periods where confidence in financial institutions' earnings and financial strength is impaired. In 2010 the markets for short-term financing functioned satisfactorily. Early in the summer of 2010 risk mark-ups rose substantially in the bond market, mainly as a result of increased risk on government securities issued by debt-burdened Euro countries. The sharp increase in the mark-up on these countries' government bonds spread to bank bonds in particular inasmuch as a number of major European banks are directly exposed to government debt in the debt-burdened countries. Norwegian banks had little direct exposure to these countries, but were affected by contagion effects spreading across money and capital markets.

Based on submitted figures, Finanstilsynet computes each quarter the ratio of banking groups' long-term funding to illiquid assets. Institutions with a funding structure that deviates substantially from the average of the 13 largest Norwegian-owned banks are followed up by letter, telephone or by on-site inspection. In 2010 a total of 24 banks were followed up in this manner. Finanstilsynet always evaluates liquidity risk during on-site inspections of small and mid-size banks.

Finanstilsynet frequently contacts funding units at the largest banks to obtain updated information on the market and the banks' liquidity position. See also the account below of the follow-up of banks' liquidity risk through on-site inspections.

On-site inspections

On-site inspections are important in identifying problem areas at individual banks with a view to starting a dialogue with the management team and board of directors at the earliest possible stage.

Finanstilsynet applies a risk-based supervisory methodology. Most resources are accordingly devoted to overseeing the systemically most important banks and areas deemed to pose the greatest risk at any time. On-site inspection is based on risk modules developed by Finanstilsynet with reference to international supervisory standards. The modules are a framework for determining banks' risk exposure and their management and control systems. The modules cover credit risk, market risk, liquidity risk, operational risk and overarching management and control. The modules are accessible on Finanstilsynet's website.

A total of 70 inspections were carried out at banks and finance and mortgage companies in 2010 compared with 58 in 2009. Eleven of the inspections were thematic inspections to review compliance with the money laundering legislation and nine were thematic inspections based on the banks' capital adequacy reports. This figure also includes six IT inspections, eight thematic inspections related to investment advice (see the chapter Securities Market Supervision on page 58) and one inspection prompted by an application for approval of internal models to compute credit risk and operational risk.

The main areas of risk at the two largest banks were macroeconomic developments in the Baltics, the outlook for shipping and risk exposure associated with acquisition financing. A further significant risk is posed by uncertain international economic prospects and possible negative knock-on effects for the Norwegian economy. Finanstilsynet emphasised that these factors will require banks to maintain a sound capital buffer ahead. Some banks will also need to review their capitalisation policy in light of new capital adequacy rules.

Matters to which attention was drawn included lack of compliance with policy adopted by the board of directors for the respective risk areas, flawed systems and routines for managing credit risk and weaknesses in the credit granting process.

In its feedback to the banks Finanstilsynet pointed out that transferring substantial loan portfolios to residential mortgage companies has a bearing on the risk present in a bank's remaining balance sheet.

In such cases higher deposit-to-loan ratios must be imposed as well as adequate market funding maturities. In several cases it was specifically pointed out that internal deposit-to-loan targets were too low.

Several banks received feedback on their exposure to and management of liquidity risk. In general Finanstilsynet expressed the view that banks need to prepare for tighter quantitative liquidity management requirements ahead. Some banks were also advised to improve their contingency plans for capital and liquidity crises.

Thematic inspections of compliance with the money laundering legislation

In 2010 a round of thematic inspections of compliance with the money laundering legislation was carried out at 11 institutions. The inspections showed that most of the examined institutions had fallen short of the steps required. This was especially true with regard to enhanced due diligence on new customers and requirements for risk-based assessment of the customer base. Finanstilsynet opted on the basis of the on-site inspections to send identically worded letters to all banks and finance and mortgage companies, asking them to review their internal systems and guidelines to ensure compliance with the legislation, and to prepare action plans with a view to risk-based customer due diligence.

Thematic inspections of capital adequacy reporting

A round of thematic inspections of capital adequacy reporting was carried out at nine institutions. Conclusions from the inspections will be finalised early in 2011. The inspections brought to light

examples of insufficient consolidation, incorrect reductions in respect of holdings in other institutions, faulty use of risk weights and faulty registration of off-balance sheet items. Conversations were also held with banks' external auditors. In Finanstilsynet's view the external auditor must conduct his own audit procedures to assure himself that financial reporting is reliable.

Accounts meetings

Management teams of the largest banking groups and Finanstilsynet's management team meet at least twice yearly. At these meetings the banks present new accounts data and describe developments in key risk factors. Moreover, updates are given on the markets in which the banks operate, on organisational matters and on strategic discussions at the individual bank.

Meetings with foreign branches

Finanstilsynet has supervisory responsibility for parts of the activity of branches of foreign credit institutions in Norway. The focus here is on the general good which essentially comes under the rules governing the relationship between institution and customer. Against this background Finanstilsynet has made the new guidelines for home loan financing applicable to foreign branches. The branches gave an account of other activities in Norway, of their interim financial statements and of any changes in group structure. In 2010 Finanstilsynet held meetings with the Norwegian branches of Handelsbanken AB, Danske Bank A/S (Fokus Bank), Skandiabanken AB, Citigroup, BNP Paribas, JP Morgan and Western Union International bank.

OTHER SUPERVISORY WORK

Guidelines for prudent home mortgage lending practices

Finanstilsynet published in March guidelines for prudent home mortgage lending practices (circular 11/2010). The guidelines are designed to limit the volume of large loans, both in relation to income and property value. The guidelines express Finanstilsynet's view of the criteria on which banks should base their lending practices.

The main requirements on banks' lending practice are a thorough-going assessment process, with particular emphasis on the borrower's ability to pay, and that a mortgage loan should not normally exceed 90 per cent of property value. All banks are required to prepare quarterly reports to the board of directors on their compliance with the guidelines.

Finanstilsynet's guidelines for home loans were prompted by the knowledge that both the international financial crisis and previous crises have shown the danger of a strong rise in debt and house prices. High debt, high loan-to-value ratios on property, floating interest rates and small debt repayments render a significant number of Norwegian households vulnerable to interest rate hikes or economic setbacks. In the interest of consumers and financial stability it is important to contribute to more robust home financing and greater stability in the housing market. In 2010 Finanstilsynet examined the 30 largest banks' adjustment to the new guidelines. Several banks have tightened their requirements on the actual lending process and clarified the terms with regard to debt servicing ability and maximum loan-to-value ratio. Banks' compliance with the guidelines on prudent home mortgage lending practices will be a theme for inspections in 2011.

Supervisory collaboration

Finanstilsynet collaborates with supervisory authorities in other countries on the supervision of financial institutions operating in countries in addition to Norway.

Norway has acceded to the EU's Memorandum of Understanding on Cooperation between the Financial Supervisory Authorities, Central Banks and Finance Ministries of the European Union on cross-border financial stability and a similar MoU between the Nordic and Baltic countries. See presentation in the chapter *International activities* on page 104.

In accordance with the EU capital adequacy directive, Finanstilsynet established in 2010 a college for supervisory authorities of countries in which the DnB NOR Group is heavily represented. The college include supervisory authorities from Denmark, Sweden, Poland, Luxembourg and the three Baltic countries. As DnB NOR's home countries supervisor, Finanstilsynet is the college's coordinating authority. Finanstilsynet participates in similar collaborative forums for eight other international banks with one or more subsidiaries or branches in Norway (Nordea, SEB, Swedbank, Société Générale, Santander, Crédit Agricole, Danske Bank and Handelsbanken).

LICENSING

Licence applications and dispensations

Finanstilsynet prepares a number of cases relating to licence applications and dispensations on behalf of the Ministry of Finance. Information on individual cases is published on both the Ministry of Finance's and Finanstilsynet's websites. Cases considered by Finanstilsynet in 2010 include the following:

- Brage Finans AS was authorised to operate as a finance company. The company offers financing products with emphasis on leasing. Brage Finans is owned by the following ten savings banks: Sparebanken Vest, Fana Sparebank, Sparebanken Sør, Helgeland Sparebank, Haugesund Sparebank, Skudenes og Aakra Sparebank, Flekkefjord Sparebank, Voss Sparebank, Luster Sparebank and Etne Sparebank.
- Ringerikes Sparebank, Sparebanken Jevnaker Lunner and Sparebanken Gran were authorised to merge. The acquiring bank, Ringerikes Sparebank, took over the savings bank business of Sparebanken Jevnaker Lunner and Sparebanken Gran, which were then wound up. Three savings bank foundations were established which will hold equity capital certificates (ECCs) in the merged entity, which has been named SpareBank 1 Ringerike Hadeland.
- Sparebanken Sogn og Fjordane and Fjaler Sparebank were authorised to merge. Sparebanken Sogn og Fjordane is the acquiring bank, and the merger was effected by transferring the savings bank business of Fjaler Sparebank to Sparebanken Sogn og Fjordane with the main settlement in equity capital certificates (ECCs). Fjaler Sparebank was thereafter wound up. A savings bank foundation, Sparebankstiftinga Fjaler, was concurrently established to which the overall settlement amount will be transferred. A further savings bank foundation, Sparebankstiftinga Sogn og Fjordane, was concurrently established, and is the holder of ECCs that are issued when parts of the ownerless capital of Sparebanken Sogn og Fjordane are converted to owners' equity.

- Høland Sparebank and Setskog Sparebank were authorised to merge. Høland Sparebank was the acquiring bank, and Setskog Sparebank was wound up. The new bank was named Høland og Setskog Sparebank. No savings bank foundations were set up in connection with the merger.
- SpareBank 1 SR-Bank and Kvinnherad Sparebank were authorised to merge. SpareBank 1 SR-bank was the acquiring bank and Kvinnherad Sparebank was wound up. The merger was effected by transferring Kvinnherad Sparebank's savings bank activity to SpareBank 1 SR-Bank, the main settlement being in ECCs. The savings bank foundation SpareBank 1-stiftinga Kvinnherad was concurrently established.
- DnB NOR Bank ASA and its subsidiary DnB NOR Finans AS were authorised to merge.
- Helgeland Sparebank was authorised to establish the savings bank foundation Sparebankstiftelsen Helgeland by converting parts of the bank's ownerless capital to ECCs owned by the foundation.
- PBS Holding A/S and Nordito AS were authorised to merge.
- Santander Consumer Bank AS was authorised to establish a special purpose entity for securitisation registered in Ireland as a private limited company.
- Totens Sparebank Boligkreditt AS was authorised to set up a residential mortgage company, established by Totens Sparebank.
- Landkreditt Boligkreditt AS was authorised to set up a residential mortgage company, established by Landkreditt Bank AS.

Permission to use internal (IRB) models to compute capital requirements

Financial institutions can use internal models to compute minimum capital charges for various categories of risk. Requirements for the use of such methods are set out in the capital requirements regulations, and require Finanstilsynet's permission.

In 2010 Finanstilsynet authorised the use of new IRB models at DnB NOR ASA for the card portfolio, a significant portion of the large client portfolio and for DnB NOR Finans.

The following institutions have previously been authorised to use the IRB approach for credit risk: DnB NOR ASA, DnB NOR Boligkreditt AS, Sparebanken Vest, Sparebanken Vest Boligkreditt AS, SpareBank 1 SR-Bank, SpareBank 1 SMN, SpareBank 1 Nord-Norge, Bank 1 Oslo AS, SpareBank 1 Boligkreditt AS, Nordea Bank Norway ASA, Nordea Eiendomskreditt AS and Nordea Finans Norway AS. Nordea Bank Norway is authorised to use the Value-at-Risk (VaR) method to compute the capital charge for market risk.

Supervision of ownership of financial institutions

In 2010 the following authorisations were granted pursuant to the Financial Institutions Act's rules on supervision of ownership of financial institutions:

- Skogbrand Forsikringsselskap Gjensidig's acquisition of a 12.47 per cent stake in Landbruksforsikring AS
- Diners Club Sweden AB's acquisition of a 100 per cent stake in Diners Club Norge AS

- Nortura SA's acquisition of a 25 per cent stake in Landbruksforsikring AS
- Eurocard AB – authorisation to acquire 100 per cent of Europay Norge AS
- SpareBank 1 Skadeforsikring AS's acquisition of a 100 per cent stake in Unison Forsikring ASA
- Verdia Holding's acquisition of a 20 per cent stake in Verdibanken AS
- SG Equipment Finance International GmbH's acquisition of a 100 per cent stake in SG Finans AS
- DnB NOR Bank ASA's acquisition of a further 49 per cent of the shares of the Danish bank Bank DnB NORD A/S from Norddeutsche Landesbank Girozentrale. Bank DnB NORD A/S becomes wholly owned by DnB NOR Bank ASA as a result of the acquisition.
- Dollar Financial U.K. Ltd's acquisition of a 100 per cent stake in Folkia AS.

Payment institutions

Since the entry into force of new regulations on payment institutions on 1 July 2010, Finanstilsynet has issued one authorisation:

- VINA Remittance Express AS was granted authorisation to provide payment services, i.e. money transfers from Norway to Vietnam.

REGULATORY DEVELOPMENT

Capital adequacy and liquidity

The Capital Requirements Directive (CRD), comprising Directive 2006/48/EC and Directive 2006/49/EC, was transposed into Norwegian legislation with effect from 1 January 2007. These documents are paralleled by recommendations in the Basel II framework issued by the Basel Committee on Banking Supervision. In the wake of the financial crisis both the Basel Committee and the EU Commission proposed and adopted changes to their bodies of rules.

As part of this process the EU has adopted amendments to the Capital Requirements Directive (CRD II and III). The amendments are based on recommendations from the Basel Committee. The Basel Committee has also adopted new capital and liquidity standards for the banking industry, known as Basel III. See account on pages 42–43. Basel III will in due course be incorporated in EU legislation through CRD IV.

On 19 March 2010 Finanstilsynet tabled amendments to regulations based on CRD II and III. The proposal was forwarded to the Ministry of Finance with a view to circulation for comment. The amendments include:

- i) Revised requirements on the quality of own funds through maximum limits for hybrid capital and overarching requirements on

characteristics of hybrid and tier 1 capital.

- ii) Clarification of the balance of responsibility between home country and host country.
- iii) Strengthening of supervision of institutions' liquidity.
- iv) Tightening of the rules governing large exposures.
- v) Strengthening of the provisions governing securitisation (not covered bonds).
- vi) Tighter requirements for use of the VaR method in the trading portfolio.

The rules on market risk and significant aspects of the rules on securitisation have been deferred, and will now apply as from 31 December 2011. Other changes were implemented with effect from 1 January 2011.

As a result of the proposed changes, and the uncertainty regarding future transitional provisions and possible further amendments, Finanstilsynet published on 15 October 2010 an account of the above on its website. The account points out that agreements on incurrence of hybrid capital and subordinated debt should contain terms conferring a right to repayment in the event that such capital can no longer be included in own funds.

New solvency and liquidity requirements – Basel III

The Basel Committee (the Basel Committee on Banking Supervision) is an international forum for development and cooperation in the field of banking regulation. The Committee, drawing members from 27 countries, frames guidelines and international standards for banks and banking industry supervisors.

The financial crisis brought to light a series of shortcomings in capital adequacy and liquidity management in the banking industry internationally. In response, the Basel Committee prepared new capital and liquidity standards designed to remedy these shortcomings. The new standards, published on 16 December 2010, are known as Basel III. The Basel Committee and the Committee of European Banking Supervisors (CEBS) concurrently published the results of a quantitative impact study (QIS) which evaluates the impact of the new standards.

Basel III will be incorporated in the EU Capital Requirements Directive (CRD IV) which will be transposed into Norwegian legislation in conformity with the EEA Agreement.

The main features of Basel III are:

1. Tighter requirements on capital and capital buffers

The Basel Committee has resolved that common tier 1 equity and non-common tier 1 equity should constitute respectively at least 4.5 per cent and 6 per cent of risk-weighted assets. This, combined with stricter qualitative requirements on non-common tier 1 capital in general and common tier 1 equity in particular, brings a clear-cut tightening of current requirements. The minimum requirement on own funds is kept unchanged at 8 per cent.

Capital buffer requirements are introduced to dampen the impact of economic and financial shocks: a capital conservation buffer capable of absorbing losses and ensuring that

capital does not fall below the minimum requirement during sharp downturns, and a countercyclical buffer designed to protect banks against exceptionally heavy losses that may be incurred in periods of strong credit growth. Both buffers will consist of common tier 1 equity. The capital conservation buffer will measure 2.5 per cent of risk-weighted assets, while the countercyclical buffer is designed such that banks must have larger buffers in periods of strong credit growth. However, the latter buffer must not exceed 2.5 per cent of risk weighted assets. Banks operating with common tier 1 equity below the sum of the minimum requirement and the buffer requirements will see restrictions on their dividend policy, bonus payments and share buybacks. These restrictions rise the smaller the difference is between actual capital and the minimum requirement.

2. Minimum leverage ratio (LR) requirement

This requirement supplements the risk-based minimum requirements. It is proposed that non-common tier 1 equity should constitute at least 3 per cent of a bank's exposure. 'Bank's exposure' means a bank's balance sheet in its entirety plus some off-balance sheet items.

3. Quantitative liquidity requirements

These requirements comprise a short-term liquidity buffer (Liquidity Coverage Ratio – LCR) and a requirement with regard to long-term stable financing (Stable Funding Ratio – NSFR). LCR is designed to ensure that banks hold sufficient unencumbered high-quality liquid assets that are readily convertible to cash to meet the need for liquidity during a stressed 30-day scenario. This scenario contains both institution-specific and market-inclusive stress elements. NSFR expresses a minimum level for the share of long-term stable funding in relation to the particular bank's assets.

The minimum requirements on own funds and buffers will be introduced step-by-step in the period 2013–2019. Both the leverage ratio and the two liquidity indicators will be monitored over a period and possibly adjusted before becoming binding minimum requirements in 2015 (LCR) and 2018 (LR and NSFR).

Other measures planned under the Basel III framework are deferred, in the first instance until 30 June 2011. This applies inter alia to contingent capital requirements specific to systemically important institutions.

About 250 European financial institutions participated in a quantitative impact study of the new standards. Participants from Norway were DnB NOR, Kommunalbanken, Sparebanken Hedmark, SpareBank 1 Nord-Norge, SpareBank 1 SMN, SpareBank 1 SR-Bank, Sparebanken Vest and Totens Sparebank. The calculations are based on figures as of 31 December 2009.

Had Basel III been in effect at the turn of 2010, the 50 largest European banks combined would have needed about EUR 50bn to meet the new requirements on common *tier 1 equity*, and a further EUR 200bn to have sufficient capital buffers to avoid dividend restrictions. By way of comparison these banks recorded an overall profit of EUR 84bn in 2009. Smaller banks emerge somewhat more favourably, although the figures in their regard are somewhat less representative.

Thanks to strict Norwegian regulation and supervisory practice, the new requirements on common tier 1 equity do not entail significant regulatory tightening for Norwegian banks. All the Norwegian participants' common tier 1 capital adequacy would have exceeded the buffer requirement of 7 (4.5 + 2.5) per cent. However, Norwegian banks' *hybrid and supplementary capital* will not meet the new quality requirements which state that such instruments must not incentivise

redemption. This capital must be gradually replaced, over a 10-year period starting in 2013, with new capital that meets the new requirements.

The calculations of *unweighted equity ratio* show that Norwegian banks will meet this supplementary capital requirement but that it could prove a challenge for institutions specialising in lending to low-risk segments. The Basel Committee is continuing its effort to formulate this requirement and is considering whether it should be made applicable to all financial institutions.

Calculations of the *liquidity indicators* suggest that many banks need to increase their holding of liquid funds, secure more long-term funding and/or reduce the most liquidity-demanding aspect of their business before the new minimum requirements take effect in 2015 (LCR) and 2018 (NSFR). The calculations suggest that smaller banks emerge somewhat more favourably than their larger counterparts, and that Norwegian banks do not differ significantly from other European banks. The results are highly uncertain, partly because the indicators are new and not yet finally formulated. Where Norwegian banks are concerned, it is worth pointing out that covered bonds are eligible for inclusion in the liquidity buffer, and that the Basel Committee is considering special rules for countries with a small market for government bonds.

As mentioned above, Basel III will be incorporated in the EU's Capital Requirements Directive (CRD IV) which is to be transposed into Norwegian legislation. CRD IV will apply as from the turn of 2013. The EU Commission plans to present a proposed Directive text by summer 2011. Norwegian authorities are closely watching the work done by the EU Commission and have taken the initiative for Nordic countries to coordinate their introduction of CRD IV.

The Norwegian Banks' Guarantee Fund and deposit insurance

In 2009 changes were made to the Deposit Guarantee Schemes Directive to harmonise cover levels and disbursement procedures. In 2010 the EU Commission tabled a proposal for a new directive, revising the current Deposit Guarantee Schemes Directive, which will further reduce the period for disbursement. If the changes are adopted and transposed into Norwegian law, the Norwegian Banks' Guarantee Fund will have first-line responsibility for all branches from other EEA countries, regardless of whether or not they have topping-up membership. The Fund will ring fence a minimum level of resources, stipulated in the directive, which cannot be used for support purposes. In the longer term a mandatory, mutual borrowing right will be introduced among all deposit guarantee schemes should a particular fund be short of resources.

On 19 May 2010 Finanstilsynet issued regulations setting requirements for the design of computer systems for members of the Banks' Guarantee Fund. The regulations are designed to enable the Fund and the administration board at a bank that has been placed under public administration to make speedy and correct payment of a sum equivalent to the guarantee provided by the Fund.

Payment institutions

New regulations on payment institutions entered into force in July 2010 against the background of the Payment Services Directive whose object is to introduce uniform rules on payment institutions across the EU. The rules are part of Norwegian legislation by virtue of their inclusion in the EEA agreement.

The Directive has a private-law and a public-law aspect. The private-law aspect is incorporated in the Financial Contracts Act as of 1 November 2009. This Act regulates the relationship between

institution and customer, and the Act's provisions on payment services etc will also apply to the relationship between a payment institution and its customers.

The public-law part of the Directive contains conduct of business rules applying to payment institutions, including licensing rules, requirements on applications and rules with regard to solvency and supervision.

Authorisation (a licence) is required to operate a payment institution in Norway. For more information on requirements with regard to licences and application procedures, see Finanstilsynet's website.

New regulations on remuneration schemes

In December 2010 the Ministry of Finance issued regulations on remuneration schemes at financial institutions, investment firms and fund management companies. The principles underlying the new regulations are broadly based on the requirements of the EU Capital Requirements Directive (CRD III), and will encompass senior employees and other employees and elected officers with tasks of substantial significance for an entity's risk exposure along with other employees and elected officers who carry out control tasks.

The principles of CRD III contain assumptions regarding variable remuneration based on accrual period and mechanisms for deferred payment. CRD III also sets requirements regarding the balance between cash and financial instruments. For senior management in banking, variable remuneration is limited to 50 per cent of fixed remuneration.

The regulations entered into force on 1 January 2011. Bonuses earned in 2010 or earlier and due for payment in 2011 will not be covered by the regulations.

Forms of capital and organisation in the savings bank sector

Amendments to the Financial Institutions Act regarding forms of capital and organisation in the savings bank sector became effective in summer 2009. Against the background of these amendments Finanstilsynet drafted, on commission from the Ministry of Finance, regulations governing the distribution of premium on the issuance of equity capital certificates by institutions that have issued such certificates previously. The ministry circulated the draft for comment in autumn 2010.

A number of applications regarding merger of savings banks, conversion of ownerless capital and conversion based in the above-mentioned amendments were considered in 2010. See “Licence applications and dispensations” on page 40 for further details.

Guidelines for stress testing and guidelines for concentration risk

New guidelines for stress testing and guidelines for concentration risk apply as from 31 December 2010. The guidelines have a basis in the publication by the Committee of European Banking Supervisors (CEBS) of revised guidelines for stress testing and revised guidelines for concentration risk. CEBS has concurrently published a position paper on the recognition of diversification gains under Pillar 2.

