

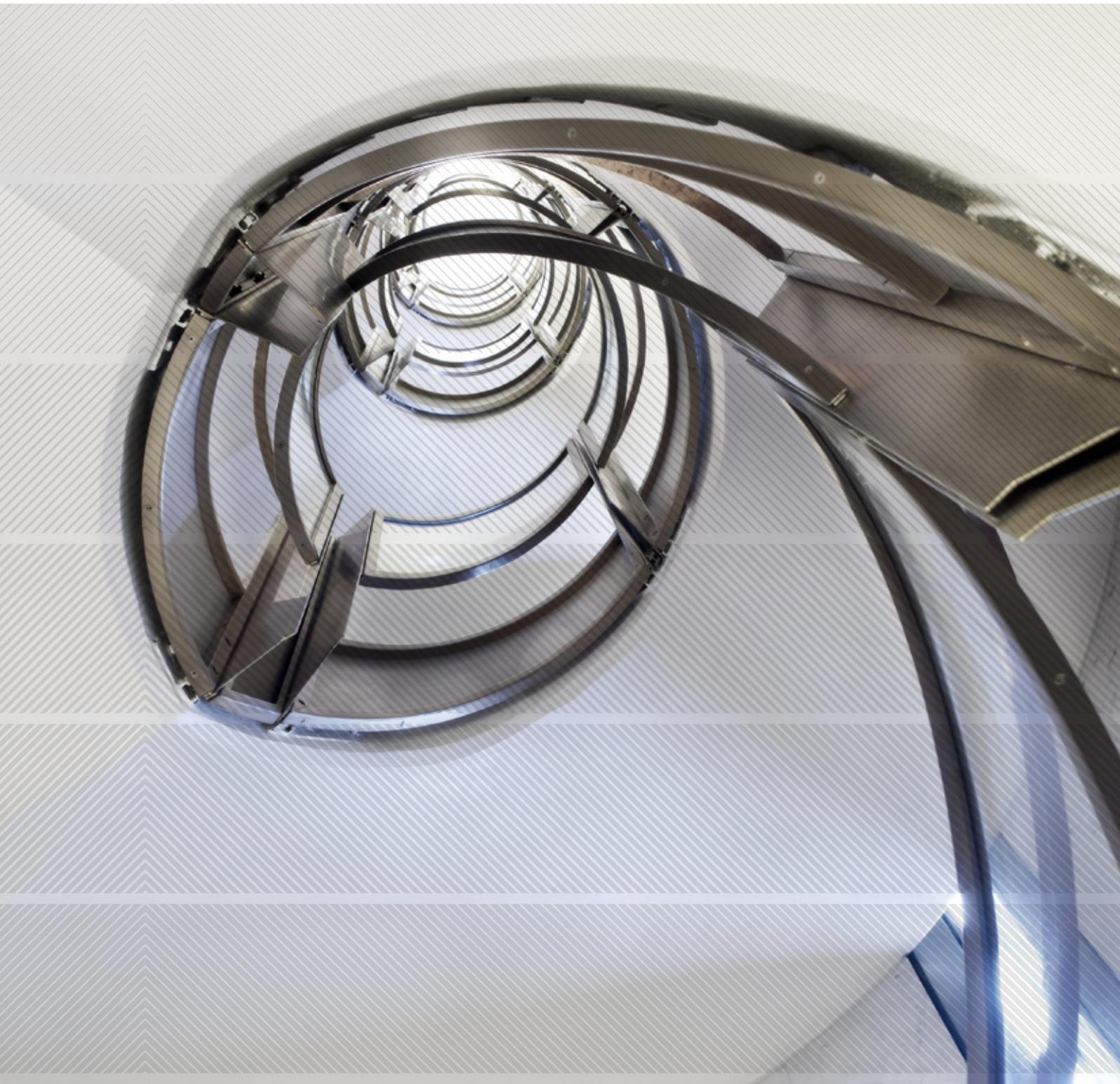


FINANSTILSYNET

THE FINANCIAL SUPERVISORY
AUTHORITY OF NORWAY

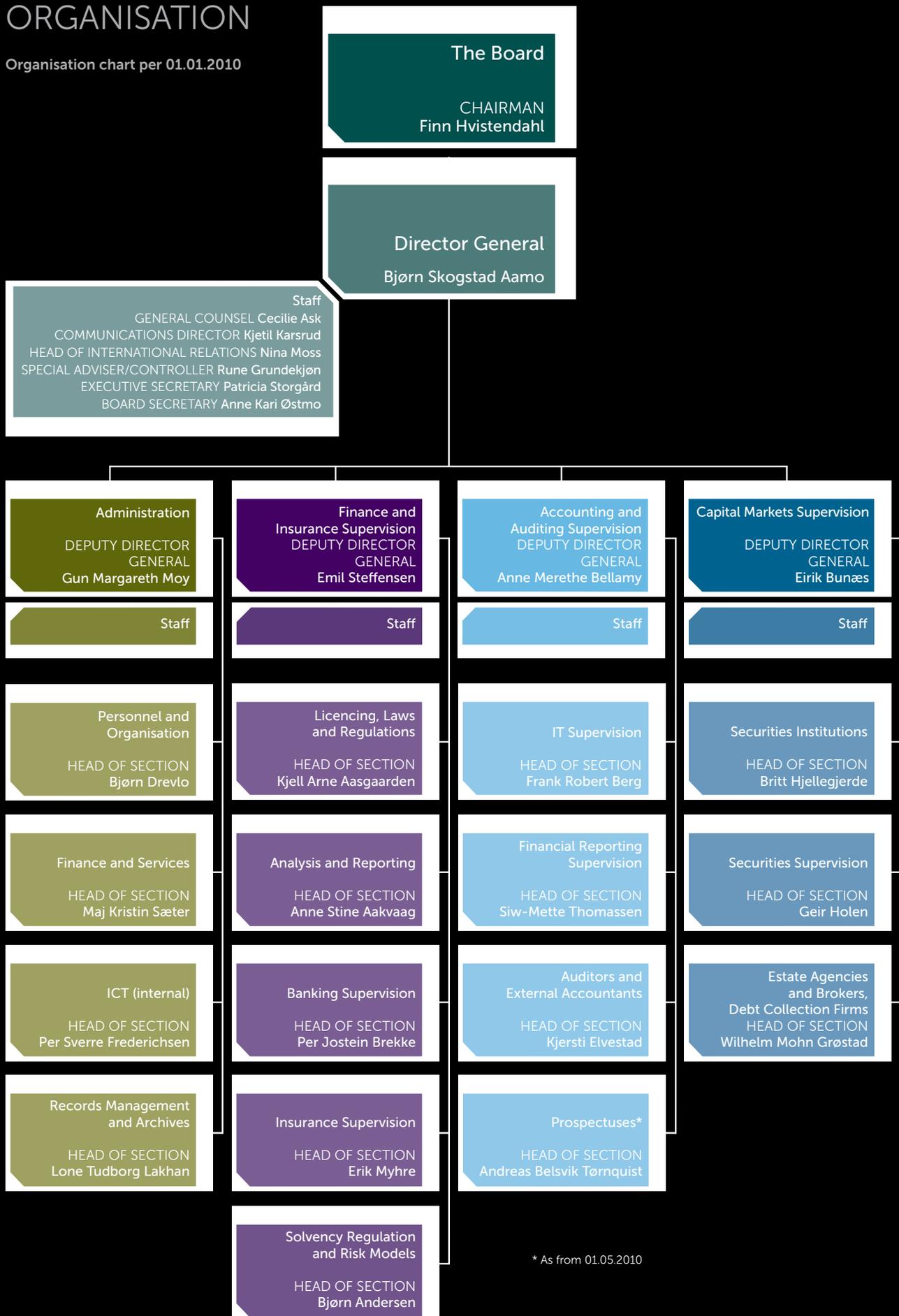
ANNUAL REPORT

2009



FINANSTILSYNET'S ORGANISATION

Organisation chart per 01.01.2010



* As from 01.05.2010

Finanstilsynet is responsible for the supervision of banks, finance companies, mortgage companies, e-money 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 listed companies' financial reporting and conduct in the securities market.

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"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)

EDITORIAL NOTE:

Kredittilsynet changed name to Finanstilsynet on 21 September 2009. Hence the annual report for 2009 largely covers activities performed under the old name. To simplify matters for the reader, the name Finanstilsynet is used throughout this annual report.

The photos show Finanstilsynet's new premises at No. 3 Revierstredet in Oslo. The premises are part of Norges Bank's building complex.
Architect: Lund + Slatto Arkitekter



PREFACE

Again in 2009, the supervisory effort was coloured by impact of the financial crisis. International markets for bank loans dried up after Lehman's demise in September 2008. Much of Norwegian banks' supply of liquidity ceased, and the banks became unsure of their ability to maintain normal lending. The establishment of a swap arrangement for bonds combined with easier borrowing from Norges Bank rapidly improved the supply of liquidity. Finanstilsynet played its part by rapidly processing licence applications for 16 new mortgage companies for covered bonds and by intensifying supervisory oversight of bank liquidity.

As from early 2009 the issue of banks' equity capital was at centre stage. 6–7 per cent tier 1 capital had sufficed for Norwegian banks to obtain funding in international markets. Heavy losses and fears of new bank losses in many countries now prompted the markets to impose stricter requirements than the supervisory authorities. A Tier 1 capital ratio of 9–10 per cent was soon considered necessary for banks intending to borrow in the markets.

It was at the same time difficult and expensive for banks to obtain fresh capital in the private markets. In most western countries the state was compelled to devise arrangements to supply such capital. With the creation of the Norwegian State Finance Fund, Norwegian banks could secure their equity capital position without having to tighten lending. Finanstilsynet was instrumental in framing relevant rules and in the Fund's practical activity.

It is now widely recognised that the international capital adequacy regime (Basel II) implemented in 2007 has significant shortcomings. Equity capital able to absorb loss has been too low. The capital requirements, together with the accounting rules, have probably boosted lending growth in good times and restrained it in bad times. Extensive regulatory work is now being undertaken that will result in new, better and more stringent international rules in the course of the coming two years or so. Finanstilsynet supports this effort through active participation in the Committee of European Banking Supervisors (CEBS) and is preparing new rules in Norway on this basis. The agency has taken the initiative for Nordic coordination of the rules.

The Basel II framework has also brought improvements. In order to use internal models to compute capital needs, Norwegian banks have built up internal risk assessment and control systems of a significantly higher standard than previously. This has also impacted on the standard of risk assessment in banks which do not use internal models.

Basel II requires banks and financial supervisors to assess risk and capital needs on an individual basis (the Pillar 2 process). In 2008 Finanstilsynet closely reviewed all banks' own assessments. Many were asked to raise their capital adequacy targets, and a fair number were asked to consider concrete steps to bolster their actual capital levels. In 2009 more than a hundred institutions had to submit documentation to show that targets had been raised and concrete steps taken. Dialogue was particularly close with banks that had been asked to raise their actual capital levels. A letter citing Finanstilsynet's power to issue administrative orders was circulated to 15 banks.

The banks significantly bolstered their capital levels in 2009 through profit retention and stock market issues. The State Finance Fund was also important for a number of mid-size and small banks. No orders on the part of Finanstilsynet were necessary.

At the start of 2010, capital ratio levels among Norwegian banks are viewed as satisfactory by Finanstilsynet. Thanks to limited losses and the good quality of Norwegian banks' regulatory capital, there has been no solvency crisis in Norway. Through its ongoing contact with the banks, Finanstilsynet noted a rapid normalisation of credit to households and residential purposes. For firms a gradual normalisation was seen, combined with a marked increase in risk margins. In the second half of 2009 stiffer competition in the corporate market, as in the retail market, caused margins to subside somewhat.

The financial crisis produced a sharp fall in share prices in the course of 2008. However, trading and settlement functioned well, so that liquidity and pricing were satisfactory. Finanstilsynet kept a close eye on the clearing and settlement systems in light of the problems related to Lehman's demise. The Norwegian stock market recovered strongly in 2009, with a large increase in stock values and a substantial issue volume.

The crisis contributed to poor returns and reduced buffer capital for Norwegian life insurers in 2008. Companies reduced their aggregate shareholding from 23 per cent at the end of 2007 to 12 per cent at the end of 2008. Hence, although returns in 2009 were significantly higher than the previous year, life insurers and their customers benefited little from the stock market recovery in 2009. In Finanstilsynet's view, changes in the rules to promote better, longer-term management and higher return need to be considered.

The financial crisis and its consequences were in focus in 2009. As this annual report shows, Finanstilsynet also performed its tasks in fields that were little affected by the crisis. Operational risk in ICT systems was closely monitored, in part through the new event reporting system. Suspicions of insider trading and market manipulation were actively followed up, and fewer major cases were noted than in previous years. The new estate agency act was followed by new licence awards, and problems at individual firms were handled without problems of note for their clients.

The real economic effects of the financial crisis are not over. The phasing out of the wide-ranging fiscal and monetary policy support measures in many countries leaves much uncertainty about the trend in the international economy. The banks must expect substantial losses on loans to firms in 2010 as previously, especially to firms that are dependent on international markets. For the individual institution and for Finanstilsynet it is important to monitor risks closely. Through the Pillar 2 process the agency will secure and further strengthen capital levels in the banking system, partly with a view to higher international requirements for the years ahead. It will be important to bring about a more robust liquidity supply for Norwegian banks on a lasting basis.

Household debt is at an all-time high, and still growing. The very low interest rates resulting from the financial crisis have made the debt easier to bear in the short term. For households and the financial system alike it is important to curb the risk by ensuring that residential loans are not unreasonably large – either in relation to property value or households' ability to pay when interest rates in due course are normalised.

Shortcomings in regulation and supervision were a major cause of the financial crisis in many countries. Imbalances in the international economy and low interest rates also contributed to the scale of the crisis. Countries where the bulk of financial risk resided in banks with good banking practices and under sound supervision incurred smaller losses and smaller problems than countries where this was not the case.

The organisation of public supervision of the financial industry has been discussed in many countries in the aftermath of the crisis. In some countries the absence of a holistic supervision has made for an incomplete overview of aggregate risk in the financial sector. The Norwegian model, which integrates supervision of all types of enterprises in a single financial supervisory body, has proven appropriate to our circumstances.

Much analysis and much discussion remain before a complete picture is gained of the lessons to be learned from the international financial crisis. In Norway the Financial Crisis Committee can make an important contribution. For its part, Finanstilsynet contributes to the work of the Committee, international supervisory bodies (and inter alia through the *Risk Outlook Report*) in order to provide the best possible basis for future rules and supervision.

At the same time as we learn from our own and others' problems in the financial markets, it is important to retain imagination and vigilance. The next financial crisis may well arise in other areas and in other ways than was seen this time round. For Finanstilsynet, further developing our organisation is the best way to prepare for and withstand new crises. Capable, motivated staff possessing broad insight and experience are a good basis on which to meet the challenges facing Finanstilsynet in the years ahead.

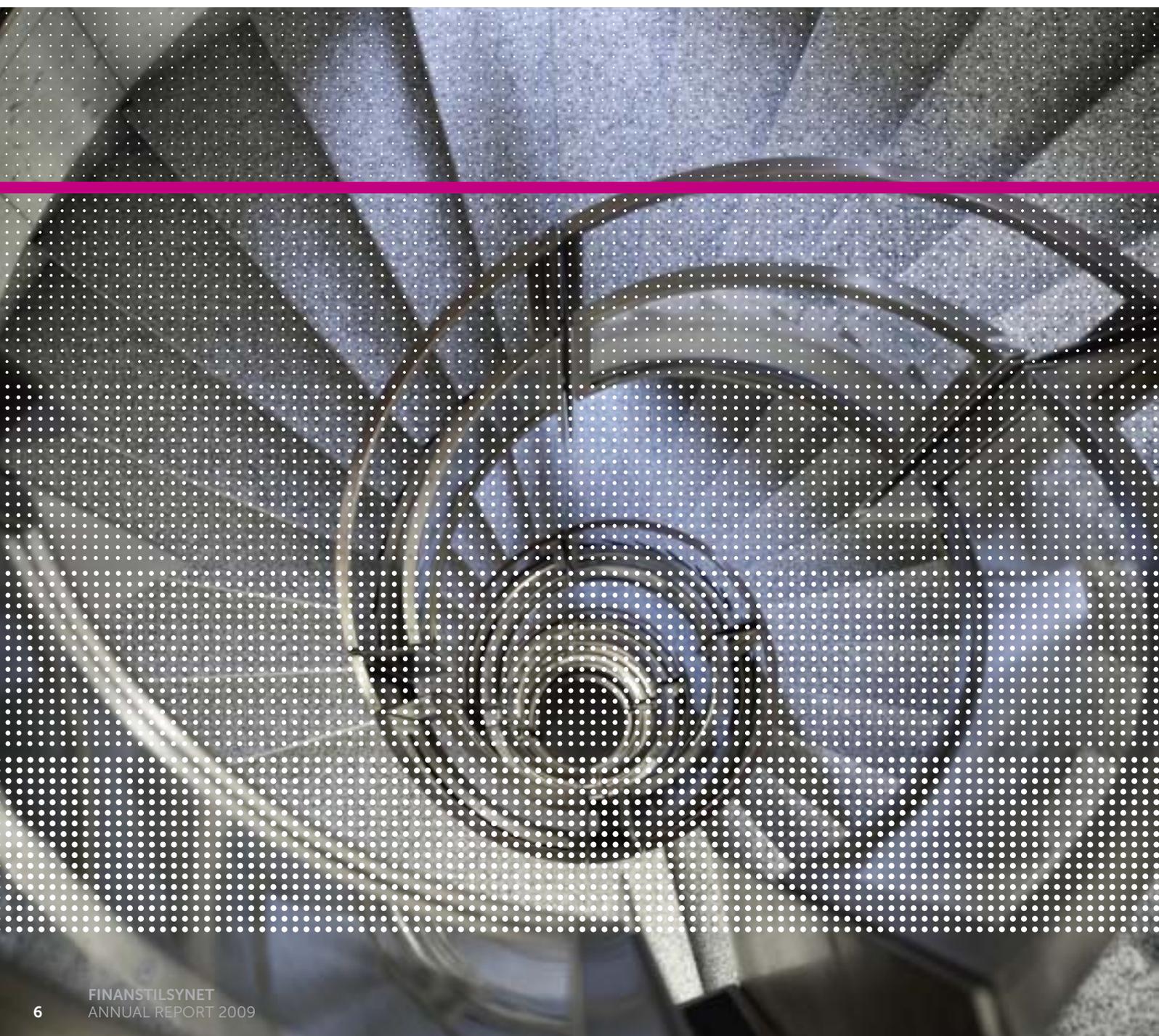
Oslo, 20 January 2010


Finn Hvistendahl
Chairman


Bjørn Skogstad Aamo
Director General



IMPORTANT EVENTS IN 2009



KREDITTILSYNET CHANGES NAME TO FINANSTILSYNET

Kredittilsynet changed its name to Finanstilsynet (The Financial Supervisory Authority of Norway) on 21 December 2009. The new name is more in keeping with international practice and better reflects

the broad array of the agency's supervisory tasks, encompassing the entire financial sector. The monogram and logo are also changed.

SUPERVISION AND MONITORING

All Kaupthing Bank's Norwegian depositors receive full cover

Upon Finanstilsynet's recommendation, the Ministry of Finance on 12 October 2008 placed Kaupthing Bank's Norwegian branch under public administration. By the end of 2009 all Norwegian depositors had received full cover for funds on deposit with the bank.

Extra reporting requirements for Norwegian banks

The financial crisis and uncertainty about developments ahead prompted Finanstilsynet in January 2009 to ask the banks to consider changes to their credit practice, and, in the case of the largest banks, to state whether their ability to service customers' needs in 2009 would be affected by the liquidity situation and capital adequacy positions. A selection of 25 banks, including the largest ones in Norway, were instructed to submit weekly reports of total customer deposits and customer deposits above NOK 2 million from the end of the third quarter of 2008 to the end of the second quarter of 2009. Further, all banks' bonds and CDs maturing in the first four months of 2009 were surveyed in the fourth quarter of 2008 based on data provided by the banks directly and by Norges Bank.

Record number of bank inspections

Fifty-eight on-site inspections were carried out at banks, finance companies and mortgage companies in 2009, including IT inspections. This is a record number of on-site inspections in the banking and financial area. Finanstilsynet gave special priority to the larger banks, where wide-ranging inspection programmes were carried out.

Norwegian financial institutions' compliance with capital requirements

Finanstilsynet monitors compliance with the revised international capital framework, Basel II. Individual institutions' capital adequacy is overseen through periodic reporting and checks on their compliance with the minimum capital requirements. Institutions are required by law to immediately report any breach of the minimum requirement to Finanstilsynet.

Compliance with the pillar 2 requirement that regulatory capital should cover all risk to which the individual institution is exposed is monitored by reviewing the institution's risk and capital assessment process (ICAAP), after which the institution is given feedback.

Pillar 3 requires banks to inform market participants of the risk and capital situation. This information was reviewed by Finanstilsynet in 2009 to check their compliance with the requirements.

Extra home mortgage loan survey

In spring 2009 Finanstilsynet conducted a simplified home loan survey, prompted by the turbulence in the banking market and uncertainty regarding banks' credit practice in relation to home mortgages. The survey showed a significant decline in loans with a high loan-to-value ratio.

Lifting of temporary ban on short trading in shares and equity certificates issued by financial institutions

In September 2009 Finanstilsynet announced that the temporary ban on short trading in shares and equity certificates issued by financial institutions that was introduced in October 2008 owing to the extraordinary market situation and unusual market movements, could be lifted now that the market had stabilised.

Strong criticism levelled at Acta Kapitalforvaltning ASA

In its final observations after an on-site inspection at Acta Kapitalforvaltning ASA, carried out in September 2008, Finanstilsynet levelled strong criticism at the company's investment advice services, citing a number breaches of the Securities Trading Act's rules governing the conduct and organisation of the company's business. The company made significant changes to the way its business is run, and Finanstilsynet is overseeing the steps taken by the company to rectify the irregularities that were brought to light.

Two thematic inspections in the audit area

Thematic inspections in 2008 focusing on the audit of foundations were completed in 2009. The main impression gained was that the auditors had failed to give due attention to matters to which attention must be given in the audit of foundations. It was also noted that the standard audit report format used did not fully meet the requirements of the Act relating to Foundations. The second of the two thematic inspections focused on auditors' discharge of their audit assignment. The main conclusion drawn was that auditors were adequately involved in the audit, but at too late a stage in the audit process.

LICENSING

Solution for Eksportfinans/Kommunekreditt

On 7 May 2009 Eksportfinans ASA signed an agreement with Kommunal Landspensjonskasse (KLP) under which KLP was to acquire all shares of the mortgage company Kommunekreditt Norge AS. The conveyance was related to financial market developments that prompted a decision by Eksportfinans to focus on core business in the export finance field. Part of the KLP Group, Kommunekreditt Norge AS is a subsidiary of the newly established KLP Banken AS, which received its licence in January 2009.

Assistance to the Norwegian State Finance Fund

The Norwegian State Finance Fund was established with resources totalling NOK 50 billion after the Government's launch of "Bank Package II" on 8 February 2009. The State Finance Fund's mission was to make tier 1 capital available to Norwegian banks in the short term to bolster their finances and enable them to maintain normal lending activity. Finanstilsynet's task was confirm whether or not a bank met the tier 1 capital requirement before applying to the Finance Fund for a capital infusion. The agency issued 38 such confirmations in the application period, which expired on 30 September 2009.

Many estate agents cease trading – fewer transactions

Many estate agency firms were compelled to close their doors when the property market tumbled, markedly so from autumn 2008 onwards, only picking up some way into 2009. There were 717 firms in January 2008, falling to 611 in December 2008. By the end of 2009 there were 516 firms. Besides the fall in the market, the decline was due to the fact that estate agents licensed under the previous Estate Agency Act had to apply for new authorisation under the new act by the end of 2009. A number of estate agents omitted to apply for various reasons. Under the new act's transitional provisions, firms licensed to engage in estate agency under the old act were able to trade until 1 January 2010 without applying for a new licence. In autumn 2009 Finanstilsynet expended much effort on processing a large number of applications for permit renewal, due in part to the new act's substantially stricter requirements.

Listed firms penalised

Eleven listed firms received violation penalties for delayed publication of financial reports. Finanstilsynet announced that as from 2010 it would suspend firms that failed to publish periodic reports within a satisfactory period.

Structural changes in the savings bank sector – several savings banks merge

New legislation governing capital and forms of organisation in the savings bank sector entered into force on 1 July 2009, paving the

way for structural changes in the savings bank sector. Following the enactment, Finanstilsynet considered merger applications involving Sparebanken Møre and Tingvoll sparebank, and Sparebanken Vest and Sauda Sparebank.

Structural changes in the securities market

The fragmentation of trading in financial instruments across several marketplaces and trading platforms will make surveillance of market abuse at the individual marketplace more difficult. Revenue lost by established marketplaces facing intense competition and possible loss of trade also impairs their financial ability to maintain the current high quality of monitoring and oversight. As a result, increased responsibility for surveillance of market abuse has to be assumed by public authorities. Responding to this development will be a key challenge for Finanstilsynet in the years immediately ahead. The introduction of a transaction reporting system (TRS) is part of this process.

Participant in the Committee on the Financial Crisis

In June 2009 the Ministry of Finance appointed a committee to examine Norwegian financial market regulation in light of the financial crisis, the causes of the international financial crisis, and how the latter has impacted the Norwegian financial market. Finanstilsynet's general counsel is on the committee. The agency also provides the committee secretariat. The committee's report is to be completed by the end of 2010.

Fund manager convicted of market manipulation by Supreme Court

In January 2009 a fund manager was sentenced by the Supreme Court to ten months' imprisonment, of which 120 days were suspended, for offences including market manipulation and breach of market conduct rules. In its judgment the Supreme Court stated that unconditional imprisonment is the required sentence for market manipulation of a serious nature.

REGULATORY DEVELOPMENT

Wide-ranging international measures to improve regulation and supervision

The financial crisis was essentially handled at the national level; international coordination was lacking. The aftermath has seen a coordinated global focus on strengthening regulation and supervision of financial institutions and markets. A greater degree of harmonisation is in focus, and all financial activity is to be subject to

supervision. In the EU and the Basel Committee alike, steps are being taken to reform capital adequacy requirements for banks. Major reforms of requirements on the level and quality of banks' capital, liquidity, crisis management and bonus schemes et al. are under way. Finanstilsynet plays an active role in this process through the EU's supervisory committees and keeps abreast of the work done by the Basel Committee and other international bodies.

Bond issue trustees guaranteed litigation rights

In November Finanstilsynet was commissioned by the Ministry of Finance to consider 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. The agency was also asked to appraise an enquiry from Norsk Tillitsmann. The backdrop was a Borgarting High Court ruling to the effect that Norsk Tillitsmann ASA was not entitled to litigate on behalf of bondholders against a bond issuer. Responding to Norsk Tillitsmann's enquiry, Finanstilsynet drafted in November a law provision securing litigation rights for bond issue trustees.

Framework conditions for the audit industry

Amendments to the Auditors Act were adopted with effect from 1 July 2009 as a step in transposing the EU Audit Directive into Norwegian law. The amendments principally entail further requirements on audit firms that audit public interest entities, while banks, insurers and stock-exchange-listed firms are now required to have in place an internal audit committee.

Continuing preparations for introduction of solvency rules in insurance

In 2009 the EU Parliament adopted new solvency rules for insurance companies (the Solvency II Directive). The new rules are principle-based and will replace all existing directives in the insurance sphere. The Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) is currently engaged in a wide-ranging process of regulatory development including implementation measures that cover all aspects of the new body of rules. Transposition of the Solvency II framework into national insurance legislation is scheduled for completion by the end of 2012. The new regime will be fully utilised from and including the financial year 2013.

Issues related to incentive systems

In the wake of the financial crisis, incentive systems have attracted much attention as a potential contributor to the crisis. Against this background the agency has initiated an in-house project to describe the most important incentive schemes in existence today, and to evaluate positive and negative aspects of the schemes. The project includes a survey to map institutions' treatment of incentives, approval systems and possible new guidelines for incentive systems. The project report will be available early in 2010, and Finanstilsynet

will on that basis consider possible recommendations or regulatory steps in this area. The intention is that future incentive systems shall promote proper and effective risk management and internal control that does not encourage exaggerated risk taking.

Law amendments proposed for short selling

In January 2009 Finanstilsynet proposed amendments to the Securities Trading Act's provisions relating to short selling. The proposal extends the prohibition against uncovered short sales to include investors, enabling sanctions to be applied directly to investors who engage in uncovered short selling. It recommends authorising Finanstilsynet to temporarily prohibit covered and uncovered short selling. The proposal was under consideration at the Ministry of Finance at the turn of 2010.

New money laundering legislation into force

New money laundering legislation entered into force on 15 April 2009 as part of a new act and regulations on measures to combat money laundering and the financing of terrorism. The Ministry of Finance has also adopted regulations on the supervisory board for measures to combat money laundering which, with some technical adjustments, take forward the current regulations on the supervisory board for measures to combat the laundering of the proceeds of crime. Finanstilsynet prepared a guide for reporting entities under the agency's supervision including important FAQs relating to the new body of rules (circular 8/2009).

Issues related to the provision of financial advice

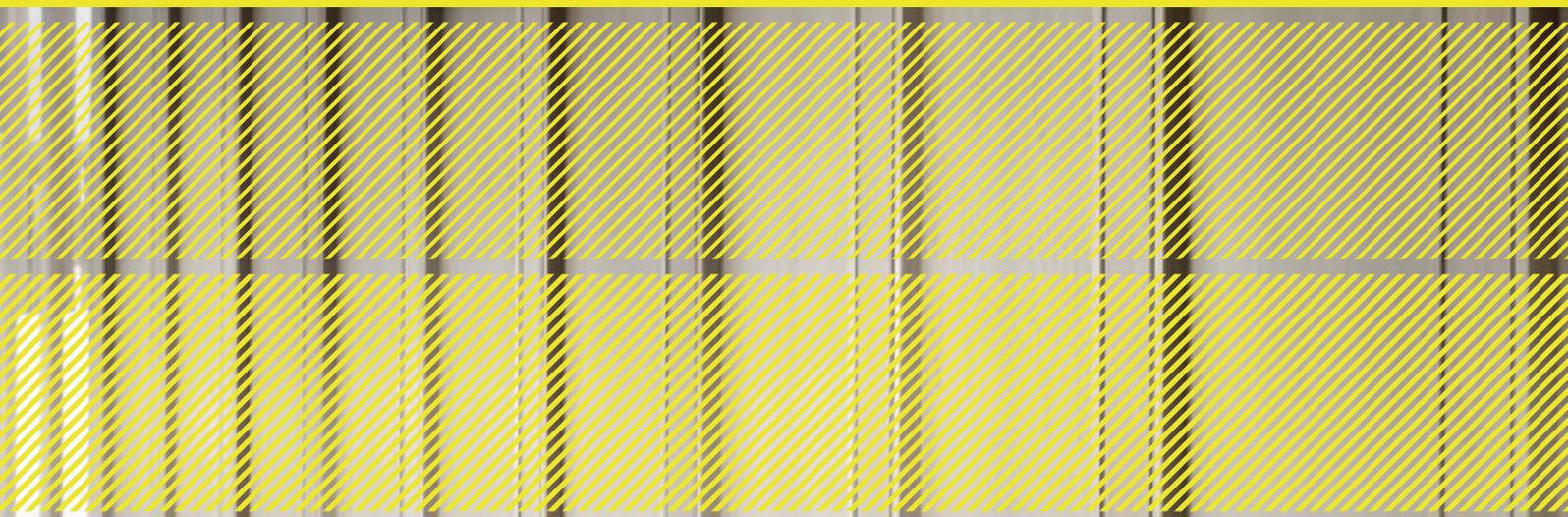
In 2009 Finanstilsynet initiated a study of key issues related to the provision of investment advice and financial advice. This included the collation of statutes and rules that regulate the field across sectoral divides. Studies of four institutions seek to describe how investment advisory services across sectoral divides are currently practised, what tools are employed between customer and institution, and challenges related to the enactment and application of legislation. A preliminary report is expected to be available early in 2010.

Ministry of Finance asked to clarify Finanstilsynet's mandate in regard to consumer protection and consumer information

In May 2009 Finanstilsynet asked the Ministry of Finance for a clarification of its mandate regarding consumer protection and information. Both the media and other sources have expressed greater expectations as to what action Finanstilsynet can and should take on behalf of consumers in parts of the financial sphere than is required of the agency pursuant to current legislation, mandate and funding. The approach to the ministry was accompanied by a project report describing Finanstilsynet's and other actors' measures addressed to consumers in the financial sphere.



GOALS AND INSTRUMENTS



MAIN GOALS

Finanstilsynet's main goal is to promote **financial stability and well functioning markets** through its supervision of institutions and markets. Behind this goal lie important economic considerations and a desire to protect consumers and investors. Financial stability and well functioning markets are crucial to economic growth and employment, which in turn are a prerequisite for a high standard of welfare and good conditions of living.

Where financial stability is concerned, Finanstilsynet has a particular responsibility for ensuring that financial institutions are well capitalised. Effective competition and sound rules of conduct and norms are important for well functioning markets. Moreover, actors' compliance with good ethical norms is a social objective of major value in its own right.

INTERMEDIATE GOALS

The main goals of **financial stability and well functioning markets** are concretised in Finanstilsynet's strategy through the following six intermediate goals:

1. Sound financial institutions and firms with a fit and proper management, and good internal control and risk management
2. A robust infrastructure ensuring satisfactory settlements and payments
3. Good monitoring of risk in the household and corporate sector and in real estate and securities markets
4. Adequate information to investors and users in the financial market, and good-quality financial reporting by listed companies
5. To promote financial market actors' compliance with the rules of conduct and to prevent conduct liable to undermine confidence in the financial market
6. To ensure that critical situations are handled with minimal harmful effects

INSTRUMENTS

Finanstilsynet's instruments are:

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

Supervision and monitoring

Supervision and monitoring are core tasks that consist in ensuring that companies adhere to laws, regulations and guidelines governing their business. Supervision is carried out by analysing reported data and by inspecting enterprises on site. This instrument also includes monitoring of macroeconomic conditions and other developments of significance for the financial sector, along with international collaboration.

Licensing

Licensing includes statutory work on licences and approvals to carry on business in Norway. Anyone intending to start a business in Norway within Finanstilsynet's field of responsibility has to apply for authorisation. Finanstilsynet also gives advice to licence applicants, and issues interpretative comments on acts and regulations.

Regulatory development

Regulatory development is designed to promote a regulatory environment for the economy and markets that contributes to profitable and competitive operations at supervised entities. It includes both developing and simplifying rules, drafting acts and regulations and participating in law committees etc. Finanstilsynet also participates in the development of international standards.

Information and communication

Information and communication promotes openness and predictability for the users of Finanstilsynet's services as well as an understanding and knowledge of the legislation and of Finanstilsynet's role as a supervisory agency. Importance is attached to good dialogue with supervised entities, trade organisations, government bodies and the media. Information and dialogue include written (electronic and paper-based) and oral information (presentations and meetings).

(Excerpts from Finanstilsynet's (Kredittilsynet's) strategy for 2006–2010, adopted by Kredittilsynet's Board 23 October 2006.)



MAIN SUPERVISORY ACTIVITIES 2006–2009

Finanstilsynet's current strategy was adopted in October 2006. In 2009 the agency started preparing for a new strategy period by launching a number of pilot projects. The new strategy will apply from autumn 2010 onwards. This chapter summarises the work done in the period 2006–2009 and assesses how far the goals set were attained.



TRENDS AND CHALLENGES

Both the international and Norwegian financial markets were marked by considerable optimism in 2006. Share prices were buoyant and issue activity high. Credit growth was strong. In its strategy document the agency expressed concern over the trend in household debt and the housing market: *In the period to 2010 particular uncertainty will attach to the trend in household debt and the housing market. An extremely high debt burden, historically high house prices and banks' substantial exposure to the housing market create the risk of a setback in the economy and markets* (page 8).

It was pointed out that the favourable economic climate could spur exaggerated optimism, overinvestment and vigorous expansion at many financial institutions and a danger of excessive risk taking by some actors. The imbalances in the international economy were also underlined.

Branches' growing significance called for greater emphasis on overall supervision of conduct and products in the market. The new capital

adequacy rules, based to a larger degree on institutions' internal models and control systems, would make greater demands on competence and capacity in the supervision of individual institutions.

Finanstilsynet also faced significant challenges in its supervision of the markets: *Financial product innovation puts a greater premium on the information provided on product characteristics, risk and return. The need for correct and relevant information is particularly great where households carry a large part of the financial risk attached to financial products – including insurance products. The marketing and selling of such products will entail substantial reputational risk for their issuers* (page 8).

The increased significance of operational risk associated with wider use of ICT was discussed, and the danger that organised crime could expose institutions and customers to fraud was pointed out.

OUTLINE OF SUPERVISORY ACTIVITIES

This description covers the four strategy instruments: *Supervision and monitoring, Licensing, Regulatory development and Information and communication.*

Supervision and monitoring

In the period under review Finanstilsynet analysed financial institutions' accounts and results on a quarterly basis and presented its findings in press releases and public reports. Every six months analyses were conducted of trends significant for financial stability and of the risk faced by institutions which were presented to and discussed with Norges Bank and the Ministry of Finance. The main lines of the analyses and surveys, which included residential loans, were made public in the annual Risk Outlook Reports.

Finanstilsynet's activities and its assessments of markets and instruments were also presented in the annual reports. In light of the credit growth, Finanstilsynet expressed the view, in the foreword to its annual report for 2005 in January 2006, that Norges Bank should not spend too long bringing the interest rate up to a more normal level.

In February 2007, in the report *The Financial Market in Norway 2006: Risk Outlook*, concern was expressed over the growth in international credit and the imbalance between developments in the US and Asia. Where Norway was concerned, it was pointed out that banks' high

loan-to-value ratios on home mortgage loans and strong growth in household debt created a vulnerable situation in the shape of higher interest rates and possible economic setbacks.

The period saw a growing volume, and somewhat indiscriminate distribution, of highly complex derivative products in the international financial markets which also had repercussions for Norwegian investors. In November 2007 Finanstilsynet announced the withdrawal of Terra Securities ASA's licences to provide investment services under the Securities Trading Act. The firm had offered complex financial instruments to a number of local authorities, a target group unsuited to such products, without informing them of significant risks.

Structured savings products were invested in and sold extensively for several years. The new Securities Trading Act that entered into force in November 2007 imposed stricter information requirements on vendors of structured products. Finanstilsynet advised banks not to lend to consumers for the purpose of investing in structured products, and instructed banks to give more objective advice. This was underlined in regulations imposing an information requirement on offerors of structured products and in a circular issued by the agency in February 2008. The new, stricter requirements have brought a hefty reduction in sales of such products.

MAIN SUPERVISORY ACTIVITIES 2006–2009

In 2007 the subprime scandal was seen as a source of considerable uncertainty in the financial market, but surveys showed that Norwegian financial institutions, insurers and pension funds were little exposed to securities based on subprime loans. When the US authorities in spring 2008 rescued the fifth largest investment bank, Bear Stearns, most market participants and authorities assumed that the impact of the financial crisis would be moderate both internationally and in Norway.

The US authorities' failure to bail out the fourth largest investment bank, Lehman Brothers, letting it collapse, left millions of contracts outstanding and triggered deep mistrust between participants in the international financial market. In Norway 20,000 trades at Oslo Børs were hit by Lehman's demise. Liquidity in the interbank market dried up. Major international financial institutions tightened their lending to the point where in 2009 the international economy saw its severest setback since World War II.

On-site inspections

In the period 2006–2009 Finanstilsynet maintained an extensive inspection regime which was broadly in line with the annual plan of operations. The results for each year are shown in table 6 on page 32. Over the course of the four years 2006–2009, 193 inspections were carried out at banks and finance companies, 25 at insurance companies, 18 at insurance intermediaries, 78 at investment firms, 150 at auditors and audit firms, 196 at external accountants, 187 at real estate agents and 36 at debt collection agencies. The figures include IT inspections.

Banking, finance and insurance

Norwegian banks were in the first instance hit by the heavily reduced supply of liquidity in the international markets and substantially higher funding costs. The repercussions this had for financial institutions and the Norwegian economy are given closer attention in the report *The Financial Market in Norway 2009: Risk Outlook*. The wide-ranging measures initiated by Norwegian authorities helped to dampen the impact. Norwegian banks' credit activity was less affected than that of their counterparts in other countries.

From October 2008 to summer 2009 Finanstilsynet required the 25 largest banks to submit weekly reports of liquidity positions and deposit movements. Frequent telephonic contact was maintained with larger banks, and there was close contact with Norges Bank on monitoring banks' liquidity situation. From the start of 2008 to the end of 2009 the agency's management held quarterly meetings with the managements of the seven largest banks where the focus was on risk monitoring and risk management. Assessment of capital needs was also an important theme at the meetings. These assessments were, however, handled primarily through the ICAAP process, the institutions' internal capital assessment process. In 2008

risk and capital needs were assessed first by the management of the individual institution, thereafter by the agency for all 154 Norwegian financial institutions. Many banks were urged to increase their capital adequacy ratios, and were closely monitored through 2009. Thanks to profit retention, capital infusions from the Norwegian State Finance Fund and stock issues, capital levels showed a marked increase and by the end of 2010 Norwegian banks' capital ratios were regarded as satisfactory.

Of particular importance were thematic inspections targeting banks' loans to commercial properties, which rose by about 30 per cent in each of the years 2006 to 2007. In 2007 such loans accounted for more than 40 per cent of banks' overall lending to the corporate sector. In winter 2008 the eleven most heavily exposed banks had their lending practice and their exposures to commercial property closely scrutinised by on-site inspections. The agency drew several banks' attention to risk concentration in this area and to the fact that their risk-taking was often higher than allowed for under their own guidelines. In the wake of the survey banks appeared to tighten their lending practice, in the first instance to bring it into line with their own guidelines and subsequently in light of the onset of the financial crisis in autumn 2008. Access to new capacity in the market was accordingly curbed and the problems facing the banks proved smaller than feared. See also the assessments given in the *Risk Outlook Report*.

Securities market

Thematic inspections targeting sales and the advice given on the products of investment firms were also of major significance. On-site inspections and subsequent withdrawal of the licences of Glitnir Privatøkonomi (which handed in its licence voluntarily upon receiving a warning), and Caveo and Totalvekst in 2008, gave clear signals of what standards were expected from vendors of such products and of the advice they gave. Comprehensive inspections and critical observations directed at Acta and DnB NOR in 2008–2009 also instilled an understanding of the standards expected.

Real estate agency

The wide-ranging inspections of estate agents encouraged the industry to downsize substantially without causing significant problems for customers in terms of settlement and other important matters. New estate agency legislation entered into force on 1 January 2008 bringing far tighter requirements on a number of fronts, inter alia in regard to corporate licences, estate agents' competence and independence, investigation and disclosure obligations and rules governing fee calculation. At the inspections much importance was given to checking estate agents' observance of the new body of rules. Inspections regularly bring to light gross breaches of estate agents' obligations, prompting licence withdrawal. A total of eleven estate agencies lost their licences in the period 2006–2009.

Financial reporting, auditor and external accountant supervision

Finanstilsynet took over the responsibility for and oversight of listed companies' financial reporting from 2005 onwards. In the period under review a number of cases were dealt with, including cases of precedent setting significance. The exposure of a major case of accounts manipulation, duly reported to the police, is seen as important for securing disciplined financial reporting by listed companies. Priority has deliberately been given to large audit firms of major significance to the audit market and to public confidence in audit quality. Thematic inspections in the audit area have also led to improved audit practices. Such inspections have included audits of banks and audits of foundations. In a move of great supervisory significance in the area of external accountancy services, quality control seminars bringing together 5,000–6,000 external accounts were arranged in conjunction with the Norwegian Association of Authorised Accountants (NARF).

Licensing

In the period under review the agency regularly reported on the position of licensing and case processing in relation to the targets set for processing various types of cases. A total of 11,142 registered cases and 151,653 registered incoming and outgoing documents were processed in the period 2006–2009.

Checking compliance with the securities trading legislation's new licensing requirements introduced as a result of the MiFID directive was among the most demanding tasks in the period. Between 2006 and 2009 the number of investment firms rose from 85 to 150. In the period the licences of 38 investment firms were revoked, 27 of which after the entry into force of the new Securities Trading Act in November 2007.

Thirty-two new licences were granted in the banking and finance area and ten new licences in the insurance area. A further 66 licences to engage in insurance mediation were granted in the period.

Revocation of the licence of Terra Securities ASA in November 2007 on account of deficient information and advice given when selling investment products to Norwegian local authorities was an important event both for those involved and for the market. The licence withdrawal was a signal to all actors of the need to take important considerations into account when mediating complex securities products.

New licensing requirements – real estate agency

The new estate agency act requires all agencies operating on a licence granted under previous legislation to apply for a new licence in the course of a two-year transitional period, i.e. by the end of 2009. The new act imposes far more and stricter requirements on licence

applicants, including fitness and propriety requirements for all members of the management board and those effectively in charge of the business, and requires documentation of professional estate agency procedures and routines and documentation of adequate capitalisation. A total of 480 estate agency firms were granted a new licence under the new act in 2008 and 2009. About 40 of the "old" firms whose trade was minimal or had effectively ceased did not apply for a new licence.

Approval of internal models

Finanstilsynet processed the first applications to use internal models (IRB) for credit risk in October 2005, so that banks would have an opportunity to use the models as from the introduction of Basel II in 2007. The following institutions were granted IRB status in the strategy period: DnB NOR Bank ASA, DnB NOR Boligkreditt AS, Sparebanken Vest, Sparebanken Vest Boligkreditt, SpareBank 1 SR-Bank, SpareBank 1 SMN, SpareBank 1 Nord-Norge, Bank 1 Oslo AS, SpareBank 1 Boligkreditt and Nordea Bank Norge ASA.

Regulatory development

Finanstilsynet expended much effort on regulatory development in the period. The following rule changes were key:

- A new capital adequacy framework (Basel II), into effect on 1 January 2007
- A new Securities Trading Act (based on MiFID), into effect on 1 November 2007
- A new Estate Agency Act, into effect on 1 January 2008
- Regulations on administration of branches of foreign banks and Regulations relating to the Norwegian State Finance Fund, into effect in autumn 2008
- Amendments to the Auditors Act, into effect on 1 July 2009

Information and communication

Finanstilsynet's information and communication activity is a strategic instrument and is integrated into the supervisory effort on an ongoing basis.

Development of new electronic solutions was at centre stage in the period. Finanstilsynet's new website went live in 2009. This includes a facility for reporting unlawful activity (market warnings). This – together with a licence register containing searchable information on all entities authorised by Finanstilsynet to operate in the Norwegian financial market – is an important service directed at investors and small savers. The new website also features a new self-service subscription facility, inter alia for circulars and press releases. Moreover, a new electronic archive of previous supervisory decisions was developed which is to be made available in a public version on the website in 2010. The agency also launched a new intranet solution in February 2008.

MAIN SUPERVISORY ACTIVITIES 2006–2009

Finanstilsynet, together with the Consumer Council and the Consumer Ombudsman, established and developed *Finansportalen.no*. This website, launched in January 2008, assembles information about products and services in the Norwegian financial and insurance market, enabling the customer to compare prices and terms etc.

In 2007 an anti-money-laundering website, *Hvitvasking.no*, was set up jointly by Finanstilsynet and ØKOKRIM (The Norwegian National Authority for Investigation and Prosecution of Economic and Environmental Crime) to present information about measures to combat money laundering and financing of terrorism.

In 2004 Finanstilsynet imposed requirements on information provided by vendors of structured products. The requirements were expanded in a circular issued in 2006. By means of presentations and through other channels the agency warned against aggressive selling and substandard advice. In 2007 a survey was carried out of 350 products, of which 218 had been loan-financed. Products not financed by borrowing had returned a moderate 4 per cent, whereas the loan-financed products had in many cases made a loss and returned on average a mere 2 per cent. When subscription costs are included, the outcomes were even poorer. As a result of Finanstilsynet's very pointed warnings against loan-financing of structured products, such financing effectively ceased early in 2008. Sales of structured products in general also fell significantly and were confined to customers with insight into the products.

Criticism has been levelled at Finanstilsynet for not intervening more comprehensively as an earlier stage to curb sales of structured products. Some of the criticism has been based on the assumption that the agency's responsibility for ensuring consumer protection and information in the financial area is greater than that actually set out in the agency's current mandate. This is one reason why Finanstilsynet scrutinised its consumer-oriented tasks and asked the Ministry of Finance to clarify the agency's mandate in this area; see the annual report for 2008, page 84–87. The agency itself points out that only with the introduction of new securities legislation in November 2007, based on the MiFID directive, did it become possible to impose on vendors of complex securities products sufficiently stringent requirements as to information and advice.

In 2008 and 2009 Finanstilsynet collaborated closely on crisis communication with the Ministry of Finance, Norges Bank, the Norwegian Banks' Guarantee Fund and the Norwegian State Finance Fund.

In 2009 Kredittilsynet took the initiative to change its name to Finanstilsynet with a view to bringing the name more in line with the agency's functions. The change was timed to coincide with the move to new premises, thereby minimising additional costs.

GOAL ACHIEVEMENT IN THE PERIOD

Finanstilsynet adopted financial stability and well functioning markets as the main goals for the strategy period. See the overview of the agency's goals and instruments, page 11.

Financial stability

Norwegian financial institutions were able to meet the financial crisis with good quality equity capital and capital adequacy levels that were basically well in compliance both with the rules and with market requirements. The Basel II framework lifted the quality of banks' risk management inasmuch as the wide-ranging requirements imposed on IRB banks have set the standard for what is now regarded as good market and banking practice. The ICAAP processes in 2007 and 2008 imparted to directors, managers and Finanstilsynet a high awareness of the risk present in each institution and of the institution's need for capital. This provided a sound basis on which to strengthen capital positions when the crisis heightened risk levels and the market imposed heavier equity capital requirements on banks wishing to borrow in the market. *Intermediate goal 1 regarding solid financial institutions can essentially be said to have been attained in the period.*

At the start of 2010 no Norwegian-owned financial institutions appear likely to fail as a result of the financial crisis. As widely reported, the Icelandic-owned subsidiary Glitnir had to turn to the Norwegian Banks' Guarantee Fund for temporary support and was sold to a group of Norwegian savings banks. Eksportfinans received government support to secure its export financing obligations to Norwegian businesses.

Kaupthing's branch was compelled to halt payments on the morning of 9 October 2008. Upon Finanstilsynet's advice, the Ministry of Finance extended in the space of two hours a political guarantee covering all deposits up to NOK 2 million, which included an advance of Iceland's home-country portion. The efforts of the administration board assured that deposits in excess of NOK 2 million were also covered. Thanks to the close cooperation between the Banks' Guarantee Fund, Norges Bank, Finanstilsynet and the Ministry of Finance, the handling of the two Icelandic bank operations in Norway helped to assure a high degree of confidence in the Norwegian deposit guarantee scheme. The disquiet in evidence in a number of other European

countries was not seen among Norwegian depositors. Both these and other critical situations were handled in such a way that the harmful effects were curbed, and intermediate goal 6 must be said to be attained.