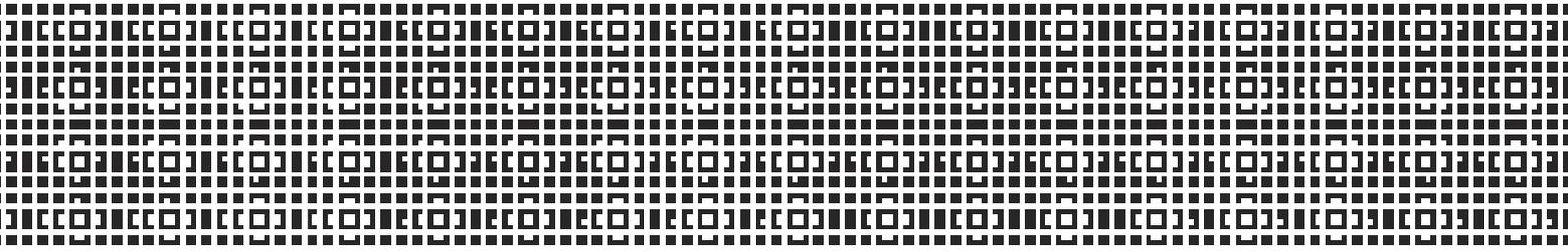
Evaluation of concentration risk and possible diversification gains should be viewed in conjunction with institutions’ stress tests and sensitivity analyses. Finanstilsynet emphasised that the guidelines should be implemented on a risk basis, i.e. consideration should be given to the individual institution’s size, complexity and risk profile.

The guidelines form part of the overarching guidelines for the Pillar 2 process and are a supplement to circular 21/2006 “Pillar 2 of the

new capital adequacy framework – guidelines for assessing risk levels and calculating capital needs” (available in Norwegian only). Finanstilsynet will incorporate the new guidelines in its supervisory methodology.

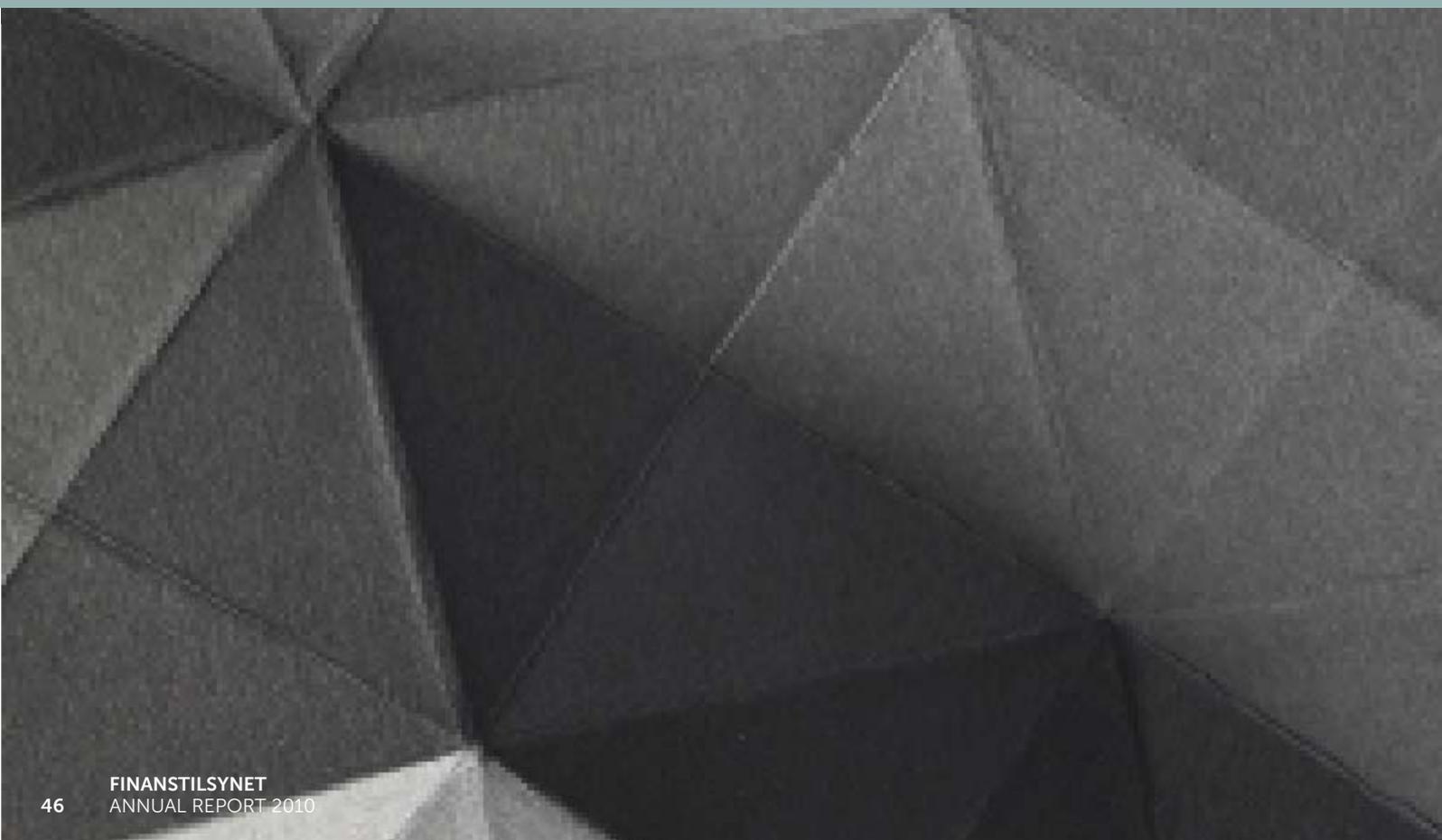
Advice on, and sale of, packaged retail investment products

A process aimed at coordinating requirements as to good business practice and information in connection with advice on and sale of packaged retail investment products (PRIPs) in the securities, insurance and banking areas has been initiated at the European level. The process aims to strengthen consumer protection by ensuring that the same requirements apply to the sale of comparable retail investment products. The EU Commission announced that a draft directive will be presented ahead of summer 2011.



INSURANCE AND PENSIONS

Regulation and supervision are important in safeguarding customers' short- and long-term rights under insurance and pension contracts, and in instilling public confidence in the market. The supervisory regime aims to foster financially solid, risk-aware companies and sound management and control. Supervision of the insurance industry also encompasses insurance intermediaries.



SUPERVISION AND MONITORING

Monitoring and analyses

Monitoring and analyses of developments in the economy and markets and of the situation in the financial sector is a prerequisite for oversight of individual institutions' liquidity and financial strength. The analyses provide the background for Finanstilsynet's assessment of the general state of the financial sector and its supervision of individual institutions.

Quarterly reports are prepared on profitability, financial strength and balance sheet composition at life insurers and non-life insurers, while reports for pension funds are half-yearly. Press releases in February, May, August and November summarise these analyses, which are also published in *Report for Financial Institutions* on Finanstilsynet's website. Overall assessments of the situation and of various risks faced by Norwegian financial institutions in light of developments in the economy and markets were published in spring 2010 in the report *The Financial Market in Norway 2009: Risk Outlook* and in autumn 2010 in the report *Financial Trends*. As from 2011 Finanstilsynet will publish its reports *Risk Outlook* in the spring and *Financial Trends* in the autumn.

Institutions' reporting is an important basis for analyses and on-site inspections. A complete overview of current requirements on reporting, along with updates on changes in the reporting regime, is available on Finanstilsynet's website.

Finanstilsynet collaborates with Statistics Norway on the quarterly reports filed by insurers through FORT (the Norwegian acronym for 'public financial and supervisory reporting by insurers'). As from 2009 pension funds are reporting along the same lines via PORT (the Norwegian acronym for 'public financial and supervisory reporting by pension funds').

Insurance companies, pension funds, defined contribution pension trusts and insurance holding companies are subject to capital adequacy rules and are required to report to Finanstilsynet.

Insurers report stress test results to Finanstilsynet on a quarterly basis. The tests, in which overall risk is measured against buffer capital, throw light on insurers' ability to meet applicable solvency requirements.

Finanstilsynet's stress test methodology and assumptions are modelled on those underlying the quantitative impact assessments under Solvency II under the auspices of the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS)¹. The

stress test is designed to track the impact of the new solvency regime up to its implementation in 2013.

In May 2010 Finanstilsynet surveyed Norwegian financial institutions' exposure to countries with sovereign debt problems (Portugal, Italy, Ireland, Greece and Spain). Exposure was low overall, and no institution had significant exposure to Greece.

Financial strength and profitability at Norwegian insurers and pension funds

Developments in securities markets have a direct impact on insurers' and pension funds' results, particularly so in recent years. After poor results in 2008, the stock market recovery in 2009 brought a substantial improvement in life insurers' position. In 2010 the overall value adjusted result was approximately on a par with the previous year. A negative first-half result due to developments in securities markets was offset by a positive trend through the autumn. For the period as a whole net interest revenues were the main contributor to the positive result.

At the start of 2009 life insurers had low buffers, and therefore less flexibility in asset management. Buffer capital fluctuated through 2010, but the positive stock market trend and good performances brought a substantial increase in buffers by year-end. However, stress testing showed that Norwegian life insurers' buffer capital is still inadequate in terms of the requirements that appear likely to result from Solvency II.

Somewhat higher levels of buffer capital gave insurers leeway to raise their shareholding through 2009 and 2010, while lowering their stock of fixed income securities. Insurers still hold a high proportion of bonds and CDs, however, and low interest rates will therefore continue to pose a challenge to insurers ahead.

For pension funds results were higher in 2010 than in 2009. Since a larger proportion of their total assets is invested in shares, pension funds are better placed than life insurers to achieve high return in a rising stock market. They are, however, far more vulnerable to a negative market trend. As in the case of life insurers, increased fluctuation reserves and improved performances bolstered pension funds' buffer capital in 2010.

On-site inspection

Life insurers

Four on-site inspections, including one IT inspection, were conducted at life insurers in 2010. The inspections had a basis in risk

¹ As of 1 January 2011 CEIOPS was replaced by the European Insurance and Occupational Pensions Authority (EIOPA).

modules designed with a view to the various areas of risk faced by life insurers.

The inspections focused on overarching governance and control systems. Matters raised included lack of documentation of, and accountability for, development and execution of strategies, guidelines and procedures in the insurance area and the asset management area. Attention was also drawn to deficient fit-and-proper testing, non-registration of insurance agents and defective procedures under the Insurance Contract Act. Aspects of the organisational set-up of one company were called into question, including ancillary tasks of the appointed actuary.

Pension trusts

In 2010 thematic inspections were conducted in the asset management area at eight large pension funds. Governance and control systems were found to be satisfactory. Finanstilsynet drew several pension funds' attention to deficiencies in strategy, investment limits, separation between asset manager and control functions, stress testing and associated processes, action required in connection with breaches of overall risk limits, monitoring of compliance with internal guidelines/statutory requirements and reporting to the board of directors. Experience gained with the thematic inspections was summarised in a synoptic report available at Finanstilsynet's website.

Non-life insurers

Inspections were conducted at five non-life insurers in 2010, one claims handling firm and one external accounting firm. One joint Nordic IT inspection of If was carried out.

Matters taken up after on-site inspections included breaches of minimum requirements with regard to capital adequacy and solvency margin capital, no strategy and business plan, no definition of the management board's risk tolerance, and no governance and control of outsourced business. Finanstilsynet emphasised the importance of a pro-active stance on risk and asset management processes. Other matters raised related to the introduction of systems and competence, inadequate documentation of significant expansion of areas of business, non-documentation of statutory audit and identification of operational risk.

Insurance intermediaries

On-site inspections were conducted at four insurance brokers and one insurance agent in 2010. One IT inspection was carried out at an insurance broker.

At the inspections it was pointed out that one and the same firm cannot engage both in insurance intermediation per se and intermediation akin to the business of an insurance agent since doing so may fall foul of the conduct of business rules, the ban on commission and the requirement of independence. It was also pointed out that the requirements of the risk management regulations must be complied with even where a firm is subject to parent company control systems. Other matters pointed to were absence of fit-and-proper testing and failure to implement the requirements of the risk management regulations.

All final reports (observations) from on-site inspections at insurance brokers are available on Finanstilsynet's website.

Specific cases

Breach of the solvency requirement

Unison Forsikring ASA was in autumn 2009 granted dispensation from the solvency margin requirement and was subsequently monitored on a monthly basis up to June 2010 when SpareBank 1 Skadeforsikring AS was authorised to take over all shares of the company. This was on condition that SpareBank 1 Skadeforsikring guaranteed the injection of sufficient share capital to enable the company to once again comply with the own-funds and solvency-margin-capital requirements.

Unlawful insurance intermediation

At the end of 2009 the following firms – Admin AS, GeSun Management AS and Nordic Insurance Service Provider AS – offered insurance with Enterprise Insurance Company Plc to members of the Small Businesses Association. Admin AS and GeSun Management AS were not registered as insurance intermediaries and were duly ordered by Finanstilsynet to cease their insurance intermediation business. In the summer of 2010 Finanstilsynet referred a separate case involving Admin AS to Oslo Police District for further investigation into possible criminal violations of the order. Finanstilsynet has published warnings regarding illegal activity on its website.

Complaint against mediation of unit-linked life insurance products

In 2009 Finanstilsynet received complaints against Berge Partners DA's sales of unit-linked life insurance products involving a virtually free choice of investment. The complaints referred to investments that were pledged as collateral, resulting in heavy losses for the customers involved. Finanstilsynet did not take a position on the specific complaints but considered whether the business had been in compliance with the Insurance Intermediation Act and associated regulations. Where this Act's information requirement was concerned, Finanstilsynet queried whether the information given to the customers was suited to providing them with a substantive picture of the product and of the risk associated with the investments. Finanstilsynet's final letter to Berge Partners is published on Finanstilsynet's website.

Deletion of insurance agents

Finanstilsynet registers insurance agents for foreign insurers in its register of licences. In 2010 two agents were deleted following decisions, or notice of decisions, to delete them from the register.

Finanstilsynet's decision to delete Nordic Insurance Service Provider AS was based on the latter's conduct in offering insurance with Enterprise Insurance Company Plc to members of the Small Businesses Association. Finanstilsynet deemed that the company had failed to show the required diligence with respect to the requirements imposed on insurance agents, including failure to formalise an agreement with the insurer.

In its preliminary report following an on-site inspection at BRA Skadeforsikring AS, Finanstilsynet gave forewarning of an order to withdraw the latter's licence to carry on insurance agency activity. The firm handed in its licence before the order was put into effect.

Supervisory cooperation

Finanstilsynet participates in Nordic supervisory groups/colleges to promote coordinated and consolidated supervision of financial conglomerates operating in two or more Nordic countries. The supervisory groups meet regularly to review the conglomerates' situation, thereby facilitating the continuing information exchange.

Nordea's life insurance business is organised as a sub-conglomerate in its own right. The parent company is headquartered in Stockholm, and the Swedish FSA (Finansinspektionen) heads the Nordic supervisory group. One meeting of the supervisory college was held in 2010.

Supervisory cooperation has been established with Finansinspektionen with regard to the Storebrand SPP Group. A supervisory college including participants from Ireland and Guernsey is currently being established for the Storebrand Group.

The Sampo Group owns If which runs a sizeable branch in Norway. The cooperation agreement between the financial supervisors in Sweden (the coordinating authority), Finland, Estonia and Norway for supervision of If has now been revised.

The Sampo Group has a holding of more than 20 per cent in Nordea Bank AB, and a supervisory agreement has been drawn up for the Sampo Group with the If Group, the Nordea Group and the Mandatum Group in which the Finnish supervisor is the coordinating authority, and the supervisors in Sweden, Denmark and Norway are participants. The agreement was signed at the turn of 2011. The group supervising the Sampo Group met three times in 2010.

LICENSING

Licence applications

Finanstilsynet prepares a number of licence cases and dispensations for consideration by the Ministry of Finance, which is also the appeal body for cases decided by Finanstilsynet. Information on individual cases is published on the websites of both the Ministry of Finance and

Finanstilsynet. Cases dealt with by Finanstilsynet in 2010 included the following:

- TryggPensjon AS was awarded a licence to operate a defined contribution pension trust.

- Scandinavian Insurance Group AS was awarded a licence to operate a non-life insurance company and is accordingly licensed for all classes of insurance bar credit insurance. The licence is not valid until Finanstilsynet has tested the fitness and propriety of owners of qualifying holdings.
- Halså Gjensidige Brannkasse and Tingvoll Branntrygdslag Gjensidige were authorised to merge, with Halså Gjensidige Brannkasse as the acquiring company.
- The non-life insurer Sjøtrygdgruppen Gjensidig Skadeforsikringselskap and Møretrygd were authorised to merge. The purpose of the merger was to assure continuation of remaining assets. It was decided to dissolve Sjøtrygdgruppen's rights and obligations. The merged entity will operate under the licence, articles of association and organisation number of Møretrygd Gjensidig Forsikring.
- Gjensidige Forsikring BA (now Gjensidige Forsikring ASA) was authorised to acquire all shares of the Danish non-life insurer Nykredit Forsikring A/S. The company was a part of the financial group Nykredit.
- Gjensidige Forsikring BA was awarded a licence to convert to a public limited company, such that the already established foundation, Gjensidigestiftelsen, became the owner of all shares of the company.
- Lørenskog Kommunale Pensjonskasse was awarded a licence to set itself up as a municipal pension fund.
- Finanstilsynet received and considered an application to set up a municipal pension fund and a non-life insurance company. Both applications were subsequently withdrawn. Finanstilsynet also reviewed the Ministry of Finance's recommendation to reject an application for extension of the deadline for start-up as life insurer for Gabler Pensjonsforsikring. The requisite licence was granted in 2008.

Winding up applications from ten private pension funds were approved.

All matters relating to supervision of holdings under the Financial Institutions Act, including those relating to insurance companies, are described in *Banking and finance*, on page 41.

Finanstilsynet also considers applications to operate as an insurance intermediary. In 2010 seven insurance intermediaries received licences – three insurance and reinsurance brokers and four insurance

agents. Several Norwegian insurance intermediaries applied in 2010 to open branches abroad. Several hundred notifications of cross-border activity into Norway from other EEA states were also processed.

Maximum guaranteed interest rate in life insurance

Finanstilsynet is required on solvency grounds to stipulate the highest interest rate available to life insurers and pension funds when calculating premiums and associated technical provisions.

As from 1 January 2006 the maximum guaranteed interest rate in the premium formula was lowered to 2.75 per cent for new life insurance contracts. In the case of collective annuity and pension insurances written prior to 1 January 2006, the maximum permitted interest rate for accrual after 1 January 2004 is 3 per cent.

As from 1 January 2011 the maximum guaranteed interest rate in the premium formula was further lowered to 2.5 per cent for new life insurance contracts. For collective annuity and pension insurances, the maximum permitted interest rate for accrual after 1 January 2012 is 2.5 per cent.

Insurance Complaints Board

Finanstilsynet acts as secretariat to the complaints board for insurance broking activities and reinsurance broking activities. The board handles disputes between principals and brokers. Private individuals or firms using an insurance and/or reinsurance broker can complain against their broker's execution of the broker assignment. General provisions on the complaints board are published on Finanstilsynet's and the Norwegian Insurance Brokers Association's websites. No complaints were received by the board in 2010.

Increase of technical provisions and new calculation base at life insurers and pension funds

New calculation bases for collective annuity and pension insurance were introduced at life insurers on 1 January 2009. Prices for asset management, interest rate risk and administrative services, as well as profit elements under the new legislation were introduced on 1 January 2008.

Three companies reported new calculation bases in 2009. These were largely based on the R2008 pension tariff which is the Norwegian

Financial Services Association's new mortality base for individual insurances.

The three companies were authorised to utilise profits to increase their technical provisions. Some companies made partial use of this opportunity in 2007. The remainder is being utilised based on a step-up plan which started in 2009. Finanstilsynet's assumption is

that the increase of technical provisions prompted by the transition to Solvency II must be completed by the end of 2012 at the latest. The matter has been referred to the Ministry of Finance for decision.

One private pension fund reported a new mortality base for collective annuity and pension insurances in 2010.

REGULATORY DEVELOPMENT

EU preparations for the new solvency regime (Solvency II)

The EU Commission's proposal for a new directive incorporating risk-based solvency rules for insurers (the Solvency II Directive) was adopted by the EU Parliament on 22 April 2009. The final version of the Directive of 25 November 2009 was published in the Official Journal on 17 December 2009. The Directive, which will supersede all current EU directives in the insurance area, is essentially principle-based. It therefore requires implementing measures in a number of areas.

Solvency II will be implemented through a standard framework, the "Lamfalussy Process", and a timetable set by the EU Commission. The Commission is currently working on provisions to implement the overarching provisions. The Commission is expected to put forward implementing provisions in June 2011 which are likely to be finally adopted by the first quarter of 2012.

The Commission bases its work on 50 consultation documents proposing implementing measures prepared by CEIOPS. CEIOPS' proposals, which were forwarded to the Commission after circulation for comment throughout the European insurance industry, cover all aspects of the new Solvency II framework, i.e. requirements as to technical provisions and capital (pillar 1), as to management and control and

the institution's own assessment of risk and solvency (pillar 2), as well as rules on market discipline and reporting requirements (pillar 3).

Since the implementing measures, which are likely to be in the form of a Commission Directive and Commission Regulation, will also be substantially principle-based, supplementary rules and guidelines will need to be drawn up under the auspices of EIOPA (the European Insurance and Occupational Pensions Authority) and EU/EEA supervisory authorities. EIOPA, the successor to the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS), has been established as a consequence of the restructuring of CEIOPS into a supervisory authority. The supplementary rules and guidelines will in large measure become binding technical standards for supervisors and insurers.

The timetable requires the Solvency II framework to be transposed into national insurance legislation by 31 December 2012 and to enter into force on 1 January 2013.

Five rounds of quantitative impact studies of the Solvency II framework have been completed. The purpose of the fifth round of such studies – Quantitative Impact Study 5 (QIS5) – which was carried out in autumn 2010, was to test calibration and methods (and simplifications) to be incorporated in the implementing provisions and technical standards.

Work on a new solvency framework for insurers – Solvency II

Preparing for the introduction of the framework in Norway

The new European solvency framework for insurers (Solvency II) is scheduled to apply as from 1 January 2013. Finanstilsynet has started work on a proposal for implementing Solvency II in Norwegian law, and aims to send draft law amendments to the Ministry of Finance in summer 2011 and draft regulations by the end of 2011. To this end Finanstilsynet has appointed a reference group drawing representatives from the insurance industry.

Finanstilsynet's stress tests and the modules developed for risk-based supervision are an important part of the preparations for implementation of the Solvency II framework in Norway.

In 2010 Finanstilsynet played an active part in CEIOPS' drafting of proposals for, respectively, implementing measures and supplementary rules and guidelines for the Solvency II Directive. This work covers all three pillars; see the account on page 51.

Internal models to calculate solvency requirements

Under Solvency II insurers will be able to calculate the solvency capital requirement (SCR) using a standardised method or internal models approved by the supervisory authorities. Finanstilsynet organised a series of meetings with insurers in 2010 focusing on internal models.

Finanstilsynet wants insurers that intend to apply for approval of internal models to enter into a preliminary dialogue with the Authority at the earliest possible stage. This will give insurers the opportunity to present their model to Finanstilsynet and to be made aware of the requirements that must be met by a fully complete application.

Finanstilsynet participates in a Nordic supervisory collaboration on internal models under Solvency II. The aim is to set the stage for harmonised processes across the Nordic region and thereby support supervisory authorities' approval of Nordic insurance groups' internal models.

Quantitative impact studies of Solvency II

The fifth round of quantitative impact studies of the proposed new solvency rules (QIS5) was carried out in 2010. Almost all Norwegian insurers complied with Finanstilsynet's request to participate in this impact study. The results of the QIS5 reports for the Norwegian companies will be published on the Authority's website in a synoptic country report on Norway.