In accordance with intermediate goal 3, Finanstilsynet completed a wide-ranging monitoring and reporting programme and drew attention in the years 2006 to 2009 to the substantial risk building up in households and housing and property markets. Given high debt-equity ratios, it was no surprise that the combination of high mortgage lending rates, which for a brief period exceeded 7 per cent, and the international financial crisis with attendant fear of significantly higher joblessness, brought a change in household expectations strong enough to constitute a threat to financial stability. Uncertainty regarding future liquidity supply after Lehman's demise also sparked, briefly, concerns over banks' ability to maintain normal lending. The last quarter of 2008 saw a dramatic decline in house purchases and a marked fall in the prices of houses that found a buyer. Car purchases dropped significantly, as did sales of other consumer durables. Layoffs and curtailments were noted in wholesale and retail trade and construction.

The consequences were less marked in Norway than in other countries, partly because financial institutions were well placed and partly because the authorities introduced wide-ranging measures to secure liquidity, financial strength and activity levels in the Norwegian economy. Of particular significance were the 'swap' scheme and other liquidity measures taken by Norges Bank and the rapid and steep reduction of the key interest rate which significantly improved household finances and rekindled optimism in the housing market and consumer-oriented business.

Thanks to a combination of Norwegian rules, steps taken by the Government and Norges Bank and Finanstilsynet's pro-active supervisory effort, the main goal of **financial stability** in the period was achieved in a satisfactory manner, despite major external strains.

Well functioning markets

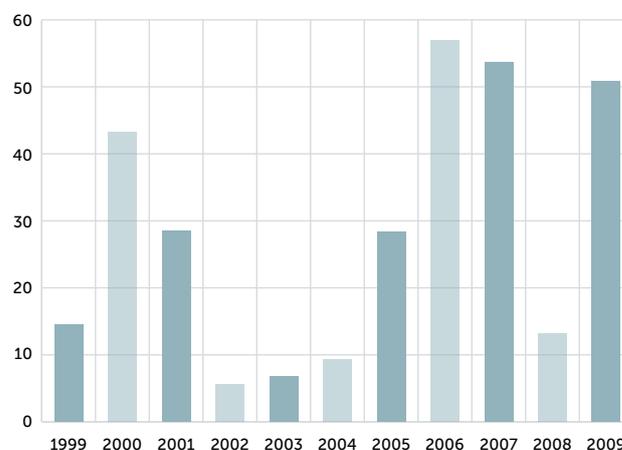
Substantial changes were seen in the market for financial instruments in the period due to the implementation of a new body of rules in Europe. Important premises for the design of the body of rules were higher requirements in relation to investor protection and a desire for keener competition between investment firms and marketplaces. Norwegian rules have been updated in step with the implementation deadlines set by our EEA obligations. Rapid, loyal compliance with changes in the international accounting rules along with the establishment of an active financial reporting supervisory regime under Finanstilsynet's auspices have fostered a satisfactory international reputation for companies listed on Oslo Børs. *Intermediate goal 4*

regarding sufficient information to investors and users can largely be said to have been fulfilled. It is possible that Finanstilsynet at an earlier stage could and should have done even more to draw attention to shortcomings in structured savings products; see the section entitled "Information and communication" above.

The development of new communications technology has also been a major factor in securities market development. Market information is distributed more rapidly, and the trading systems linked to stock exchanges and trading platforms have become more efficient. The fact that the new rules have paved the way for the establishment of multilateral trading facilities, i.e. multilateral systems that facilitate trading in financial instruments admitted to quotation on the established exchanges, has generated keen competition on transaction pricing. This has however impaired the earnings base for established stock exchanges in Europe, and also for Oslo Børs.

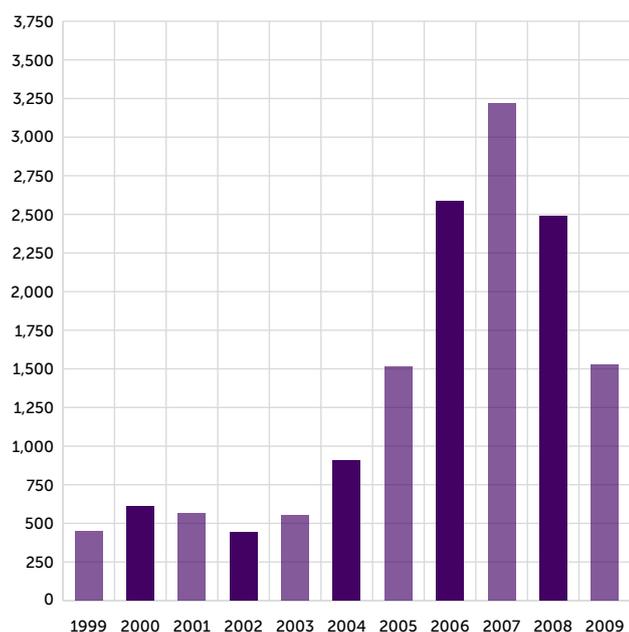
The Norwegian stock market can point to a positive trend over the past four years. There is particular cause to highlight the excellent trend in market liquidity reflected in turnover figures, even though 2008 and parts of 2009 were coloured by a wait-and-see stance among investors. Ample liquidity is a prerequisite for attracting major portfolio investors to a market. The positive liquidity trend is therefore both a precondition for and a result of major foreign institutional investors' decision to invest in the Norwegian market. The market has also functioned well as a source of capital in the period. In 2006 and 2007 it provided risk capital worth more than NOK 110 billion in the form of share capital increases. This is substantial compared with other European markets in the same period. After a slight reduction in activity levels in 2008 and the first half of 2009, issue activity again turned positive, providing a capital supply in 2009 of NOK 50.8 billion in shares and equity capital certificates.

Chart 1: Issue volume 1999–2009 at Oslo Børs (NOKbn)



Source: Oslo Børs

Chart 2: Turnover at Oslo Børs 1999–2009 (NOKbn)



Source: Oslo Børs

A weakness of the Norwegian stock market is its high volatility, due partly to firms' relatively high exposure to commodity prices, in the first instance energy. Moreover, investor composition in the Norwegian equity capital market shows little diversity. Throughout the period, foreign investors and the Norwegian state have together accounted for some 70 per cent of equity interests in Norwegian listed companies. Whereas the state represents a stabilising element, foreign investors often view investments in the Norwegian market as marginal in a wider portfolio and are likely to pull money out of the Norwegian market in turbulent periods. Hence the absence of sizeable domestic investor groups able to take over large volumes poses a major challenge in relation to the goal of well functioning markets.

Interest on the part of foreign investors is both a result of and a precondition for large foreign intermediary firms' decision to enter the Norwegian securities market by becoming members of Oslo Børs. Foreign intermediaries' activity builds on confidence that the rules and framework conditions largely resemble those elsewhere in Europe. There is reason to believe that Oslo Børs's and Finanstilsynet's active oversight of compliance with the market conduct rules in the market has strengthened general confidence in the Norwegian market as an investment option. In the strategy period Oslo Børs, Finanstilsynet and ØKOKRIM jointly prepared a comprehensive report on their collaboration on combating securities crime. While it found little reason to recommend changes, the joint committee did emphasise that adequate resources to operate effective market conduct supervision are of major significance for confidence in the market. Several

important court convictions in the securities market area are the outcome of joint efforts by the three institutions. Intermediate goal 5: *to promote financial market actors' compliance with the rules of conduct and to seek to prevent conduct which may undermine confidence in the financial market* is a demanding goal. Although intensified efforts must be assumed to have contributed to greater awareness on the part of market participants, further efforts are needed.

The changes in trading patterns resulting from new technology and keener competition among marketplaces will be a key challenge to market conduct supervision ahead. See the chapter *Securities market*, page 63.

A further precondition for non-residents' interest is a well functioning settlement system and securities register. Oversight of this area has been and will remain a high priority in the supervisory effort.

Lehman Brothers International (Europe) Ltd was a remote member of Oslo Børs and an indirect participant in the central securities settlement process with DnB NOR ASA as settlement agent. At the time of its bankruptcy Lehman Brothers had about 20,000 trades outstanding in the Norwegian settlement system. The situation was closely followed by VPS (the central securities depository) as the securities settlement system operator, by DnB NOR Bank ASA as a settlement agent and Finanstilsynet. Outstanding settlements were completed without loss to any participant in the settlement process. The situation was somewhat eased by the fact that falling market prices enabled investment firms to make good undelivered holdings by purchasing in the market at lower prices.

However, the strained situation brought to light ambiguities as regards settlement agents' responsibility for their clients' ability to meet their obligations in the settlement process. Part of the problem will be resolved by the introduction of central counter-party (CCP) clearing and settlement in respect of quoted equity instruments in the first half of 2010. There will however, independently of this, be a need to review settlement agents' responsibilities in the settlement process. Work on the issue had yet to reach completion at the end of 2009.

In terms of price formation and liquidity, the market for quoted shares functioned satisfactorily through the turbulent period in the second half of 2008 and the first quarter of 2009.

Fixed income markets, however, were sluggish in parts in the second half of 2008. At times liquidity was so thin that trading was difficult. Low activity also left a poor basis for pricing instruments. Securities funds that had invested in fixed income instruments consequently faced potential problems in handling redemption claims, since

selling instruments and fixing unit prices were both problematic. Finanstilsynet kept a close watch on the situation and was in continuous touch with the Norwegian Mutual Fund Association which coordinated information from its member undertakings. The option of utilising the opportunities available to refuse to redeem fund units in order to protect the interests of remaining unit holders was considered daily. The situation improved somewhat towards the end of 2008, and normalised in the course of 2009.

The financial industry's technological infrastructure, including the payment systems and their associated undertakings, was also subject to active supervision. Annual systematic risk and vulnerability analyses, supplemented by the introduction of mandatory event reporting in the ICT area, provided a better overview and a better basis for effective follow-up of serious errors. *In general the Norwegian settlement systems managed well, and intermediate goal 2 of a robust infrastructure must in all essentials be said to have been achieved.*

ADMINISTRATION AND PERFORMANCE OF ACTIVITIES

The agency increased its staff from 205 to 255 in the period. A section for financial reporting supervision was set up along with a specialised section for solvency regulation and risk models. Preparations for taking over the practical responsibility for prospectus control are well under way.

Finanstilsynet will attain its goals in an effective manner by utilising the possibilities offered by ICT. To that end, eight electronic forms were developed for reporting via the Altinn internet portal, a computer warehouse solution was developed and put into use, and integrations were established between the agency's central content management system (*Sentralfag*) and case processing system (*WebSak*). A transaction reporting system was developed in the securities area through a Nordic collaboration designed to comply with EU requirements. The system went live on 1 November 2008. A common capital

adequacy reporting system (COREP) was also developed in keeping with recommendations from the Committee of European Banking Supervisors (CEBS).

Three working processes were reviewed and harmonised across various segments of the organisation. These working processes are associated with licensing, supervision and analyses. Finanstilsynet puts a premium on recruiting and retaining members of staff with high competence levels, including industry experience. See also page 25 in the chapter entitled *Organisational set-up and resource use*. Compared with its counterparts in other countries, Finanstilsynet has a relatively low staff turnover. The international financial crisis was met with experienced staff, many of whom possess experience extending back to the Norwegian banking crisis in the early 1990s.



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 Board, appointed on 1 March 2006, was altered in March 2009. The present Board comprises:

Finn Hvistendahl, chartered engineer, chair
Eli Aas, lawyer, deputy chair
Marianne Berg, district court judge, board member
Hilde C. Bjørnland, professor, board member
Bjørn Arild Gram, municipal council chairman, board member

Mette Bjørndal, professor, first alternate
Jostein Skaar, director, second alternate

Arild J. Lund, director at Norges Bank, attends as observer. **Sindre Weme**, is his alternate.

Former deputy chair, **Endre Skjørestad**, was on 6 March 2009 appointed chairman of the Board of the Norwegian State Finance Fund and simultaneously released from his post with the Board of Finanstilsynet. Board member **Eli Aas** was appointed as new deputy chair for the remainder of the Board's term of office, ending on 1 March 2010. Municipal council chairman **Bjørn Arild Gram** was appointed as new board member.

Former observer **Birger Vikøren** was granted leave of absence from his post at Norges Bank upon being appointed as managing director of the Norwegian State Finance Fund. He was accordingly released from his post as Norges Bank's observer to the Board. Director **Arild J. Lund** was appointed as new observer and assistant director **Sindre Weme** as his alternate until 1 March 2010.

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**.

Twelve ordinary board meetings were held in 2009. The Board dealt with a total of 35 administrative matters and 81 supervisory matters requiring decisions. The Board received information on a further 72 administrative matters and 79 supervisory matters, bringing total items received to 267. 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

From left: Marit Sletta, Hilde C. Bjørnland, Mette Bjørndal, Bjørn Arild Gram, Jostein Skaar, Marianne Berg, Finn Hvistendahl, Knut Godager, Eli Aas and Arild J. Lund
Photo: Jarle Nyttिंगnes



Finanstilsynets's Management Team

From left: Cecilie Ask, Kjetil Karsrud, Bjørn Skogstad Aamo, Eirik Bunæs, Gun Margareth Moy, Emil Steffensen and Anne Merethe Bellamy
Photo: Jarle Nytingnes

PRIORITIES IN 2009

Finanstilsynet's supervisory activities start out from the tasks imposed on the agency 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 (2008–2009), 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 2009:

- 1.** Playing a part in dealing with the challenges posed by the financial crisis for Norwegian institutions and customers, so that depositors' and other customers' interests are protected. Financial institutions should increase their revenues and adjust their expenses to enable them to bear increased losses without depleting equity capital. In a volatile property market it is important to assure prudent conduct on the part of estate agents.
- 2.** Further developing risk-based supervision, above all with a view to assuring that firms' risk exposure is commensurate with their financial position and the quality of their governance and control systems. In the interest of financial stability Finanstilsynet will adapt its discretionary powers to the cyclical situation.
- 3.** Monitoring the financial position of individual institutions and financial stability by following structural developments and changes in the Norwegian and the international economy that are of importance to financial institutions and financial markets. Monitoring the trend in money and capital markets and the property market in light of the international financial crisis, the banks' tight liquidity situation and measures set in train by the Norwegian authorities to remedy the situation.
- 4.** Further developing practice as regards conduct-of-business requirements for investment firms. Following up supervision of investment advisers, in particular with a view to investor protection. Securing good quality financial reporting by listed companies.
- 5.** Conducting sufficient on-site inspections. This is particularly important in light of the increased uncertainty in the markets and the economy.
- 6.** Continuing to give weight to ICT-oriented supervisory activities with a basis in risk and vulnerability analyses in order to ensure security at internet banks and other electronic solutions for distribution of products and services.
- 7.** Preparing the introduction of a new solvency framework for insurers (Solvency II), including supervisory methods, model approval and reporting. Assessing the rules governing life insurance with a view to increasing long-term return.
- 8.** Ensuring the follow up required by a new body of rules in the audit area and continuing to prioritise supervision of the largest audit and external accounting firms.
- 9.** Continuing the effort to increase efficiency and simplify operations, inter alia through greater use of electronic solutions in reporting, analysis and case processing.
- 10.** Promoting the provision of good information to consumers and investors about risk and other characteristics of financial products through further collaboration with the Consumer Ombudsman and the Consumer Council on information posted on Finansportalen.no and through continued collaboration with the trade organisations.
- 11.** Conducting a user survey among supervised entities, trade organisations and collaborating authorities. Starting work on preparing a new strategic plan to be considered by the Board of Directors in 2010.
- 12.** Planning and implementing relocation to new premises.

ACCOMPLISHMENT OF PRIORITIES

The chapter on the period 2006–2009, page 12, concerning implementation of the strategy, gives a general assessment of the degree to which the goals for the period were achieved.

What follows is an overview of the accomplishment of the highest priority tasks in 2009:

1. No Norwegian-owned banks incurred solvency problems necessitating support from the Norwegian Banks' Guarantee Fund. A group of savings banks were authorised to take over the Icelandic-owned Glitnir. There were no losses for depositors or significant problems for other customers. Finanstilsynet appointed and kept in continuous touch with the administration board for the branch of Kaupthing. This branch was wound up without loss for Norwegian depositors. The Banks' Guarantee Fund and the Ministry of Finance were in 2009 reimbursed funds made available in autumn 2008. Eksportfinans received assistance from the Government to secure its export financing obligations. Finanstilsynet oversaw the adequacy of Eksportfinans's capital and liquidity position on a continuous basis.
2. Assessments of risk and capital needs in the banking sector were followed up in close dialogue with the banks concerned, to ensure that their equity capital was sufficient to meet the challenges posed by the international financial crisis. The creation of the Norwegian State Finance Fund and the collaboration between Finanstilsynet and the Fund on processing applications for capital infusions was important in enabling the banks to maintain reasonably normal credit activity.
3. The 25 largest banks were instructed to report on liquidity and deposit movements once a week from 1 October 2008 to summer 2009. In addition to close monitoring of solvency at individual institutions, two surveys were carried out of home mortgage loans along with special follow up of loans to commercial property and shipping.
4. The surveys of investment advisory services were followed up with comprehensive, critical reports on major actors such as Acta and DnB NOR. Many financial statements were examined with a view to assuring good financial reporting on the part of listed companies. Critical observations were issued along with rectification orders, and guidelines were drawn up for sanctions to be imposed for late filing of accounts.
5. On-site inspections at banks along with finance companies and mortgage companies were both more numerous (58) and wider ranging than ever before. In other areas the number of on-site inspections was approximately as previously; see table 6 on page 32. In view of the large number of estate agency firms needing a new licence under the new legislation, fewer on-site inspections were planned and conducted in this area in 2009 than in 2008.
6. Comprehensive risk and vulnerability analyses were carried out in 2009 as previously, along with numerous on-site inspections designed to assure secure internet banks and other ICT-based systems. The infrastructure and its bearing on risk in a well functioning financial market were charted, and there was a special follow-up of ICT service deliveries outsourced to other countries.
7. Finanstilsynet played an active part in international preparations for new solvency rules for insurers (Solvency II) and started preparing for their implementation in Norway by taking stress test development a stage further and investigating Norwegian insurers' planned use of models. An in-house project on rules governing life insurance is under way with a view to increasing long-term return.
8. The agency was instrumental in framing new audit legislation based on the relevant EU directive. Finishing work needs to be done with regard to the auditor register and regulations. Inspections were conducted at, and meetings held with, the largest audit firms. Further, two thematic inspections were carried out; one focusing on the audit of foundations, the other on the content of auditor's responsibility for the overall assignment.
9. The introduction of electronic reporting solutions is a continuous process at the agency. Implementation of the Altinn II internet portal was delayed, in turn delaying the conversion of existing forms and the introductions of new forms. Further electronic reporting by supervised entities was introduced in the period.
10. Cooperation with the Consumer Council and the Consumer Ombudsman on information posted on *Finansportalen.no* was taken forward. A report on Finanstilsynet's consumer-oriented work and responsibilities in this area was prepared and forwarded to the Ministry of Finance which circulated it for comment in autumn 2009. The agency's new website gives a voluminous overview of alerts warning of attempted investor fraud.
11. A new user survey was prepared which is to be carried out in the first quarter of 2010. A survey of changes in markets, legislation and international supervisory methods was initiated with a view to the consideration of a new strategy for coming years by the Board of Directors in 2010.
12. Relocation to new premises was completed in the period 18–21 December, accompanied by a name change to **Finanstilsynet** effective from 21 December 2009.

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 2009 totalled NOK 1,164,000, and the Chairman of the Board's remuneration was NOK 195,000.

Forty-four vacancies were advertised in 2009 compared with 53 in 2008. Ten of these were in-house compared with 18 in 2008. Applicants totalled 976 in 2009 compared with 553 in 2008.

At the end of 2009 Finanstilsynet had 246 full-time staff compared with 235 at the end of 2008. Fifty-two per cent of the full-time staff are women. Eighty-seven per cent of the staff hold a university degree or the equivalent.

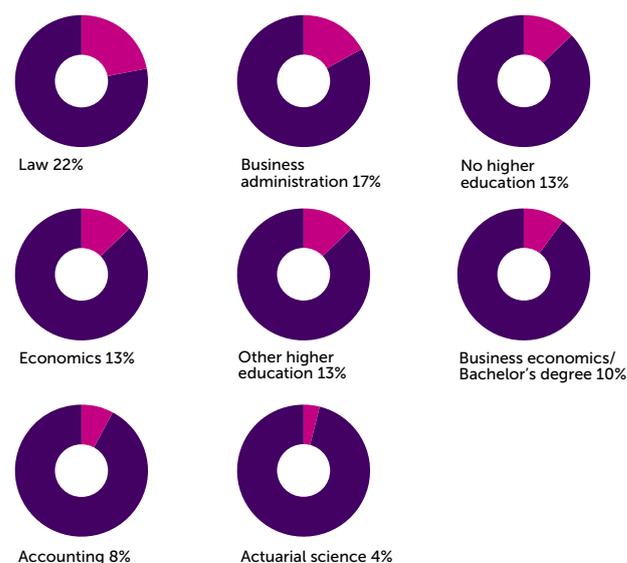
Women made up 43 per cent of Finanstilsynet's management team in 2009 and 48 per cent of all staff with managerial responsibilities. Women employees' pay measured 87.7 per cent of men's pay in 2009 compared with 88.5 per cent in 2008.

The gender equality effort is anchored in the work-environment and gender-equality committee, which is 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 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 discharge its tasks in a good and effective manner. More members of staff than previously wish to return to Finanstilsynet after taking leave of absence.

At the end of 2009 60 members of staff had solid experience (generally more than five years) from industries under supervision. Staff turnover in 2009 was 6 per cent compared with 10 per cent in 2008. 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.

Chart 3: Staff educational background as at 31.12.2009



Inclusive employment

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 and gender equality committee monitors sickness absence and the advisability of initiating measures. Sickness absence fell from 5.1 per cent in 2008 to 4.8 per cent in 2009. The swine flu pandemic caused an increase in short-term absence in autumn 2009.

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 underrepresented group is invariably called in for interview provided the qualification requirements are met.

Cases and case processing time

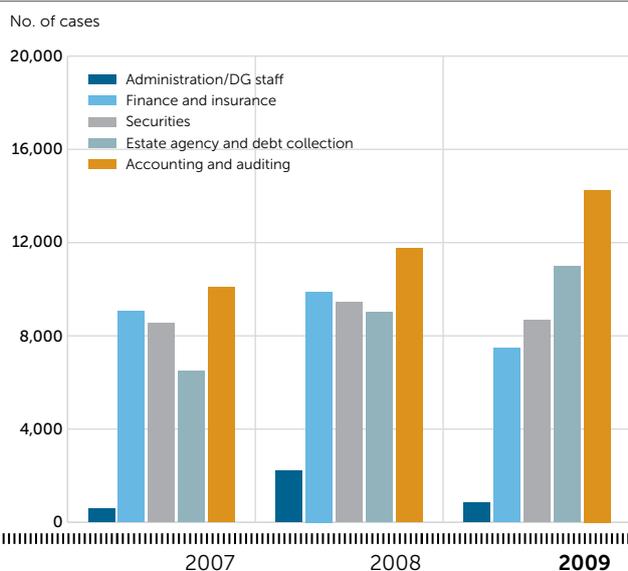
In keeping with Finanstilsynet’s strategy, specific targets are set for the time spent on a selection of administrative cases and for supervisory reports and resulting observations. The aim is to process 90 per cent of administrative cases within 30 days. A longer period is allowed for some types of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

Table 1: Case processing time at Finanstilsynet in 2009

	No. of cases	Target attainment
Total no. of cases with processing time target	4,049	65%
- Cases with 30-day deadline	3,174	78%
- Cases with deadline longer than 30 days	875	19% *
Supervisory reports	194	81%
Supervisory observations	181	78%

* Many 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 new appeal body.

Chart 4: Registered case documents – by sector*



Total number of cases	34,776	42,300	42,241
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* 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 2009 was roughly on a par with the 2008 figure.

The year 2009 saw a large increase in the number of case documents related to estate agency and debt collection, the reason being that all estate agents were required to apply for licence renewal under the new Estate Agency Act. A large increase was also seen in the audit and external accountancy areas. This was a consequence of the implementation of the Statutory Audit Directive, as a result of which any termination of an audit assignment had to be explained in writing to Finanstilsynet.

Document numbers fell in the finance and insurance area: fewer notifications were received of establishments of cross-border business out of and into Norway since the financial crisis had diminished interest in providing services outside institutions' core area. Activity in terms of structural changes was also low inasmuch as banks', finance companies', mortgage companies' and insurers' attention was focused elsewhere.

Efficiency improvements

An important part of the agency's efficiency drive has been to develop new and existing computer systems and solutions, both in

the supervisory areas and the administrative area. In the supervisory areas reporting and analysis systems are in focus, while in the administrative area new solutions have been introduced for budgeting and budget follow-up.

New office premises for Finanstilsynet

Finanstilsynet relocated to new office premises at No. 3 Revierstredet in the centre of Oslo on 18–21 December 2009. The move went according to plan, and office spaces and the ICT system were up and running when staff arrived for work in the new premises on Monday 21 December. The relocation had no effect on the agency's primary tasks.

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. In connection with the move to new premises, a special security agreement was drawn up with the new lessor, Norges Bank, which is responsible for the building's security. New routines and guidelines have been established for securing the office premises.

FINANCES

Expenditure

The Storting determines Finanstilsynet's budget as part of the government budget. The budget for 2009 originally totalled NOK 247.3 million. An additional appropriation of NOK 8 million was made comprising NOK 5 million to cover extra salary expenses, NOK 1.5 million for an ICT project to further develop a computer warehouse solution, NOK 1 million to develop a transaction reporting system and NOK 0.5 million to further develop Altinn reporting.

An additional NOK 1.8 million was appropriated in compensation for the public sector wage settlement. Including funds of just over NOK 8.2 million carried forward from 2008, the budget came to NOK 265.3 million. Finanstilsynet received an additional NOK 6.6 million in refunds of maternity and sickness benefits. The aggregate

disposable budget accordingly came to NOK 271.9 million, while aggregate expenditure came to NOK 266.7 million, an increase of 12.9 per cent from 2008. Total salary expenditure rose by 13.5 per cent, and expenditure on goods and services increased by 11.8 per cent. Finanstilsynet's aggregate expenditure was NOK 5.1 million less than disposable revenues. Unutilised revenues are carried forward to 2010.

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 26 May 2009 from the Office of the Auditor General on the accounts for 2008 had no adverse comments about the accounts or Finanstilsynet's implementation of the budget.

Table 2: Finanstilsynet's accounts

	2007	2008	2009
Salaries bill	134,216	154,593	175,516
Of which:			
Salaries and social costs (all positions)	129,511	150,756	169,745
Stand-ins/substitutes	3,817	3,144	4,975
Other emoluments (directors, consultants, other fees)	888	693	796
Goods and services	64,032	81,607	91,220
Of which:			
Operating expenses	24,047	35,558	43,957
Information	2,921	2,930	2,728
Travel and meeting attendance, subscriptions	6,513	7,173	7,863
Inspections and other supervisory work	2,280	3,795	3,754
Organisation development, management and competence development	4,953	4,671	4,318
IT expenditure	23,318	27,480	28,600
Total expenditure	198,248	236,200	266,736

Figures in NOK 1000s

(Preliminary accounts for 2009)

Comments

The salaries bill, in particular, was considerably higher in 2009. The increase, of NOK 21 million, is explained by staff increases and the general increase in pay. Operating expenses rose by NOK 8.4 million, not due to any general increase in operating expenses per se but to extraordinary outlays on relocation to new premises and purchase of furniture and equipment. The relocation expenses will be apportioned on 2009 and 2010, and the project is expected to be completed within budget. The increase in ICT expenses is related to higher 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 2008 and due for payment in 2009 was NOK 219.5 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 maternity and sick pay outlays. The levy proposed by Finanstilsynet for 2008 was approved by the Ministry of Finance on 27 May 2009 after prior consultation with the trade organisations concerned. Supervised entities liable to pay the amount levied for 2008 numbered 12,003 of which 70 were foreign branches. The largest category of supervised entities is accountants, numbering 8,314. The overall figure in 2007 was 11,823 entities. The apportionment of the levy among the various categories of supervised entities is shown in chart 5.

Chart 5: Levy distributed on supervised groups

Percentage of total levy

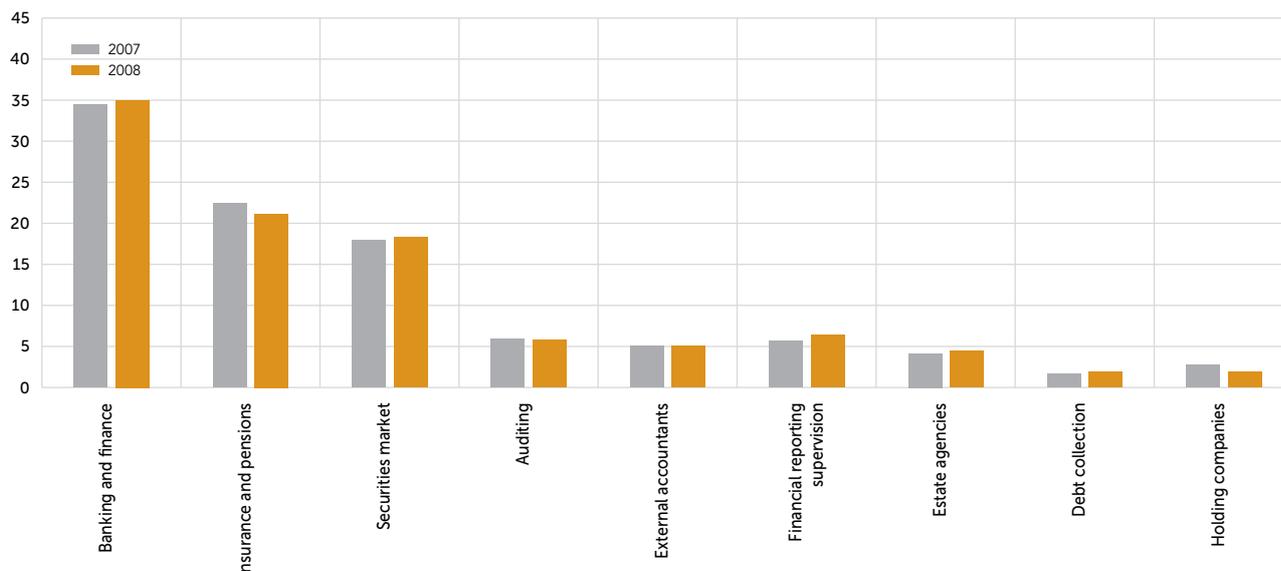


Table 3: Total levy as a percentage of the calculation base

Supervised groups	Calculation base	Percentage of calculation base	
		2007	2008
Credit institutions	Total assets	0.0023	0.0021
Insurance	Premium income	0.0360	0.0314
Investment firms	Income from investment and ancillary services	0.1261	0.1858
Management companies	Assets under management	0.0018	0.0025
Estate agency	Commission income	0.1499	0.2525
Debt collection	Debt collection proceeds	0.1692	0.1894
Auditors	Turnover	0.2319	0.2481

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 1,328 at the assessment for 2008). Expenditure on financial reporting supervision is in principle met by Oslo Børs, which then recovers its costs from the listed companies.

Resource input by area of supervision

Table 4 shows an increase in resource input from 2008 to 2009 equivalent to 18.7 full-time positions. The table shows resource input in the various areas.

Table 4: Resource input by area of supervision

	2007		2008		2009	
	FTEs	%	FTEs	%	FTEs	%
Banks	41.7	21.5	44.7	21.7	47.6	21.1
Finance companies	2.5	1.3	2.3	1.1	2.3	1.0
Mortgage companies	2.4	1.2	2.7	1.3	3.1	1.4
Insurers	26.3	13.6	25.4	12.3	31.0	13.8
Holding companies	3.5	1.8	3.2	1.6	3.1	1.4
Pension funds	6.1	3.1	7.0	3.4	6.3	2.8
Securities market	30.5	15.7	32.8	15.9	36.3	16.1
Estate agents	7.1	3.7	8.2	4.0	8.7	3.9
Debt collection	2.7	1.4	3.4	1.6	2.9	1.3
Auditors	9.5	4.9	8.8	4.3	12.1	5.4
Accounting rules et al.	0.6	0.3	0.1	0.0	0.2	0.1
Financial reporting	8.0	4.1	9.5	4.6	8.9	3.9
External accountants	6.9	3.6	8.6	4.2	9.2	4.1
Miscellaneous	2.2	1.1	3.3	1.6	4.2	1.9
Undistributed	43.6	22.5	46.3	22.4	49.0	21.8
Total	194	100	206.3	100	225	100

APPEAL PROCESSING – REGISTER OF COMPANY ACCOUNTS

Finanstilsynet has been the appeal body in respect of decisions by the Register of Company Accounts to turn down applications for remission of penalties imposed for late filing of annual accounts, annual reports and audit reports with the Register of Company Accounts. After being asked by Finanstilsynet to consider transferring this function to another body, the Ministry of Finance resolved that the Norwegian National Collection Agency should be assigned this function as from 1 January 2010.

As from the financial year 2007 penalties have also been imposed on entities other than private limited companies, public limited companies, mutual insurance companies and savings banks. Stricter enforcement of the filing deadline brought an increase in appeals. 810 appeals were processed in 2009 compared with 518 in 2008 and 262 in 2007. Finanstilsynet waived the late filing penalty completely or in part in 69 cases.

Imposition of late filing penalties prompted reactions from officers at foundations, among others, since such penalties make it more difficult for foundations to discharge their function. In Finanstilsynet's view, organisational form is not in itself a basis for penalty remission. The agency has none the less found reason to treat officers in

foundations differently than officers in other submitting agencies that receive late filing penalties based on solidary liability. Its view is supported inter alia by the fact that 2006 was the first year that late filing penalties were imposed on foundations, and that a number of their officers were unaware of the new regime. A further factor is that elected officers in foundations often hold their posts for idealistic reasons. Finanstilsynet accordingly in some cases exempted board members of foundations from solidary liability in respect of penalties imposed for the financial year 2006.

The Ministry of Finance asked Finanstilsynet to draw up a consultation paper proposing differentiated penalties for small foundations that file annual accounts with the Register of Company Accounts after the due date. The ministry circulated the paper for comment on 7 October 2009. At the ministry's behest, Finanstilsynet in November 2009 drafted a consultation paper on the legal basis for imposing late filing penalties in cases where annual accounts etc., submitted to the Register of Company Accounts are incomplete or flawed. The matter is under consideration by the Ministry of Finance.

104 outstanding cases were passed on to the National Collection Agency when it took over as appeal body on 1 January 2010.

KEY FIGURES AND DATA ON SUPERVISORY ACTIVITIES

Table 5: Figures for supervised entities as at 31.12.2009

	2005	2006	2007	2008	2009
Banks and financial institutions					
Savings banks	126	124	123	121	118
Commercial banks	14	15	16	18	20
Finance companies and mortgage companies	41	41	41	46	59
Foreign branches of Norwegian banks and other credit institutions	13	16	16	13	16
Norwegian branches of foreign banks and credit institutions	27	29	32	46	44
E-money institutions					
E-money institutions	5	4	3	3	3
Insurance					
Life insurers	6	9	10	11	12
Non-life insurers	46	44	44	45	45
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
Norwegian branches of foreign insurers	39	41	46	37	41
Insurance intermediaries ²	56	73	91	103	201
Private pension funds	93	91	86	81	75
Municipal pension funds	29	28	29	30	31
Pension schemes	22	19	17	15	9
Holding companies					
Holding companies	8	9	12	12	11
Securities institutions					
Investment firms ³	75	85	132	154	150
Norwegian branches of foreign investment firms	11	9	10	13	17
Fund management companies	21	23	23	22	26
Clearing houses	2	3	3	3	3
The Norwegian Central Securities Depository	1	1	1	1	1
Regulated markets, incl. stock exchanges	3	3	6	5	6
Auditors					
Auditors	5,495	5,567	5,670	5,777	5,943
Audit firms	569	730	789	825	820
External accountants					
External accountants	7,179	7,472	7,966	8,340	8,780
External accounting firms	2,632	2,652	2,691	2,676	2,693
Estate agency					
Estate agency firms	642	682	717	611	516
Lawyers' practices incl. estate agencies	1,213	1,355	1,324	1,307	1,346
Cooperative building associations	39	38	37	24	14
Debt collection					
Debt collection agencies	121	117	112	110	105
Debt purchase businesses	8	6	8	5	6

Finanstilsynet also oversees the financial reporting of some 280 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*)

	2005	2006	2007	2008	2009
Banks/finance	52	49	49	37	58
E-money institutions	–	1	–	–	–
Holding companies	1	–	–	–	–
Insurers	9	5	6	6	8
Insurance intermediaries	1	5	3	3	7
Pension funds	1	1	2	6	4
Investment firms	22	18	20	19	21
Other securities institutions (incl. fund management companies)	14	7	6	1	3
Auditors	52	52	22	29	47
External accountants	56	46	41	60	49
Estate agencies	22	40	51	66	30
Debt collection agencies	7	5	6	13	12
Data processing centres/IT providers	5	3	4	4	2
Other	–	1	–	–	–

* Twenty-two IT inspections were conducted, either singly or in conjunction with ordinary on-site inspections. Finanstilsynet also conducted 21 simplified IT inspections and processed six notifications received under the Payment Systems Act.

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

	2005	2006	2007	2008	2009
Cases pursuant to the Savings Banks Act (No. 1 of 24 May 1961)	71	71	53	46	93
Cases pursuant to the Commercial Banks Act (No. 2 of 24 May 1961)	21	27	7	7	18
Cases pursuant to the Financial Institutions Act (No. 40 of 10 June 1988)	131	149	119	140	222
Cases pursuant to the Insurance Activity Act (No. 39 of 10 June 1988)	50	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
Cases pursuant to the Guarantee Schemes Act (No. 75 of 6 December 1996)	–	–	–	–	–

Notes to the tables:

¹ There are 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. Entities engaged in accessory insurance agent business are included as from 2009 (92 firms).

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

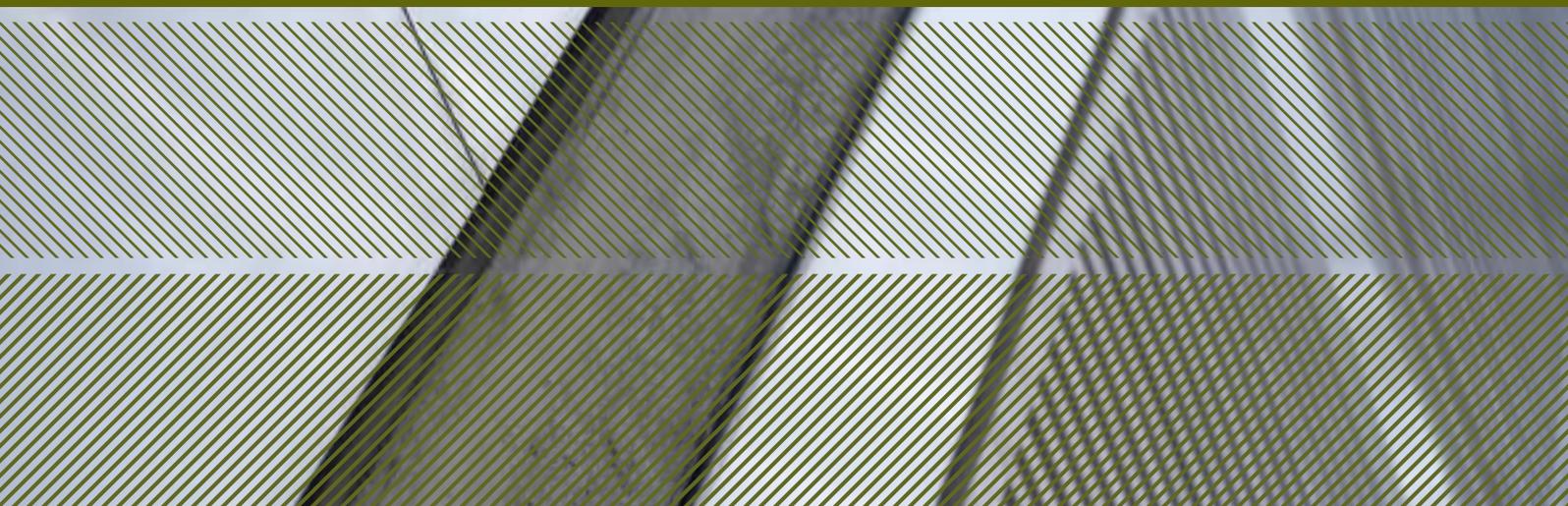
⁴ This figure includes decisions pursuant to both the new and the old Insurance Activity Act.

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* are 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. When a new main strategy and a new communication strategy are drawn up in 2010, the agency's information and communication planning will be guided by the new central government communication 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.

In 2009 the agency started work on a new user survey addressed to firms under supervision. User surveys are conducted at regular intervals to obtain feedback on Finanstilsynet's supervisory activity, competence, routines and information. The user survey conducted early in 2010 will be taken on board when a new main strategy is drafted.

MEDIA COVERAGE OF FINANSTILSYNET

Finanstilsynet has in general been well covered by the media, particularly media focusing on business and industry and the financial sector. In 2009 much of the media's coverage of Finanstilsynet focused on the agency's follow up of financial institutions and the situation in the Norwegian financial market in the wake of the financial crisis. The

agency's supervision of financial advisers and Acta Kapitalforvaltning also attracted media attention, as did cases in the auditing field – based on collaboration with the Tax Administration and ØKOKRIM. According to the media monitoring service Retriever, Finanstilsynet received 6,284 hits in 2009.

SEMINARS AND PRESENTATIONS

Finanstilsynet participates widely in seminars for trade organisations and institutions under supervision, and numerous presentations are given about 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 2009 Finanstilsynet, in cooperation with Oslo Børs, organised seminars for investment firms on topical issues in the securities sphere. The presentations are available on the agency's website.

CIRCULARS AND PRESS RELEASES ETC.

Twenty circulars were issued in 2009 compared with 14 in 2008, and superseded or obsolete circulars were removed. An overview of removed circulars was published in Circular 1/2010. As from 2010 circulars are no longer distributed on paper. Firms under supervision and other interested parties can subscribe to electronic editions on Finanstilsynet's website and receive alerts whenever a new circular is published.

annual report for 2008 and the reports entitled *The Financial Market in Norway 2008: Risk Outlook* and *Risk and Vulnerability Analysis*.

Finanstilsynet also issued 38 press releases, compared with 53 in 2009. One press conference was held at the end of February, to present the

A key channel for communication with the world at large is the large number of letters written by Finanstilsynet each year. A total of 14,652 letters were sent in 2009. A central aim is to write in a style that is clear and comprehensible to the recipients.

NEW WEBSITE LAUNCHED IN 2009

Finanstilsynet's new website was launched in May. The website is a primary channel for information from the agency 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 register of all licensed firms and an overview of market warnings against firms that are not licensed to engage in the business they are pursuing. When

the agency changed name on 21 December, the website's graphic interface was upgraded in keeping with the new visual profile.

The website, www.finanstilsynet.no, received 183,000 unique visitors in 2009, who accounted for a total of 450,000 visits. A new statistical tool put to use in conjunction with the launch of the new website renders visitor figures for 2009 incomparable with previous years.

DOCUMENT ACCESS AT FINANSTILSYNET

Finanstilsynet received a total of 565 requests for document access involving orders for 3,155 documents in 2009. Of these, 2,669 were in the public domain, 237 were distributed as public versions, while

248 were not released since their entire content was barred from publication. The great majority of access requests are e-mailed.

Table 8: Requests for document access

	2007	2008	2009
Orders placed	2,894	2,916	3,155
Not released	428	429	248

NEW NAME – FINANSTILSYNET

In March 2009 Kredittilsynet submitted to the Ministry of Finance a proposal to change the agency's name to Finanstilsynet in connection with the relocation to the centre of Oslo at the end of 2009. The rationale for the name change is that 'Finanstilsynet' is more accurate and better reflects the breadth of the agency's supervisory mandate. The new name is also more in line with equivalent agencies in other

Nordic countries (Finanstilsynet in Denmark, Finansinspektionen in Sweden and Finland), and with the English name. The Ministry of Finance supported the proposal and submitted the matter to the Storting on 24 April. After a positive recommendation was made by the Standing Committee on Financial Affairs on 4 June, the Odelsting chamber and the Lagting chamber of the Storting adopted,

on 11 June and 16 June respectively, the law amendments needed, inter alia in the Financial Supervision Act, to enable the name change to go ahead on 21 December 2009.

CONSUMER PROTECTION AND CONSUMER INFORMATION – WHAT IS FINANSTILSYNET’S MANDATE?

In May 2009, the agency forwarded to the Ministry of Finance the report from a pilot project entitled to *Kredittilsynet’s contribution to consumer protection and information*. The ministry was at the same time asked to clarify the agency’s mandate with regard to consumer protection and consumer information.

Consumer protection is directly and indirectly an important aim of large sections of the legislation administered by Finanstilsynet. However, in parts of the legislation, for example those dealing with financial stability and financial institutions’ solidity, long-term considerations often rank ahead of more short-term consumer considerations.

In both the media and other quarters, expectations as to what Finanstilsynet can and should achieve in some areas are greater than what is required by current legislation and the agency’s mandate, or what is feasible based on its funding. The agency’s annual report for 2008 describes its tasks in relation to consumer protection and consumer information (pages 84–87).

To provide the Ministry of Finance with a basis on which to consider possible changes to Finanstilsynet’s mandate, Finanstilsynet has sought to chart, and to provide an overall picture of, the status as regards consumer protection and information in the financial sphere in Norway. Particular emphasis is given to clarifying Finanstilsynet’s

present mandate in relation to other actors. A description is also given of consumer-oriented measures taken by financial supervisors in some other countries.

Finanstilsynet’s preliminary conclusion is that consumer protection in the financial area is relatively sound, but fragmented. For example, responsibility is split between three ministries: the Ministry of Finance, the Ministry of Justice and the Police and the Ministry of Children, Equality and Social Inclusion. Finanstilsynet accordingly recommends that any changes in its mandate should only be made after an overall assessment of the need for consumer protection and information in the financial sphere.

From Finanstilsynet’s vantage point, a concrete measure likely to promote a more cohesive regime would be to transfer responsibility for the two central consumer-oriented statutes in the financial area (the Financial Contracts Act and the Insurance Contracts Act) from the Ministry of Justice and the Police to the Ministry of Finance, alternatively to the Ministry of Children, Equality and Social Inclusion.

The pilot project and the report are inputs to the review of Finanstilsynet’s strategy in 2010. The report was circulated for comment by the Ministry of Finance in autumn 2009, and the matter is under consideration at the ministry. It is unclear when the Ministry of Finance will provide feedback on the inputs from Finanstilsynet.



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 is designed to promote solid financial institutions with good risk awareness, management and control. The aim is to ensure that financial service provision is in compliance with the regulatory framework and in the best interest of society and the users of financial services.



SUPERVISION AND MONITORING

Monitoring and analyses

Monitoring and analyses of developments in the economy and markets and of the situation in the financial sector are prerequisites for ongoing supervision of liquidity and financial strength of individual institutions. The analyses form the background 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. The analyses are also referred to in *Report for Financial Institutions* which is published 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 are published in the report *The Financial Market in Norway 2009: Risk Outlook*.

Norwegian banks' profitability and financial strength

The Norwegian economy and Norwegian banks have thus far emerged well from the financial crisis compared with other countries. The improvement in the international economy and international financial markets has also improved the situation for Norwegian banks, whose results in 2009 were somewhat better than in 2008. Having been low for a long period, losses rose somewhat in 2008, especially in the year's last quarter. In 2009 loan losses in the first nine months were slightly higher than 2008 levels but were still moderate. Concurrently banks' revenues from securities and financial instruments rose sharply, maintaining profit levels and compensating for the decline in net interest revenues and higher loan losses.

Banks significantly strengthened their capital adequacy in 2009 through profit retention and stock market launches. The Norwegian State Finance Fund also played a significant role for several banks. At the start of 2010 Norwegian banks' capital adequacy was deemed to be satisfactory by Finanstilsynet. Banks' actual capital needs are further detailed in a separate section on page 41.

Norwegian banks' liquidity situation posed a serious challenge in 2008 due to great uncertainty and reticence among investors and banks. A survey conducted early in 2009 showed that a majority of banks retained this sentiment. The government stimulus packages were seen as an important contribution to stabilising liquidity risk. Banks'

access to funding improved substantially through 2009. The supply of short-term funding was virtually normalised, and a considerable improvement was also seen in the markets for long-term funding. Finanstilsynet kept a close eye on banks' liquidity reports, and monitored liquidity risk against the background of those reports.

After showing a steep trend for several years, growth in lending by Norwegian banks slowed sharply in 2008 with the onset of the cyclical downturn. In 2009 growth in lending to corporates fell further, and was falling on a 12-month basis towards year-end. Growth in lending to retail customers concurrently picked up somewhat. The financial crisis and uncertainty about developments ahead prompted Finanstilsynet in January 2009 to ask the banks to comment on changes in credit practice and on the extent to which the liquidity and solvency conditions would affect the largest banks' ability to meet customers' borrowing needs in 2009. At the start of the year the general expectation was that growth in lending would be substantially lower in 2009 than in 2008, both to corporates and retail borrowers. However, the survey suggested that the solvency and liquidity position of most banks would enable them to meet the demand expected in 2009, and that normal lending activity could continue.

While the slower growth in lending to corporates was primarily a result of lower demand due to lower activity levels in the economy, it was also a result of tighter credit practice caused by many banks' higher pricing of risk related to corporates' business. Norwegian business and industry has been hit both by the impact of the recession among our main trading partners and by a sharp slowdown in domestic demand in 2009. In the course of autumn 2008 prospects for the corporate sector deteriorated, but profitability nonetheless picked up slightly in 2009. However, the bankruptcy rate continued to rise, and firms' debt-servicing ability was further impaired as a result of debt growth, high funding costs and lower sales revenues. In autumn 2009 Finanstilsynet conducted a survey of banks' exposures and risk assessments of loans to selected industries, including shipping and property management.

In recent years household sector finances have been coloured by an increasing debt burden, and high loan-to-value ratios on home mortgage loans - factors which have increased the household sector's vulnerability in the event of an economic setback. Growth in credit to households held up in 2009. According to a survey of banks' practice in 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. Prompted by the turbulence in financial markets and uncertainty as regards banks' credit practice with respect to home loans, Finanstilsynet supplemented the

2009 autumn survey with a survey conducted in the spring of that year, which showed a substantial decline in loans granted with high loan-to-value ratios. The autumn 2009 survey gave only partial confirmation of a more sober practice, and the proportion of high loan-to-value ratios was back to the same high level as previously.