If the existing proposals for calibration and methods are not revised before Solvency II enters into force, insurers' capital needs are likely to be significantly larger under the new framework. This applies especially with regard to life insurance.

Product legislation in life insurance

In its assessment of the implementation of Solvency II in Norwegian law, Finanstilsynet is also looking at possible changes to the product legislation for life insurers. The Authority will send a proposal for amendments to the Insurance Activity Act to the Ministry of Finance at the end of the first quarter 2011.

A process is under way at the EU level with a view to arriving at harmonised solvency rules for pension funds. It is currently not clear which body of rules will apply to pension funds in Norway once Solvency II is introduced for insurers.

Norwegian Natural Perils Pool

In June 2008 Finanstilsynet proposed the appointment of a working group to look into aspects of natural disaster insurance in general. The Ministry of Finance delegated to Finanstilsynet the task of appointing the working group, which it did in February 2010. The working group will focus on rules governing overall accounts. To this end it will consider the issue of the Pool's assets and ownership, and examine its instructions with a view to revising the rules that regulate the Pool's technical provisions. The working group is headed by Pål Lillevold, actuary, and draws representatives from the Confederation of Norwegian Enterprise, Finance Norway, the Norwegian Confederation of Trade Unions and Finanstilsynet. The working group completed its report at the end of March. The deadline for finalising the study has been extended to 31 March 2011.

Liquidity regulations for insurers

In December 2010 the Ministry of Finance issued new rules on prudent liquidity management. The regulations apply to financial holding companies, banks, finance and mortgage companies, insurers, pension trusts, investment firms and fund management companies. The new rules reflect amendments to the EU's Capital Requirements Directive and impose further requirements on institutions' liquidity management.

The Insurance Guarantee Scheme – the position in the EU

There is a consensus in the EU on the need for minimum harmonisation of insurance guarantee schemes. The EU Commission requested CEIOPS' recommendation on how insurance guarantee schemes should be configured. CEIOPS' working group submitted 13 recommendations, most of which were acted on in the Commission's *White Paper 2010*. The recommendations enshrine the home country principal and that the schemes should cover life and non-life, as well as all physical persons. Finanstilsynet has headed CEIOPS' working group. The Norwegian insurance guarantee scheme will probably need to be altered in light of the EU process. Finanstilsynet is expected to issue a consultation statement in the course of 2011.

New asset management regulations for insurance

In 2009 Finanstilsynet proposed, on commission from the Ministry of Finance, amendments to the regulations on life insurers' and pension trusts' asset management and the regulations on non-life insurers' asset management which were circulated for comment with the deadline for responses set at 6 November 2009.

On 21 December 2010 the Ministry of Finance incorporated the proposed amendments in the regulations governing insurance companies' asset management. The amendments allow life insurers and pension funds to invest to a larger extent in securities not admitted to trading on a regulated market and in shares issued by companies that operate or own infrastructure. The amendments entail an adjustment, but not a material change, that is designed to encourage a longer-term approach to asset management on the part of pension funds and insurers.

Life insurers and pension funds can now invest a somewhat larger proportion of clients' assets in securities not admitted to trading on a regulated market inasmuch as the general limit on alternative investments is raised from 7 to 10 per cent. Further, subject to Finanstilsynet's approval, investments in limited companies that own infrastructure and receivables secured by mortgages on registered assets included in infrastructure investments can now be assigned to separate investment categories – which will also widen the scope for alternative investments. Moreover, some changes are made to life insurers' and pension funds' right to invest in mutual funds. An upper limit of 10 per cent is set for investments in any single government bond fund, irrespective of whether the fund is a UCITS fund or not.

New legislation for non-life insurance

The Insurance Activity Act was amended with effect from 1 January 2011. The amendment adds a new chapter 12 to the Act and makes for more integrative regulation of non-life business. The Act now deals with matters so far not regulated by law, including self-insurance schemes, insurers' vending of other insurers' products and prohibition against marketing or offering insurances against criminal law sanctions if such insurance is an offence against the legal order. Moreover, central provisions of secondary legislation have become primary legislation.

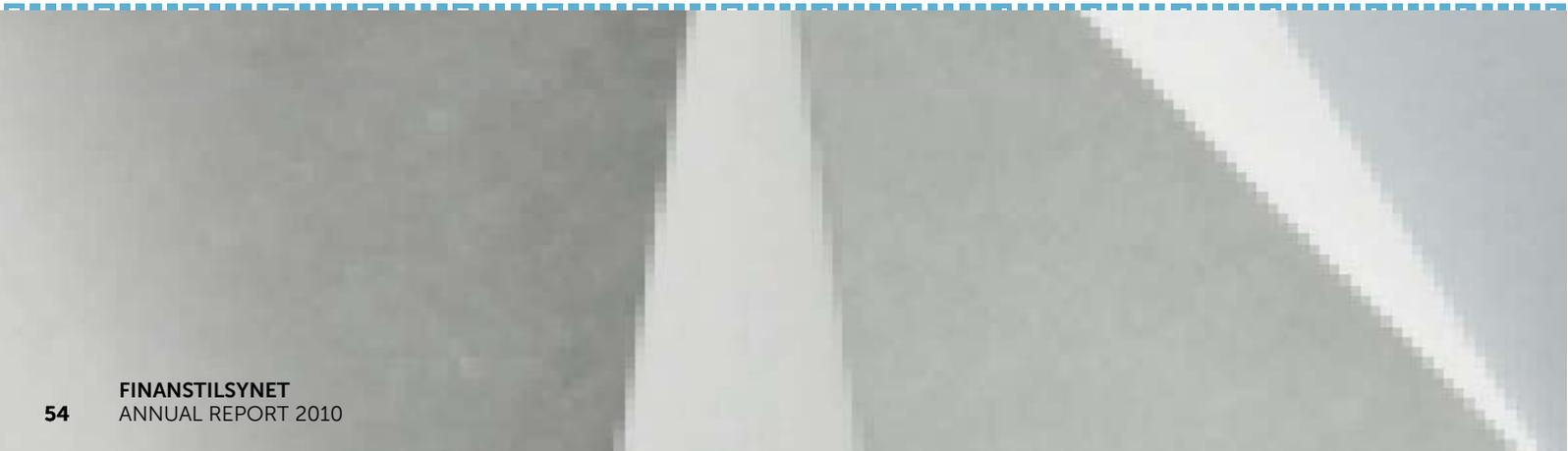
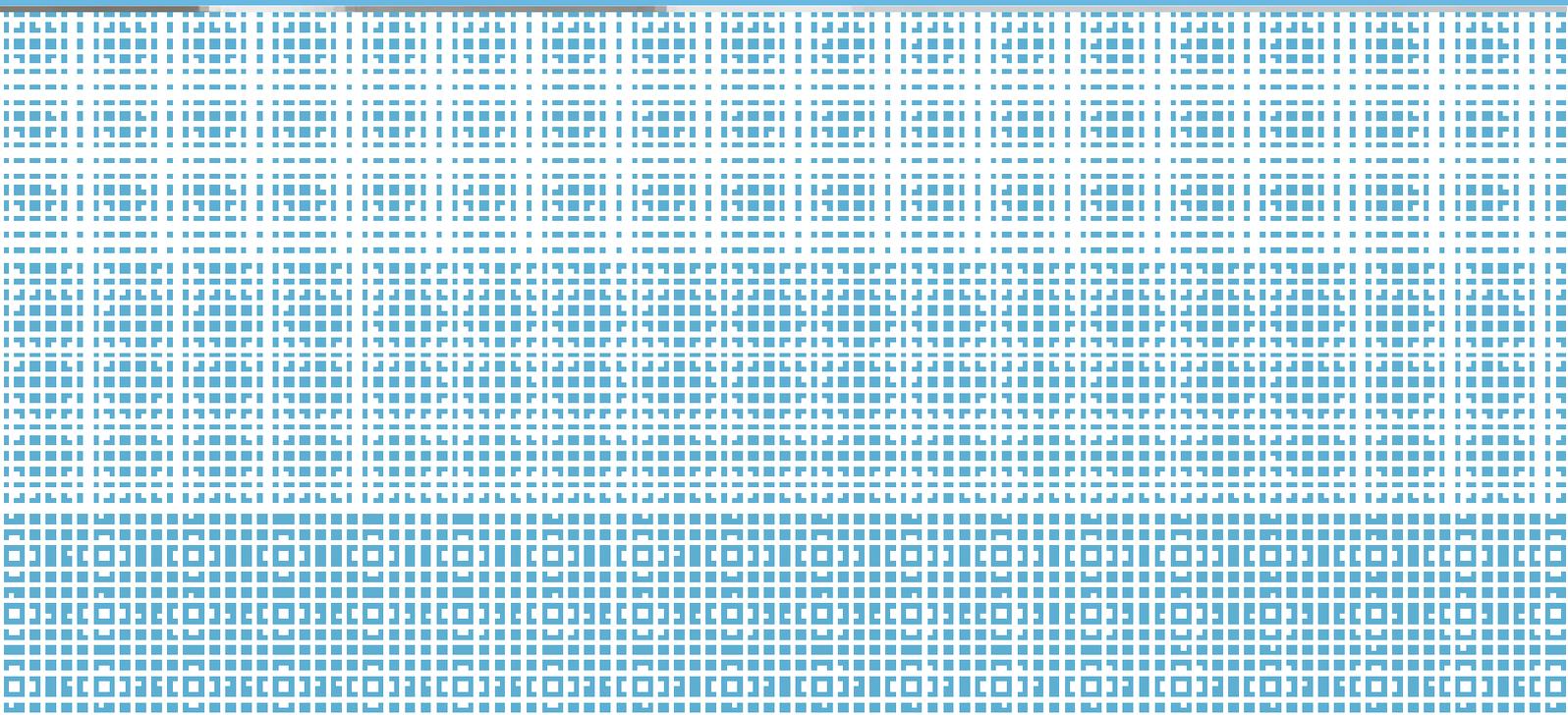
Advice on and sales of packaged retail investment products (PRIPs)

A project has been initiated at the European level to coordinate requirements for good business practice and information when giving advice on and selling packaged retail investment products in the securities, insurance and banking areas. The coordination aims to strengthen consumer protection by extending the existing requirements to comparable savings products. The EU Commission has announced that a draft Directive will be presented ahead of summer 2011.



SECURITIES AREA

Finanstilsynet plays a key role as supervisory authority for the securities market. Supervision includes overseeing issuers' information to the market, securities institutions' financial position and operations, and their compliance with business rules and general rules of conduct.



TRENDS AND CHALLENGES

The equity capital market and the fixed income market functioned well in 2010, as previously, as a source of capital for business and industry in Norway. Many Norwegian firms were involved in acquisitions financed through listing on the stock exchange Oslo Børs. The stock market was recovering and prices were very volatile.

The market for equity instruments in 2010 was affected by macroeconomic factors arising mainly abroad. While oil prices bear heavily on prices of shares quoted on Oslo Børs, other factors such as attempts to cool down the Chinese economy have also played a significant role. Market prices have grown increasingly volatile, and many shares showed very wide fluctuations in the period. The OBX index rose by a total of 18 per cent in 2010. There were however a number of upward and downward movements over the year, and the rise in December alone was in excess of 10 per cent. The volume of shares traded was about 20 per cent higher than in 2009, probably due to the price volatility. The stock market was generally flush with liquidity, whereas trading in the fixed income market was thin.

2010 saw 20 new admissions to Oslo Børs and Oslo Axess, and equity capital worth NOK 61.9bn was absorbed. 387 new bonds and CDs were quoted on Oslo Børs (153) and Oslo Alternative Bond Market (Oslo ABM) (234). Issues launched in the fixed income market, plus tap issues, totalled NOK 634bn on Oslo Børs and NOK 109bn on Oslo ABM. The unprecedented figures for new admissions and bond issues were due to Norwegian firms' involvement in major acquisitions financed essentially through the securities market. Issuers in this market are often banks and residential mortgage companies.

At the end of 2010 203 firms were listed on Oslo Børs – ten were new entries while 13 were delisted. Corresponding figures for Oslo Axess were 34 listed firms in total, ten new admissions and four deletions. At year-end quoted bonds totalled 488 at Oslo Børs and 666 at Oslo ABM. These had a nominal value of, respectively, NOK 855bn for bonds quoted on Oslo Børs and NOK 283bn for bonds quoted on Oslo ABM.

Oslo Børs is experiencing keener competition for new listings, in particular by the larger listed companies, whereas virtually the entire volume of exchange traded derivatives tied to shares quoted in Norway is traded on Oslo Børs. A steadily increasing share of derivatives trading on stock exchanges is done electronically, although combination orders and other complex orders are still executed using the stock exchange's derivatives desk, often in conjunction with EDX. EDX is owned by the London Stock Exchange and the Canadian TMX Group.

Looking ahead, the European securities markets are expected to become further fragmented as new market platforms (multilateral trading facilities) take over much of the turnover of traditional stock exchanges. This tendency is expected to continue in the Norwegian stock market in the years ahead. The fragmentation is augmented by the emergence of *dark pools*, i.e. unregulated, non-transparent marketplaces where major actors trade large holdings without affecting the official market. Falling transaction costs are resulting in an increasing number of trades. Given the rapid technological advances, this is reflected in a sharp increase in algorithmic (high-frequency) trading. Such trading boosts market liquidity, but also heightens the risk of market disturbances such as the *flash crash* seen in New York in 2010. Algorithmic trading could also intensify natural market reactions or create unnatural market reactions. The fragmentation of securities trading, when no marketplace has a total overview, poses major challenges to the effort to expose market abuse. Traditional stock exchanges' squeezed operating margins mean that market monitoring is given less priority than previously and is increasingly left to the public authorities. This could entail new or expanded tasks for Finanstilsynet.

Changes in infrastructure and trading patterns will pose challenges. In particular, a new European settlement system (T2S) will bring major changes to the systems for clearing and settlement of securities and the nationally based securities settlement systems. Hooking up to T2S could significantly change the regulatory and operating environment for Norway's Central Securities Depository (Verdipapirsentralen, or VPS).

Accurate and sufficient, as well as timely, information about issuers and securities offered is a prerequisite for a well-functioning market and a basic obligation for issuers of quoted securities. This applies to periodic reporting as well as ongoing information about events likely to affect market actors' assessments. Market participants' confidence in the information given by issuers is of great significance for investment and credit decisions. Finanstilsynet will continue to apply a risk-based approach in its oversight of this area. Competence and insight into industries that are heavily represented on Oslo Børs is imperative.

Relevant and adequate prospectus information about firms and securities offered is a prerequisite for raising capital and admission to stock exchange listing. Approving prospectuses within the time limits set will be an important task in the period ahead. New prospectus requirements will apply which will need to be implemented by mid-2012. Reliability, timeliness and retrievability of periodic information are important. Imminent changes to the EU's Reporting Directive to

promote coordinated storage and publication of information from listed firms will need to be transposed into Norwegian law.

Through its supervision of advisers and product providers, Finanstilsynet aims to ensure that product sales and advice are safe and appropriate to the individual customer. The customer's ability to understand various financial products is key. Finanstilsynet will, as part of its consumer protection remit, act on the new European requirements regarding key information on savings and investment alternatives. While proposed new legislation on securities funds sets statutory requirements for Finanstilsynet's case-processing time, thereby increasing the burden on processing capacity, it will also remove discretionary elements from a number of public administration decisions, thereby significantly easing case processing.

At the European level a project has been initiated to coordinate requirements on good business practice and information in connection with advice on and sales of packaged retail investment products (PRIIPs) in the securities, insurance and banking areas. The aim is to strengthen consumer protection by extending the scope of the requirements to sales of comparable savings products. The EU Commission has announced that a Directive proposal will be presented ahead of summer 2011.

Since the entry into force of a new Securities Trading Act in 2007, the advisory services segment has been prioritised at on-site inspections in the securities area. In preparation for the implementation of a new Act on securities funds, on-site inspections at fund management companies will be given somewhat higher priority ahead.

SECURITIES MARKET SUPERVISION

The overarching aim of regulation and supervision of the securities market is to ensure secure, orderly and efficient trading in financial instruments, thereby enabling the securities market to function as a source of capital for business and as a basis for saving and investment. Supervision encompasses actors' financial position and operations, and their compliance with business rules and general rules of conduct.

INVESTMENT FIRMS

SUPERVISION AND MONITORING

Finanstilsynet's on-site inspections aim to promote an informed attitude to risk among firms and to maintain a high level of client protection in the securities market by ensuring that firms comply with the conduct of business rules. Supervision also promotes market integrity. There were 154 investment firms in Norway at the end of 2010.

Twenty on-site inspections were conducted at investment firms in 2010, and two inspections at Norwegian branches of foreign investment firms. Two inspections specifically targeted investment firms' ICT solutions.

The on-site inspections were resource-demanding owing to the firms' size, to a complex body of rules hitherto not applied in the supervisory context, and to the nature and number of breaches of provisions of the Securities Trading Act. Finanstilsynet examined the firms' organisational set-up to see how they ensured effective and independent control over compliance with the Securities Trading Act and associated regulations. Finanstilsynet also looked into some of the larger firms' guidelines and procedures for

information handling and handling conflicts of interest. It also looked at several firms' reception of orders and provision of investment advice over the phone as well as a number of firms' compliance with the rules for good business practice when selling contracts for difference (CFDs).

Finanstilsynet made a point of writing fuller concluding supervisory comments than was previously the norm. Finanstilsynet's perception is that supervisory observations, which are publicly available on the Authority's website, are viewed by many entities under supervision. Finanstilsynet considers it positive if a more informative approach has a preventive and instructive effect across the market. Several of the largest investment firms had on-site inspections in 2010. Some were severely censured. Finanstilsynet checks that firms fall into line with its observations. Several firms took wide-ranging action.

Finanstilsynet keeps a close watch on investment firms by reviewing their periodic reports, and focused in 2010 as previously on firms' compliance with the capital adequacy legislation. Although

investment firms experienced a better market situation in 2010 than in the previous year, some saw their earnings and financial position weaken once again. Twenty firms undertook capital increases to strengthen their own funds. Eleven warnings of licence revocation were issued due to capital inadequacy, and three firms had to hand in their licences for this reason.

Finanstilsynet has given greater attention to firms' classification of exposures as part of the trading portfolio, and the significance this has for compliance with the rules governing large exposures.

Large investment firms' counterparty risk arising from claims on customers in connection with unsettled trades and lending was looked into in 2009. Finanstilsynet conducted similar investigations in March 2010 which were followed up with on-site inspections at a number of firms.

In 2010 Finanstilsynet finalised its effort to refine the quarterly return forms completed by investment firms and fund management companies and paved the way for returns to be filed via the Altinn internet portal. Further refinement of data extract reporting is highly likely to bring efficiency gains for periodic reporting in the securities area.

Finanstilsynet examined in 2010 a case in which own account trading and the reception and transmission of orders of financial instruments (derivatives) were carried on without the requisite licence. The company is registered in Norway, and offered its services in Norway and a number of European countries. Finanstilsynet ordered a halt to the business, after which the company announced that it would not appeal against the order, and duly wound up the business in question.

Thematic inspections concerning sales of savings products to consumers

Complex financial markets, with new product solutions constantly being marketed, require Finanstilsynet to give close attention to consumer-related issues. As part of its oversight of banks and investment firms, Finanstilsynet surveyed in 2010 savings products

sold in 2009 and 2010 by a selection of 29 banks, including the largest ones. The survey was followed by on-site inspections at eight banks. No bank, apart from one, had sold complex savings products or granted loans that were directly linked to the savings product in question. The review showed that advisers' remuneration was product-neutral at seven of the eight inspected banks. Finanstilsynet comments that banks could do more to sell lower-priced funds, and that many savers would be well served by including index and bond funds in their portfolio.

Finanstilsynet will in the period ahead continue to oversee investment firms' ability to document that the products they have sold are appropriate to the customer and that customers have received adequate individualised, balanced and correct information about the risk attending such investments.

Market warnings

Finanstilsynet published 30 warnings against firms that had provided financial services in Norway in 2010 without the requisite licence. A further 338 warnings given by foreign supervisory authorities were published. Very often these firms are engaged in some or other form of fraud, and individuals who transfer money to such firms must in many cases consider the money lost. Finanstilsynet posts its own market warnings and warnings given by foreign supervisory authorities on its website to warn consumers against dealing with such firms. The website also contains information on investment fraud, advising investors on how to protect themselves against fraudsters. As from November 2010 Finanstilsynet's market warnings are also available on the website Finansportalen.no.

LICENSING

Authorisation process

Since the reorganisation of the licensing regime that accompanied the new Securities Trading Act of 2007, Finanstilsynet has processed significantly more applications to provide investment services than previously. It also received a large number of licence applications in 2010. Sixteen new investment firms were licensed to provide investment services, compared with nine in 2009. A further four licences were granted to existing firms (expanded licences). Licence applications include those from new firms as well as applications due to various types of restructuring at existing financial conglomerates. A number of the new firms under supervision in the securities area are relatively small and have few employees.

In addition to the licences handed back due to capital inadequacy, 11 licences were revoked due to restructuring, mergers and corporate acquisitions, and business area reorganisations.

Fitness and propriety testing

A substantial number of fit-and-proper tests were carried out of board members and managers at supervised entities in the securities field. Relatively thoroughgoing assessments are made of qualifications, job experience and previous conduct. Testing is carried out based on licence applications and management changes. Firms have acted on Finanstilsynet's assessments where the individual is deemed not to possess the qualifications needed by a manager. Most such decisions cite a lack of relevant experience of the type of business the individual intends to manage. In some cases it is a matter of unsuitability due to previous conduct at a firm guilty of serious law violations.

REGULATORY DEVELOPMENT

Remuneration of investment advisers

Finanstilsynet, on commission from the Ministry of Finance, examined certain issues under the rules governing conflicts of interest in relation to investment firms' remuneration systems. Finanstilsynet's conclusion, supported by the Ministry of Finance, was that a remuneration system for investment advisers that involves a direct link between remuneration and customers' investments is counter to the Securities Trading Act. Detailed guidelines are given in circular 17/2010.

Tied agents

Amendments to the provisions of the Securities Trading Regulations governing tied agents entered into force on 1 January 2011. The amendments, based on Finanstilsynet's consultation paper from 2008, prevent an investment firm from entering into agreements with tied agents numbering more than 50 per cent

of the investment firm's workforce. This assures that the bulk of specialist competence lies in the investment firm, not in the agent network, and facilitates the firm's control over the agents. The regulations also establish that an agent cannot have sub-offices. This has necessitated adjustments at some investment firms with a large agent network.

Voice recordings

In December 2009 the Ministry of Finance amended the provisions of the Securities Trading Act governing investment firms' obligation to voice record telephone conversations. The amendments, building on Finanstilsynet's consultation paper of 26 August 2008, extend this obligation. They are essentially grounded in a need for more effective oversight of investment firms and investor protection. Entry into force of the amendments was deferred to 1 April 2011 to give firms more time to test technical solutions.

FUND MANAGEMENT COMPANIES

At the end of 2010 27 management companies were licensed to manage securities funds. Sixteen of these were licensed to carry on “active management of investors’ portfolios of financial instruments”. The number of securities funds managed by these companies rose marginally from 421 in 2009 to 428 in 2010. Net new subscription for

Norwegian management companies’ securities funds came to NOK 41bn in 2010. Total assets rose by about 20 per cent in 2010, reaching NOK 498.8bn by year-end. Of this new subscription, the bulk – NOK 34.4bn of which NOK 14.9bn in was in equity funds – was accounted for by Norwegian institutions.

SUPERVISION AND MONITORING

Finanstilsynet’s supervision of management companies is both on-site and off-site, and based mainly on current reporting. Although Finanstilsynet selected a broader range of companies for on-site inspection in 2010, there was still a need to prioritise the advisory services segment and larger investment firms. Two on-site inspections were conducted at fund management companies, and on-site inspections at such companies will be given somewhat higher priority in 2011.