Each year since 2004 TNS Gallup, on commission from Finanstilsynet, has conducted a survey among banks' home-loan borrowers. The survey has provided Finanstilsynet with significant information on the purpose of such borrowing. It has also provided information able to throw light on the competitive situation in the market for home loans.

Finanstilsynet has for several years followed the banks' practice as regards debt financing of securities investments. The 2009 survey charted the extent, and banks' handling of, loans secured by financial instruments. The volume of such lending is traditionally low in Norway, and overall exposure remains limited.

Liquidity monitoring

Liquidity risk has been monitored by general on-site inspections and by special review of liquidity risk at seven individual banks. At the turn of 2009 eight banks that had reported figures giving indications of high liquidity risk were asked to take specific steps to reduce risk or improve their liquidity management. Additionally, in the first half of 2009, regular overviews were obtained and assessments made of customer deposits at 25 banks. Finanstilsynet was in regular contact with large banks and some other banks to obtain their views on developments in capital markets and prices and their comments on the liquidity situation.

Liquidity risk and liquidity preparedness were a theme at the quarterly meetings held with the largest banks in 2009. Several regional banks revised their internal targets in 2008 and 2009 by extending the period they intend to survive without external supply of capital.

Finanstilsynet collaborated closely on liquidity monitoring with Norges Bank in 2009.

Revision of liquidity indicators

Finanstilsynet employs two liquidity indicators to monitor liquidity risk at individual banks and mortgage companies. The indicators show what proportion of institutions' illiquid assets is long-term financed by, respectively, residual maturities exceeding one year, and one month. The indicators are calculated on the basis of data reported to Finanstilsynet. Each bank's risk level is assessed based on average indicator values for a reference group comprising of 13 of the largest Norwegian banks.

In 2009 Finanstilsynet revised the model used to calculate the liquidity indicators with effect from and including the first half of 2009. In the calculation of the liquidity indicators allowance is made for banks' assets in residential mortgage companies, other banks and other mortgage companies. Account is also taken of the government funding measures prompted by the financial crisis. These measures comprise changes in Norges Bank's lending rates and banks' opportunity to exchange residential bonds against government securities.

A working paper entitled "Calculation model for Finanstilsynet's liquidity indicator 1 and 2" is available on Finanstilsynet's website.

On-site inspections

On-site inspections are important in identifying problem areas at individual banks in order to start a dialogue with the management team and board of directors at the earliest possible stage. Finanstilsynet applies a risk-based supervisory methodology based on international supervisory standards.

On-site inspection of banks is based on the use of risk modules developed by the agency. The modules are a framework for determining risks and risk level at the institution and the institution's management and control of risk. In the case of banks use is made of modules for credit risk, market risk, liquidity risk, operational risk and a module for overall governance and control. The module for liquidity risk was updated in 2009 as a result of Finanstilsynet's revision of its liquidity indicators. The modules can be accessed on Finanstilsynet's website.

Fifty-eight on-site inspections, including seven IT inspections and six IRB follow-ups, were carried out at banks, finance companies, mortgage companies and foreign branches in 2009. The 58 inspections include inspections conducted in conjunction with other Nordic supervisors at Fokus Bank, DnB NOR and Nordea. Finanstilsynet gave special priority to the larger banks where separate inspections related to the shipping segment and the Baltics were also carried out.

Credit risk was a central theme at many inspections in 2009. In the present phase of the economic cycle, attention has focused primarily on banks' own monitoring and follow-up systems to assess their ability to capture changes in customers' financial position and whether they have established action plans for customers who encounter financial problems. Asset assessments, including review of individual exposures and securities holdings, were undertaken, as well as assessments of valuation practice as regards loans and securities.

Monitoring of liquidity risk was also a priority task for Finanstilsynet in 2009; see the above account.

Six on-site inspections were conducted at IRB banks, which were asked to account for important items related to operations, quality assurance and development of the IRB system.

Follow-up inspections were conducted at five relatively recent bank start-ups.

As a part of the round of inspections in 2009, compliance with the money laundering legislation was specifically assessed at nine banks. Flawed ID checks were brought to light at four banks, and at one bank breaches of internal ethical guidelines related to documentation of the deposit put up in a loan application were brought to light.

Finanstilsynet held meetings with the largest banks in connection with their quarterly results presentations in 2009, at which the themes were the solvency situation, liquidity situation, credit risk picture and accounting results.

In 2009 Finanstilsynet held meetings with the Norwegian branches of SEB, Danske Bank A/S (Fokus Bank), RBS and Handelsbanken AB. The three first-mentioned are the largest foreign bank branches established in Norway. The meetings were held to update the agency on the business in Norway and at group level. The banks gave an account of their quarterly financial statements and updated Finanstilsynet on any changes in group structure since the previous meeting.

Calculating minimum regulatory capital

Pillar 1 of the capital adequacy framework (Basel II) which was introduced in Norway in 2007 contains rules for the calculation of minimum capital charges for credit risk, market risk and operational risk. Where credit risk is concerned, banks can either calculate the charge using a standardised method with given risk weights, or apply to Finanstilsynet to use an internal ratings-based (IRB) approach. IRB applications are processed in accordance with procedures and assessment criteria prepared by the Committee of European Banking Supervisors (CEBS).

As of 31 December 2009 the following banks were authorised to use the foundation IRB approach: DnB NOR Bank ASA, Nordea Bank Norway ASA, SpareBank 1 Nord-Norge, SpareBank 1 SR-bank, SpareBank 1 Midt-Norge, Sparebanken Vest and Bank 1 Oslo. In the case of all the above banks bar one, authorisation refers to the foundation IRB approach (FIRB). DnB NOR is introducing the advanced IRB approach (AIRB) in stages: in 2009 it received approval for an AIRB model for the corporate market. Some mortgage companies and finance companies have also received IRB approval, the concrete models first being approved for use in one or more owner institutions. This applies to DnB NOR Boligkreditt AS, SpareBank 1 Boligkreditt,

Sparebanken Vest Boligkreditt, Nordea Eiendomskreditt and Nordea Finans Norway.

The floor designed to curb reductions in the level of IRB banks' regulatory capital in the period 2007–2009 is to be retained by both the Basel Committee and the EU. The EU has opted for an extension to the end of 2011. According to this floor the capital requirement may not fall below 80 per cent of the requirement that would have applied under Basel I.

Banks' actual capital needs (ICAAP)

In addition to calculating the minimum own funds required under Pillar 1, institutions are required under Pillar 2 to conduct an Internal Capital Adequacy Assessment Process – ICAAP – to determine their actual need for capital.

The ICAAP capital requirement is designed to cover risks not included in the capital requirement calculated under Pillar 1. It also covers risks arising from the fact that risk and capital needs are quantified using inherently uncertain methods and data. Institutions must recognise that capital needs have to be future-oriented, and take into account business plans, growth and access to capital markets. The capital base must be sufficient to live through an economic downturn accompanied by negative results and problems in obtaining fresh capital.

All Norwegian banks are required to conduct an ICAAP on an annual basis.

Supervisory authorities are required to evaluate banks' ICAAP process and the results arrived at by the individual bank (Supervisory Review Evaluation Process, SREP).

In 2007 SREPs were conducted of six IRB banks and seven other banks that had opted for the standardised method for reporting credit risk. In 2008 Finanstilsynet gave its response to 137 banks and 17 finance companies and mortgage companies. Evaluation focused on the management board's responsibility for the process, on actual tier 1 capital adequacy and the target tier 1 capital adequacy ratio. In 2008 Finanstilsynet drew attention to matters related to the banks' own assessment of capital needs. About 70 per cent of the institutions were asked to consider steps to strengthen their actual capital adequacy and/or raise their tier 1 capital adequacy target.

In 2009 the priority was to dialogue closely with institutions which, in the feedback given after the previous year's ICAAP process, had been instructed to consider raising their actual capital adequacy ratios. In March 2009, 15 banks received letters from Finanstilsynet citing low tier 1 capital adequacy ratios and reminding them that the agency, in

connection with the 2009 evaluation of their ICAAP process, would consider ordering them to strengthen their capital adequacy.

A total of 104 ICAAPs were evaluated by Finanstilsynet in 2009. Again emphasis was given to management board responsibility for the process, and to actual capital adequacy ratios and tier 1 capital adequacy targets. More than 20 banks were subsequently asked to take steps to strengthen their capital adequacy in the course of 2009.

The main conclusion is that banks acknowledged the need to strengthen their capital base and are now taking appropriate steps in the shape of stock market flotations or recourse to the State Finance Fund. The establishment of the State Finance Fund has had a positive impact, for one thing by bringing calm to the issue of access to capital. There was no need to issue formal orders in 2009, and Finanstilsynet has underlined the banks' own responsibility for information to the market on action taken by them.

Banks not required to submit ICAAP documentation in 2009 were asked to run their ICAAPs in the normal manner. Some were evaluated in conjunction with ordinary inspections.

Each year Finanstilsynet prepares "overall risk assessments" (ORAs) of the largest banking conglomerates as a part of the ICAAP evaluation. The ORAs are internal analyses for the purpose of comparing risk exposures at the largest banks and form part of the agency's ICAAP evaluation (SREP).

Disclosure of financial information

The capital requirements regime regulates (in Pillar 3) institutions' publication of information on their capital and risk exposures. In 2009 Finanstilsynet published results of a review of reports from

banks authorised to apply the foundation IRB approach. Its conclusion was that these reports provided a good basis for compliance with the regulations, although several lacked information on some key points. Further development of the reports will raise their information value to the market, in part because there is still much information on banks' risk exposures and risk profile which is not competitively sensitive and could therefore be included in Pillar 3 reporting.

Reporting to Finanstilsynet

Institutions' reporting is an important basis for analyses and on-site inspection. A complete overview of current reporting requirements is available on the agency's website.

Basel II brought a major reorganisation of capital adequacy reporting by banks, finance companies, mortgage companies and holding companies in 2008, when Finanstilsynet introduced a reporting regime based on EU-wide Guidelines on Common Reporting (COREP). In 2009 a technical solution for COREP reporting was further developed, based on the XBRL reporting standard, which is recommended by CEBS. The technical solution is reaching completion. Changes are under preparation in COREP in 2010 as a result of changes in the capital adequacy regime.

Several changes were made to the system for public financial reporting by banks, finance companies and mortgage companies (ORBOF). Further, improvements were introduced in the industrial classification under ORBOF, making it simpler to track exposures to various risk-exposed industries. Changes relating to liquidity reporting are described in the section on liquidity monitoring on page 40. A switch is being prepared to the pan-European guidelines on financial reporting (FINREP) by banking conglomerates, the first reporting being likely in the first quarter of 2011.

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 2009 included the following:

- Warren Bank AS was authorised to establish a limited banking operation.
- KLP Bank was authorised to operate as a commercial bank. The bank was set up with an intermediate holding company, KLP Bankholding AS.
- Terra Kortbank AS was authorised to operate as a commercial bank. The bank will until further notice be subject to a minimum capital requirement of 10 per cent of a basis weighted pursuant to the rules in effect at any time.
- SpareBank 1 Nord-Norge (SNN) was granted a licence to set up a subsidiary in Russia. The bank acquired 75 per cent of Agrokredbank, while SNN's partner, Bank Tavrechesky, acquired the remaining 25 per cent. A condition is that the bank is taken over with no other activity or assets than are needed to maintain the Russian banking licence. A further condition is that SNN's management board undertakes a special review of risk factors related to the purchase of an existing Russian bank.

- Sparebanken Møre and Tingvoll Sparebank were authorised to merge, with Sparebanken Møre as the acquiring bank. Permission was concurrently given to wind up Tingvoll Sparebank and establish a foundation, Sparebankstiftelsen Tingvoll.
- Sparebanken Vest and Sauda Sparebank were authorised to merge, with Sparebanken Vest as the acquiring bank. Permission was concurrently given to wind up Sauda Sparebank and establish a foundation, Sparebankstiftelsen Sauda.
- Volkswagen Møller BilFinans AS was authorised to operate as a finance company.
- Kredinor Finans AS was authorised to operate as a finance company.
- Gothia Finans AS fikk was authorised to operate as a finance company. This authorisation applies to the buying of accounts receivable (factoring).

As a result of the stimulus package offered by the Ministry of Finance and Norges Bank in autumn 2008, several banks/groups applied to set up special investment vehicles (SIVs) able to issue covered bonds. By the end of 2009 the following SIVs had received the requisite licence:

- Sparebanken Øst Boligkreditt AS, established by Sparebanken Øst
- Helgeland Boligkreditt AS, established by Helgeland Sparebank
- Fana Sparebank Boligkreditt AS, established by Sparebanken Fana
- Gjensidige Bank Boligkreditt AS, established by Gjensidige Bank ASA
- Verd Boligkreditt AS, established by Sparebanken Vest, Haugesund Sparebank and Spareskillingsbanken
- Eiendomskreditt AS
- SpareBank 1 Næringskreditt AS, established by SpareBank 1 SMN, SpareBank 1 SR-Bank, Sparebanken Hedmark, SpareBank 1 Nord-Norge
- DnB NOR Næringskreditt AS, established by DnB NOR Bank ASA
- Storebrand Eiendomskreditt AS, established by Storebrand Bank ASA
- KLP Kommunekreditt AS, established by Kommunal Landspensjonskasse (KLP) with KLP Bank AS as owner

Including previously awarded licences, 22 mortgage companies were issuing covered bonds at the end of 2009.

The licence register available at Finanstilsynet's website gives a complete overview of undertakings licensed to operate banking/financing business.

Supervision of ownership of financial institutions

In 2009 the following authorisations were issued pursuant to the Financial Institutions Act's rules on supervision of ownership of financial institutions:

- Western Union Ireland Holding Ltd's acquisition of a 100 per cent stake in Fexco Money Transfer Norway AS
- SpareBank 1 SR-Bank and SpareBank 1 SMN's acquisition of respectively 33.77 per cent og 20.17 per cent of the shares of SpareBank 1 Boligkreditt AS
- SpareBank 1 Gruppen AS's acquisition of a 100 per cent stake in SpareBank 1 Gruppen Finans Holding AS
- SpareBank 1 Gruppen Finans Holding AS's acquisition of a 100 per cent stake in SpareBank 1 Factoring AS, Sparebanken Factoring AS and SpareBank 1 LTO AS
- Pitney Bowes Norge AS's acquisition of a 100 per cent stake in Pitney Bowes Finans Norge AS
- Gaia Insurance AS's acquisition of a 100 per cent stake in NEMI Forsikring ASA
- KLP Banken AS's 100 per cent stake in Kommunekreditt Norge AS. Kommunekreditt Norge AS was acquired from Eksportfinans ASA
- Valset Invest AS's acquisition of a 20 per cent stake in Bank 2 ASA
- Skogbrand forsikringsselskap's acquisition of an 11.67 per cent stake in Landbruksforsikring AS
- SpareBank 1 SMN's acquisition of a 40 per cent stake in BNBANK ASA
- The following enterprises were authorised to acquire a stake in Bank 1 Oslo AS: SpareBank 1 SMN (19.5 per cent), SpareBank 1 SR-Bank (19.5 per cent), SpareBank 1 Nord-Norge (19.5 per cent), Samarbeidende Sparebanker AS (19.5 per cent), Sparebanken Hedmark (12 per cent) and the Norwegian Confederation of Trade Unions (LO) (10 per cent)
- Landkreditt SA's acquisition of a 55.88 per cent stake in Landbruksforsikring AS
- Sparebanken Vest's acquisition of up to 20 per cent of the shares of the shares of Voss Veksel- og Landmandsbank ASA
- Voss Sparebank's acquisition of up to 20 per cent of the shares of Voss Veksel- og Landmandsbank ASA

In addition licences were granted to establish various mortgage companies. In 2009 new provisions on supervision of ownership in the event of acquisition of a qualifying stake in financial institutions were added to the Financial Institutions Act; see page 47.

Foreign branches' membership of the Norwegian Banks' Guarantee Fund

Finanstilsynet approved the Norwegian Banks' Guarantee Fund decision to admit Skandiabanken AB NUF and Handelsbanken AB NUF as members of the Fund. Skandiabanken joined on 10 February 2009, Handelsbanken on 29 April 2009.

Measures in 2008–2009 related to the financial crisis

2008 and 2009 saw a greater number of meetings held with managements at the larger banks at which the key themes were liquidity, risk, capital situation and lending capacity. The frequency of meetings with the larger insurance companies was also intensified. Monitoring of and preparedness for potential problems at smaller financial institutions was heightened.

Frequent tripartite meetings were held between the Ministry of Finance, Norges Bank and Finanstilsynet for the exchange of information on and analyses of the situation in the financial markets, and to discuss possible responses and promote crisis management preparedness. The agency also provided information on the situation in the financial sector by means of numerous presentations and lectures and publication of reports and analyses.

Finanstilsynet intensified its monitoring of liquidity in 2008 and 2009 through its contacts with liquidity managers at the larger banks, inspections and extraordinary reporting, including reporting of movements in large customer deposits. Norges Bank and Finanstilsynet held regular meetings.

The agency examined and provided feedback on all banks' risk exposures and capital positions in 2009, and on all larger and most smaller banks in 2009. Many banks were asked to raise their capital targets and capital adequacy, in part with a view to their ability to maintain normal lending activity.

The winding up of the crisis-stricken Icelandic banks in Norway, Kaupthing and Glitnir, was achieved without detriment to the Norwegian financial market or depositors.

Finanstilsynet furnished the Ministry of Finance with proposals for measures and comments ahead of the establishment of the 'swap' arrangement (Bank Package I) and the creation of the Norwegian State Finance Fund (Bank Package II). The agency also drew up regulations for the State Finance Fund governing capital contributions made by the Fund through the acquisition of tier 1 capital instruments issued by banks.

Up to 30 September 2009 Norwegian banks that met the requirement as to tier 1 capital by a good margin were entitled to apply for a capital infusion in the form of hybrid equity and/or preference capital in conformity with the regulations governing the State Finance Fund. Finanstilsynet decided whether a bank met the requirement as to tier 1 capital by good margin and its eligibility for a capital infusion from the Fund. Thirty-eight confirmations of eligibility were issued in the application period.

As a result of Bank Package I, launched in autumn 2008, a number of banks applied for permission to set up special investment vehicles (SIVs) able to issue covered bonds. Finanstilsynet issued a total of 16 licences to set up such companies after October 2008. By the end of 2009, 22 SIVs were issuing covered bonds.

Finanstilsynet participated in a number of international bodies where reforms of international rules prompted by the financial crisis were discussed. Finanstilsynet has started preparing for the implementation of the changes in international rules. See *International activities*, page 94.

Kaupthing Bank NUF into public administration

Upon Finanstilsynet's recommendation, the Ministry of Finance on 12 October 2008 put Kaupthing Bank hf.'s Norwegian branch into public administration. Finanstilsynet appointed on the same day an administration board to oversee the winding up of the business.

By the end of 2009 all depositors had received full cover for funds on deposit with the bank. NOK 380 million was advanced by the Norwegian government on behalf of the Icelandic deposit guarantee scheme, while the Norwegian Banks' Guarantee Fund disbursed about NOK 800 million. Both amounts were refunded in their entirety from the resources of the estate.

REGULATORY DEVELOPMENT

Capital adequacy and liquidity

The Capital Requirements Directive – directives 2006/48 and 2006/49 – were transposed into Norwegian legislation with effect from 1 January 2007. It is widely acknowledged that this body of rules has significant shortcomings, and the rules, which are paralleled in recommendations from the Basel Committee (Basel II), are now being thoroughly analysed and discussed. There is nonetheless a clear consensus among central banks and supervisory authorities that Basel II should continue, but be strengthened and further developed. Despite their shortcomings, the rules have brought improvements. Norwegian banks have built up internal risk-assessment and control systems of significantly higher quality than previously. While analyses and discussions related to possible changes in the rules take place inter alia under G-20 auspices, the principal forums are the Basel Committee and the EU. Below are discussed:

- (a) Rule changes bearing directly on Norwegian institutions, i.e. mainly EU directives already, or highly likely to be, adopted. These directives have an implementation deadline of 31 October 2010 and are to enter into force on 31 December 2010.
- (b) Proposals for future changes and announcements of further changes put forward in a consultation document from the Basel Committee in December 2009 ("Strengthening the resilience of the banking sector").

a) EU directives to be introduced in 2010

"Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009", known as CRD II. This directive:

- i) Revises requirements on the quality of own funds by means of maximum limits for hybrid capital and overarching requirements on characteristics of hybrid and tier 1 capital. The requirements will be elaborated in guidelines issued by CEBS.

- ii) Clarifies the division of responsibilities between home country and host country. Rules on supervisory colleges are designed to promote uniform supervisory practice, and to ensure cooperation on supervision of major cross-border banking groups and the involvement of the host country when dealing with systemically important branches in the context of crisis management.
- iii) Strengthens the supervision of institutions' liquidity. Supplements have been made to the current directive's rules on routines for management of liquidity risk and requirements as to matters to be assessed by the supervisory authorities.
- iv) Tightens rules governing large exposures, in part by removing a number of national options, including the maturity-based exemption provisions in respect of interbank exposures. Uniform reporting requirements are to be introduced as from 31 December 2012.
- v) Strengthens provisions in the area defined in CRD as securitisation. This does not apply to covered bonds.

The EU Commission's proposed directive of 13 July 2009, known as CRD III. This proposes:

- i) Higher requirements where the capital requirement in the trading portfolio is calculated using internal methods, i.e. the value-at-risk method.
- ii) Further provisions concerning securitisation, including stricter treatment of resecuritisation positions, i.e. securitisations with other securitisations as the underlying.
- iii) That institutions should have in place a remuneration policy adhering to principles of good risk management and that this policy should form part of the Supervisory Review Evaluation Process (SREP). This requires Finanstilsynet to evaluate the institution's capital assessment processes.

b) Consultation documents from the Basel Committee concerning capital and liquidity requirements

A proposal is put forward to strengthen global capital and liquidity regulation. The Basel Committee has concurrently published a document concerning liquidity rules: "International framework for liquidity risk measurement, standards and monitoring". The aim is to strengthen the banking sector's ability to withstand financial and economic shocks so as to ensure that stress in the financial sector does not affect the real economy.

Where liquidity is concerned, the Basel Committee proposes minimum quantitative liquidity requirements. The two standards *Liquidity Coverage Ratio* and *Net Stable Funding Ratio* focus, respectively, on the importance of maintaining a holding of high-quality liquid assets to survive a stress period of 30 days, and the importance of stable, long-term (above one year) funding sources. The Committee has also developed common indicators for monitoring of liquidity risk designed to better enable supervisory authorities to identify and analyse the level of liquidity risk in a bank and in the banking system in general.

In the capital regulation document, the Committee makes recommendations intended to:

- i) Strengthen the quality etc. of banks' capital through stricter requirements on loss absorption in a going concern, increased international harmonisation and improved information to the market on the composition of each bank's capital.
 - ii) Cover further risks (partly incorporated in CRD III), for example by strengthening the rules on counterparty risk when using the Internal Model Method; these rules are designed to provide capital requirement incentives to use a recognised clearing house where OTC derivative contracts have been entered into.
 - iii) Supplement the risk-based capital requirement with a leverage ratio to dampen debt build-up in the banking sector and to avoid destabilisation that may result from sudden debt reduction.
 - iv) Reduce procyclicality and promote use of countercyclical buffers.
- The Committee states that it is too early to decide whether Basel II is proving more cyclical than expected, and cites the supervisory authorities' existing opportunities for achieving capital stability under both Pillar 1 and Pillar 2. The Committee announces studies of various proposals related to probability of default (PD) in the use of internal models.

- The Committee supports the initiative from the International Accounting Standards Board (IASB) to apply the *expected loss model* instead of the *incurred loss model* for loss provisions.
 - The Committee puts forward a proposal to promote the build-up of capital buffers in good times which can be drawn on when losses are incurred. It proposes requirements as to profit retention in cases where that part of banks' buffer that is surplus to the minimum requirement is insufficient. It proposes establishing upper and lower bands for capital buffers in excess of the minimum requirement. Where a bank has capital above the upper band, no retention will be required, whereas the degree of retention rises the closer actual capital falls towards the lower band.
 - The Committee heralds the preparation of proposals giving supervisory authorities in the respective countries the opportunity to apply some measure of discretion and to revise upwards the above-mentioned bands for capital buffers in times where there is a substantial risk of excessive credit growth. Work is under way on identifying suitable macro variables for use in such a framework.
- v) Handle system risk and mutual dependence in the financial system. The Committee announces its intention to review proposals in the first half of 2010, which will include assessing the merits of introducing extra capital requirements for system-important institutions.

The Basel Committee will in the first half of 2010 conduct a comprehensive study of the proposals for new rules on capital and liquidity in which banks will report capital and liquidity requirements etc to enable the effects of the proposals to be carefully considered in the second half-year. A corresponding calculation study will be conducted in Europe under CEBS auspices. The Basel Committee's plan is to present a fully complete new body of rules towards the end of 2010 for introduction towards the end of 2012.

Norwegian Banks' Guarantee Fund and deposit insurance

In 2008 the Ministry of Finance asked Finanstilsynet to consider the need for amendments to the Guarantee Schemes Act. The assignment included an assessment of issues related to moral hazard and information about the depositor protection guarantee. Finanstilsynet set up a working group which forwarded its evaluation to the ministry in April 2009. Finanstilsynet's input was forwarded to the Bank Law Commission for further consideration.

On commission from the Ministry of Finance, Finanstilsynet also drafted a Norwegian consultation response to the EU Commission in connection with changes to Directive 94/19/EC on deposit guarantee schemes. In its draft Finanstilsynet stated that in Norway's view a total harmonisation of cover levels at EUR 100,000 would have detrimental consequences for the country. A review of responses from other countries subsequently showed that Norway was virtually alone in holding this view. Finanstilsynet will follow further developments.