Management companies are required to report possible breaches of investment limits set out in the Securities Funds Act and funds’ statutes. The number of reported breaches in 2010 was as expected, and none were of a sizeable, serious nature. Trustees’ obligation to inform Finanstilsynet of any management company where rule breaches are brought to light is an important supplement to off-site supervision in general. Such reports by trustees are few in number.

Finanstilsynet monitors management companies’ financial situation and their compliance with the rules governing capital adequacy and large exposures on the basis of quarterly reports they file with Finanstilsynet. Overall, management companies achieved far better profits in 2010 than in the two previous years, albeit well short of the levels seen in the peak years 2006 and 2007. Three management companies found themselves compelled to increase their capital in 2010 in order to meet own funds requirements.

Finanstilsynet dealt with two cases of unlawful fund management in 2010. Two associations had in aggregate just over NOK 60m under management. Both were issued with a preliminary warning to halt their unlawful activity, which they did on their own initiative without Finanstilsynet needing to issue a final order to that end.

LICENSING

Finanstilsynet has in recent years received somewhat more applications for licences to engage in securities management than was previously the case. In 2010 licences were granted to three new management companies, bringing the total number of management companies to 27 by year-end. New management companies are generally small operations intending to operate in a small segment of the market.

In 2010 the articles of association of 25 new securities funds were ratified, while 13 securities funds were wound up. A number of applications for approval of amendments to securities funds' articles of association were also dealt with.

Spesialfond (non-UCITs)

The provisions of the Act on Securities Funds governing *spesialfond* and provisions on *spesialfond* in certain regulations to that Act entered into force on 1 July 2010. The legislation permits the establishment of Norwegian *spesialfond* which may be sold to professional

investors and empowers Finanstilsynet to authorise the marketing of foreign *spesialfond* to professional investors in Norway.

Spesialfond are largely exempt from the provisions of the Securities Trading Act governing investments, including the Act's constraints with respect to investment area, liquidity, risk diversification and borrowing, securities borrowing and lending, provision of security and short trading. Hence *spesialfond* are likely to have a different management strategy and to utilise a wider range of investment techniques than ordinary securities funds. The risk and complexity attending these funds may exceed those in ordinary securities funds. Under a transitional rule *spesialfond* may not be marketed or sold to non-professional customers. This rule is in keeping with Finanstilsynet's original law proposal and Finanstilsynet sees no immediate need for any change here.

In 2010 Finanstilsynet issued three licences to establish Norwegian *spesialfond* and six licences to market foreign *spesialfond* in Norway.

REGULATORY DEVELOPMENT

Revision of the Act on Securities Funds

On commission from the Ministry of Finance, Finanstilsynet appointed in 2009 a broadly composed working group to undertake an overall review of the Securities Funds Act. The working group's mandate included recommending changes to the Act to transpose the new Directive on undertakings for collective investment in transferable securities (UCITS IV) into Norwegian law by the deadline of 1 July 2011. The working group forwarded its report to the Ministry of Finance on 22 June 2010. Among the main changes brought by the

new UCITS Directive are requirements as to key information, new rules governing the merging of securities funds, simplified notification procedures for cross-border marketing of securities funds and a wider right to invest a securities fund's assets in another securities fund. After presenting its first report, the group was given an additional mandate to draft regulatory changes following from four implementing Directives/Regulations adopted pursuant to UCITS IV. Draft regulations were forwarded to the Ministry of Finance at the end of January 2011.

MARKET INFRASTRUCTURE

SUPERVISION AND MONITORING

The securities market infrastructure comprises Oslo Børs ASA, the Norwegian Central Securities Depository (VPS ASA), Oslo Clearing ASA, Spectron Energy Services Ltd Norway Branch (previously International Maritime Exchange ASA (Imarex)), Fish Pool ASA, NOS Clearing ASA (NOS), and Nasdaq OMX Oslo NUF (previously Nord Pool Clearing ASA).

The clearing houses reported quarterly through 2010 on the trend in own funds and risk exposure in keeping with applicable provisions. The new reporting regime is part of the effort to strengthen the supervision of clearing houses.

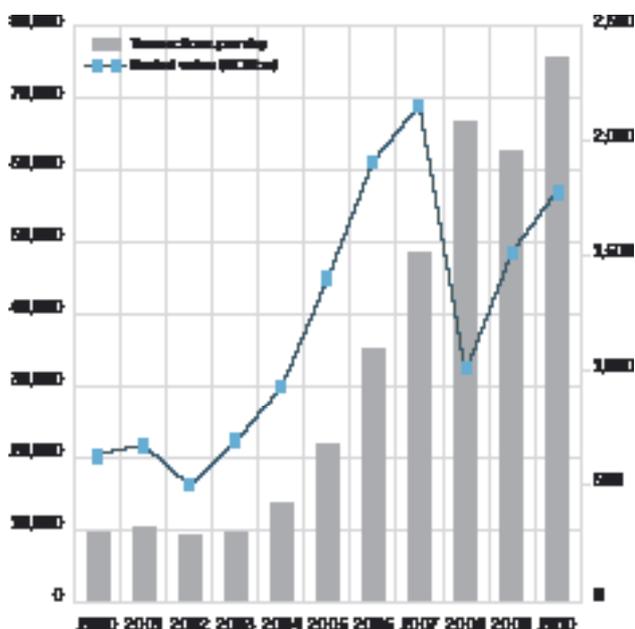
In April 2010 Oslo Clearing ASA's licence was expanded to allow it to carry on business as a clearing house for equity instruments. It was required, prior to start-up, to ensure that it had sufficient in-house IT personnel to operate and maintain the clearing system. The new business went live in June by clearing five shares in the OBX index. Mandatory clearing of all equity instruments quoted on Oslo Børs and Oslo Axess was introduced as from 27 August 2010. Finanstilsynet also monitored Oslo Clearing ASA's organisation of the business to check its compliance with the terms and conditions set for its licence, and scrutinised activities associated with testing, start-up and operation of the system, including test results from the Central Securities Depository (VPS) covering the central securities settlement process. Thus far, experiences with clearing equity instruments appear favourable.

Finanstilsynet kept a close watch on the situation that arose after its Swedish counterpart Finansinspektionen revoked HQ Bank's licences in August 2010. HQ Bank was a remote member of Oslo Børs and a direct participant in the securities settlement at VPS. Finansinspektionen's revocation order was consequently of significance for the Norwegian securities settlement. Institutions handled the situation in such a way that the Norwegian securities settlement process suffered no disturbance.

Finanstilsynet conducted an inspection at Fish Pool ASA in 2010. In addition IT inspections were conducted at Oslo Børs ASA and Nasdaq OMX Oslo ASA. Finanstilsynet monitored infrastructure institutions closely as part of its consideration of a number of major cases in 2010.

Oslo Børs ASA operates the marketplaces Oslo Børs, Oslo Axess and Oslo Alternative Bond Market (Oslo ABM), the first two of which are regulated marketplaces. It also operates the multilateral trading facility Oslo Connect on which OTC derivatives are traded.

Chart 4: Market value and number of transactions per day at Oslo Børs



Source: Oslo Børs

Clearing of quoted equity instruments through a central counterparty (CCP) was expected to bring a decline in the number of transactions for settlement at the securities settlement and a decline in the settlement rate. In 2009 43.2 million transactions were settled compared with 31.2 million transactions in 2010. The settlement rate now stands at about 96 per cent compared with just over 98 per cent before clearing of equity instruments was introduced.

Electricity market and electricity derivatives market

Prices in the electricity market were high in 2010 compared with previous years due to low reservoir levels in Norway and Sweden and, above all, to some price areas in Norway. Uncertainty surrounding Swedish nuclear power production and unprecedented high consumption through 2010 also influenced prices. Derivative and spot prices both rose substantially, especially towards year-end, and settled at a very high level. Electricity prices in the Nordic market area fluctuate with European prices, but are now tending to move more in step, suggesting a tendency for greater market integration. Increasing electricity exchange between areas and market coupling are important contributors. Carbon contract prices were relatively stable over the year, suggesting that these products have now taken their place in the market.

Finanstilsynet has cooperated with the Competition Authority and the Norwegian Water Resources and Energy Directorate on supervision of the electricity market since 2003. This cooperation is now under revision with a view to adjustment to developments in the electricity and electricity derivatives market, and will accordingly continue.

Fish derivatives market

The market for salmon derivatives saw high price levels 2010 compared with the previous year. Price fluctuations through 2010 were substantial, demonstrating high volatility. For the year as a whole, spot market price rose significantly, from about NOK 29 per kilo at the start of the year to about NOK 40 per kilo by year-end. A possible reason for the rise may be the sizeable disease problems faced by the fish farming industry in Chile. Fish Pool offers financial forward contracts with delivery one month ahead. Forward prices for delivery in January 2011 showed a steady rise through 2010 from about NOK 30 per kilo to about NOK 39 per kilo. The forward market was far less volatile than the spot market in 2010.

LICENSING

Monitoring compliance with the conditions set for the merger between Oslo Børs Holding ASA and Verdipapirsentralen Holding ASA

The Ministry of Finance's decision of 8 November 2007 set a number of conditions for the merger of Oslo Børs Holding ASA and Verdipapirsentralen Holding ASA. Finanstilsynet monitors compliance with conditions on an ongoing basis. In 2010 Finanstilsynet considered requirements on the size of the Central Securities Depository's (VPS) own funds and prepared a recommendation to the ministry regarding payment of VPS's group contribution. Further, Finanstilsynet approved agreements on outsourcing of support functions and infrastructure services related to the operation and maintenance of a new clearing system for equity instruments at Oslo Clearing ASA.

Acquisition of Nasdaq OMX Oslo ASA assessed against rules governing significant holdings

Finanstilsynet made a recommendation to the Ministry of Finance regarding OMX AB's application to own all shares of Nasdaq OMX Oslo ASA (previously Nord Pool ASA). The ministry approved the application on 12 May 2010.

Changes in the central securities settlement system (VPO/NOK)

Finanstilsynet considered an application regarding changes in the central securities settlement system (VPO/NOK), and approved a system (new VPO/NOK) to replace the one previously approved in 2001. The new approval was prompted by changes in the system's guarantee scheme, the introduction of power of attorney for

registration, the right to make partial delivery and new prioritisation rules.

Clarification regarding the central securities settlement process

After Lehman Brothers' default and application for bankruptcy protection in September 2008, perceptions of some aspects of the agreements underlying the securities settlement system have been discussed among the settlement process participants. For Finanstilsynet it is

vital that the settlement system should be predictable and rules clear-cut as regards the obligations resting on the participants, including settlement participants who also act on behalf of remote members or other indirect participants. The rules have accordingly been clarified to explicitly state participants' responsibilities. Participants are required to bring their activity into line with their responsibilities/liabilities within the system, including their responsibility, if they intend to act on behalf of others, to hold sufficient capital to cover the risk this involves.

REGULATORY DEVELOPMENT

The right of bond issue trustees to bring legal action

Finanstilsynet has previously examined the need for rule changes to secure trustees for bond issues the right to bring legal action in cases concerning loan agreements and associated agreements, and proposed the addition of a new provision on litigation rights in the Securities Trading Act. In 2010 the question of such right to bring

legal action was tried by the Supreme Court which established that Norsk Tillitsmann does have such a right. Further, in another case the Supreme Court ruled that Norsk Tillitsmann can petition for an issuer's bankruptcy. In view of the above judgments, efforts to enshrine in law Norsk Tillitsmann's competence to exercise bondholders' rights in a court of law no longer have high priority.

MARKET CONDUCT RULES

SUPERVISION AND MONITORING

The overarching aim of supervision and monitoring of compliance with the market conduct rules is to safeguard the reputation of the Norwegian market and thereby its role as a well-functioning source of capital.

The rules on unlawful insider trading, market manipulation and due care in handling inside information are at centre-stage. Finanstilsynet also oversees compliance with the rules on the drawing up of insider lists, the duty to investigate, the prohibition of unreasonable business methods, notification rules and rules requiring the disclosure of acquisitions of large shareholdings. Hence a wide range of supervised entities is involved: investors, advisers, issuers of financial instruments and their partners, including investment firms. The object is to bring to light and prosecute unlawful conduct in the securities

market and, insofar as the conduct rules are applicable, in the markets for commodity derivatives. The aim is for the supervisory effort to have both a general and an individual deterrent effect in the market.

Most of the large number of cases dealt with by Finanstilsynet in 2010 were referred to it by Oslo Børs, in addition to some that were reported by investment firms, the media and investors. Finanstilsynet also exposes irregular and unlawful conduct in the course of its own investigations.

As previously, a number of the insider trading and market manipulation cases handled by Finanstilsynet were time-consuming, especially where the investigations involved other countries. Finanstilsynet also assisted foreign supervisory authorities in their investigations in a number of cases.

In 2010 Finanstilsynet investigated:

- 60 new cases of unlawful insider trading and/or violations of confidentiality
- 48 new cases of market manipulation/unreasonable business methods
- 37 new cases of securities trading requiring disclosure
- 35 new cases of securities trading requiring notification
- 62 new cases received from investment firms under an obligation to report transactions giving rise to suspicion of insider trading or market manipulation

Administrative fines

Finanstilsynet is empowered to impose an administrative violation charge for violation of the Securities Trading Act's provisions requiring disclosure of substantial share acquisitions or disposals. The availability of this sanction permits far more effective rule enforcement. Finanstilsynet imposed ten such fines in the course of 2010. Finanstilsynet publishes these cases on its website on the presumption that doing so has a preventive effect.

Notifications to the prosecuting authority

Two cases of suspected unlawful insider trading and/or breach of the duty of confidentiality were reported to the prosecuting authority in 2010. Four cases of market manipulation were reported as were seven failures to disclose the acquisition of a large shareholding. Finanstilsynet also issued a number of warnings after minor breaches in the last-mentioned area.

Major investigations

In 2010 Finanstilsynet investigated share transactions at Reservoir Exploration Technology ASA (RXT), a stock exchange listed company. This was prompted by repeated delivery problems related to sale transactions in the period 8 April to 23 April 2010. At issue were the prohibition of unreasonable business methods and the sale of financial instruments not owned by the customer. The case will be finalised early in 2011.

Finanstilsynet also investigated extensively transactions at Crew Golf Corporation (CRU), focusing on blocks of shares registered to nominee

accounts, with several layers of sub-nominees. The case involves possible failure to disclose acquisitions of major shareholdings.

Follow up of reported cases

As in previous years Finanstilsynet maintained close, fruitful cooperation on reported cases with ØKOKRIM¹ and local police districts in 2010. This cooperation makes for more effective and efficient combating of crime in the securities market. Finanstilsynet assisted the prosecuting authority at interviews and in analysing share transactions. In 2010 the Authority entered a cooperation agreement with the Oslo Police District designed to ensure proper, expeditious consideration of cases reported by Finanstilsynet as well as optimal resource use during the exposure, investigation and prosecution of cases in the securities area.

In addition to the cooperation on individual cases, a seminar on market conduct was held under ØKOKRIM auspices which was attended by Oslo Børs and Finanstilsynet.

While the cooperation on exposing and prosecuting crime in the securities market is fruitful, the resource situation at ØKOKRIM is nonetheless a critical constraint. Reference is made to "Report on the cooperation between Oslo Børs, Kredittilsynet and ØKOKRIM" from 2007, one of whose conclusions was that ØKOKRIM should be supplied with resources to increase its case-handling capacity in the securities area. This conclusion still stands.

Further development of the transaction reporting system

Finanstilsynet receives transaction reports from investment firms on a daily basis. Reported transactions are also exchanged with European supervisory authorities.

In 2010 Finanstilsynet devoted much resources to checking that entities subject to a reporting obligation actually meet that obligation and that the incoming data are of regulatory quality.

The volume of reports received by Finanstilsynet is substantial. An effective review is best served by procuring a separate analysis system

¹ National Authority for Investigation and Prosecution of Economic and Environmental Crime

to supplement existing solutions. Steps have been taken to gain an overview of available solutions and of analysis systems used by a number of other supervisory authorities and market participants.

The transaction reporting system (TRS) is being developed by the Nordic countries' supervisory authorities under a cooperation agreement that assures a common reporting regime in the Nordic region. In view of the extended reporting obligation resulting from the revision of the Markets in Financial Instruments Directive (MiFID), the TRS will need to be further developed on a continual basis ahead. Finanstilsynet is playing an active role at all levels of the development process. Much resources have been devoted to establishing a system that meets the Directive requirements and to assist firms subject to a reporting obligation. Assuring predictability and establishing a platform for coordination of Nordic interests in the EEA context have also been important.

Court rulings

- In July 2010 the Supreme Court rejected the appeal in an inside information case. A journalist was convicted in the district court of violating insider trading provisions after writing an article containing inside information. The journalist was found guilty on one count in the case, and the Supreme Court rejected the appeal against the district court's decision to refuse this aspect of the case to be tried. The rest of the case will be heard by the district court in 2011.
- In June 2010 the Supreme Court ruled that Oslo was the correct venue for an indictment against an investor for unlawful insider trading despite the fact that the investor was living in Drammen at the time the orders concerned were entered.
- In June 2010 the Borgarting High Court handed down a judgment in an appeal by two brothers and their broker who had been convicted in the City Court of violating the own-account trading rules and the duty of confidentiality by possessing inside information. The High Court sentenced all three to a term of imprisonment. The broker also had funds confiscated.
- In July 2010 Oslo City Court sentenced the client of an investment firm to reimburse the losses his broker had inflicted on him. The client's broker had traded without an order, and a point of contention in the case was whether the client was nonetheless liable for the transactions under contract law. The court concluded that there was a tacit agreement on «active management» between the parties as a result of which the client was held to be liable for the transactions. The judgment is final and unappealable.
- In March 2010 Oslo City Court heard an action for compensatory damages after alleged market manipulation in connection with a company acquisition. The court found against the plaintiff's claim for compensation and ruled that the defendant had not contributed to market manipulation. The judgment is final and unappealable.
- In October 2010 Oslo City Court found two day traders guilty of market manipulation by manipulating an algorithm machine to their own advantage. The traders traded independently of each other and understood how the machine worked. They exploited this to their advantage by creating an incorrect picture of volumes in a number of illiquid shares. The court ruled that their conduct fell within the concept of market manipulation. The judgment has been appealed.
- In December Oslo City Court handed down a judgment on the validity of a decision by the Stock Exchange Appeals Board to impose a fine for violation of the duty of confidentiality towards Oslo Børs. The City Court ruled that the Appeals Board decision was a valid sanction order. The deadline for appeal has not expired.

LICENSING

The Public Limited Companies Act, Securities Register Act and Securities Fund Act permit investors to register holdings of Norwegian securities in the name of a nominee. For shares of Norwegian companies this right is confined to foreign investors (companies that are registered abroad unless the head office is in Norway, and foreign nationals who do not tax to Norway). The right to register in the name of a nominee allows foreign investors to assemble the management of their securities under one manager and, by the same token, in one jurisdiction. This is considered to make investments in Norwegian shares and other securities more attractive than they would have been in the absence of such a right.

Finanstilsynet notes keen interest on the part of foreign banks and investment firms in acting as nominee in Norwegian securities funds' unit-holder registers and in shareholder registers for shares admitted to trading on a Norwegian regulated market.

In 2010 22 licences were awarded to act as nominee in unit-holder registers for securities funds and 12 new licences to act as nominee in respect of shares and other securities qualifying for registration on nominee accounts in a Norwegian securities register (the Central Securities Depository, VPS). Corresponding figures for 2009 were, respectively, 16 and 13. These figures include licences issued to a small number of Norwegian companies.

REGULATORY DEVELOPMENT

A number of amendments were made to the Securities Trading Act with effect from 1 July 2010. These included a new provision on financial instruments sold, but not owned, by the seller. Changes were also made to the provisions on securities trading subject to disclosure, with Finanstilsynet being empowered to impose fines for violation of the provisions. Finanstilsynet considers that the power to impose such fines will enable more effective enforcement of the rules.

In a consultation paper of 29 September 2010, Finanstilsynet recommended a number of changes to the Securities Trading Act, including the provisions on the ongoing information requirement and on the notification requirement for primary insiders. Many of the recommendations entail further harmonisation of Norwegian law with relevant Directive provisions.

Finanstilsynet has played a part in several rounds of consultation on possible Directive amendments. These include proposed new EEA-wide rules on short selling, where an initiative under consideration is the establishment of a register of short sales. A further area is revision of the Transparency Directive (2004/109/EC), where consideration is being given to extending the scope of the rules governing disclosure

of acquisitions of large shareholdings to include certain derivatives subject to financial clearing.

Common European settlement and account system

Increased efficiency and integration of the capital market have been a key concern within the EU. The complex existing infrastructure in the securities area, in particular on the clearing and settlement front, have made it difficult to establish a competitive common European securities market, and the costs of cross-border clearing and settlement are high. The European Central Bank (ECB) has accordingly set up a project to develop and introduce a single European platform for the settlement of securities known as TARGET2-Securities (T2S). Further, the EU Commission has adopted common European regulation of clearing and settlement houses, currently under consideration by the EU Parliament. The Commission is also engaged in introducing common European regulation of securities registers and rules ensuring priority over other parties in connection with registration of financial instruments. Finanstilsynet is participating in these processes through, inter alia, its membership of CESR which, as from 1 January 2011, was replaced by the European Securities and Markets Authority (ESMA).

PROSPECTUS CONTROL – TRANSFERABLE SECURITIES

A prospectus is required in the case of public offers for subscription or purchase of transferable securities worth at least EUR 2,500,000 calculated over a period of 12 months that are directed at 100 or more persons in the Norwegian securities market. All such prospectuses must be inspected and approved by Finanstilsynet. The same applies where transferable securities are to be admitted to trading on a Norwegian regulated market, including where a company whose shares are already traded plans to increase its capital. Finanstilsynet has to approve all above-mentioned prospectuses prepared by Norwegian issuers or by issuers from non-EEA countries that have selected Norway as their home state.

BACKGROUND

The Europe-wide body of rules governing prospectuses requires operative prospectus control to be exercised by the member states' supervisory authorities as from 1 January 2011. Operative prospectus control was accordingly transferred from Oslo Børs to Finanstilsynet with effect from 1 May 2010. Prospectuses which had been submitted for control to Oslo Børs prior to that date but had not been approved were transferred to Finanstilsynet for further inspection and approval. Finanstilsynet has in principle continued Oslo Børs's practice in this area, giving emphasis to compliance with the five and ten day time-limits set for initial response to, respectively, listed companies/listing applicants and unlisted companies.

Control and approval of prospectuses

The market for transactions subject to a prospectus requirement has remained at a stable, high level since Finanstilsynet took over responsibility for prospectus control. This applies both to equity securities and debt securities. Even so, in historical terms the year 2010 was a year of normal market activity rather than a year of abnormally high activity. Market activities in 2011 are expected to be on a par with or higher than in 2010 both as regards new admissions and issue volume. However there is still some uncertainty surrounding the market trend ahead.

Handling a relatively large number of prospectuses within the time limits set, at the same time as fitting in new staff and new procedures, posed a challenge. Viewed in retrospect, Finanstilsynet discharged its control responsibilities in a satisfactory manner. In a move to improve efficiency, Finanstilsynet is introducing, as from 2011, stricter criteria for acceptance of initial draft prospectuses. The control process will not start until a prospectus has a minimum prescribed content. This content will be communicated to market participants by various means. Finanstilsynet will in addition consider raising prospectus charges if there is reason to believe they are low.

The following table summarises document control figures for the past five years.

Table 9: Controlled documents

	2006	2007	2008	2009	2010
No. of prospectuses controlled (total) of which:	172	342	178	211	158
Shares	114	277	125	102	105
Of which quoted shares	53	119	57	64	82
Bonds	58	63	53	94	44
Warrants	–	2	10	15	9
Discontinued control	–	32	16	13	21
Supplements to prospectus	22	20	31	2	17
Equivalent documents	6	25	14	4	4

Source: Oslo Børs and Finanstilsynet

In addition to the above table, a number of documents have been notified to and from the EU/EEA area. These are notifications of prospectuses being passported. Prospectuses for new admissions involve a great deal of work. 20 new admissions to trading of shares

(IPOs) were undertaken in 2010, while a total of 25 prospectuses related to new admissions were approved. In addition, a number of controls were discontinued at various stages of the process.

Table 10: New admissions, share issues and overall issue volume

	2006	2007	2008	2009	2010
No. of actual new admissions (Oslo Børs and Oslo Axess)	32	57	16	3	20
No. of share issues (Oslo Børs)	260	308	160	168	162
Amount in billions of NOK (Oslo Børs)	56.9	53.7	13.2	50.8	59.7

Source: Oslo Børs

In addition to the actual control of prospectuses and related documents and the dialogue with the market participants in that connection, a fairly large number of enquiries and approaches were received in 2010 concerning interpretation of the rules.

Posting information on Finanstilsynet's website is given much attention. The level of service to market participants where this type of enquiry is concerned may need to be reviewed.

Major individual cases

Finanstilsynet has handled prospectuses for a number of sizeable transactions since start-up, including Norsk Hydro ASA's issue in connection with the acquisition of Vale Aluminium. This involved a combined offer document and listing prospectus: the transaction comprised a rights issue in favour of Norsk Hydro ASA's existing shareholders combined with a placing of compensation shares with the owners of Vale Aluminium and ensuing admission of the shares to trading.

Further, Statoil's spin-off and the admission to trading of Statoil Fuel & Retail ASA's shares on 22 October 2010 was among the major prospectus cases in 2010. Another sizeable prospectus case handled

in autumn 2010 was the public offering and admission to Oslo Børs of Gjensidige ASA's shares on 10 December 2010. Seawell Limited's shares, including the compensation shares issued in connection with Seawell's acquisition of Allis-Chalmers Energy Inc. were also admitted to trading. Seawell Limited was quoted for the first time on Oslo Børs on 26 November 2010.

Regulatory development

Finanstilsynet is represented on the Corporate Finance Standing Committee (CFSC), a subcommittee of the Committee of European Securities Regulators (CESR), which among other tasks has reformulated requirements on the content of prospectuses for oil, gas and mining companies (Mineral Companies). Finanstilsynet played an active part in this process. Finanstilsynet also participated in a working group charged with drawing up common European procedures for approval of prospectuses from third countries. This work is expected to reach completion in the course of the first half of 2011.

The most wide-ranging regulatory development issue in the prospectus area relates to the recently revised Prospectus Directive. The deadline for transposition of the new rules into Norwegian law is 1 July 2012.

FINANCIAL REPORTING SUPERVISION – LISTED COMPANIES

All listed companies are required to apply International Financial Reporting Standards (IFRS) when preparing and presenting consolidated accounts. Finanstilsynet is responsible for ensuring that this is done correctly. Supervision encompasses all Norwegian-registered enterprises that are listed on a stock exchange or a regulated market in Norway or a regulated market elsewhere in the EEA, as well as foreign enterprises that have chosen Finanstilsynet as the competent authority. It also encompasses enterprises that do not report according to IFRS. The supervision applies to periodic reporting such as annual accounts at the group and company level, directors' reports and interim accounts.

TRENDS

At the end of 2010, 240 Norwegian companies were subject to Finanstilsynet's supervision of financial reporting. Just under 200 were issuers of shares and equity capital certificates. Several issuers of shares and equity certificates also issued bonds that are quoted on Oslo Børs. Norway is the home state for issuers from the EEA, subject to certain conditions. Thirty-three foreign companies have chosen Norway as their home state. Finanstilsynet is prepared for the possibility that the turbulence in international markets could still pose

a challenge for valuation of company assets and liabilities. Adequate, precise notes to financial statements are accordingly imperative.

Upon review, the audit reports for 24 issuers were found to contain qualifications or emphasis of matters. Only nine of these issuers had given notification of deviating audit reports as required by the Securities Trading Act section 5-5 subsection (5). This shows that preparing the 2009 accounts was a challenge for many issuers.

SUPERVISION OF FINANCIAL REPORTING

Supervision includes all Norwegian-registered issuers listed on a stock exchange or regulated market in Norway, or on a regulated market elsewhere in the EEA. Listed issuers as well as issuers that have applied for listing are covered. Foreign companies from other EEA countries that are listed on Oslo Børs are subject to the supervision of the regulatory authorities in their respective home countries. Issuers listed on a regulated market in Norway and not registered in the EEA are covered provided they have chosen Norway as their home country. Central government, municipal and county authorities are not covered by the supervision, nor are municipal or intermunicipal enterprises/companies. State-owned enterprises are, however, included.

Finanstilsynet checks that annual accounts (at both the group and company level), directors' reports, interim reports and other financial reporting from issuers of transferable securities that are quoted, or for which admission to quotation has been sought, on a regulated market in the EEA, are in conformity with relevant laws or regulations.

Supervision covers companies' periodic reporting, irrespective of what accounting standards have been applied. A combination of techniques is applied in selecting enterprises for control. A three-pronged model has been established whereby some companies are selected based on submitted reports, and others based on risk assessments.

Risk-based analyses are carried out based on reports received via the Altinn internet portal. A rotation system is employed to ensure that the financial reporting of all enterprises is reviewed within a given period.

In 2010 Finanstilsynet reviewed all or parts of the financial reporting of 31 companies. Particular attention was focused on issuers of equity instruments such as shares and equity certificates, and certain bond issuers. As a result of this review, four cases were given closer scrutiny; several had yet to be finalised at year-end. No information was received in 2010 from the companies, their elected officers, senior employees or auditors to indicate that the financial reporting of the issuers failed to provide a true and fair view in conformity with the provisions of the Securities Trading Act. Finanstilsynet also reviewed the audit reports of all listed companies.

Violation charge for late publication of periodic financial reports

Finanstilsynet's supervision of periodic reporting includes verifying that reports are published within relevant deadlines. The deadlines for the periodic reporting are absolute, and in principle any violation results in a violation charge. A concrete assessment is made in each case. Finanstilsynet has no power to grant dispensation from the deadlines.

The charges vary between NOK 5,000 and NOK 200,000, depending on the company's market value or nominal value of the quoted instruments. The charge was doubled in four cases where reports were published unacceptably long after the deadline.

Ten issuers were censured for late publishing of annual reports for 2009 while violation charges were imposed on a further eight issuers. Four issuers received a violation charge for late publication of the half-yearly report for 2010. No delays were identified as regards fourth quarter reports for 2009 or first quarter reports for 2010.

Valuation of investment property

During the financial crisis little variation was observed in the value of investment property in life insurers' balance sheets, whereas mutual funds and listed companies showed a significant decline in values. In 2010 Finanstilsynet took a closer look at valuation of investment property at three stock exchange listed groups having life insurance as a part of their business. This supervision covered both the model used to value properties and the assumptions applied in the case of a number of individual properties across several periods.

According to IAS 40 *Investment Property* (IAS 40) an investment property's fair value should reflect market conditions at the end of the reporting period. The best evidence of fair value is given by current prices on an active market for similar property in the same

location and condition and subject to similar lease and other contracts. The market for commercial property in Norway is illiquid and not transparent: information about executed transactions is not readily available, and is often insufficient to judge whether the pricing in a transaction is relevant to the property to be valued. In the absence of such information the IAS 40 permits the use of discounted cash flow projections based on reliable estimates of future cash flows. Such estimates should as far as possible be supported by external market information.

In the absence of an active market, entities largely use discounted cash flows. In Finanstilsynet's view, assigning values to underlying factors – in particular future market rent and discount rate – is a challenge due to the absence, or incompleteness, of market data. Moreover, the selection of underlying factors is poorly documented, and Finanstilsynet considers that any exercise of judgement must be documented to permit verification. Finanstilsynet called on market participants to show greater openness about their transactions in the interest of a better basis for property valuations. The report "Valuation of investment property" is available on the Authority's website.

Impairment assessments

Owing to the financial crisis many companies had a low price-book ratio at the end of 2008, and impairment assessments and associated notes to accounts for 2008 received special attention when annual financial statements were inspected.

Finanstilsynet scrutinised several companies whose impairment assessments and notes to the accounts were flawed. In several cases Finanstilsynet drew attention to shortcomings in the model used to determine the discount rate. At one company, Kongsberg Automotive ASA (KA), goodwill was essentially tied to the acquisition of Global Motion Systems at the end of 2007. After the acquisition the company experienced poor turnover, operated at a loss and carried out major reorganisation and restructuring. The company's impairment test showed value in use in excess of recognised goodwill at the end of 2008, and the company had accordingly not written down its goodwill balance. The company had utilised finance theory models (WACC and CAPM) to estimate the discount rate. KA reported estimating the pre-tax discount rate at 9 per cent, but had increased it to 11 per cent to be prudent.

Finanstilsynet commented that several assumptions included in the calculation of the discount rate had not been determined in accordance with the requirements of IAS 36 and finance theory underlying the calculation of WACC – resulting, in Finanstilsynet's view, in a low discount rate. This was not of significance for the impairment assessment as of 31 December 2008 since value in use was still higher than the carrying value. The company will have to take Finanstilsynet's

observations into account when conducting impairment tests in the future. Finanstilsynet also pointed to inadequate note disclosures in relation to IAS 36.

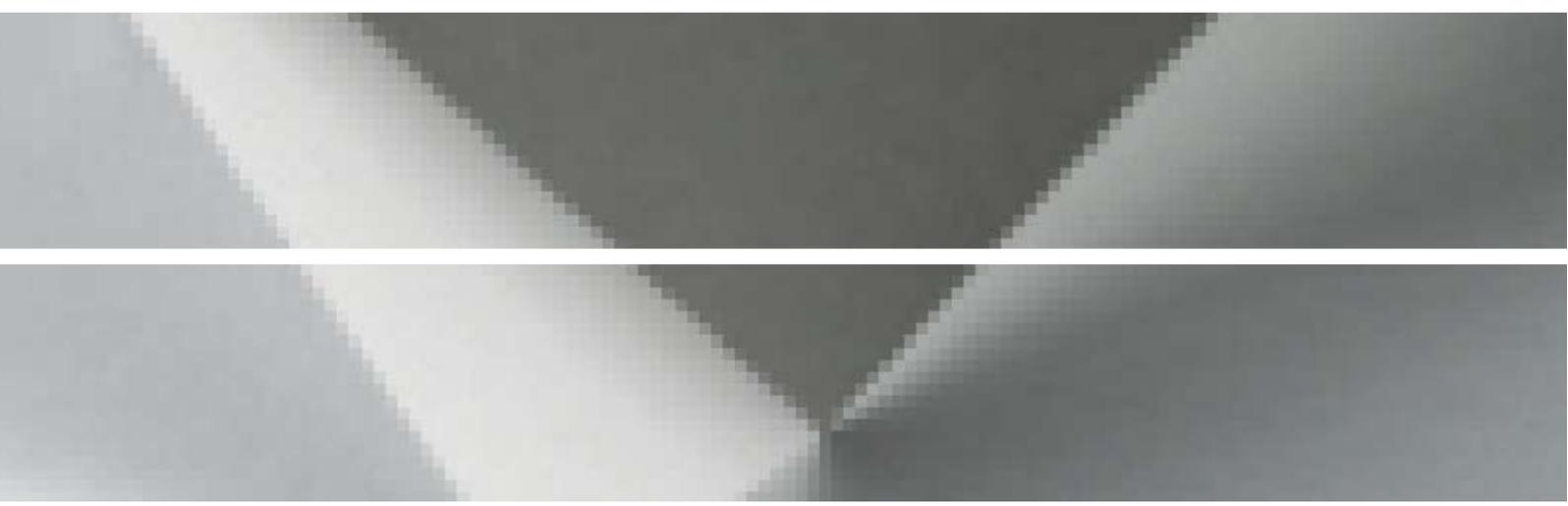
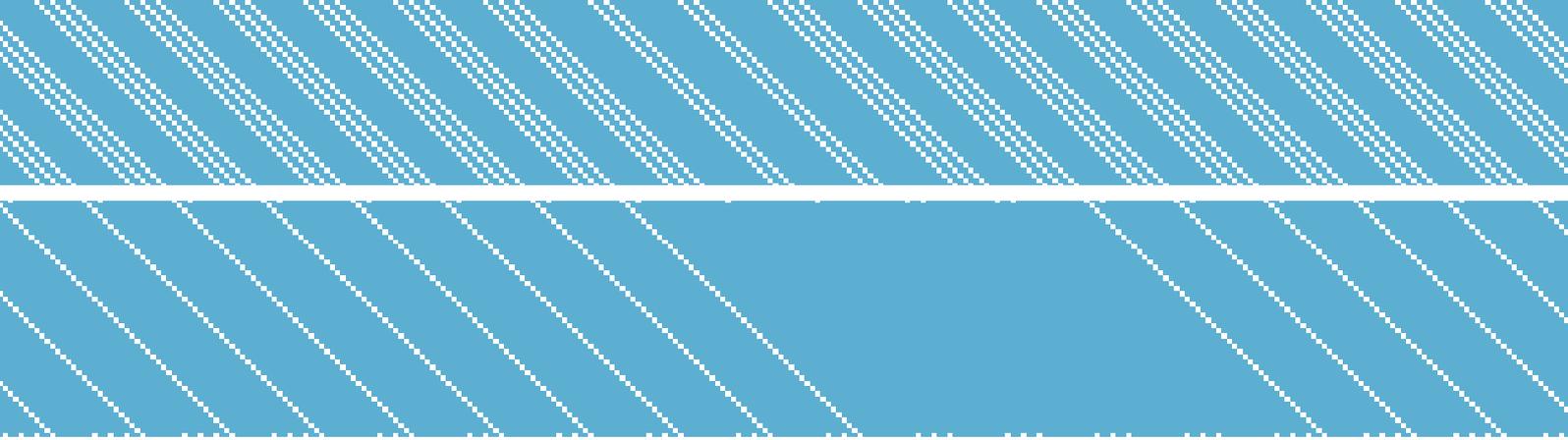
EXPERT PANEL ON ACCOUNTANCY

An important complement to Finanstilsynet's resources is the Expert Panel on Accountancy. The panel was appointed by the Ministry of Finance on 13 October 2005 based on Recommendation to the Odelsting No. 17 (2004–2005) submitted by the Standing Committee on Finance and Economic Affairs. Finanstilsynet is secretariat to the Expert Panel.

The Expert Panel met seven times in 2010, and had four matters referred to it for comment or discussion, some of which were considered on two or more occasions. Its advice is announced as a part of Finanstilsynet's final letters as and when the letters are made public. The letters are available on Finanstilsynet's website.

The Expert Panel as at 31 December 2010

Frøystein Gjesdal (chair)
Aase Aa. Lundgaard (deputy chair)
Ståle Christensen
Stig Enevoldsen
Bjørgunn Havstein
Erik Mamelund
Signe Moen
Karina Vasstveit Hestås (alternate)
Jørgen Ringdal (alternate)
Elisabet Sulen (alternate)



REGULATORY DEVELOPMENT

Accounting legislation for the financial industry

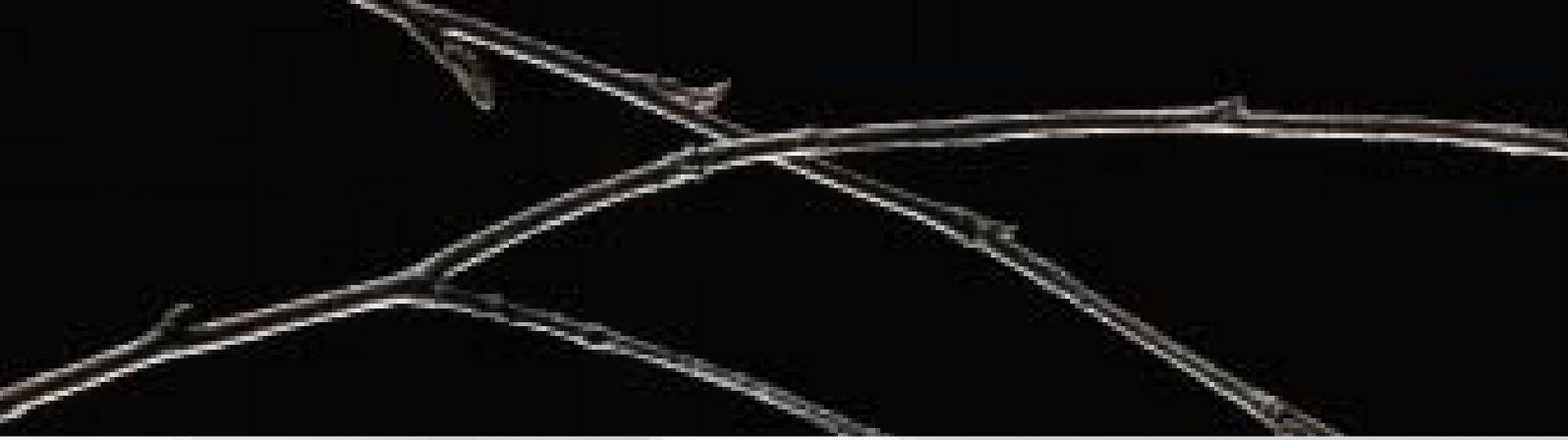
A comprehensive guide to the accounting rules for insurance companies was finalised on 11 February 2010 and announced in circular 8/2010. Finanstilsynet intends to update the guide on a regular basis to include changes to, and new interpretations of, the body of accounting rules.

The Ministry of Finance asked Finanstilsynet by letter of 18 December 2009 to consider the merits of further expanding the scope for exemptions from the note disclosure requirements, and of further exemptions from the note disclosure requirements for small insurers. Finanstilsynet prepared a consultation paper recommending changes

to regulations which it forwarded to the Ministry of Finance on 6 May 2010. After circulation for comment the recommendations were adopted on 12 January 2011 with effect for the financial year 2010.

Finanstilsynet is drafting a consultation paper with a view to regulations specifically governing the annual accounts of pension funds. This will be forwarded to the Ministry of Finance in the first quarter of 2011.

Finanstilsynet keeps abreast of international developments in the accountancy field, particularly with regard to insurance contracts and new rules with regard to impairment write-downs.



Finanstilsynet's oversight of auditors comprises approval or licensing of individuals and firms in accordance with the legal requirements applying to this profession, as well as registration and supervision. Supervision includes checking that auditors maintain their independence, and that they discharge their assignments in a satisfactory manner and in compliance with law, regulations and good audit practice.

AUDITING



TRENDS

Market participants' confidence in financial reporting by business and industry is key to achieving well functioning markets. This is particularly true for public interest entities, i.e. banks and other credit institutions, insurance companies and listed companies. Good quality audits support that confidence. In order to properly perform the role of representative of the general public, it is imperative that the auditor is independent and performs the audit in conformity with the requirements of the Auditors Act. In October 2010, in the wake

of the financial crisis, the EU Commission circulated for comment a green paper setting out measures likely to strengthen auditing as an institution. Any widening of small firms' exemption from the statutory audit obligation is likely to impact on the audit industry by encouraging more auditors to apply for a licence to offer external accounting services. This, together with the processing effort involved in assigning auditor register numbers, will increase Finanstilsynet's workload in the licensing area.

SUPERVISION AND MONITORING

Finanstilsynet inspects compliance with the requirements on auditing activities as such, that requirements on auditor independence are met and that the quality of audits performed is satisfactory. Inspections cover compliance with the money laundering legislation, and that auditors and audit firms submit their accounts and tax returns on time.

Finanstilsynet carries out inspections based on its own risk assessments, reports received and other signals, for example in the media. Matters that come to light in other areas supervised by Finanstilsynet may also prompt investigation of the work of an auditor. Moreover, recurring inspections of auditors of entities subject to statutory audit are required at least every sixth year, while auditors and audit firms that audit public interest entities are subject to recurring inspections at least every third year.

Since 2002 the recurring inspections have been coordinated with the quality assurance reviews conducted by the Norwegian Institute of Public Accountants (DnR) in respect of its members. Should DnR bring to light circumstances that may prompt withdrawal of an auditor's licence, the matter is referred to Finanstilsynet for further action. DnR's report for 2010 is reproduced on page 79. Finanstilsynet carries out inspections of non-members to ensure fulfilment of the recurring inspections obligation. The Audit Directive requires the recurring

inspections of auditors and audit firms that audit public interest entities to be performed by an independent supervisory authority. As from 2011 the Norwegian Institute of Public Accountants (DnR) will no longer conduct quality assurance reviews of those of its members that are part of an audit firm that audits public interest entities. These auditors will now be subject to Finanstilsynet's inspections, in addition to other supervisory activity directed at auditors who audit public interest entities.

Finanstilsynet received about 100 reports on auditors in 2010 from DnR, the tax authorities and bankruptcy administrators, in addition to other signals possibly indicating deficient audit practice. This figure is on a par with previous years. Since Finanstilsynet's resources are largely applied at cases where there are clear indications that the audit was not performed in conformity with the Auditors Act, most cases examined by Finanstilsynet conclude with critical remarks on the conduct of the audit or withdrawal of the auditor's licence. Cases not given priority by Finanstilsynet may conclude with the auditor being asked to submit a documented self-assessment of whether the audit practice should be modified for the future.

Eighty-five on-site inspections were conducted in 2010 in addition to other supervisory activities. Some cases will only reach completion in 2011. Two IT inspections were also carried out.

Table 11: Revocation of auditors' licences

	2007	2008	2009	2010*
State authorised auditors, licences revoked	3	3	1	10
Registered auditors, licences revoked	4	9	4	13
Audit firms, licences revoked	0	0	3	1

* Of a total of 24 licence revocations in 2010, 21 were due to failure to respond to off-site supervision conducted in 2009.

Follow-up of the largest audit firms and their audit of listed companies

Audit firms are required by law to establish adequate internal quality control systems. The systems that are established are of significance for the quality of all audit assignments taken on by the firm. Finanstilsynet therefore conducts inspections targeting audit firms' policies and procedures. Compliance with the audit legislation and internal policies and procedures is checked during reviews of selected audit assignments.

KPMG AS was subject to such an inspection in August 2009. Final observations were issued in 2010. Similar inspections were conducted at BDO and PwC. Finanstilsynet's observations after the inspection of BDO included some remarks, e.g. that guidelines for sales of non-audit services to audit clients need to be better reflected in the company's policies and procedures. Observations after the inspection at PwC are yet to be finalised. Audit firms eligible to audit companies registered in the US are also subject to recurring inspections by the Public Company Accounting Oversight Board in the US (PCAOB). Finanstilsynet was unable to conduct joint inspections with the PCAOB in 2010 of Norwegian audit firms since cooperation on joint inspections has yet to be formalised in accordance with the requirements of the Audit Directive.

Finanstilsynet reviewed the transparency reports which audit firms that audit public interest entities are required to submit. The reports vary widely in terms of scope and content, and several were filed after the deadline. This was the first time transparency reports were prepared in Norway. Finanstilsynet will consider measures that will help to ensure that next year's reporting is more in line with applicable requirements and the purpose of the reports.

Other individual cases

Finanstilsynet inspected the audit of four insurance companies in 2010 and found that the auditor had relied too heavily on the assessments of the appointed actuary without considering whether the latter's assessments provided sufficient audit evidence.

At the end of 2008 bankruptcy proceedings were opened against the main firms in the estate agency chain Notar. Many firms are involved.

Finanstilsynet decided to review the auditor's work, but chose to await the results of the administration boards' enquiries. While the auditor review resulted in no significant observations regarding the audit, Finanstilsynet nevertheless found it necessary to emphasise that it is important for the auditor to send numbered letters to the management advising them of any rule violations and/or matters giving rise to liability.

Finanstilsynet focused particular attention on auditor independence. In one case Finanstilsynet commented that an audit firm was barred from taking on an audit assignment because it had in the previous year delivered services which compromised its independence as auditor. Finanstilsynet also reviewed the audit of the Centre Party's accounts and brought to light evident deficiencies. These included failure to take sufficient account of the fact that the party is subject to the Political Parties Act. The press also queried auditor independence at Lillestrøm Sparebank, and Finanstilsynet looked into the matter despite the bank having replaced its auditor. The case has yet to be finalised.