Supervision of ownership of financial institutions

Amendments to the provisions of the Financial Institutions Act governing supervision of ownership in respect of qualifying holdings acquired in financial institutions entered into force on 1 July 2009. The scope for discretionary judgement in fit-and-proper testing is reduced. Moreover, shorter time limits are set for case-handling. The amendments were needed in order to transpose into Norwegian financial legislation the EU directive concerning procedural rules and evaluation criteria for prudential assessment of acquisitions and increase of holdings in the financial sector.

Measures to combat money laundering and financing of terrorism

Private and public sector measures to combat money laundering and financing of terrorism were evaluated by the Financial Action Task Force (FATF) in 2005. After this evaluation Norway was placed on the regular FATF follow-up process, which included reporting back to the FATF on actions taken. In June 2009 Norway was removed from the follow-up process. Actions taken by Norway include the passage of a new act and regulations setting out measures against money laundering and financing of terrorism which entered into force on 15 April 2009. Key obligations under the new rules relate inter alia to customer checks that go significantly further than identity checks under the previous body of rules; registration and retention of data; the obligation to investigate and report suspicious transactions; and internal control and communication routines. A guide to the new body of rules is available in Finanstilsynet's circular 8/2009 and at the website *Hvitvasking.no*, established jointly by ØKOKRIM and Finanstilsynet.

Payment Services Directive

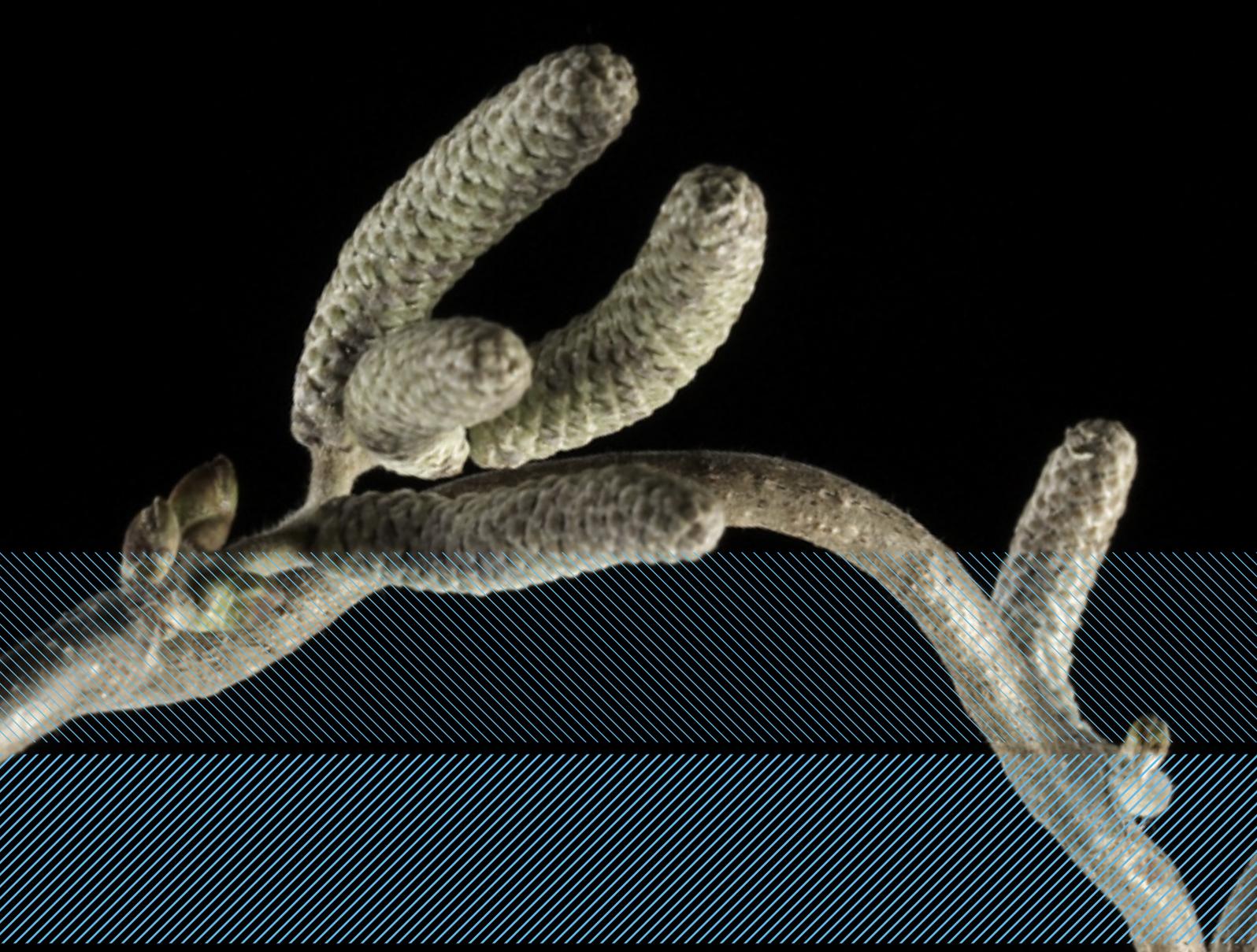
The Payment Services Directive entered into force on 1 November 2009 in the EU/EEA. The Norwegian amendments to Norway's Financial Contracts Act, which transpose the private-law aspects of the directive, entered into force on the same date. The directive's regulation of institutions has thus far not been implemented in Norway and is expected to be considered during the Storting's spring session 2010. Since Norway has made a constitutional reservation in the parliamentary EEA Committee, Norway will not be obliged to implement the directive before this reservation is waived. Nor will Norway be obliged to accept other EEA states' notifications of undertakings wishing to pursue business in Norway in conformity with the directive. Finanstilsynet received several notifications of cross-border activity into Norway as early as 1 November. Finanstilsynet notified the supervisory authorities concerned of Norway's constitutional reservation, stating that it give notification once the directive is implemented in Norwegian law.

NOU 2009: 2 *Forms of capital and organisation in the savings bank sector*

New legislation on capital and forms of organisation in the savings bank sector entered into force on 1 July 2009. The new legislation regulates key issues related to structural and corporate changes in savings banks and other financial institutions not organised as limited liability companies. It opens the way for structural changes, subject to limitations.

Moreover, the rules governing savings banks' primary capital certificates (now termed equity capital certificates) and other capital instruments conferring owner rights that are issued by financial institutions not organised as limited liability companies, are modernised.

Finanstilsynet issued a consultation response to the new legislation in 2009. After the act entered into force, Finanstilsynet considered two cases concerning merger and winding up of savings banks, viz. the merger of Sparebanken Møre and Tingvoll Sparebank and the merger of Sparebanken Vest and Sauda Sparebank. See also the account of licensing and dispensation cases, page 42–43.



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. 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 insurance companies and non-life insurance companies, 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*. See Finanstilsynet's website for further information. Overall assessments of the situation and of various risks faced by Norwegian financial institutions in light of developments in the economy and markets are published in the report *The Financial Market in Norway 2009: Risk Outlook*.

Finanstilsynet met regularly with the five largest life insurers in connection with their quarterly accounts presentations in 2009. Themes addressed were the risk situation and accounting results. The issue of allocations to supplementary provisions and pricing of the interest guarantee were discussed. Meetings were also held with the largest non-life insurers in connection with their presentation of the annual accounts.

Insurance companies' results largely reflect the trend in the securities markets. The stock market recovery in 2009 made a positive contribution to insurers' and pension funds' results. Life insurers in particular had reduced the equity component in their balance sheets substantially in 2008, and in addition entered 2009 with low buffers resulting in less flexible asset management. Equity components at the end of 2009 were still lower than at the end of 2007.

Finanstilsynet follows developments at insurance companies by means of stress tests. As from 2008 almost all insurance companies, and the largest pension funds, report stress tests to Finanstilsynet on a quarterly basis. The results of the stress tests are followed up in relation to individual institutions, but are also an important contribution to assessing risk for the companies as a whole. In the macroeconomic surveillance emphasis is given to developments in securities markets and to assessing the consequences of low interest rates for insurers.

Analyses for insurance intermediaries

Good analyses of the mandatory annual financial reporting are important to singling out firms for follow up. The analyses were further developed in 2009 and are an increasingly important tool for a

risk-based approach to the operative supervision. In 2009 firms in a negative equity capital position were followed up, in part due to increased risk of embezzlement of client funds. The same was the case for firms having failed to report statutory insurances and/or too low insurance amounts.

Every six months Finanstilsynet receives an auditor's statement from firms that handle client funds. The 2008 accounts of 38 firms contained audit remarks. The statements were reviewed and some firms were contacted for further explanation.

On-site inspection

Finanstilsynet monitors insurance companies by means of on-site inspections, stress tests and analyses. Assessments are conducted of risk exposures, management and control at the largest insurers.

Risk-based supervisory methodology is employed based on international supervisory standards and experience from supervisory work. Risk modules have been developed in respect of key areas of risk managed by life and non-life insurers. The modules developed for life insurers are also employed in pension trusts in so far as appropriate. The modules promote a uniform structure and a uniform content of inspections. Guidance documents support the assessments made by indicating best practice as regards governance and oversight.

All in all, there were somewhat fewer on-site inspections in 2009 than 2008. Owing to the negative trend in the securities market, on-site inspections received lower priority in 2009 since more resources needed to be devoted to investigations and to following up on individual institutions where the impacts were particularly large.

Life insurance companies

Three on-site inspections, including one IT inspection, were conducted at life insurers in 2009. One was a total inspection, while another focused on asset management. One insurer was told that the overarching strategy document appeared not to apply on a consolidated basis since important subsidiaries were omitted. At two insurers it was pointed out that the management board had assigned broad asset management powers, giving the administration substantial scope for action. Two companies were informed that their failure to draw up a liquidity strategy was in breach of the liquidity regulations. The independence of one insurer's risk-monitoring unit was questioned since the unit was unable to extract data on an independent basis. One inspection prompted the observation that some clients had been charged reduced prices, possibly indicating discriminatory treatment based on non-objective criteria.

Pension funds

In autumn 2008 Finanstilsynet asked the pension funds to submit their most recent stress tests. The results were used in 2009 as a basis for selecting pension funds for on-site inspection.

In view of financial market developments and reduced buffers, many pension funds kept a closer eye on their capital situation. Several pension funds received capital injections. By the end of 2009 decisions had been taken to wind up seven pension funds.

On-site inspections were conducted at four pension funds in 2009. Common to all four were deficiencies and shortcomings related to their strategy documents. Finanstilsynet pointed to the need for strategy documents adopted by the board of directors that reflect the institution's overall risk tolerance in both the asset management and risk area. The agency also pointed out that risk control exerted by the boards through investment limits was inadequate, such that the pension funds' administration and external managers were given a wide degree of freedom in asset management.

Deficiencies were consistently noted in written guidelines for approval of new financial instruments. Nor had pension funds drawn up liquidity strategies as required under the liquidity regulations.

At several pension funds it was pointed out that the stress tests failed to cover all significant risks. Finanstilsynet has called for stress testing to be incorporated in pension funds' risk monitoring.

One pension fund has repeatedly breached the capital adequacy requirement. After an inspection in 2009 it was instructed to submit extraordinary reports to Finanstilsynet.

Non-life insurance companies

Inspections were conducted at five non-life insurers in 2009, one of which was an IT inspection.

At one inspection Finanstilsynet suggested a review of the company's form of ownership in as much as it expanded its range of products. Another company was advised that its pricing of customers should

be risk-oriented and that the target combined ratio should be 95 per cent or higher. Other matters taken up after inspections at non-life insurers included the appointed actuary's independence, the need to strengthen competence and systems, confusion of roles of the board chairperson, injection of capital and management of currency risk.

One claims settlement agency was inspected on-site in 2009. Claims settlement agencies are in principle not subject to Finanstilsynet's oversight. According to the regulations on risk management and internal control, work done by such firms on behalf of Norwegian insurers is not exempt from public control, and the insurer is responsible for risk management and internal control in respect of any outsourced business. After the inspection Finanstilsynet advised that routines for regular reporting by the claims settlement agency to the insurer showing that the assignment is discharged as per agreement, must be in place.

Finanstilsynet held its annual contact meeting with If's Norwegian branch in December 2009.

Insurance intermediaries

On-site inspections were conducted at seven insurance intermediaries in 2009. An inspection at a large insurance broking firm brought to light deficient internal controls and problems of governance and oversight on the finance side. Another firm was advised that it would be a breach of the independence requirement if, apart from in cases of ordinary renewal, the broker contacted the client to offer products from his own agency business. This can only be done in conjunction with ordinary renewal provided competing offers are obtained. Any placing of insurance agreements in the broker's own agency for the purpose of receiving commission, and not on the basis of the best offering, is a breach of the prohibition against commission.

Supervisory cooperation

Finanstilsynet participates in Nordic supervisory groups to promote coordinated and consolidated supervision of financial conglomerates with establishments in two or more Nordic countries. The supervisory groups meet regularly to review the situation at the conglomerates, and their work facilitates the ongoing information exchange.

In 2009 Finanstilsynet participated in the Nordic supervisory group responsible for supervising the Finnish insurance conglomerate Sampo, the owner of If. The cooperation agreement for supervision of If is being revised due in part to changes in If/Sampo's operations in the Baltics and in Sampo's corporate structure.

Finanstilsynet is a participant in the supervisory group for TrygVesta under the auspices of the Danish FSA.

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, of which Finanstilsynet is a member. Supervisory cooperation has been established with Finansinspektionen with regard to the Storebrand SPP Group.

Follow up of the solvency regime

Stress testing

The Ministry of Finance adopted on 17 December 2007 regulations on life insurers' and pension funds' asset management and regulations on non-life insurers' asset management. The two sets of regulations essentially widen insurers' and pension funds' space for action as regards management of assets to cover insurance obligations. The regulations' requirements on management and control systems are accordingly tightened to ensure proper asset management. An important element here is the requirement for stress testing.

Finanstilsynet adopted on 22 February 2008 regulations on reporting of stress tests by insurance companies and pension funds. All insurers and the three largest pension funds report quarterly. Finanstilsynet emphasised that concrete capital adequacy or investment limits will not be inferred from the reports. The intention was to provide Finanstilsynet with a better basis on which to monitor entities' financial position. The reports are also an important part of the preparations for a new solvency framework (Solvency II).

Finanstilsynet has devised two stress tests. One is based on fair value of assets and liabilities and a definition of buffer capital assuming company liquidation (stress test I). An alternative stress test devised

by the agency is based on book values and a definition of buffer capital on a going concern assumption (stress test II). The stress tests cover market risk, credit risk and insurance risk.

Stress test I is a simplified version of Solvency II. Finanstilsynet will revise the stress test continuously based on the progress of the Solvency II project. Changes made in 2010 changes will accordingly be in keeping with provisions so far proposed for implementation of Solvency II.

Changes in reporting

An important basis for supervision and analysis is the regular reporting by the institutions themselves. A complete overview of applicable reporting requirements is available on Finanstilsynet's website.

Finanstilsynet cooperates with Statistics Norway (SSB) on the quarterly reporting by insurers through FORT (the Norwegian acronym for 'public financial and supervisory reporting by insurers'). In 2009 pension funds reported for the first time along the same lines through PORT (the Norwegian acronym for 'public financial and supervisory reporting by pension funds'). PORT reports are filed via the Altinn internet portal. Both FORT and PORT reports are checked against the institutions' capital adequacy reporting and also in part against their reporting of key figures and ratios.

Regular reporting by life insurers' appointed actuaries are an important basis for analyses and for checking compliance with legislation. The reports, of an insurance technical nature, focus above all on solvency. The reporting format was changed in line with new insurance legislation and is coordinated with other reporting by the institutions (FORT). The changes took effect as from the financial year 2008.

LICENSING

Licence cases

Finanstilsynet prepares a number of licence cases and dispensations for the Ministry of Finance. This ministry 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.

Health trusts that had been members of Buskerud county authority pension fund since before the public health reform ultimately agreed with Buskerud county authority to withdraw from the pension fund on 1 October 2009. The health trusts set up their own pension arrangements with Vestre Viken Pensjonskasse which was granted a licence to engage in life insurance business in 2009.

Finanstilsynet resolved in 2008 not to approve the statutes of Drammen Kommunale Pensjonskasse, a municipal pension fund, on the ground that the statutes contained provisions entitling the employer – in this case Drammen municipality – to adopt the statutes and to appoint the board chair. The reasoning given for the rejection cited the need for legal and de facto independence between the pension fund and any company, association or institution whose pension scheme is entrusted to the pension fund. The decision was appealed to the Ministry of Finance. The ministry dismissed the appeal, and Finanstilsynet's decision in the matter was upheld.

Of about 75 private pension funds holding a licence in 2009, seven gave notice of winding up.

Finanstilsynet also processes applications to operate as insurance intermediaries. Twelve such firms were licensed in 2009. Of these, seven were insurance broking and reinsurance broking firms and five were insurance agent firms. Several Norwegian insurance agent firms applied for permission to establish branches abroad in 2009, and several hundred notifications of border-crossing operations into Norway from other EEA states were 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 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. These rates have been reviewed in the past three years, but have been retained unchanged.

Solvency measures in life insurance

Life insurance companies' level of supplementary provisions was uniformly low at the start of 2009. Finanstilsynet accordingly expected, based on the results for the third quarter of 2009, that the surplus return in 2009 would provide a basis for increased supplementary provisions. In its letter of December 2009 to all life insurers, the agency made it clear that significant portions of the excess return in 2009 should be used to strengthen supplementary provisions. It also assumed that when considering the need to strengthen supplementary provisions, insurers should take into account the level of buffer capital and the need for any strengthening of premium reserves.

Finanstilsynet also expects life insurers to intensify their effort to adjust to the requirements regarding valuation of insurance obligations consequent on the European solvency framework which will apply from 2013 onwards.

Pension funds' level of supplementary provisions at the start of 2009 varied widely. After a general assessment of expected surplus return in 2009, pension funds were in December 2009 asked to consider strengthening supplementary provisions based on the same criteria as applied to life insurers.

Insurance Complaints Board

A complaints board for insurance broking activities and reinsurance broking activities was established on 1 December 2007. 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. Finanstilsynet acts as secretariat to the board. 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 2009.

REGULATORY DEVELOPMENT

EU preparations for a new solvency regime (Solvency II)

The EU Commission's proposal for a new directive incorporating risk-based solvency rules for insurance companies (the Solvency II Directive), was adopted by the EU Parliament on 22 April 2009 after extensive discussions between the Commission, Parliament and Council. 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.

In the course of 2009 the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) prepared about 50 consultation documents proposing implementation measures covering 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). The recommended implementation measures were forwarded to the Commission after circulation for comment throughout the European insurance industry.

The consultation documents also include a proposal for calibration of the various modules to be utilised in the calculation of the new solvency capital requirements, as well as proposals for simplifying the methods used to calculate

technical provisions and capital requirements. The calibration and simplification proposals will be tested in the fifth round of quantitative impact studies of the Solvency II framework in the second half of 2010.

The implementation measures will in all probability be incorporated in or implemented as a combination of directive and commission regulation. The Commission started this process in the fourth quarter of 2009, and towards the end of 2010 a proposal will exist which is expected to be adopted in autumn 2011. Since the implementation measures will also be substantially principle-based, supplementary rules and guidelines will also need to be drawn up under the auspices of EU/EEA supervisory authorities. In view of the expected restructuring of the EU-wide supervisory committees into supervisory authorities, 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 the end of October 2012, but the EU Commission has now proposed that transposition be postponed until 1 January 2013. The new framework will in practice be utilised to the full as from the financial year 2013.

Work on a new solvency framework for insurance companies – Solvency II

In autumn 2009 Finanstilsynet conducted a general survey of the consequences of Solvency II for Norwegian rules in the insurance area. Work on proposed changes to these rules will be intensified in the course of 2010.

In October 2009 letters were sent to all insurers asking them to give an account of processes initiated in preparation for Solvency II. The companies were also asked for their preliminary assessment of capitalisation needed as a result of the new solvency framework. A review of the responses shows differences in the level of preparation. For many insurers, capital needs are assessed based on the Quantitative Impact Study QIS4 and the stress tests reported to Finanstilsynet. The agency's stress test represents a simplified version of capital requirements proposed under Solvency II, and is calibrated with reference to QIS4. The capital requirements under Solvency II will, however, be significantly tightened compared with QIS4 and the agency's stress test if a basis is taken in CEIOPS' consultation documents. The stress test will be updated in the first half of 2010 when CEIOPS' final advice on calibration benefits is available and the specifications for the final Quantitative Impact Study (QIS5) have been drawn up. Based on the existing proposals, the solvency requirement will be significantly tightened under Solvency II, and life insurers in particular can be expected to face challenges with regard to capitalisation. Twenty-five insurers are contemplating the use of internal models to calculate parts of the solvency requirement, as permitted under Solvency II.

Finanstilsynet has played an active role in CEIOPS' work on proposals for implementation measures within all three pillars, particularly in regard to methods for designing risk-free interest rate curves (extrapolation techniques) and methods for calculating the risk margin which will constitute an addition to the best estimate for insurance obligations.

Follow up of the new Insurance Activity Act

A new Insurance Activity Act entered into force in July 2006, although chapter 7 of the Act (on pension funds) and chapter 9 (on collective and individual life insurance) only came into force on 1 January 2008. Under the new legislation, life insurers and pension funds are subject to new rules on product pricing, division of managed assets between owners and policyholders and on profit sharing.

Wishing to ascertain how life insurers have adjusted to chapter 9 of the act, Finanstilsynet conducted in autumn 2008 a survey addressing each of the chapter's provisions. The survey results are now being used in the agency's further work on implementation of and adjustments to the new act.

In May 2009 Finanstilsynet stated in a letter to all life insurers that price differentiation (prices for asset management, the interest guarantee and administrative services) that lacks an objective basis is not permitted. In November 2009 this was followed up with a letter making it clear that it is not permitted to offer insurance policyholders premiums diverging from the calculation base reported to Finanstilsynet, for example where the premiums were fixed by negotiation at a lower level than reported.

In 2009 Finanstilsynet prepared several new sets of regulations to the Insurance Activity Act. These are described below. Changes in the annual accounts regulations are described in *Financial Reporting Supervision*, page 69.

New actuarial regulations

Work on new actuarial regulations started in autumn 2009. The proposed amendments will in the first instance be adapted to the new Insurance Activity Act and will be implemented in the first half of 2010. Adjustment to Solvency II will be attended to in due course.

New regulations on account keeping

In autumn 2009 Finanstilsynet sent a draft version of new regulations on account keeping and ledgers in life insurance to the Ministry of Finance after a prior round of consultation in June 2009.

New rules on account keeping and ledgers were adopted by the Ministry of Finance on 3 December 2009, and are incorporated in chapter 8 of the regulations to the Insurance Activity Act. A transitional arrangement applies in 2009 allowing use of the old regulations, as was the case in 2008.

Proposed amendment to regulations to the Insurance Activity Act

Life insurers' supplementary provisions are distributed on individual contracts and may at most constitute 12 per cent of the premium reserve for each contract. The regulations to the Insurance



Activity Act permit insurers, when determining the year's supplementary provisions, to apply a higher percentage in the case of contracts with low supplementary provisions (up to 2 per cent of the premium reserve for the individual contract). Finanstilsynet has assessed the regulations' restrictions on individual build-up of supplementary provisions. In a letter to the Ministry of Finance in December 2009, the agency proposed raising the limit for individual build-up of supplementary provisions from the current 2 per cent to "one year's interest guarantee" for these contracts, on average about 3.5 per cent. The proposal follows up Finanstilsynet's request to strengthen supplementary provisions and inputs from the life insurance industry.

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 in life insurers on 1 January 2008. Pension funds had until 1 January to introduce equivalent new mortality bases. Prices for asset management, for any interest rate risk and for administrative services, as well as profit elements under the new legislation were introduced on 1 January 2008.

Pension funds reported their new calculation bases in 2008. These were largely based on the K2005 pension tariff comprising the Norwegian Financial Services Association's new mortality base and civil status elements (including cohabitation probabilities) which are the basis for new net tariffs in collective pension insurance. The paid-up policy portfolio arising from collective pension insurance is covered by the transitional arrangement.

New calculation bases and increases of technical provisions for pension funds follow the same principles as for life insurers. Permission has been granted to utilise surpluses to increase technical provisions. Half of the pension funds made full use of the opportunity to increase technical provisions in 2007. The remainder opted for a step-up plan starting in 2009 at the latest.

In order to ease pension funds' problems resulting from the situation in the financial market, the Ministry of Finance in November 2008 paved the way for pension funds to be allowed to extend their step-up plans by up to two years. A minority of pension funds have availed themselves of this opportunity.

Norwegian Natural Perils Pool

In June 2008 Finanstilsynet proposed the appointment of a working group to look into factors related to natural disaster insurance in general. After obtaining the views of the Ministry of Justice and the Police, the Ministry of Finance in September 2009 asked Finanstilsynet to draft the mandate for a working group and to recommend the group's composition. The draft mandate was forwarded to the Ministry of Finance in October 2009. The working group, to be appointed in January 2010, will focus on rules governing overall accounts for the Natural Perils Pool.

Prohibition of commission – insurance mediation

As from July 2008, insurance broking firms were prohibited from accepting commission or other remuneration for the insurance mediation from an insurance provider. Insurance brokers were polled on their views of the prohibition in 2009. Work on processing the responses to the survey continues into 2010.

New regulations on calculation of return on capital in life insurance etc.