Thematic inspections

In spring 2010 Finanstilsynet conducted a thematic inspection focused on auditor acceptance and continuance assessments, as well as assessments related to termination of audit engagements. In Finanstilsynet's view, compliance with Auditors Act is less than fully satisfactory in this area. The documentation was not sufficient to verify an auditor's deliberations and actions. Thematic inspections are conducted on an annual basis, and aggregate reports are published on Finanstilsynet's website.

After the thematic inspection in 2008/2009 of audits of foundations, Finanstilsynet was again in contact with the Foundations Authority in 2010 with regard to follow up of individual auditors.

Off-site supervision

All auditors and audit firms are subject to off-site supervision every second year. In the supervision programme conducted in autumn 2009 auditors filed their returns via the Altinn internet portal. A summary of the results was published on Finanstilsynet's website in spring 2010.

Individual auditors and audit firms are followed up based on the returns received, with a particular focus on compliance with the

continuing education requirement and delivery of non-audit services to audit clients.

LICENSING

Table 12: Number of approved auditors and audit firms

	31.12.2007	31.12.2008	31.12.2009	31.12.2010	Licensed in 2010
State authorised auditors	2,642	2,728	2,826	2,984	234
Registered auditors	3,028	3,049	3,117	3,226	206
Audit firms	789	825	820	776*	24

The figures do not include licences handed in during the year.

* The decline is probably related to the fact that a company that owns audit firms no longer needs to be an approved audit firm itself.

Finanstilsynet authorises auditors as either registered or state authorised auditors. State authorised auditors are subject to higher education requirements than are registered auditors. In addition to statutory minimum education requirements, a practical examination has to be passed in order to qualify for authorisation. The examination is prepared by an examination board and is organised by Agder University College on behalf of Finanstilsynet. 377 candidates passed the examination in 2010.

Finanstilsynet has upgraded the Register of Auditors to enable more data to be fed in. All auditors who take on statutory audit engagements are assigned an auditor register number. This has taken longer than planned due to technical changes needed in the IT systems.

The issue of whether an audit firm owned by one or more municipalities can audit companies subject to statutory audit that are owned by the same municipalities has been unresolved for some time. With basis in Ministry of Finance statements with regard to amendments to the Auditors Act, Finanstilsynet stated that the provisions of the Act governing auditor independence do not preclude such assignments provided that further conditions regarding organisation etc are met.

Processing of notifications to Finanstilsynet of the grounds for terminating an auditor assignment on a date other than the date of the ordinary general meeting or partners' meeting has been deprioritised. Finanstilsynet has recommended rule changes to the Ministry of Finance.

REGULATORY DEVELOPMENT

In June 2007 Finanstilsynet proposed new provisions to implement and supplement the law amendments adopted by the Storting to transpose Directive 2006/43/EC (Audit Directive) into Norwegian law. The Ministry of Finance made a number of changes in the Auditors Regulations with effect from 1 July 2010. These related to approval of audit firms from elsewhere in the EEA and to auditor supervision, including exemption from the rules of the Auditors Act and the Financial Supervision Act governing confidentiality. Regulations on registration and supervision of third country auditors and third country audit firms were also adopted. A provision was added to the Auditors Regulations permitting entities subject to statutory audit that become public interest entities to defer compliance with the auditor rotation requirement until the year after they become public interest entities. Moreover, some clarifications were made to provisions governing continuing education and provisions regarding retention of documentation.

In November 2008 Finanstilsynet prepared a consultation document on implementation of Directive 2005/36/EC on the recognition of

professional qualifications. The Ministry of Finance amended with effect from 30 September 2010 provisions of the Auditor Regulations governing approval of professional qualifications from other countries, and a new provision on carrying on audit business on a temporary basis was adopted.

In March 2007 Finanstilsynet prepared a consultation document with a view to a common appeals board for decisions directed at auditors and external accountants. The Ministry of Finance circulated a reworked proposal for comment in March 2010. Finanstilsynet issued a statement in June 2010 highlighting the importance of the board's and secretariat's independence in relation to the two lines of business. The board has yet to be established.

Finanstilsynet also provides consultative comment on new audit standards set by the industry. The standards go a long way to supplementing the legal standard for "good auditing practice" in the Auditors Act. In 2010 Finanstilsynet's comments focused on the design of the audit report.

Finanstilsynet
 Postboks 1187 Sentrum
 0107 Oslo

Oslo, 26 January 2011
 Our ref.: HA/bb

DnR Quality Assurance Review – Annual Report 2010

With reference to the “Guidelines for periodic quality assurance reviews of auditors and audit firms”, 2.3(j), the Board of DnR hereby presents a summary of the quality assurance reviews conducted in 2010.

Organisation of the quality assurance review

The procedures of the quality assurance review are described in “Details of the quality control programme 2010” as posted on www.revisorforeningen.no. It is designed to test compliance with good auditing practice, including standards on auditing, with a specific focus on the provisions of the Auditors Act concerning auditors’ finances, independence, indemnity insurance and continuing education.

The review team comprised 38 state authorised and registered auditors, all with a broad professional background.

Selection of auditors for quality assurance reviews

In 2010 the quality assurance programme included 1,529 statutory auditors. 280 statutory auditors were selected for ordinary review, including two ordinary reviews deferred from 2009. Upon being notified that they had been selected for ordinary review, 13 of these 280 auditors announced that they would wind up their business or retire as statutory auditors in the course of 2010. In addition ten members were selected because they had already been notified of follow-up reviews by Finanstilsynet. One member died before the review was conducted. This left a total of 256 statutory auditors to undergo ordinary reviews in 2010. Seven of these reviews were deferred to 2011 and will be included in the statistics for the year in which they undergo review. In addition 41 statutory auditors were subject to follow-up reviews, including one review deferred from 2008. In total 290 reviews were conducted in 2010.

Result of the quality assurance reviews

It is our opinion that Norwegian statutory auditors maintain a high professional standard, and that their work is of high quality. Nevertheless, it is a continuing aim of DnR to reduce the number of cases in which follow-up measures are required. We will seek to achieve this by delivering technical information and guidance to our members.

	Number	%
Approved	258	89.0
Audit flaws and/or other shortcomings – action plan and new review	28	9.6
Referrals to Finanstilsynet for further action	4	1.4
Total number of reviews conducted	290	100.0

Yours sincerely

(sign.)

Håvard S. Abrahamsen

Chair

Norwegian Institute of Public Accountants





EXTERNAL ACCOUNTING SERVICES

Finanstilsynet's tasks in relation to external accounting services comprise authorisation of individuals and firms in accordance with the legal requirements applying to this profession, as well as registration and supervision. Supervision includes checking that the activities of providers of external accounting services comply with laws and regulations and with good accounting practice.

TRENDS

The industry comprises almost 20 large external accounting firms and networks along with a large number of smaller firms. Given the industry's development of good-accounting-practice standards and the complexity of the legislation in general, staying updated is a challenge for external accounting firms, especially the smaller ones.

Any changes made to the statutory audit requirement may impact on the external accounting industry in as much as more auditors will apply for authorisation as external accountants. Companies

that choose not to have an auditor will more likely obtain advisory services from external accountants than previously. Increasing use is being made of electronic systems in the execution of external accounting assignments. System errors may cause accounting material to be lost, and business shutdowns can cause problems for clients who are dependent on simultaneous accounting. In addition to the increased risk involved in the use of IT, the above development makes outsourcing by external accounting firms, and non-residents' access to the Norwegian market, more likely.

SUPERVISION AND MONITORING

Finanstilsynet checks compliance with the requirements applying to external accounting firms. This includes examining firms' quality control of the work done by staff who are not authorised external accountants, their compliance with duties under the Accounting Act, the Bookkeeping Act and the money laundering legislation, and external accountants' and external accounting firms' timely submission of their own accounts and tax returns.

In view of the large number of external accountants and external accounting firms, the quality control performed by the Norwegian Association of Authorised Accountants (NARF) of its members every seven years is a useful contribution to the supervisory effort. Guidelines for collaboration with the NARF have been drawn up. The NARF's quality control report for 2010 is reproduced on page 85. In addition to reports from the NARF, Finanstilsynet conducts inspections on the basis of reports received from the tax authorities, liquidators of bankruptcy estates, clients of external accountants and media coverage. Some inspections are carried out without being prompted by suspicion of rule breaches. When external accountants

are selected for inspection, a criterion is whether or not they are quality controlled by NARF. Finanstilsynet has a particular focus on the largest external accounting firms and groups.

Finanstilsynet received 130 reports regarding external accountants in 2010 from the NARF, the tax authorities and estates in bankruptcy, along with other indications of possible deficiencies in the execution of assignments.

Finanstilsynet conducted 56 on-site inspections in 2010 in addition to other supervisory activities. Two IT inspections were carried out. Some cases will only be finalised in 2011. The Authority's resources are largely deployed to cases where there are clear indications that external accounting services are not in conformity with applicable rules. A large proportion of supervisory cases accordingly result in critical observations or licence withdrawal. Finanstilsynet also notes cases where on-site inspections cannot be conducted at the appointed time, and where external accountants hand in their licence when informed of an on-site inspection.

Table 13: Revocation and suspension of authorised external accountants' licences

	2007	2008	2009	2010
External accountants, licences revoked	49	19	47*	15
External accounting firms, licences revoked	19	0	47**	18
Suspension	1	1	0	0

* Thirty-six of these revocations were due to failure to respond to a questionnaire (off-site supervision).

** Thirty-two of these revocations were due to non-compliance with the law requiring an authorised external accountant to be in charge.

All authorised external accountants and external accounting firms are subject to off-site supervision once every two years. This is a useful instrument both because it ensures contact with all supervised entities and because it involves a clean-up of the profession in as much as entities no longer needing their licence hand it in. Failure to respond to Finanstilsynet's questionnaire normally leads to revocation of authorisation as an external accountant or external accounting firm. The number of licence revocations is accordingly higher every second year.

Off-site supervision was carried out in autumn 2010 and reports were submitted via Altinn, as previously. A synoptic report, presented in spring 2011, is available on the Authority's website.

In addition to providing an overview of the industry, the questionnaire responses provide a basis for scrutiny of individual external accountants and external accounting firms. Finanstilsynet will give particular attention to breaches of the statutory requirement for continuing education and to external accounting firms in a negative equity capital position.

Seminars for external accountants

In 2010 Finanstilsynet gave presentations at nine seminars under NARF auspices. The body of rules with which authorised external accountants are required to comply was reviewed and supplemented with practical advice. Finanstilsynet also highlighted the obligations consequent on authorisation and on being an entity under supervision. Almost 600 external accountants attended. Finanstilsynet gave further presentations at five seminars organised by Økonomiforbundet, attended by 170 persons.

Unlawful external accounting activity

Finanstilsynet has limited resources available to investigate unlawful external accounting activities. It is in clients' own interests to utilise the competence and security inherent in the authorisation scheme. Users of external accounting services should therefore check that the external accountant they are using is duly authorised and is listed in Finanstilsynet's licence register, which is available on the Authority's website.

Table 14: Unlawful external accounting activity

	2007	2008	2009	2010
Reports received	33	19	19	10
Activities suspended	9	7	3	1
Reports to the police	0	0	1	0

LICENSING

A standardised application form exists for external accountants and external accounting firms. The application form and guidance are available on Finanstilsynet's website.

As from 31 December 2009 all external accountants have been required to comply with the continuing education requirement which was adopted in 2006. In 2010 as previously Finanstilsynet handled a number of applications for deferment of the deadline, and applied a restrictive practice.

Table 15: Number of authorised external accountants and external accounting firms as at 31.12.

	2007	2008	2009	2010	Licences granted in 2010
External accountants	7,966	8,340	8,780	9,260	807
External accounting firms	2,691	2,676	2,693	2,691	200

The figures do not include licences handed in during the year.

REGULATORY DEVELOPMENT

In January 2009 Finanstilsynet circulated for comment rule changes to implement Directive 2005/36/EC on the recognition of professional qualifications. It subsequently amended, with effect from 24 February 2010, the provision of the Accounting Regulations regarding approval of professional qualifications from other EEA states. In addition a new provision was adopted on the right to provide, on a temporary and basis and in certain cases, external accounting services in Norway.

In March 2007 Finanstilsynet prepared a consultation paper with a view to a setting up a common appeals board for decisions directed at auditors and external accountants. The Ministry of Finance circulated a reworked proposal for comment in March 2010 on which Finanstilsynet issued a statement in June 2010.

Oslo, 31 January 2011

NARF Quality Control – Annual Report 2010

The Norwegian Association of Authorised Accountants (NARF) conducted its quality control programme in 2010 with a basis in the cooperation agreement in effect with Finanstilsynet, in keeping with adopted guidelines and in accordance with the plan for its operations forwarded in 2009. We hereby present an overview of controls conducted in 2010.

Number of controls

A total of 343 quality controls were conducted in 2010, of which 56 were follow-up controls. The number of quality controls carried out was lower than planned, mainly because 31 external accountants reported their intention to wind up their business while 39 controls were postponed until 2011 due to illness or reorganisation of the entity concerned.

Level of control and implementation

As part of a continuing aim to improve members' service quality, eight quality control seminars were held in autumn 2010. The focus was on statutory requirements and good accounting practices. Finanstilsynet played a contributory role.

The control programme for 2010 was based on previous control programmes, but focused to a greater degree than previously on risk management and internal control.

A total of 33 controllers were engaged in the 2010 control programme, the great majority having attended a two-day seminar in advance. The seminar focused on controller – controlled entity, the control procedure proper, internal control and risk management as well as requirements applying to the conduct of the profession and to appraising the quality of controlled members.

Result of the quality control programme

The 2010 quality control programme produced the following results:

	Ordinary controls				Follow-up controls			
	Individuals	%	Firms	%	Individuals	%	Firms	%
Approvals	483	90	245	86	72	87	47	84
Follow-up controls	53	10	40	14	11	13	9	16
Total	536	100	285	100	83	100	56	100
Control results yet to be processed	2		2		–		–	

NARF considers on a continuous basis measures able to enhance quality levels in the industry, with a particular focus on risk and materiality.

Four cases were referred to Finanstilsynet in 2010 for further action.

Yours sincerely

(sign.)
 Sandra Riise
 Managing Director
 Norwegian Association of Authorised Accountants





Supervision of estate agents encompasses the activities of firms licensed to practise estate agency and lawyers who have put up security for estate agency, as well as housing cooperatives licensed to provide estate agency services. Firms, lawyers and housing cooperatives are checked for compliance with the requirements of the law and regulations, including observance of good estate agency practice. In addition, Finanstilsynet is also assigned administrative, consultative and information tasks under the Estate Agency Act.

ESTATE AGENCY



TRENDS

Increase in the number of estate agency firms

2008 and 2009 combined saw a steep decline in the total number of estate agency firms. This was a result of two factors: a) the financial crisis and b) the requirement that firms licensed to engage in estate agency under the previous Estate Agency Act had to apply for a new licence under the new Estate Agency Act by the end of 2009. 2010 showed new growth in the number of agencies due to the continuation into 2010 of the rise in property market activity seen in the second half of 2009. While 516 firms were licensed to carry on estate agency at the start of 2010, this figure increased to 550 as at 31 December 2010.

Banks' increased involvement in estate agency

Banks have acquired an increasingly prominent position in the estate agency industry over the last ten years and are at the forefront of the chain formation process that characterises the industry. Banks' share of the total market, based on the total number of transactions at estate agency firms having a bank as their predominant owner and/or franchiser, increased from around 40 per cent in 2003 to some 63 per cent in 2010. Banks regard estate agency firms as important distribution channels for services sold within the framework permitted by the Estate Agency Act. Loan sales are most relevant in this context, although house insurances and contents insurances can also be sold through an estate agent.

Alternative estate agent concepts – "be your own estate agent"

As from 2010 internet portals that market real estate are no longer allowed to cater exclusively to estate agents. Since portals such as FINN Eiendom can now carry private property advertisements, there are far more opportunities for property owners to take charge of the sale process themselves; this does not however apply to the financial settlement which is difficult to do properly without the services of an intermediary. Some estate agents and lawyers have developed web-based services to sell properties and to attend to the financial

settlement. This usually involves offering do-it-yourself "packages" to property sellers enabling them to take care of a large or small portion of the sale process themselves.

However, this type of sale causes a problem with regard to the Estate Agency Act which permits only two types of estate agency assignment, i.e. a) sale assignment and b) settlement assignment, limited to contract and financial settlement, or settlement only. Finanstilsynet also believes that the estate agent cannot lawfully sell such products that carry the agent's name, logo, identifying marks, etc., which may leave the average buyer with the impression that the information given in property-for-sale descriptions etc is controlled by the estate agent in accordance with the Estate Agency Act's rules.

The Consumer Council has approached the Ministry of Finance with a call to amend the estate agency legislation so as not to prevent the development of new products in the area of property sales. It points out that obtaining information about a property should be able to be left to the seller, but that the information should be presented using the estate agent's forms with company logos etc., and the estate agent should carry out the bidding round and otherwise finalise the sale. However, in its assessment to the Ministry of Finance, Finanstilsynet has pointed out that the current Estate Agency Act builds on the presumption that the estate agent is in charge of the entire sale process and that the agent's control of and responsibility for the information that is communicated to the buyer is closely tied to his/her role in the negotiations between buyer and seller. If the estate agent is not to be responsible for obtaining and checking the information provided, it could lead to the seller paying a lower price for the estate agent's services. The disadvantage is that the buyer is given a false sense of security, which in Finanstilsynet's opinion weakens the buyer's consumer protection. Based on an overall assessment, including consideration of other factors, Finanstilsynet does not recommend changes at this point in time.

SUPERVISION AND MONITORING

Inspections in 2010

Finanstilsynet conducted 48 on-site inspections in 2010, including 43 at estate agency firms and five at the offices of lawyers offering estate agency services. One additional IT inspection was carried out. Inspections focused on aspects of estate agency that are of significance to consumer buyers and sellers – in particular the agent's handling of client funds and its compliance with the rules governing risk management and internal control. The agent's compliance with the obligation

to make the enquiries needed and to fulfil the statutory information requirement was also checked. The estate agent's duty of care is regarded as particularly important where one or both parties are in a consumer role. Estate agency firms and lawyers still consistently fail to apply fully satisfactory controls to the reconciliation of client funds documenting that the estate agent has handled client funds in the manner prescribed by the Estate Agency Act. The problem here is normally *not* that client funds have gone missing, but that the required control

ESTATE AGENCY

procedures have not been carried out by the correct person, i.e. the estate agent in charge. It is therefore not possible to establish that the estate agent has the necessary control over client funds.

Where financial settlement is concerned, instances continue to be brought to light of serious dereliction of the agent's obligation to ensure that clients are not, at the settlement stage, exposed to or inflicted with a financial loss because the estate agent has failed to observe basic routines for safe and secure settlement. Criticism must clearly be levelled in cases where the agent, prior to the transfer of property title, pays the purchase sum or parts of it to the seller with

no form of security, or without ascertaining whether the buyer has received the guarantee(s) required under the Housing Construction Act. This Act applies solely to a business's sales to consumer buyers, and it is therefore especially important for estate agents to ensure that consumer buyers' rights are protected when it comes to the sale of properties under construction.

Two lawyers had their licences to carry on estate agency revoked as a result of circumstances brought to light during inspections. In these cases the main reason for licence revocation was improper handling of client funds.

LICENSING

Licensing of 'transitional estate agents'

The Estate Agency Act of 29 June 2007 introduced competence requirements for all persons at estate agency firms who perform key estate agency tasks. A transitional arrangement was introduced to enable estate agents without the requisite estate agency or legal training to continue to operate in the industry. Under this arrangement persons wishing to apply for the right to be designated estate agent in charge must have worked in estate agency for at least three years, at least two of which must have been in the last five years. They are also

required to take certain tests and to meet conduct requirements. By the end of 2010 Finanstilsynet had issued 1,036 such licences.

The transitional arrangement was to be discontinued on 1 January 2011 but the Ministry of Finance extended it by six months to 1 July 2011. This was in line with Finanstilsynet's recommendation, based on a request from the Association of Real Estate Agency Firms for a one-year extension grounded in concern that there might be too few estate agents at the end of 2010 to meet the anticipated need.

REGULATORY DEVELOPMENT

When the Estate Agency Act became law on 1 January 2008 several supplementary provisions were needed. Adjustments also proved necessary in some areas.

In 2010 provisions regarding the winding up of estate agency firms, and provisions implementing EEA obligations, were added to the Act. Provisions were also introduced to enable cultivation of the role of 'estate agent in charge', by allowing one and the same person to hold this role at two or more estate agency offices. This could, it is presumed, contribute to increasing the quality of estate agency services.

Rules governing continuing education for estate agents were given effect on 1 January 2011. Further, the 24 hour rule with regard to bidding was changed to prevent estate agents from passing on bids with a shorter deadline for acceptance than noon on the day after property viewing.

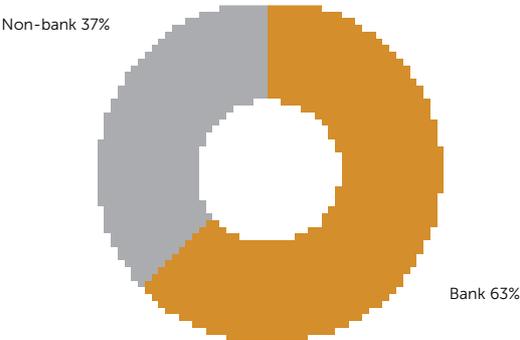
At the request of the industry Finanstilsynet has also considered other rule changes, inter alia recommending termination of the estate agent's obligation to specify in his/her invoice the time spent on an assignment based on commission or a fixed price.

INFORMATION AND COMMUNICATION

Finanstilsynet operates a relatively extensive advisory service to both the estate agency industry and the general public. The industry has a continuing need for updates on changes to regulations and Finanstilsynet’s view of what constitutes good estate agency practice. A large number of inquiries are received annually from individuals in need of advice and guidance in a purchasing or selling situation. Questions typically relate to the estate agent’s

obligations and responsibilities. However, Finanstilsynet is not an ordinary complaints body, and therefore refers complainants who desire a solution to their problems to *Reklamasjonsnemnda for eiendomsmeglingstjenester*, the body dealing with complaints regarding estate agency services. Enquiries from the public provide useful input regarding industry practice which is turned to account in Finanstilsynet’s ongoing oversight.

Chart 5: Share of total properties sold in the first half of 2010



“Bank” denotes firms that are owned by a bank, and/or are franchisees in a chain that is owned or controlled by a bank. The data are based on information regarding chain membership and ownership provided by the estate agency firm.

Source: Finanstilsynet



DEBT COLLECTION

Supervision of the debt collection industry encompasses agencies' financial position and their treatment of client funds, agencies that collect overdue debt on behalf of other businesses and organisations as well as agencies that purchase overdue debt and collect it themselves. Collection of own claims and lawyers' debt collection activities lie outside the scope of Finanstilsynet's supervision. At on-site inspections Finanstilsynet checks in particular that recovered funds are properly handled and that the business in general is conducted in accordance with good debt collection practices.

TRENDS

Decline in total number of debt collection agencies

The number of ordinary debt collection agencies, 110 at the start of 2010, fell to 102 by the end of the year. This is a fairly significant divergence from the very stable industry structure in evidence over the previous ten years. There is reason to believe that the decline in the total number of agencies is related to the marked reduction in collection fees as from 1 January 2010. For many agencies this change puts significant pressure on profitability, and a number of owners have consequently sold out to larger debt collection agencies or wound up their debt collection business.

A few debt collection agencies dominate the industry

Based on agency reports, the debt collection industry is dominated by the ten largest agencies. These account for 70 per cent of the market in terms of total debt collection cases in process, and 81 per cent of the market in terms of claims for recovery and total collected funds.