Finanstilsynet adopted on 26 May 2009 regulations on calculation of return on capital in life insurance etc. after a prior round of consultation. The regulations are adapted to the new Insurance Activity Act's requirement of division into several portfolios. The regulations entered into force on 1 January 2010.

Amendments proposed to asset management regulations for insurance

The Ministry of Finance adopted on 17 December 2007 regulations on life insurers' and pension funds' asset management and regulations on non-life insurers' asset management. Numerous enquiries have been received about correct interpretation of the regulations. In March 2009 the Ministry of Finance commissioned Finanstilsynet to recommend amendments to the regulations. The agency drafted a proposal to ease some quantitative limits and to pave the way for infrastructural investments. The Ministry of Finance circulated these proposals for comment, setting the deadline for responses at 6 November 2009. Work on the regulations continues in dialogue and contact with the ministry.



SECURITIES MARKET

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.

TRENDS

Structural changes in the securities market

There is a trend in the EU to move control and supervisory tasks thus far attended to by stock exchanges and self-regulating organisations to the supervisory authorities. This is related to changes in the traditional structure featuring a dominant stock exchange in each country or geographical area. New, competing marketplaces based on advanced communications technology are being established.

The new Securities Trading Act paved the way for the establishment of multilateral trading facilities (MTFs). An MTF can be operated by an investment firm or a regulated market and organises trading in financial instruments quoted on regulated marketplaces, in the first instance the traditional stock exchanges. The chief motive for permitting this type of trading platform is to strengthen competition in the field of transaction broking services so as to reduce the costs associated with executing transactions. Another motive is to secure some regulation of trade, which up to now has been organised by investment firms under their licences. MTFs compete with the established stock exchanges, and the new trading platforms offer highly cost-effective trading solutions. Moreover, some established stock exchanges are offering trading and price quotation in shares quoted on competing exchanges. An example of the latter is Nasdaq OMX which offers trading in shares quoted on Oslo Børs. Under the Securities Trading Act's best execution requirement, investment firms must utilise the marketplace that provides the best execution for the customer. Complete success on this front will require investment in advanced control systems.

Existing marketplaces are in some cases undergoing major overhauls to adjust to the new competitive situation. Competition on price caused Oslo Børs, like most established stock exchanges, to significantly reduce its transaction charges in 2009.

Reduced transaction charges are reflected in a rising number of transactions. In a European and global perspective, the upshot is an increase in programme trading and algorithmic trading. Institutional investors use advanced ICT-based systems to initiate transactions based on pre-defined criteria. The systems are able to exploit arbitrage opportunities between trading systems and can optimise purchase and sale of shares by always exploiting the best price. Programme trading is so far limited among Norwegian actors, but is probably utilised by foreign actors trading in Norwegian shares.

The past few years have seen a growing proportion of share transactions in Europe executed outside the regulated markets and MTFs. Only a small portion of these transactions is reported to the marketplaces. While transactions executed by banks and investment firm

are reported to supervisory authorities, there is growing concern that markets are becoming less transparent because this type of market data is not made public. The trading pattern involved is often termed 'dark pools'. At the end of 2009 views differed on how large a portion of aggregate trading this constitutes. The potential difficulties in identifying insider trading and manipulation associated with this form of trading are causing some concern among market participants and supervisory authorities. Finanstilsynet has thus far not mapped the extent to which Norwegian shares are traded in international markets through dark pools.

The fragmentation of trading in financial instruments across a larger number of marketplaces and trading platforms makes monitoring of market risk at the individual marketplace more difficult. Moreover, revenue losses due to intense price competition and possible loss of trade also impair marketplaces' financial ability to maintain today's high quality of monitoring and control. A consequence is that more monitoring of market abuse has to be done by public authorities. Tackling this development will be a main challenge for Finanstilsynet in the years immediately ahead. The introduction of a transaction reporting system (TRS) is a step in this process.

Follow up of the financial crisis in 2009

Clarifications related to the central securities settlement

Lehman Brothers was a remote member of Oslo Børs and an indirect participant in the central securities settlement system with DnB NOR ASA as settlement agent. After Lehman Brothers had filed for bankruptcy protection in mid-September 2008, Verdipapirsentralen ASA and participants in the securities settlement system discussed perceptions of some aspects of the body of agreements governing the system. These included the issue of settlement agents' responsibility for settling transactions entered by remote members, and changes made in some areas. Finanstilsynet kept a close eye on this process and is keen to secure a clear-cut body of rules. The establishment of a central counterparty for equity instruments in the first half of 2010 will make for a more robust securities settlement system in Norway.

Short selling

Finanstilsynet tabled in January 2009 a proposal to amend the Securities Trading Act's provisions on short selling. The proposal extends the prohibition against uncovered short sales to include investors, and entails that sanctions can be applied directly at investors engaging in short selling. Finanstilsynet also proposed that the agency be given a clear-cut legal basis to impose a temporary ban both on covered and uncovered short selling. The proposal was prompted by the extraordinary market conditions in autumn 2008, when most countries in Europe introduced temporary restrictions on short

SECURITIES MARKET

selling. Finanstilsynet has regulated access to financial instruments in connection with uncovered short selling to prevent delivery problems arising in the securities settlement process. The proposal has been

circulated for comment and is under consideration at the Ministry of Finance. A bill is expected to be introduced in the Storting early in spring 2010.

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. Investment firms vary widely in terms of size, organisational set-up and services provided. Risk-based criteria are used to select firms for on-site inspection. They include liquidity, capital adequacy, changes in revenues, earnings and profitability as well as criteria bearing on licensing and market conduct such as client complaints and suspected breaches of conduct of business rules.

Fourteen on-site inspections were conducted at investment firms in 2009, one inspection at a Norwegian branch of a foreign investment firm and one inspection specifically targeting an investment firm's IT solutions. Finanstilsynet also participated, in conjunction with Swedish authorities, in an on-site inspection at a Norwegian institution's branch in Sweden and Swedish institutions' branches in Norway.

Since the widening of the range of businesses subject to licensing under the Securities Trading Act, which became effective on 1 November 2007, on-site inspections have focused largely on the advisory services segment. In 2008 Finanstilsynet levelled in a number of cases remarks at firms which geared their business to selling products at the highest possible profit for the firm, not to protecting clients' interests in terms of risk and expected return. The products' cost elements were often so high that clients' opportunity to achieve their investment targets was significantly reduced. Moreover, in some cases debt financing of investments was advised. Finanstilsynet also kept a close eye on the advisory services segment in the first half of 2009. As in 2008 Finanstilsynet focused on making management accountable for product choice and product composition in order to minimise the conflicts of interest that are inherent in the business. Firms in this segment are expected to have in place clear guidelines for what product compositions can be sold to defined client segments

and to carefully document any deviations from such guidelines. Finanstilsynet's impression is that a considerable improvement has taken place in the segment, in particular where the major participants are concerned. No licences were revoked on grounds of rule breaches related to advice given in 2009.

The Ministry of Finance decided appeals against the revocation of the licences of Totalvekst ASA, Caveo ASA and Handelspartner AS. All the appeals were dismissed. The two first-mentioned involved breaches of the conduct-of-business rules. The third concerned unlawful active management and trading for own account.

The general public showed much interest in Finanstilsynet's supervisory observations after inspections of Acta Kapitalforvaltning ASA and the advisory services division of DnB NOR Bank ASA. Where Acta Kapitalforvaltning is concerned, Finanstilsynet levelled strong criticism at the firm for breaches of the conduct-of-business rules when providing investment advice. Documentation of the firm's business activity was also found to be inadequate. Finanstilsynet's criticism of DnB NOR essentially targeted poor compliance with documentation requirements in connection with investment advice and related themes, i.e. flawed routines and deficient internal control.

A general improvement in conduct in the advisory services segment prompted a broader selection of firms and inspection themes in the second half of 2009.

Finanstilsynet keeps a close eye on investment firms in its off-site supervision, and in 2009 maintained a strong focus on their compliance with the capital adequacy rules. Investment firms' market situation in 2009, particularly in the second half-year, was somewhat better than the previous year. Even so earnings and financial positions were in a number of cases impaired, and 30 firms carried out capital increases to bolster their regulatory capital positions. Six firms handed in their licences due to low capital adequacy.

Two investment firms were ordered to rectify breaches of the rules governing large exposures; one was subsequently warned of licence revocation for non-compliance. The orders were issued because the firms' exposures exceeded the limit of 25 per cent of their own funds. One firm complied with the order while the other opted to hand in its licence to provide investment services.

The larger investment firms' counterparty risk arising from derivative positions and lending was scrutinised in 2009. Surveys from autumn 2008 were followed up with new surveys in January and March, thereafter with on-site inspections.

Market warnings

In 2009, as previously, Finanstilsynet was made aware of firms that had approached Norwegian investors offering financial services without

the requisite authorisations. 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 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. Finanstilsynet published 24 warnings against firms that had provided financial services in Norway in 2009 without the requisite licence. A further 136 warnings given by foreign supervisory authorities were published.

LICENSING

Authorisation process

In the past three years Finanstilsynet has processed significantly more applications to provide investment services than previously. This is mainly due to the reorganisation of the licensing regime imposed by the new Securities Trading Act as from 2007, as a result of which provision of investment advice became a licensable service. At the end of 2009 there were 150 investment firms in Norway, compared with 85 in 2006. In 2009 nine new investment firms were licensed to

provide investment services. In addition, three licences were granted to existing firms (extended licences). Given the larger number of investment firms under supervision, other types of cases related to investment firms have also increased.

In addition to the revocations due to poor capital adequacy, five licences were revoked on account of restructuring, mergers and corporate acquisitions, and business area reorganisation.

Table 9: Investment firms

	2007	2008	2009
Firms holding a licence	132	154	150
Branches of foreign firms	10	13	17
New firms holding a licence	58	38	9
Firms whose licence was handed in or revoked	9	16	11

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. The assessments are normally made with a basis in written documentation. In some instances interviews are held with the appointed manager. These are cases where Finanstilsynet, based on written documentation, is in doubt as to whether the fit-and-

proper requirements are met and where the alternative is to disallow the person concerned on grounds of inadequate documentation of compliance with the qualification requirements. The interview then forms part of the basis for deciding the outcome of the fit-and-proper test. The procedure with respect to such interviews has been clarified with the Ministry of Finance.

REGULATORY DEVELOPMENT

Regulation of investment services related to shares in limited partnerships ('KS') and general partnerships ('ANS')

Finanstilsynet drafted in April 2009, on commission from the Ministry of Finance, amendments to the Securities Trading Act with regard to shares in limited partnerships and general partnerships. Under the proposal, intermediary services to non-professional investors related to partnership shares can only be provided by investment

firms, i.e. firms licensed to provide investment services. This places partnership shares on a par with financial instruments in terms of licensing requirements, and investors will enjoy the same protection when purchasing partnership shares as when purchasing products defined as financial instruments. The proposal will promote equal treatment of products offered in the saving and investment market in terms of investor protection.

FUND MANAGEMENT COMPANIES

SUPERVISION AND MONITORING

At the end of 2009 26 management companies were licensed to manage securities funds. Thirteen of these were licensed to carry on business described in the Securities Trading Act section 2-1 subsection (1) no. 4 as "active management of investors' portfolios of financial instruments". The number of securities funds managed by these companies fell marginally from 426 in 2008 to 421 in 2009.

Finanstilsynet's supervision of management companies is both on-site and off-site. One management company was inspected on-site in 2009. Since the implementation of the MiFID directive in Norwegian law the advisory segment has been given priority for on-site inspection. Most of Finanstilsynet's supervision and monitoring of management companies has been off-site. On-site inspections of investment firms in 2009 showed that they were largely in compliance with the new legislation. On this basis, and in preparation for the implementation of a new directive for securities funds (UCITS IV – Undertakings for Collective Investment in Transferable Securities), on-site inspections at management companies will receive somewhat higher priority in 2010.

Management companies are required to report any breaches of investment limits set out in the Securities Funds Act and funds' statutes.

The number of reported breaches in 2009 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 filed with Finanstilsynet by the companies. Due to the difficult market conditions, management companies saw a sharp decline in earnings in 2008 and into the first quarter of 2009. Five management companies found themselves compelled to increase their own funds in 2009 due to poor earnings and weak financial positions.

However, management companies are seeing positive net subscription figures for equity funds, offering potential improvement in management companies' earnings over time. Profit reports showed improved earnings in the course of 2009.

LICENSING

Finanstilsynet has noted a tendency for more firms to apply for a licence to engage in securities management than was previously the case. In 2009 licences were granted to five new management companies, one of which was for the extension of an existing firm's services. This is a relatively high number given the total number of 26 management companies at the end of 2009. Actors appear to favour establishing niche management companies in which securities funds are set up with narrower investment strategies.

One application to engage in securities management was turned down, and two applications were withdrawn before final processing

was completed. One licence to engage in securities management was revoked.

In 2009 the articles of association of 28 new securities funds were ratified, while 35 securities funds were wound up.

A number of cases concerning approval of amendments to securities funds' articles of association were considered. The simplified amendment procedure involving passive consent, see circular 14/2007, was utilised in many cases.

REGULATORY DEVELOPMENT

Revision of the Act on Securities Funds

On commission from the Ministry of Finance, Finanstilsynet appointed a broadly composed working group to undertake an overall review of the Securities Funds Act. The working group is mandated to recommend changes to the Act to enable implementation of the new UCITS IV in Norwegian law by the deadline of 1 July 2011. Under its mandate the working group is to recommend amendments that safeguard small investors' interests by assuring that securities funds are a

well functioning saving and investment alternative, within the obligations set by the EEA agreement. Finanstilsynet aims to complete the proposal in the course of June 2010.

Finanstilsynet recommended in the course of 2009 minor amendments to the Securities Funds Act and drafted new regulations in some areas.

MARKET INFRASTRUCTURE

SUPERVISION AND MONITORING

The securities market infrastructure comprises Oslo Børs ASA, the Norwegian Central Securities Depository (VPS ASA), Oslo Clearing ASA, Nord Pool ASA, NOS Clearing ASA, International Maritime Exchange ASA (Imarex) and Fish Pool ASA.

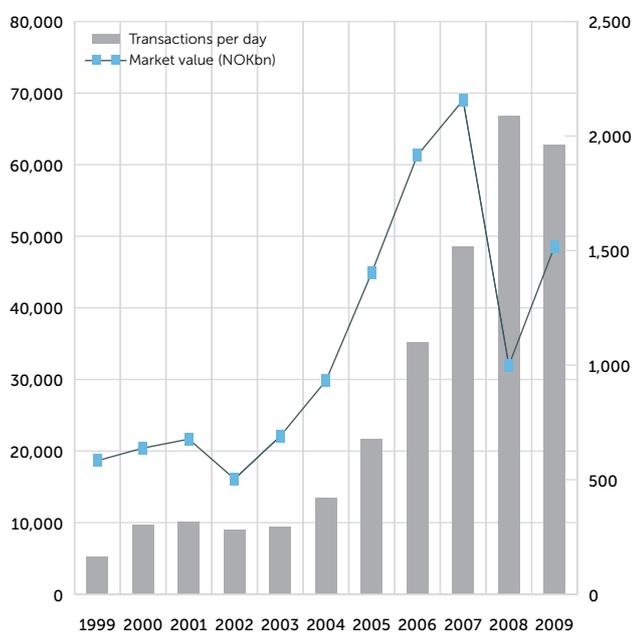
The business of Nord Pool Clearing ASA was transferred at the end of November to a branch of Nasdaq OMX Stockholm AB. The transfer constitutes stage 2 of a wider transaction encompassing the transfer of large sections of Nord Pool ASA's business to Nasdaq OMX Stockholm AB. Upon Finanstilsynet's recommendation, the Ministry of Finance granted Nasdaq OMX Stockholm AB a licence to engage in clearing and settlement business in Norway through the branch. Finanstilsynet has signed a supervisory cooperation agreement with Finansinspektionen (the Swedish FSA).

In a move to strengthen the supervision of clearing houses, Finanstilsynet required them as from October to report their own funds and risk exposure on a regular basis; see Finanstilsynet's circular 13/2009. The new reporting regime was put into operation after a consultation round among clearing houses in Norway.

The infrastructure institutions base their business on extensive use of ICT systems, and the operational risk associated with these systems is of increasing significance. On-site inspections were conducted at NOS Clearing ASA and the Central Securities Depository. Finanstilsynet monitored the institutions closely, in particular through its consideration of a number of major cases in 2009.

SECURITIES MARKET

Chart 6: Market value and number of transactions per day at Oslo Børs



Source: Oslo Børs

Prospectus control

Pursuant to the Securities Trading Act Finanstilsynet is the overarching supervisory authority in relation to prospectus control. Regulations of 9 December 2005 no. 1423 on the implementation of prospectus control assign the exercise of this control to Oslo Børs. Finanstilsynet has received a written account and confirmation from Oslo Børs that the control tasks have been discharged in conformity with law, regulations and Oslo Børs' in-house guidelines and instructions. Finanstilsynet takes over operative responsibility for prospectus control on 1 May 2010.

Electricity market and electricity derivatives market

A feature of the electricity market is its high short-term volatility. However, prices in the electricity market were relatively stable in

2009 compared with previous years despite a slight decline over the year, particularly in the first quarter. Reservoir levels were on the low side compared with a normal year. Price effects from the electricity market on the continent appear to be significant, with forward prices on Nord Pool and the German electricity exchange in particular appearing to show a high degree of covariation, although price levels in Germany are substantially higher. The CO₂ quota market exerts much influence on electricity prices. The quota price fell significantly in the first quarter, thereafter stabilising at a somewhat higher level through the year. This market, like the electricity market, is relatively volatile, particularly in the short term. Finanstilsynet has cooperated with the Competition Authority and the Norwegian Water Resources and Energy Directorate on supervision of the electricity market since 2003, and cooperation with these two agencies will continue.

Freight derivatives market

Prices were historically speaking very low at the start of 2009, both in the dry bulk and the tanker market. A tendency for higher freight prices was noted around summer, and towards year-end prices rose significantly. A natural assumption is that freight and freight derivative prices were lifted by increased confidence in the international economy, spurring greater needs to transport raw materials to manufacturers and finished goods to end-user markets. Market participants are now seeing, more so than in previous years, the need to use a clearing house to settle derivative contracts. It is uncertain whether they will continue to avail themselves of this service to the same extent ahead.

Fish derivatives market

Prices in the fish and fish derivatives market rose significantly from the start of 2009 to the summer, at which point the trend reversed and fell rapidly to the initial level, thereafter stabilising to year-end. Volume traded at Fishpool has risen slowly but surely since the start. Even so, viewed in relation to other commodity derivatives markets, turnover value in the fish derivatives market remains low.

LICENSING

New multilateral trading facility (MTF)

Oslo Børs ASA was authorised on 13 October to establish a multilateral trading facility (MTF) for non-standardised derivatives. The licence covers operation of a new marketplace for non-standardised derivatives which is marketed under the trade name *Oslo Connect*.

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 2009 Finanstilsynet asked the Central Securities Depository (VPS ASA) to remove tenants with which the VPS was previously co-located in order to ensure securer conditions for proper information treatment and prevent confidential information going astray. Finanstilsynet has stipulated the minimum size and composition of the VPS's own funds, and has prepared a recommendation to the ministry regarding payment of dividends and group contributions by the VPS.

Finanstilsynet approved agreements concerning Oslo Clearing ASA's outsourcing of two IT systems, and one agreement on insourcing the operation of an IT system to the VPS. The scope of the condition regarding outsourcing of core business was clarified with the Ministry of Finance. This issue was actualised by Oslo Børs's switch to a new trading system from the London Stock Exchange.

Mandatory clearing of equity instruments quoted on Oslo Børs and Oslo Axess

Finanstilsynet has recommended to the Ministry of Finance that it extends Oslo Clearing ASA's licence to conduct clearing and settlement activity related to equity instruments. This activity, due to start in the second quarter of 2010, entails a new clearing and settlement model in Norway for equity instruments.

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

Finanstilsynet considered an application for approval of changes in the central securities settlement system. The application was prompted by changes in Norges Bank's clearing and settlement system. The system was originally approved by Finanstilsynet in 2001.

REGULATORY DEVELOPMENT

Proposal to regulate bond issue trustees' right to bring legal action

Finanstilsynet, on commission from the Ministry of Finance, looked at 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 to the Securities Trading Act. The agency proposed that a firm nominated in an agreement with a borrower as representative for the borrowers (trustee for bond issues etc.), may under specified conditions sue and be sued with binding effect for all borrowers in cases concerning the loan agreement and associated agreements.

The background to the matter is a Borgarting High Court ruling of 30 September 2009 to the effect that Norsk Tillitsmann ASA was not entitled to litigate on behalf of bondholders against a bond issuer. Although the court's judgment was appealed to the Supreme Court and is therefore not final under Norwegian law, it creates uncertainty as regards the litigation rights of trustees who represent bondholders. Uncertainty about such an important requisite for the established trustee scheme in the Norwegian bond market impairs confidence in and the functionality of the bond market. The situation must be rectified as soon as possible if the bond market is to function optimally as a source of capital. The Ministry of Finance has circulated Finanstilsynet's recommendation for comment, and rapid legislative treatment is anticipated.

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

SECURITIES MARKET

methods, notification rules and rules requiring 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. Finanstilsynet aims to show potential lawbreakers that they risk exposure, and it will also apply other measures to discourage criminal acts.

Many of the large number of cases dealt with by Finanstilsynet in 2009 were referred to it by Oslo Børs. Several cases were reported by investment firms. Finanstilsynet also initiated a number of investigations itself based on market events or media coverage.

A number of the insider trading and market manipulation cases handled by Finanstilsynet were time-consuming, especially where the investigations involved other countries. As in 2008, Finanstilsynet availed itself on several occasions of cooperation agreements with foreign supervisory authorities when conducting investigations. Finanstilsynet similarly assisted foreign supervisory authorities in their investigations in a number of cases.

Administrative fines

The introduction of a new Securities Trading Act puts Finanstilsynet in a position to impose an administrative violation charge for breach of the rules requiring disclosure of substantial share acquisitions or disposals (Securities Trading Act section 4-2). The availability of this sanction streamlines rule enforcement and puts in place an adequate response to less serious violations. Finanstilsynet expects publication of the charges handed down to promote market discipline and potentially reduce the number of violations in the longer term. By the end of 2009, 17 administrative fines had been issued. One administrative fine was appealed to the Ministry of Finance and is under review. In one instance, where Finanstilsynet opted to report a breach of disclosure rules to the prosecuting authority rather than impose a administrative fine, the offence was regarded as serious since it involved repeated breaches of the obligation to disclose major share acquisitions. This compares with one notification to the prosecuting authority in 2008, and three in 2007.

Notifications to the prosecuting authority

Five cases of suspected unlawful insider trading and/or breaches of the duty of confidentiality were reported to the prosecuting authority in 2009. Four cases of market manipulation were reported as were one

case of unlawful business activity, one failure to disclose the acquisition of a large shareholding and ten breaches of the notification rules. Finanstilsynet also issued several warnings after minor breaches in the two last-mentioned areas.

Investigation of transactions at DNO International ASA

In 2009 Finanstilsynet investigated various aspects of transactions at DNO International ASA involving representatives of Iraq's self-governing Kurdish region.

Based on the information at hand, Finanstilsynet found it appropriate to turn the matter over to ØKOKRIM for review and possible further action. Behind this decision was the perception that the case could have ramifications beyond the bounds of securities law. Moreover, international police cooperation appeared to be the best way to clarify the circumstances surrounding the transactions in question at DNO.

Follow up of reported cases

Finanstilsynet assisted ØKOKRIM and local police authorities in their follow up of reported cases in 2009 by conducting interviews and analysing share transactions. Finanstilsynet views the assistance it provides to the prosecuting authority in winding up cases of securities crime to be in line with the agency's overarching goals.

In addition to cooperation in individual cases, emphasis was given in 2009, as previously, to extensive contact between Finanstilsynet, Oslo Børs and ØKOKRIM. The cooperation is designed to enhance overall market surveillance.

Supervisory effort more effective and simpler

In 2009 Finanstilsynet was granted search access by the Central Securities Depository (VPS) on a basis allowing it to make direct searches five years back in time. Up to that point searches were confined to the preceding two years. This has improved the chances of bringing market abuse to light and added an effectiveness gain to the ongoing work on such cases.

Further development of transaction reporting

Finanstilsynet receives transaction reports from investment firms on a daily basis. Moreover, reported transactions are exchanged with foreign supervisory authorities (CESR members). As from 1 April 2009 the reporting facility was extended to financial instruments assigned an Alternative Instrument Identifier (AII) code. This made it possible to report transactions in instruments not having an ISIN, including transactions in financial instruments quoted on Imarex.

As from 15 September 2009 the agency also received instrument reference data (IRD) reports from regulated markets. These reports are used inter alia as a basis for deciding which national supervisory authority is the relevant supervisor for the individual instrument, and for routing forwarded transactions.

The implementation of AII and IRD has had some system-related implications, including the need for changes in data storage. As a result the effort to improve the quality of transaction reporting took longer than desired in the second half of 2009. This effort was stepped up towards year-end and will be given priority in 2010.

In 2009 a project group was set up to examine ways to improve the efficiency of periodic reporting by investment firms and fund management companies. The project group has worked on identifying potentials present in existing systems and on recommending appropriate solutions.