Increase in the number of debt collection cases

In recent years there has been fairly strong growth in the number of new debt collection cases. About 2.8 million new cases were referred to debt collection agencies in the first half of 2010, an increase of about 67,000 cases over the same period of 2009. In total, debt collection agencies had 3,460,000 cases in process as at 30 June 2010. These cases represented claims for recovery totalling NOK 64.4 billion, NOK 5.7 billion more than in the first half of 2009. Judging by figures that Finanstilsynet receives from debt collection agencies in their mid-year returns, severe payment difficulties are not at the root of a large number of cases since as many as 800,000 cases were closed before dispatch of a demand for payment.

At the end of the first half of 2010 1,870 full-time equivalents were employed in debt collection agencies. The number of full-time equivalent positions in the industry has steadily increased. This is probably related to the increase in the total number of debt collection cases referred to the agencies.

SUPERVISION AND MONITORING

At on-site inspections the agency's general debt recovery procedures and agreements with clients are reviewed, and the procedure followed in individual cases is checked on a random basis.

The agency's risk management and internal control and general routines for the handling of client funds are also checked. Further, the agencies' accounts are reviewed, including client credit balances in relation to client liability.

Inspections in 2010

Finanstilsynet conducted 12 on-site inspections at ordinary debt collection agencies in 2010. Most of the inspections were conducted on the basis of signals received by Finanstilsynet from consumer debtors or clients of debt collection agencies. One additional IT inspection was carried out. A number of limited off-site inspections were also carried out based on correspondence with the relevant agencies to investigate allegations of faulty debt collection procedures.

The on-site inspections revealed a number of flawed assignment agreements with regard to the respective responsibilities of debt

collectors and their clients, and the use of deficient debt collection notices, demands for payment and other claim letters. The inspections also discovered debt collection agencies that had charged debt collection fees in violation of the debt collection legislation. This was due to system errors resulting in fees being stepped up at an earlier stage than permitted under the debt collection regulations. These are errors that the ordinary consumer debtor would not normally be in a position to identify, and which it is especially important to check during the ongoing supervision of debt collection agencies. Finanstilsynet pointed out that the debt collection agencies' handling of objections has been counter to good debt collection practice, and that agencies have not adhered to the notification rules in the Debt Collection Act section 9 and 10 regarding additional claims. Finanstilsynet also had individual comments on agencies' routines for handling client funds, and some comments on agencies' compliance with the regulations governing ICT systems at banks etc.

Some agencies were found to be non-compliant with the regulations relating to risk management and internal control.

LICENSING

Complaints/enquiries

Finanstilsynet received 203 written complaints relating to agencies licensed to engage in debt collection in 2010. The complaints related in particular to debt collectors' handling of objections, conditions for charging fees, design of letters demanding payment, and their registration of debtors on the debtors list and not being expunged from that list.

In 35 cases Finanstilsynet decided to undertake a supervisory review of the complaints. Most of these complaints were from consumer debtors. In other cases Finanstilsynet referred the complainant to the Debt Collection Complaints Board if he/she was a consumer. Businesses are required to take their own steps to resolve a dispute, possibly with the help of a lawyer. Rejected requests can form the basis for further investigation at a later date.

Most of the enquiries that resulted in further investigations were concluded on the basis of a statement from the debt collection agency.

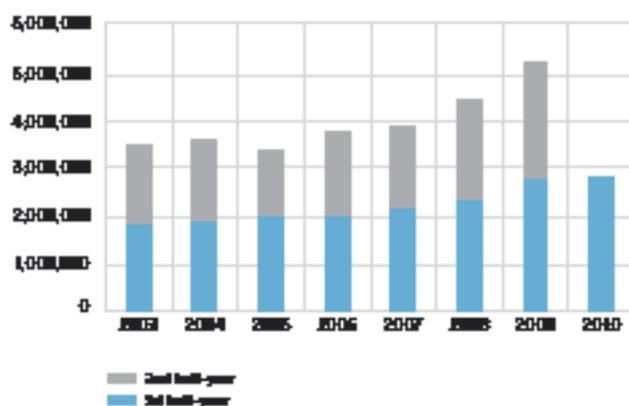
This was usually because there was no basis to conclude that the debt collection agency had displayed censurable conduct, or because the debt collection agency itself had moved to correct minor errors. A few cases were followed up more closely with the result that the debt collection agency was censured.

In the autumn of 2010 the media focused attention on instances where the debtor is sought out at the workplace or home. This procedure is employed to some extent, particularly where the creditor has a charge over an asset such as a car and it is necessary to inspect the asset in order to assess its condition and value, and/or also the place where the asset is located. In one case in particular, serious allegations of improper conduct were levelled at a representative of a large debt collection agency who had sought out a debtor. He was claimed to have acted in a threatening manner and to have breached his duty of confidentiality. Finanstilsynet investigated the case, and determined that such a breach had been committed inasmuch as the debt collection agency representative had indicated to the debtor's

employer that he wished to speak with the debtor in connection with a debt collection matter. This clearly conflicts with good debt collection practice.

In light of the above case, Finanstilsynet issued a circular to debt collection agencies clarifying the guidelines to be followed when approaching debtors. The circular explains that debtors who are to be approached in person are entitled to written notification in advance. The duty of confidentiality must be safeguarded throughout the process to ensure that no unauthorised person receives information pertaining to the unsettled debt. The circular also draws attention to the debt collection agency manager's personal responsibility for ensuring that suitable persons are employed to approach debtors and that these persons receive the necessary training in good debt collection practice.

Chart 6: Number of debt collection cases received



Source: Finanstilsynet



SUPERVISION OF IT AND PAYMENT SYSTEMS

IT supervision covers financial institutions' use of information and communication technology (ICT) and is carried out in close cooperation with the respective supervisory departments at Finanstilsynet. IT supervision also covers payment systems, to ensure that payment services are performed in a sound, coordinated and rational manner and with acceptable risk. The regime includes checking that institutions operate in a satisfactory manner and in compliance with the ICT regulations and other rules.

TRENDS

Outsourcing

ICT services are delivered over a global telecommunications network, virtually without delay and at low cost. Globalisation enables the growth of large, resourceful and professional ICT environments. At the same time globalisation involves new risks, including concentration risk, particularly where large parts of the industry use the same supplier. In outsourcing, information about how the software works can be abused for financial gain, and this must be taken into account in the risk assessment. The same applies to access to customer data. Long distances can increase the risk of operational disruptions.

The use of ICT by financial institutions represents a significant cost, which is constantly under pressure. The offshoring of ICT tasks, i.e. outsourcing to another country, can provide a reduction in costs. The above factors in combination appear to have led to pressure to move ICT-related tasks to low-cost countries. By moving ICT tasks out of Norway, Norwegian banks are able to achieve cost reductions, but the process requires a good understanding and management of the risks involved on the part of the bank, ICT providers and the authorities.

Crime targeting online banking

Internet banking solutions play an important role in the transfer of payments and represent large transaction volumes and amounts. Financial services on the internet are persistently under attack from organised crime. This applies to online banking solutions and internet commerce. Attacks tend to come in waves, and there are long periods without attacks. After a long period without serious attacks

in Norway, in 2010 online banking solutions again came under attack. So-called trojans of the “Zeus” type were used. Attempts were initially stopped, but the financial sector must be prepared for new, more advanced attacks. Close cooperation between banks, industry organisations and authorities, both nationally and internationally, is preventive and helps to limit the consequences of attacks. No direct losses were recorded in 2010 as a result of this problem.

Crime targeting ATMs

In the period 2006–2009, there were, to Finanstilsynet’s knowledge, no serious skimming attacks, i.e. attacks involving the copying of the contents of the magnetic strip, on Norwegian ATMs. Criminal attacks using various types of skimming equipment were however carried out on self-service machines at petrol stations, but not to the same extent as on ATMs. In 2009, the solutions used by Norwegian merchants (EFT/POS) were exposed to serious skimming attacks. The attacks subsided after a series of measures were implemented, but still represented a direct loss to banks.

In 2010, ATMs were again exposed to serious attacks involving a technical solution that was sophisticated and evaded the anti-skimming measures that had been established. Through active collaboration between banks, industry organisations and authorities, the attacks were contained, but the banks suffered direct losses. Effective measures are being gradually introduced to stop this type of attack. Of the 2,180 ATMs installed in Norway, 42 were registered as being exposed to skimming or attempted skimming attacks in 2010.

SUPERVISION AND MONITORING

IT inspections

In 2010 Finanstilsynet conducted 26 IT inspections and inspections of payment service systems at banks, insurance companies, finance companies, securities institutions, at auditors and external accountants and at real estate agencies and debt collection agencies. Inspections were also carried out at ICT service providers under the ICT Regulations section 12 on the outsourcing of ICT operations. A further 31 simplified IT inspections were carried out as part of ordinary inspections and one auditor inspection involving scrutiny of the IT audit. Inspections focused particularly on institutions of national importance and were otherwise based on a risk assessment in which priority was given to electronic payment solutions, among other factors. Important issues in 2010 were:

- Absence of, or insufficient, risk and vulnerability (RAV) analyses. Shortage of competence needed to conduct risk and vulnerability analyses is a pervasive problem.
- Competence with regard to traditional mainframe solutions is about to be lost at the national and Nordic level. Those who currently operate and maintain these solutions are retiring, and young people are not acquiring these types of skills.
- Concentration risk with respect to IT service providers is substantial. This is particularly true of EDB Business Partner ASA where inspections have shown that all operations of mainframe-related IT services for banks in the Norwegian financial industry are carried out using the same physical machine. This is potentially detrimental.

- Problems still attend change management and the poor basis on which decisions to implement new solutions are taken, often the result of poor coordination between the specialist areas affected by the changes.
- Inadequate management and control of public infrastructure and infrastructure solutions. Competence in companies is weakened by outsourcing, and responsibilities for collaborative solutions are blurred.
- Outsourcing makes it hard to maintain adequate key competencies, particularly in areas that lack industry standards.
- Companies that are largely self-developed lack adequate process descriptions and documentation.
- Disaster recovery solutions are not checked or tested sufficiently.

Payment systems

The Payment Systems Act requires institutions under supervision to notify Finanstilsynet if they establish new payment systems or make changes to existing payment systems. The notification obligation is part of Finanstilsynet's risk surveillance. In 2010 Finanstilsynet received 18 such notifications. Most of the notifications were received subsequent to a questionnaire survey. Prior to the survey, the received notifications did not provide a sufficient basis on which to undertake an overall assessment of risk. A review and evaluation of individual payment service system functions has been initiated, also to ensure that they are subject to adequate management and control. Finanstilsynet works closely with Norges Bank in the payment systems field. This ensures reciprocal information and coordination in cases where this is expedient.

Crime targeting payment systems

Payment services are repeatedly exposed to attack by criminal groups. In 2010 both ATM and internet banking systems in Norway suffered. The heaviest losses arose however from crime targeting the use of

debit and credit cards outside the country. To be effective, measures must in the main be based on international cooperation, updated security requirements, enforcement of those requirements along with effective measures to stop skimming and hacking into collection centres for card transactions. It is important to give card owners guidance on careful card use.

Risk and vulnerability analysis (RAV)

Early in 2011, repeating previous practice, Finanstilsynet published an RAV analysis of ICT use in the financial sector in 2010. Based on in-house analyses and available data sources, Finanstilsynet has prioritised specific risk areas requiring further follow-up and concrete action. Finanstilsynet's RAV analysis for 2010 gives a detailed account.

The risk areas examined in the RAV analysis for 2010 are:

- Skimming attacks on ATMs
- Attacks on online banking solutions (the use of trojans, hacking and phishing)
- Inadequate testing and verification of disaster recovery solutions
- Inadequate management and control when outsourcing
- Lack of risk management with regard to offshoring
- Reduced quality of operations as a result of major organisational changes at IT suppliers

Event reporting

2010 was the first full year of event reporting to Finanstilsynet under the regulations requiring entities to report serious events. Companies are clearly making active use of information on such events in their effort to ensure sufficient quality and acceptable risk. Event report data are used in the RAV analysis and as a basis for addressing current issues directly with relevant companies. In 2010 the reporting was also utilised in the supervisory context. It provides Finanstilsynet with thoroughly prepared material, adding to the accuracy of

Finanstilsynet's statistics. Bilateral meetings and joint meetings are held with personnel responsible for financial institutions' reporting to ensure that the correct reporting level is used and to press home the importance of reporting. The most important problems that came to Finanstilsynet's attention through reports filed in 2010 were serious operational issues in the savings bank area and persistent tendencies for operational problems at the Norwegian Central Securities Depository (VPS).

Emergency preparedness

Efforts to assure adequate emergency preparedness in the ICT area in the financial sector continue through close cooperation with the Financial Infrastructure Crisis Preparedness Committee (BFI). By participating in disaster recovery exercises, Finanstilsynet has gained valuable competence in this area. A high level of cooperation exists with the Directorate for Civil Protection and Emergency Planning (DSB) and the Norwegian National Security Authority (NSM) in this area.

Cooperation

As part of the ICT security effort at financial institutions, Finanstilsynet participates in the Coordinating Body for Preventive Information Security (KIS) and the Financial Infrastructure Crisis Preparedness Committee (BFI). Finanstilsynet took over the role of secretariat to the BFI from Norges Bank in 2010. The cooperation established with Norges Bank in the payment systems area

is steadily improving, and is achieving good results. The National Security Authority, the Norwegian Post and Telecommunications Authority, the Data Inspectorate and trade organisations are also important partners for Finanstilsynet. Cooperation with the Data Inspectorate is particularly fruitful in the area of data integrity. Finanstilsynet participates in international IT supervisory cooperation through the Information Technology Supervisors Group (ITSG) and in groups working on international standardisation in banking and security and on electronic signatures.

In 2010 Finanstilsynet was invited to present its experience with ICT inspections on several occasions, including under the auspices of the European Supervisor Education Initiative – a collaboration between CESR, CEBS and CEIOPS. The aim was to review EU countries' supervision of financial institutions' ICT operations with a view to establishing a "best practice".

Finanstilsynet participates in an inter-European project focusing on internet security and notification (*Communication Middleware for Monitoring Financial Infrastructures*). The project, partly funded by the EU, will be brought to completion in 2011. It aims to arrive at pan-European measures enabling safer use of the internet in the financial sector. Finanstilsynet gave more than 40 external presentations on ICT and payment systems in 2010, largely in response to invitations from groups in Norway and elsewhere.

REGULATORY DEVELOPMENT

No changes were made to the ICT regulations or Payment Systems Act in 2010. However, a guide to the individual sections of the regulations and the law was drawn up.



INTERNATIONAL ACTIVITIES

The development and implementation of measures to strengthen the banking sector and prevent new financial crises was high on the agenda in 2010, with the leaders of the G20 countries, the IMF and the Financial Stability Board as driving forces. There is a global consensus on the need for macroprudential supervision and for international coordination of macroeconomic surveillance and measures related to financial stability. The Basel Committee on Banking Supervision has been concerned with developing new requirements for capital and liquidity, and the EU has adopted a new financial supervisory structure involving a European Systemic Risk Board and three new European Supervisory Authorities with greater power and competence than the previous committees.

GLOBAL MEASURES TO STRENGTHEN REGULATION AND SUPERVISION

The after effects of the financial crisis and economic problems in some European countries have dominated the international financial picture. Comprehensive international measures have been put in place to achieve better regulation and supervision in the financial sector.

To tackle the financial and economic crises, the G20 members have taken steps to strengthen international cooperation, and several summits have been held. G20 has developed common principles for reform of the financial markets and, in accordance with the G20 countries' Washington plan, the International Monetary Fund (IMF), in collaboration with the Financial Stability Board (FSB) and others, had a leading role in the work to learn from the financial crisis and suggest rule changes. In addition to expanding its lending activities, the IMF will improve its risk analyses, develop early warning exercises and revise programmes for the evaluation of various countries' financial sectors (FSAP). The G20 meeting in Korea in the autumn of 2010 supported the main features of the Basel Committee on Banking Supervision's proposed new capital and liquidity requirements (Basel III).

The Financial Stability Board (FSB), which was established through the conversion of the Financial Stability Forum in 2009 to promote international financial stability, was mandated to assess the vulnerability of the international financial system, propose changes in regulation and supervision on the basis of considerations for financial stability, monitor developments in the markets, evaluate the work of international standard setters, prepare guidance on supervisory cooperation, and collaborate with the IMF on an early warning system. The FSB has set up various expert committees and published a

number of reports and recommendations in the wake of the financial crisis, including on procyclicality, principles for remuneration in financial institutions, and strengthening the financial regulatory regime. In connection with the FSB's *Framework for strengthening adherence to international standards*, the FSB has started processes to encourage the implementation of international standards for regulation and supervision, and to ensure global consistency in approaches to regulation and supervision. The FSB will carry out peer reviews to measure how effectively countries implement standards. The first round of reviews dealt with recommendations regarding remuneration/incentive schemes.

Norway is not a member of G20 or the FSB, but follows this work closely as a member of the international supervisory organisations and EU committees.

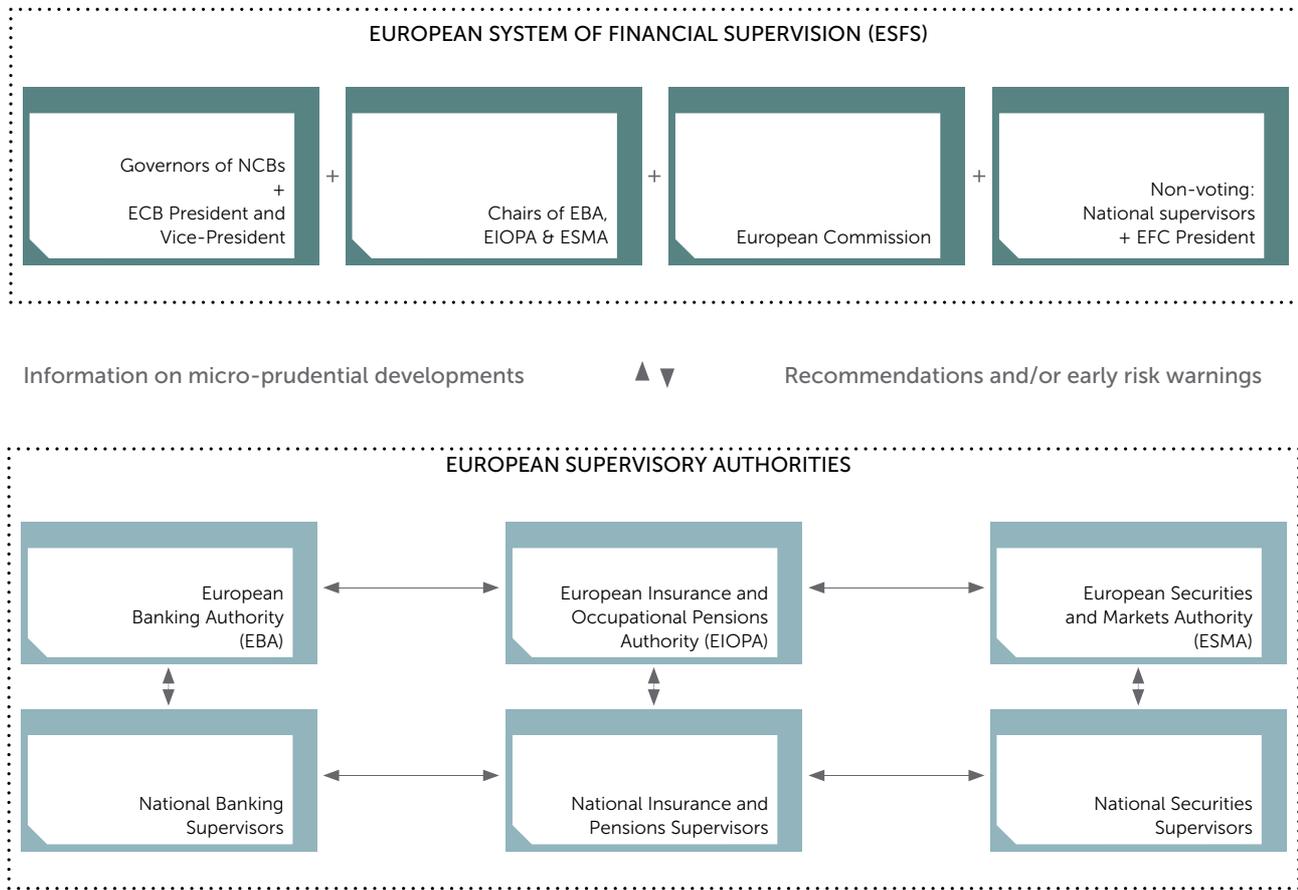
The financial crisis has focused attention on the importance of sound macroeconomic monitoring in the supervision of the financial sector. This has led to discussion about the distribution of responsibility between central banks and supervisory authorities in monitoring the financial markets. While a distinction is made between macroprudential supervision and microprudential supervision (supervision of individual institutions), emphasis is given to the need for increased cooperation between central banks, which are traditionally responsible for the macro economy, and the supervisory authorities, which in many other countries have traditionally given little emphasis to macroeconomic surveillance. This need for coordination and cooperation is taken into account in the new EU supervisory structure.

REFORM OF EU SUPERVISORY STRUCTURE – NEW EUROPEAN REGULATORY BODIES

In the wake of the financial crisis, it was decided that the supervisory structure in Europe should be strengthened, and in February 2009 a group led by Jacques de Larosière presented recommendations for the reorganisation of financial sector supervision in the EU. The report contained proposals for reorganisation of the supervision of financial institutions and markets in the EU, strengthening European cooperation on monitoring financial stability, early warning, crisis management, and making global supervisory cooperation more effective and efficient. In November 2010, EU institutions adopted a new supervisory system, which was established on 1 January 2011.

The new structure of financial supervision in the EU (the European System of Financial Supervision – ESFS) includes the European Systemic Risk Board (ESRB), which has overall responsibility for macroeconomic monitoring of systemic risk (macroprudential oversight), three European regulatory bodies (European Supervisory Authorities – ESAs) that will have the overall responsibility for coordinating financial supervision in the EU (micro-prudential supervision), and the national supervisory authorities; see the chart on page 100. The ESFS aims to promote financial stability, ensure confidence in the financial system, and ensure adequate protection for users of financial services.

Chart 7: The new EU supervisory structure



European Systemic Risk Board

The European Systemic Risk Board (ESRB) has overall responsibility for macroeconomic monitoring of the financial system in the EU, and will help to ensure that risk build-up in the financial system does not threaten financial stability. To this end the ESRB will analyse macroeconomic trends, identify systemic risks, issue warnings when risk is considered to be substantial, and recommend measures. This will be done in close cooperation with the supervisory bodies.

The ESRB includes representatives from the national central banks, the European Central Bank (ECB), the chairs of the new supervisory authorities, and representatives from the European Commission. Representatives of national supervisory bodies participate as observers, and the ECB acts as secretariat to the ESRB. The technical work is largely performed by an expert group under the ESRB, the Advisory Technical Committee.

The ESRB keeps the European supervisory authorities (ESAs) informed of developments affecting systemic risk and issues recommendations and warnings. The ESRB can also provide advice to the European Commission if it considers there is a need for new legislation or regulatory changes to ensure stability in the market. Recipients of recommendations or warnings from the ESRB will be expected to take the necessary measures and inform the ESRB accordingly. If recommendations or warnings are not acted on, an explanation will be required. The ESRB may decide that the recommendations and warnings should be made public, and they will be reported annually to the European Parliament and the Council of Ministers.

EEA/EFTA countries will be entitled to participate in ESRB Board meetings on an ad hoc basis when matters of particular relevance are discussed. The Regulation requires a plan to be prepared to enable EEA/EFTA to participate in the work of the ESRB on an ad hoc basis,

but there is still uncertainty surrounding both the way forward and the specifics. Norway was not invited to attend the first meeting on 20 January 2011.

European Supervisory Authorities (ESAs)

The new European supervisory authorities, EBA, EIOPA and ESMA¹ are replacing CEBS, CEIOPS and CESR². They have secretariats in London, Frankfurt and Paris respectively. The Board of Supervisors of each ESA comprises a chair, the heads of the national supervisory authorities, a commission representative, an ECB representative, an ESRB representative and a representative from each of the other ESAs. In addition, representatives from national central banks without supervisory responsibility participate in the EBA. The Management Board comprises a chair and six other members from the Board of Supervisors. The Board of Supervisors and Management Board meet at least five times a year. The Chair and Executive Director are full-time employees and independent specialists, and will be appointed for a term of five years.

The ESAs will protect public interests by promoting a stable and efficient financial system and ensuring well-functioning financial markets, undertaking economic analyses of markets and, together with the ESRB, developing criteria and common quantitative and qualitative indicators to identify and measure systemic risk.

The ESAs will draft technical standards for adoption by the Commission as legislative acts. The ESAs may adopt guidelines and recommendations relating to national supervisory authorities or financial institutions, and are empowered to apply individual decisions at national supervisory authorities or financial institutions if guidelines or recommendations are not observed. The primary responsibility for day-to-day supervision remains with the national supervisory authorities.

The ESAs will oversee that national authorities implement legislative acts, guidelines and recommendations, identify supervisory best practice and ensure coordination of supervisory activities. They will mediate in disputes between supervisory authorities and work to

prevent regulatory arbitrage. They will in addition promote protection of investors and depositors and a level playing field.

In the event of violations or suspected violations of legislative acts, including technical standards, the ESAs will conduct necessary investigations and recommend appropriate measures. With a basis in legislative acts, the ESAs can direct individual decisions at financial institutions in cases where national authorities fail to fulfil their obligations.

Colleges of Supervisors have been established or will be established for each cross-border financial institution, and the ESAs are entitled to participate in these supervisory colleges. The ESAs can initiate stress tests, and will ensure consistent implementation of stress testing methods. They can make recommendations to the supervisory authorities in a college, draw up standards for the college, require the home-country supervisory authority to convene a meeting of the college, and take on the role of mediator. In the event of disagreement between supervisory authorities in cross-border situations, the ESAs can assist the authorities in reaching an agreement. If no agreement is reached, an ESA can impose measures that are binding on the authorities in question. If such an order is not complied with, the ESA can take action against the financial institution concerned.

In crisis situations the ESAs will facilitate and coordinate measures from the respective national authorities. An ESA will also be entitled to attend relevant meetings with national authorities.

In 2010, Finanstilsynet engaged in work to further secure observer status in the new European supervisory authorities, and ensure a smooth transition to the new structure. EEA/EFTA countries are in principle not entitled to participate in discussions on individual institutions unless the discussions are of direct relevance to them. In practice this means that Finanstilsynet can still attend all meetings and relevant supervisory colleges, and that Finanstilsynet will continue to participate in the new European supervisory bodies as actively as before. Finanstilsynet will continue to chair two or so sub-committees under CEIOPS (EIOPA) and CESR (ESMA).

¹ The European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority

² The Committee of European Banking Supervisors, the Committee of European Insurance and Occupational Pensions Supervisors and the Committee of European Securities Regulators

INCREASED FOCUS ON CONSUMER PROTECTION

Since the financial crisis more emphasis has been given to consumer information and consumer protection. In the final phase of negotiations on the establishment of the new European Supervisory Authorities, there was agreement on the need to clearly profile the supervisory authorities' responsibility towards consumers. The ESAs must ensure that the market for financial products and services is transparent, simple and fair for consumers, by collecting and analysing data on consumer trends, evaluating and coordinating national

authorities' educational and information measures related to the financial market, developing training standards for the industry, and contributing to common information standards.

The ESAs will set up a Committee on Financial Innovation to assure a consistent approach to the regulation and supervision of new products and services. The ESAs may temporarily prohibit a financial activity that threatens a well-functioning and stable market.

SECURITIES MARKET

Finanstilsynet is a member of the International Organization of Securities Commissions (IOSCO) and participates in the European Regional Committee and IOSCO Commodity Futures Task Force. IOSCO has developed a multilateral agreement (Multilateral Memorandum of Understanding - MMoU) for cross-border cooperation and information exchange to which Finanstilsynet acceded in 2006.

Finanstilsynet attends meetings of the Enlarged Contact Group on Supervision of Collective Investment Funds. The group is a global forum for supervisory authorities overseeing securities funds. The main purpose of the group is to exchange experience and information related to the supervision of securities funds.

At the EU/EEA level, Finanstilsynet has been a member of the CESR (Committee of European Securities Regulators) which has served as an advisory committee to the European Securities Committee and the European Commission and has worked for consistent follow-up and enforcement of community laws in member countries. As from 1 January 2011 the CESR was replaced by the ESMA, the European Securities and Markets Authority. In 2010 Finanstilsynet was given the task of hiring a working group in the CESR to give the EU Commission practical advice regarding the possible introduction of a requirement that listed companies should report transactions/activity on a country by country basis, which could prove a great strain on companies. The issue is largely politically motivated, and could receive significant attention ahead. The work continues under ESMA auspices from 2011 onwards.

BANKS AND FINANCIAL INSTITUTIONS

The Basel Committee on Banking Supervision, under the Bank for International Settlements (BIS), sets international standards for banking supervision and coordinates global collaboration on banking supervision. Norway is not a member of the Basel Committee, but Finanstilsynet has become more closely connected to the Basel Committee through being invited to participate in the Basel Consultative Group in 2010. Finanstilsynet attended the Basel Committee's International Conference of Banking Supervisors (ICBS) in Singapore. The Basel Committee was active in reforming the regulatory framework for banks in 2010, and introduced stricter capital and liquidity requirements. See a summary of the proposals in the *Banking and finance* chapter, pages 42–43).

Finanstilsynet has attended meetings of the Banking Supervision Committee (BSC) as an observer. The BSC will be replaced by the Advisory Technical Committee under the new European Systemic Risk Board, ESRB, and held its last meeting in November 2010. Together with Norges Bank, Finanstilsynet also has annual bilateral meetings with representatives from the ECB.

Finanstilsynet has played an active role at meetings of the Committee of European Banking Supervisors (CEBS), and in most of the committee's subgroups, including the Groupe de Contact, which is CEBS' most important technical subcommittee. Finanstilsynet will continue to actively engage with the new European Banking Authority (EBA).

INSURANCE AND PENSIONS

Finanstilsynet is a member of the International Association of Insurance Supervisors (IAIS) and plays a part in developing international principles for the supervision of insurance activities. Finanstilsynet attends the IAIS annual conference and is represented on the technical committee, which has overall responsibility for standard setting. The IAIS held its 17th annual conference in Dubai in October 2010, and the annual meeting adopted several new standards and guidelines.

Finanstilsynet is also a member of the International Organization of Pensions Supervisors (IOPS), and attended the IOPS annual conference in 2010. IOPS develops standards for the regulation and supervision of private pensions.

At the EU/EEA level, Finanstilsynet attended meetings of the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS). Finanstilsynet also participates in most of the committees and working groups under CEIOPS, and will continue to participate actively in EIOPA, the new European Insurance and Occupational Pensions Authority.

Finanstilsynet has chaired a subcommittee under CEIOPS, the Task Force on Insurance Guarantee Schemes (TF-IGS), which in 2009 prepared a report and draft of recommendations regarding possible future harmonisation of insurance guarantee schemes in the EU which CEIOPS presented to the European Commission. The work continues under the auspices of EIOPA.

ACCOUNTING AND AUDITING

Finanstilsynet is a member of the International Forum of Independent Audit Regulators (IFIAR), which was set up in 2006. IFIAR's mission is to promote cooperation and coordination between countries on the regulation and supervision of auditors. In addition to providing a forum for contact between supervisory authorities in various countries, IFIAR promotes the sharing of knowledge about the industry, practical regulatory and supervisory experience, and other matters. Finanstilsynet participates in arranging IFIAR Inspection Workshops. The Director of accounting and auditing supervision at Finanstilsynet is a member of IFIAR's Advisory Council, which acts as IFIAR's Board.

Norwegian auditing firms that are involved in the auditing of issuers listed on a stock exchange in the US must be registered with the Public Company Accounting Oversight Board (PCAOB). Finanstilsynet attaches importance to good supervisory collaboration with the PCAOB.

Together with the Ministry of Finance, Finanstilsynet attends meetings of the EU Accounting Regulatory Committee (ARC) which assesses

the International Financial Reporting Standards (IFRS) and how these should be implemented in the EU. Finanstilsynet has played an active role in the European Enforcers Coordination Sessions (EECS) under the CESR (now ESMA), which harmonise and coordinate decisions on the enforcement of IFRS in the European Economic Area. The group holds regular meetings with the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC), which are, respectively, a standards setting agency and an interpretation agency, to ensure that IFRS standards are enforced in the same way throughout the EEA.

Finanstilsynet actively participates in EU efforts to develop rules and standards for auditors in the area of supervisory cooperation, including as adviser to the Ministry of Finance through the Audit Regulatory Committee (AuRC). Finanstilsynet is a member of the European Group of Auditors' Oversight Bodies (EGAOB), headed by the EU Commission. Finanstilsynet also attends meetings of several EGAOB subgroups, including the subgroup on inspections, subgroup on third countries, sub-group on intra-EU/EEA cooperation, and subgroup on ISAs.

IT SUPERVISION

Finanstilsynet participates in a number of international bodies as part of its ICT security effort. These include the Nordic IT supervisory cooperation, international IT supervisory cooperation through the Information Technology Supervisors Group (ITSG), which also has a European subgroup, groups on international standardisation in banking and security, on electronic signatures (ETSI ESI), and in the IT security

working group under the International Federation for Information Processing (IFIP). Finanstilsynet is the Norwegian representative in the European Security Research and Innovation Forum (ESRIF), an EU body that works with security. Finanstilsynet also participates in an EU-supported project to develop measures that can improve the ability to detect and respond to security incidents on the internet.

COMBATING MONEY LAUNDERING AND TERRORIST FINANCING

Finanstilsynet plays a part in developing national and international measures against money laundering and terrorist financing. It attends meetings of the Financial Action Task Force (FATF), which develops

international standards for measures to combat money laundering and terror financing, and participates in the FATF Terrorist Financing Working Group, which collaborates with the UN in this field.

EFTA COOPERATION

Finanstilsynet has for several years chaired EFTA's Working Group on Financial Services, and participates in EFTA's Working Group on Company Law. The remit of these working groups – which operate under EFTA's Subcommittee II in the EFTA pillar within the EEA structure – is to coordinate viewpoints and to incorporate into the EEA agreement legislative acts in the financial sector and in the areas of capital movements and company law (including accounting and auditing). The working groups are also useful forums for obtaining updates on legislative developments in the EU. At each meeting,

representatives of the European Commission or other EU institutions are invited to give presentations on a variety of measures and to give updates on the decision-making process in the European Council and the European Parliament. In the summer of 2010, Finanstilsynet, together with the Ministry of Finance and Norges Bank, hosted a seminar organised by the EFTA's WG Financial Services, where the main themes were the changes in banking regulations, crisis management and the new EU supervisory structure.

NORDIC-BALTIC COOPERATION

Nordic cooperation remains a high priority, and Finanstilsynet attaches importance to good dialogue, both formal and informal, with its Nordic colleagues. The Nordic supervisory authorities have signed a joint cooperation agreement, and Finanstilsynet has also signed individual cooperation agreements on the supervision of particular financial groups. In addition to the annual meeting of the Nordic supervisory authorities at director general level, which in 2010 was held in Finland, ad hoc meetings and meetings in the various sectors and in the administrative area were also held.

The Nordic countries also cooperate closely with the Baltic countries. In 2010, a cooperation agreement was signed between the Nordic and Baltic countries with a view to preventing, managing and resolving any problems in banks with activities spanning two or more of these countries. A Nordic-Baltic cross-border stability group has been set up, drawing representatives from the supervisory authorities, central banks and finance ministries in the respective countries, who

meet at least once a year. The Nordic-Baltic cooperation agreement is a regional enlargement of the cooperation agreement between the authorities of EEA Member States regarding coordination and cooperation in managing cross-border financial crises, to which Norway acceded in July 2010. Nordic-Baltic cooperation on financial stability in the region has been similarly developed between central banks and supervisory authorities.

There was more frequent contact between the Nordic supervisory authorities and central bank leaders in 2010 than previously, partly to prepare for issues related to cross-border activities, and partly to coordinate the implementation of new rules. Coordination with a view to participation in the ESRB will be a further theme for this cooperation ahead. In 2010 Finanstilsynet assisted the Icelandic supervisory authorities through presentations and seminars offered to the Board, management and other supervisory staff in Iceland.

Since 2005 regular meetings have also been held between the audit supervisory authorities in Sweden, Denmark, Finland and Norway. The meetings showed that closer contact and cooperation are also

useful in the auditing area, not least in order to exchange experiences and discuss issues regarding interpretation and follow-up of the EU Statutory Audit Directive.

OTHER MEETINGS AND BILATERAL COOPERATION

Finanstilsynet attends meetings of the OECD Insurance Committee and the OECD Capital Markets Committee on a regular basis, in addition to a number of other meetings under OECD auspices. Finanstilsynet also sends a representative to meetings of the UN-coordinated Project Link, a macroeconomic research project.

Finanstilsynet has annual contact meetings with representatives from the Federal Reserve Bank and the European Central Bank. Finanstilsynet also receives an annual visit from the International Monetary Fund (IMF), and in 2010 was visited by Chinese, Korean and Russian delegations. In 2010 Finanstilsynet gave a presentation at a seminar for Caribbean supervisory authorities, and organised a seminar in Bulgaria.

Although much international supervisory cooperation takes place under the auspices of international organisations and in EU committees and working groups, Finanstilsynet continues to attach importance to good bilateral collaboration with relevant supervisory authorities. Finanstilsynet has signed bilateral MoUs to facilitate information exchange with other supervisory authorities. The MoUs are designed to strengthen cooperation between Finanstilsynet and the respective parties. Multilateral MoUs are in effect between all EEA countries in the insurance, pensions and securities fields, and Finanstilsynet has also acceded to IOSCO's multilateral MoU for securities market supervision.

During the drafting of the new Finanstilsynet strategy in 2010, it was decided that the Authority should visit international organisations and other supervisory authorities to gauge their assessment of developments in the markets and in financial sector regulation and supervision in the light of the financial crisis. In 2010 meetings were held with the supervisory authorities in Finland, Switzerland and Canada, and Finanstilsynet visited the Basel Committee and the Financial Stability Board.

Chart 8: International meetings attended by Finanstilsynet

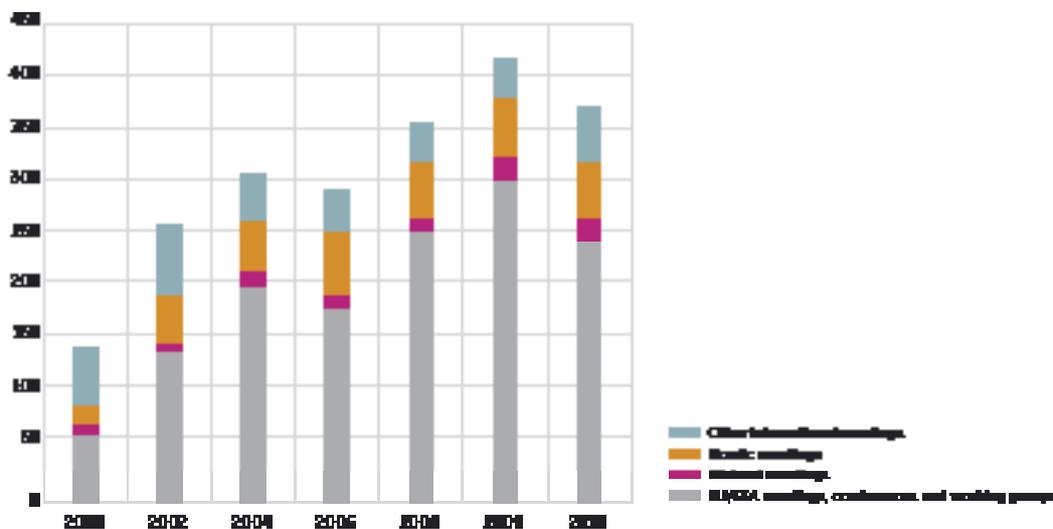


Table 16: International organisations and EU/EEA related committees in which Finanstilsynet participates

Cross-sectoral meetings

- Integrated Financial Supervisors Conference, held annually
- European Financial Conglomerates Committee (EFCC) – Level 2
- Joint Committee (previously the Joint Committee on Financial Conglomerates, JCFC)
- Nordic supervisory meetings
- Various cross-sectoral working groups under the EU supervisory bodies
- Project Link, the UN's annual macroeconomic meeting
- Nordic-Baltic Cross-Border Stability Group

Banking/finance

- International Conference of Banking Supervisors (ICBS), arranged by the Basel Committee every two years
- OECD's Financial Markets Committee
- European Banking Committee (EBC) – Level 2 – and various working groups under the EU Commission and the EBC
- European Banking Authority (EBA) – previously the Committee of European Banking Supervisors (CEBS) and subordinate committees and working groups – www.eba.europa.eu
- Banking Supervision Committee (BSC) under the European Central Bank (ECB), now replaced by the Advisory Technical Committee under the European Systemic Risk Board (ESRB)
- Nordic meetings on banking supervision and financial stability

Insurance

- International Association of Insurance Supervisors (IAIS) – www.iaisweb.org
- International Organisation of Pension Supervisors (IOPS) – www.iopsweb.org
- OECD's Insurance Committee
- European Insurance and Occupational Pensions Committee (EIOPC) – Level 2 – and various working groups under EIOPC and the EU Commission
- European Insurance and Occupational Pensions Authority (EIOPA) – previously the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS), with subordinate committees and working groups – www.eiopa.europa.eu
- Nordic supervisory meetings for insurance

Securities

- International Organization of Securities Commissions (IOSCO) – www.iosco.org
- Enlarged Contact Group on Supervision of Collective Investment Funds (ECG)
- European Securities Committee (ESC) – Level 2
- European Securities and Markets Authority (ESMA) – previously the Committee of European Securities Regulators (CESR), with subordinate committees and working groups – www.esma.europa.eu
- Nordic supervisory meetings for securities

Accounting and auditing

- International Forum of Independent Audit Regulators (IFIAR) – www.ifiar.org
- Accounting Regulatory Committee (ARC)
- Accounting Contact Committee
- Audit Regulatory Committee (AuRC)
- European Group of Auditors' Oversight Bodies (EAOB), with several subcommittees and working groups
- Nordic meetings

Money laundering and terror financing

- Financial Action Task Force (FATF) – the international forum for measures against money laundering and the financing of terrorism, with its secretariat in the OECD – www.fatf-gafi.org
- Committee on the Prevention of Money Laundering and Terror Financing (CPMLTF)
- Nordic meetings

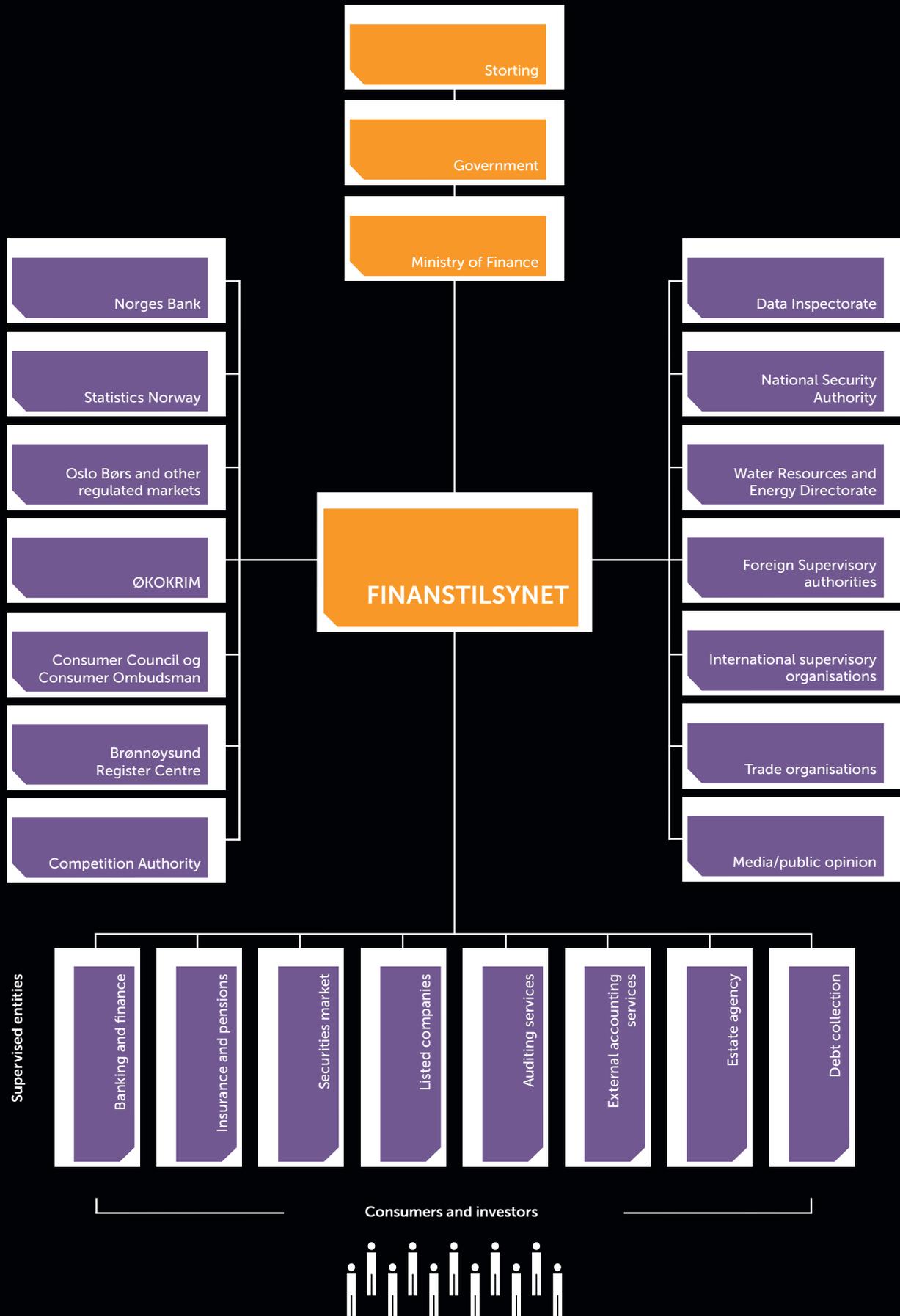
ICT supervision

- European Security Research and Innovation Forum (ESRIF)
- Information Technology Supervision Group (ITSG)
- Nordic supervisory meetings for IT
- Security working group under the International Federation for Information Processing (IFIP)
- ETSI ESI – Groups working on international standardisation in banking and security and on the standardisation of electronic signatures
- Communication Middleware for Monitoring Financial Infrastructures (CoMiFin) – a European collaborative network under the EU's seventh framework programme

EFTA

- EFTA Working Group on Financial Services
- EFTA Working Group on Company Law (also covers accounting and auditing)

FINANSTILSYNET'S KEY RELATIONS



RISK OUTLOOK 2011: THE FINANCIAL MARKET IN NORWAY

Since 1994 Finanstilsynet (Kredittilsynet) has systematically analysed and assessed potential stability problems in the Norwegian financial market against the background of developments in the Norwegian and international economy. This is a necessary supplement to Finanstilsynet's ongoing supervision of individual institutions. Much of the assessment of individual institutions' profitability and financial strength needs to be carried out in light of the general state of the financial market. As from 2003 Finanstilsynet has given its view of the state of the financial market in a separate report. The report summarises financial institutions' results for the previous year, and assesses risks facing banks and other institutions in the Norwegian financial market and potential sources of future stability problems in the Norwegian financial system. As from 2011 Finanstilsynet publishes the reports "Risk Outlook" in the spring and "Financial Trends" in the autumn.

The report is available in electronic form at www.finanstilsynet.no.

The printed version can be ordered from Finanstilsynet.

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