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

Court rulings

- In March 2009 Oslo City Court sentenced two persons to one-and-a-half year's and one year's imprisonment respectively for breach of the Securities Trading Act's rules governing own-account trading by employees of investment firms, and for complicity therein. The main perpetrator, employed at an investment firm, was also convicted of breaches of the Securities Trading Act section 3-4 (previously section 2-4) on confidentiality, and of breaches of the Tax Assessment Act (gross tax fraud). The two individuals were subject to confiscation of NOK 10 million and NOK 1 million respectively.
- In August 2009 Oslo City Court sentenced a person to four months' unconditional imprisonment, and to confiscation of NOK 12,261, for breaches of the insider trading provisions. The individual was convicted of purchasing shares in a listed company after receiving information from a former broker.
- In June 2009 Agder High Court handed down a new judgment for breaching the rules governing provision of investment services and conduct of business, after the Supreme Court had quashed the previous high court judgment due to incorrect application of the law and insufficient grounds for judgment. The High Court convicted three persons of breaching the prohibition against providing investment services without the requisite licence and the prohibition against unreasonable business methods. All the accused, along with two companies, were in aggregate sentenced to confiscation of NOK 6,057,756. Two of the accused were sentenced to 45 and 30 days' unconditional imprisonment respectively. They also received suspended prison sentences of 75 and 60 days respectively. The third accused received a suspended 90 day sentence. When sentencing, the High Court took the confiscation into account.
- In January 2009 the Supreme Court convicted a fund manager of violations committed in the course of his work. The fund manager was found guilty of violating the Securities Trading Act's provisions concerning market manipulation and conduct of business, and of one count of social security fraud. The fund manager bought shares on the year's last trading day at a price clearly below the final market price prior to the final auction. The Supreme Court assumed that the trade was made to "touch up the performance" of the fund he managed. The Supreme Court also stated that price manipulation of a certain degree of seriousness normally qualifies for unconditional imprisonment. The Supreme Court sentenced the individual to ten months' imprisonment, of which 120 days were suspended.

REGULATORY DEVELOPMENT

In 2008 Finanstilsynet drafted several new regulations and law amendments which are still under consideration at the Ministry of Finance. They concern access to tele-traffic data, amendments to the Freedom of Information Act and administrative fines for non-compliance with the notification obligation. The agency saw no need to initiate work on further rule changes in 2009.

Finanstilsynet issued circular 9/2009 entitled "Securities Trading Act – comments to Chapter 3 and Chapter 4" in 2009. The circular assembles all previous circulars in this field, and largely reproduces the text of previous circulars, with some corrections and additions. The additions refer in particular to the interpretation of provisions requiring disclosure of major share acquisitions.



All listed companies are required to apply the International Financial Reporting Standards (IFRS) when preparing and presenting consolidated accounts. Finanstilsynet is responsible for ensuring that they do this correctly. The 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 opted for Finanstilsynet as the competent authority. It also encompasses enterprises that do not report under IFRS. The supervision applies to periodic reporting such as annual accounts at group and company level, directors' reports and interim accounts.

FINANCIAL REPORTING SUPERVISION – LISTED COMPANIES

TRENDS

At the end of 2009 276 Norwegian companies were subject to Finanstilsynet's oversight 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. In the course of the year three new issuers were admitted to listing on Oslo Axess, while 22 were delisted (12 on Oslo Børs and ten on Oslo Axess). Under the new Securities Trading Act, Norway is the home state for issuers from the EEA, subject to certain conditions. Thirty foreign companies have opted for Norway as their home state, and communication with most of them is in English.

Finanstilsynet appreciates that the financial crisis may pose greater challenges as regards valuation of companies' assets and liabilities, and underscores the importance of presenting sufficient and precise information in notes to accounts.

Upon review, the audit reports on 30 issuers were found to contain reservations or clarifications. Only five of these had given the notification regarding deviating audit reports required by the Securities Trading Act section 5-5, subsection (5). This shows how demanding it was for many issuers to prepare and present the 2008 accounts.

SUPERVISION OF FINANCIAL REPORTING

Oversight 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 included. Foreign companies from other EEA countries that are listed on Oslo Børs are subject to the oversight of the regulatory authorities in their respective home countries. Issuers listed on Oslo Børs and not registered in the EEA are covered provided they have opted for Norway as their home country. Central government, municipal and county authorities are not covered by the oversight, nor are municipal or intermunicipal enterprises/companies. State-owned enterprises are, however, included.

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

Supervision covers companies' periodic reporting – i.e. annual accounts (at both group and company level), directors' reports and interim reports – 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, 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 checked within a given period.

In 2009 Finanstilsynet reviewed all or parts of the financial reporting of 33 companies. Particular attention was focused on issuers of equity instruments such as shares and equity certificates, and some bond issuers. As a result of this review, ten cases were given closer scrutiny; several had yet to be finalised at year-end. No information was received in 2009 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 checking that reports are published within deadline. In 2009 it introduced a violation charge for late publication.

The deadlines for the periodic reporting are regarded as absolute, and in principle any violation attracts a violation charge. A concrete assessment is made in each case. Finanstilsynet has no power to grant dispensation from the deadlines.

In order to give issuers the opportunity to come into line with the new guidelines for violation charges, and in view of the shorter deadline for publication of their annual reports, "critical letters" were in the first instance sent in the less serious cases. The charges imposed range from NOK 5,000 to NOK 200,000, depending on the company's market value and the nominal value of the quoted instruments. In four cases the charge was doubled since the reports were published unacceptably long after the deadline.

Table 10: Overview of critical letters and violation charges in 2009

Accounting period	Critical letters	Violation charge imposed
Fourth quarter 2008	4	–
First quarter 2009	–	1
Annual report for 2008	16	8*
Half-year report for 2009	–	2

* Two appeals against violation charges are under consideration.

Business combinations – Wega Mining ASA

When reviewing Wega Mining ASA's annual accounts for 2007, Finanstilsynet questioned the company's accounting treatment of a business acquisition.

Wega Mining acquired 92.8 per cent of the shares of Goldbelt in December 2007. The purchase was treated as purchase of individual assets in Wega Mining's annual accounts for 2007. Goldbelt's business consists in the acquisition, exploration, and development of precious metal properties, and was listed on the Canadian Stock Exchange at the time of the acquisition. At the same point Goldbelt held 28 licences in five different areas, but no producing mine. Goldbelt earned no income in 2006 or 2007. Goldbelt carried out a number of activities such as exploration, geophysical mapping, trial drilling, analysis, agreement-signing with the authorities and projecting of future mine development under several of the licences. In the most advanced project, Goldbelt had by the acquisition date confirmed the presence of resources, started to modify the dam structure and acquired construction machinery. Part of the work was done by Goldbelt's own employees (totalling 38 of whom 29 were local employees lacking specific skills), while tasks such as trial drilling and analysis of rock samples were carried out by hired-in rig companies and independent laboratories.

After an overall assessment Finanstilsynet concluded that in this particular case the acquired company was a business according to IFRS 3 Business Combinations. It viewed the activities as an "integrated set of activities" with the "clear purpose of providing a return directly to investors". In that connection Finanstilsynet attached importance to Goldbelt's portfolio of licences that it was developing. On 12 March 2009 the agency ordered Wega Mining to account for the acquisition of Goldbelt Resources Inc. as a business combination and not as a purchase of individual assets. The order also required Wega Mining to make a new assessment of whether other similar acquisitions classified as purchase of individual assets should be accounted for as business combinations. Wega Mining was ordered to make the required corrections in the next round of financial reporting. Wega Mining appealed against the order by letter of 3 April 2009. The order was given suspensive effect.

Review of quarterly accounts

Finanstilsynet's supervision of periodic financial reporting includes oversight of interim reporting, and the agency reviewed a selection of interim reports for the fourth quarter of 2008. The purpose of the interim report is to give an update on the latest complete annual accounts and to indicate any change in financial position and earnings since the last annual accounts were presented. A basic premise for

the interim report is that users also have access to the company's latest annual report. The interim report describes new activities, events and circumstances, and does not repeat previously reported information;

see IAS 34.6 and 34.15. However, IAS 34 imposes some minimum requirements with regard to the content of an interim report and its notes. Finanstilsynet's findings are summarised in circular 12/2009.

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 four times in 2009, 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 2009:

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

The Annual Accounts Regulations for insurance companies were amended on 30 January 2009 to bring requirements on notes to accounts into line with IFRS. As recommended by Finanstilsynet in a consultation paper dated 27 May 2009, further amendments to regulations (simplifications) affecting smaller insurance companies will be adopted early in 2010. An extensive guidance on the annual accounts regulations will be issued in a circular, also early in 2010.

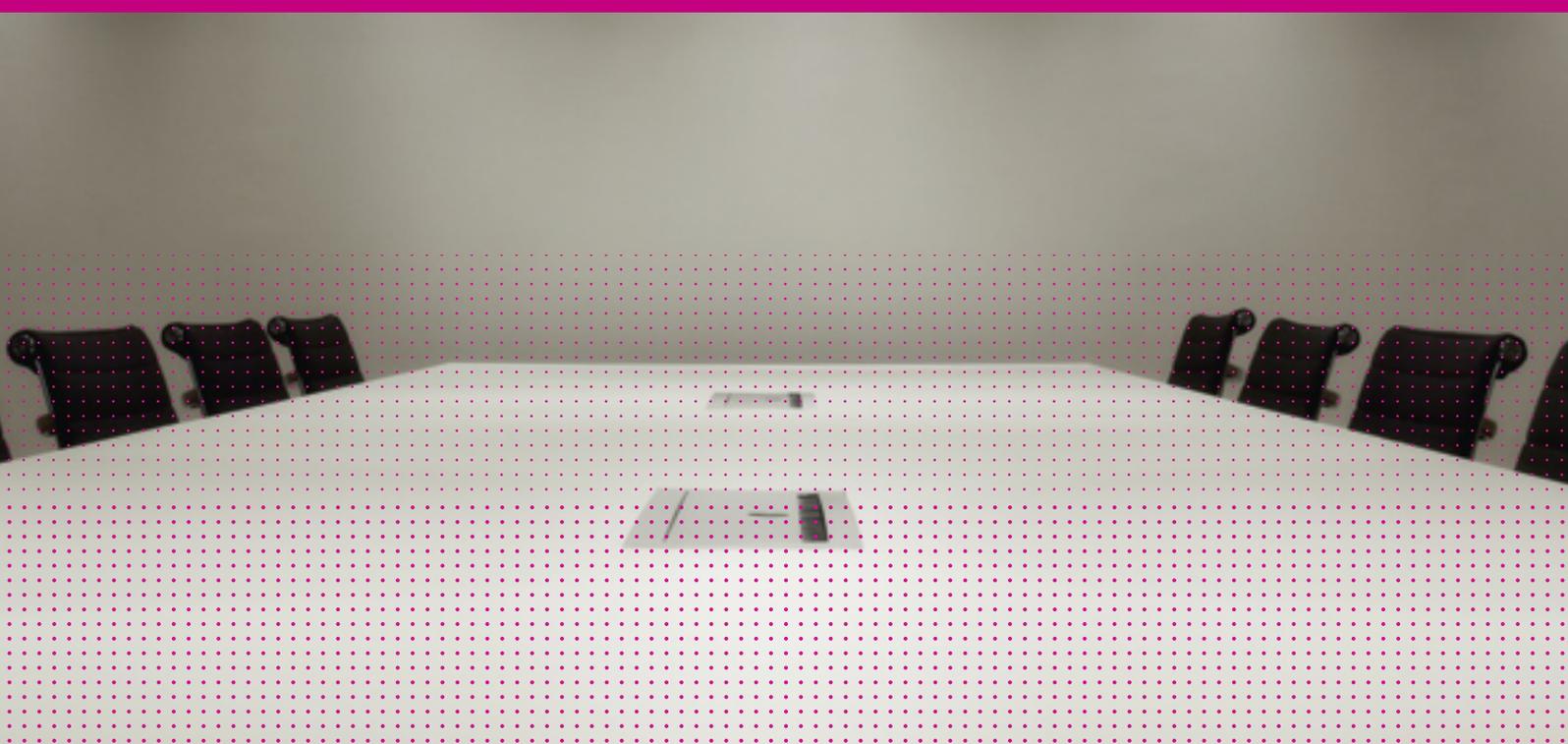
The Annual Accounts Regulations for banks, finance companies and mortgage companies were amended on 30 January 2009, bringing the rules on simplified application of IFRS into line with the regulations on simplified application of IFRS applying to other financial reporting entities.

Finanstilsynet has kept abreast of international developments in the accountancy field, particularly as regards financial instruments, including losses on lending.



AUDITING

Finanstilsynet's tasks in relation to auditors comprise 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.



TRENDS

The auditing profession has a bipartite structure: a small number of international audit firms that audit the majority of listed companies, and a large number of smaller audit firms that mainly audit small and medium-sized clients. What significance any limitation of auditor liability may have for the industry structure in Norway and internationally is uncertain.

Market participants' confidence in financial reporting by public interest entities – i.e. banks and other credit institutions, insurance companies and listed companies – is key to achieving well functioning markets. Good quality auditing supports that confidence. In order to properly perform the role as the representative of the general public, it is imperative that the auditor should be independent and perform the audit in conformity with the requirements of the Auditors Act.

The requirement on public interest entities to set up an audit committee, and regulation of the audit committee's communication with the auditor, must prompt board of directors to focus more attention on the work of the auditor. Investors and other users of financial information should also be concerned with auditor independence and the scope of the audit assignment.

Any widening of small firms' exemption from the statutory audit obligation is likely to impact heavily on the audit industry by enabling more auditors to offer external accounting services and advisory services. Conducting audits in conformity with the audit standards established by the industry and being developed, also with respect to the smallest audit clients, poses a challenge.

SUPERVISION AND MONITORING

Finanstilsynet has not found it necessary to address specific measures to the industry as a result of the financial crisis, beyond recalling the importance of auditors' ability to document their assessments after the event, and the need to include reservations or clarifications in the audit report. Auditors' reporting obligations under the Financial Supervision Act, Guarantee Schemes Act and Securities Trading Act have also been highlighted as important.

Finanstilsynet checks 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. Checks are also made to ensure that the money laundering legislation is complied with, and that auditors and audit firms submit their accounts and tax returns on time.

Finanstilsynet carries out supervision based on its own risk assessments, reports received and signals emerging, for example in the media. Matters that come to light in other areas supervised by Finanstilsynet may also prompt scrutiny of the work of an auditor. Periodical quality assurance reviews of auditors of entities subject to statutory audit is required at least every sixth year. Since 2002 the periodical quality assurance reviews 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 2009 is reproduced on page 75. Finanstilsynet checks non-members, ensuring that all statutory auditors are inspected in the

same six-year period. With the implementation of the Audit Directive into Norwegian law, new guidelines have been prepared to ensure that the periodical quality assurance review conforms to the directive. In the case of auditors and audit firms that audit public interest entities, periodic assurance review is required every third year. The quality assurance reviews, performed in principle by Finanstilsynet, are in addition to other supervision targeting these auditors.

Finanstilsynet received 163 reports on auditors in 2009 from DnR, the tax authorities and bankruptcy administrators, in addition to other signals potentially indicating deficient audit practice. 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 checked 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.

Ninety cases were concluded in 2009 after on-site inspections.

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

The guidelines and routines adopted and applying at any time to an audit firm, which must be complied with by the statutory auditors and others in the audit team, will be crucial to the quality of all audit assignments taken on by the firm.



Table 11: Revocation of auditors' licences

	2006	2007	2008	2009
State authorised auditors, licences revoked	5	3	3	1
Registered auditors, licences revoked	9	4	9	4
Audit firms, licences revoked	1	0	0	3

Finanstilsynet's observations after inspecting Ernst & Young AS concluded that the firm's guidelines were satisfactory. Based on its review of the selected audit assignments, Finanstilsynet asked the firm to look at its routines for assuring a) that an independent audit is performed of each group entity that is subject to statutory audit, b) that the implementation and documentation of formal consultations is appropriate and adequate, c) that circumstances to which the attention of the audited entity's management must be drawn in writing are documented in numbered letters and d) that audit assignments are quality controlled before the audit report is submitted.

Finanstilsynet conducted an on-site inspection at Deloitte Statsautoriserede Revisorer AS (Deloitte) in December 2008. The inspection was conducted together with the Public Company Accounting Oversight Board in the US (PCAOB). In order for a company to be registered on a stock exchange in the US, its auditor must be subject to PCAOB oversight. Deloitte audits US-listed companies, and a significant subsidiary of such a company. In its final observations Finanstilsynet asked the firm to change its guidelines to bring forth more clearly the limits that good audit practice sets for the work of an internal audit function and to ensure that all audit procedures are documented before the audit report is signed. Based on its review of the selected audit assignments, Finanstilsynet asked the firm to examine its routines to ensure that the guidelines for timely completion and quality control of the audit documentation are adhered to and that the audit team also has sufficient competence and capacity

in cases of unforeseen absence. The PCAOB will prepare its own report on the inspection.

In August 2009 a similar inspection was conducted at KPMG AS. This was not done as a joint inspection with the PCAOB as planned inasmuch as the Audit Directive had entered into force and the approval that was needed from the EU Commission in order to collaborate with the PCAOB was not to hand. Finanstilsynet found flaws in the procedure for verifying that statutory auditors' training complied with the minimum requirements set out in the Auditors Act. A number of other matters were addressed in preliminary observations made after the inspection. Final observations are expected to be available in the course of the first quarter of 2010.

Other individual cases

In January 2008 Fast Search and Transfer ASA decided to prepare new accounts for 2006 due to faulty revenue recognition, resulting in part from irregular transactions. After taking a closer look at the audit of revenues and trade debtors in the original accounts for 2006, Finanstilsynet concluded that the auditor had failed to take sufficient account of risk factors identified at the planning stage, and that the auditor had failed to perform audit procedures sufficient and appropriate to confirm the validity of revenues from a major contract. The agency also noted that the other booked transactions that required correction in the 2006 accounts were due to accounting manipulation which would have been difficult for the auditor to detect.



Finanstilsynet conducted an on-site inspection at a debt collection agency, Intrum Justitia AS, which revealed serious system errors, and checked to see if these errors ought to have been brought to light by the auditor during the audit. In previous cases the agency has underlined auditors' obligation, in line with good audit practice, to take account of any special legislation to which the audit client may be subject. In this case Finanstilsynet concluded that the auditor had taken sufficient account of how the requirements on the operation of debt collection business impact on the audit of such business, and that this had been satisfactorily documented. In monetary terms the errors were below a materiality threshold for the annual accounts, and were not of such a nature that the auditor should have detected them in the course of the annual audit.

In one case Finanstilsynet found that the auditor had for several years noted the same breaches of central legislation on the part of the audited entity without drawing attention to them in numbered letters. The most serious breaches were non-compliance with the obligation to use a tax deduction account. Moreover, the audit client was an authorised external accountant, and the auditor had not considered the significance of the offences for the accountant's authorisation and continued operation.

At the end of 2008 bankruptcy proceedings were opened against the main firms in the estate agency chain Notar. Many firms were involved, and Finanstilsynet has opted to await the results of the administration boards' enquiries. Finanstilsynet expects to bring the case to completion early in 2010.

Thematic inspections

In 2008 Finanstilsynet conducted a thematic inspection of audits of foundations. A synoptic report was prepared dated 12 March 2009. Finanstilsynet's main impression is that auditors had failed to properly attend to matters specific to the audit of foundations. It

also found that the standard audit report that had been drawn up for foundations fell short of the requirements of the Foundations Act. At Finanstilsynet's initiative, contact was established between the Foundations Authority and the Norwegian Institute of Public Accountants to clarify the content of the audit of the management of a foundation and what should receive comment in the audit report.

In spring 2009 Finanstilsynet conducted a thematic inspection of statutory auditors' role and tasks. It did so having in several cases questioned the adequacy of the statutory auditor's involvement in the audit. Further, given the very large number of audit clients some statutory auditors have on their books, doubt can be cast over their capacity to do a proper job. The agency checked a total of 78 audit assignments. The inspections showed that the statutory auditor had by and large been involved in the audit but, according to the documentation, at so late a stage that there was a risk that the audit report had been prepared without the presence of sufficient and appropriate audit evidence for the conclusion. Moreover, in some cases the statutory auditor had only documented his involvement after presentation of the audit report. A synoptic report is available on Finanstilsynet's website.

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 responses via the Altinn internet portal. All entities listed in the Register of Auditors are required to answer the questionnaire, regardless of whether or not they are active in the profession. Finanstilsynet sent reminders and warnings of licence revocation to 148 auditors who had failed to respond to the questionnaire. Finanstilsynet will make a synoptic report available on its website in spring 2010. The replies to the questionnaire will be used to check and follow up each auditor's and audit firm's compliance with the legal requirements governing auditor approval.

LICENSING

Table 12: Number of approved auditors and audit firms

	31.12.2006	31.12.2007	31.12.2008	31.12.2009	Licensed in 2009
State authorised auditors	2,554	2,642	2,728	2,826	122
Registered auditors	3,113	3,028	3,049	3,117	111
Audit firms	730	789	825	820	52

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

Finanstilsynet authorises auditors as either registered or state authorised auditors. State authorised auditors are subject to higher education requirements than are registered auditors. Students who entered the education programme in 2000 or later are also required to pass a practical examination in order to qualify for authorisation. The examination is prepared by an examination board and is organised by Agder University College. All 324 candidates passed the examination when it was held for the fifth time in autumn 2009.

Finanstilsynet has upgraded the Register of Auditors to enable more data to be fed in. All auditors who take on statutory audit tasks will be assigned an auditor register number in the course of 2010. The stage has also been set for registration of auditors who audit companies domiciled in countries outside the EEA and listed on a stock exchange in Norway.

As a result of the implementation of the Audit Directive in Norwegian law, provisions have been added to the Auditors Act requiring both auditor and client, in cases where an audit assignment is terminated before the expiry of the period of service provision, to inform Finanstilsynet of the grounds. These reports are additional to the obligation to report such termination to the Register of Business Enterprises in Brønnøysund. "Before the expiry of the period of service provision" means cases where the assignment is terminated on a date that is not the date of the ordinary general meeting or partners' meeting. In 2009 Finanstilsynet received 2,813 such reports. The agency has not had the capacity needed to actively follow up the reporting obligation or the reports.

REGULATORY DEVELOPMENT

In 2009 amendments were adopted to the Auditors Act and other legislation implementing the Audit Directive in Norwegian law, and Finanstilsynet has drafted regulations. The draft regulations cover registration of auditors who audit firms domiciled elsewhere in the EEA that have issued securities quoted on Oslo Børs or Oslo Axess.

The EU Commission has issued two recommendations related to the Audit Directive. One deals with public oversight of auditors that audit public interest entities. Auditor supervision in Norway conforms to this recommendation. The other recommendation deals with limitation of auditors' liability. This was circulated for comment by the Ministry of Finance in December 2008, and Finanstilsynet provided consultative comment. The matter is still under consideration at the ministry.

In July 2009 the Ministry of Finance circulated for comment NOU 2008: 12 *The audit obligation for small enterprises*. The matter is still under consideration at the ministry.

At the request of the Ministry of Finance, Finanstilsynet drafted in autumn 2008 amendments to the Auditors Act to implement Directive 2005/36/EC on the recognition of professional qualifications. The Ministry of Finance circulated the proposal for comment in January 2009. The proposal is under consideration at the ministry.

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 audit practice" in the Auditors Act.

Finanstilsynet
Postboks 1187 Sentrum
0107 Oslo

Oslo, 28 January 2010
Our ref.: AF/Ib

DnR Quality Assurance – Annual Report 2009

With reference to the “Guidelines for cooperation between Finanstilsynet (The Financial Supervisory Authority of Norway) and Den norske Revisorforening (DnR) – the Norwegian Institute of Public Accountants) regarding quality reviews of statutory auditors”, the Board of DnR hereby presents a summary of the results of the quality assurance reviews conducted in 2009.

Organisation of quality assurance reviews in 2009

The procedures of the quality assurance review is described in “Details of the quality control programme 2009” as posted on www.revisorforeningen.no. It is designed to check compliance with good auditing practice, including standards on auditing, and focuses on the provisions of the Auditors Act concerning auditors’ finances, independence, indemnity insurance and continuing education.

The review team comprised 39 state authorised and registered auditors, all with a broad professional background.

Selection of auditors for quality assurance reviews

The quality assurance programme in 2009 encompassed 1,514 statutory auditors. 282 statutory auditors were selected for ordinary review, including two ordinary reviews deferred from 2008. Upon being notified that they had been selected for ordinary review, 19 of these 282 auditors announced their intention to wind up their business or to retire as statutory auditors in the course of 2009. A further three members were taken out of DnR’s quality assurance programme since they had already been notified of follow-up reviews by Finanstilsynet. One member selected for review lost his licence. This left 259 statutory auditors to undergo ordinary review in 2009. Two of these ordinary reviews were deferred to 2010 and will be included in next year’s statistics. A further 44 statutory auditors were subject to follow-up reviews, including one deferred from 2008, while one follow-up review has been deferred to 2010.

Result of the quality review programme

In our opinion Norwegian statutory auditors maintain a high professional standard, and 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 means of technical information and guidance to our members.

	Number	%
Approved	252	83.8
Audit flaws and/or other shortcomings – action plan and new review	44	14.6
Referrals to Finanstilsynet for further action	5	1.6
Total number of reviews conducted	301	100.0

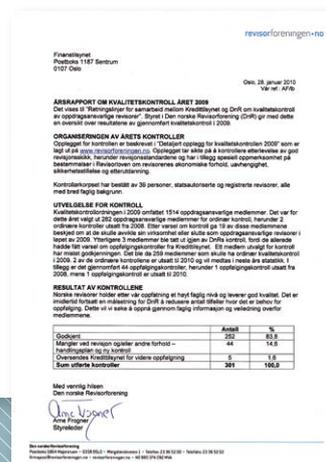
Yours sincerely

(sign.)

Arne Frogner

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 practices.

TRENDS

The industry comprises just under 20 large external accounting firms and groups 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 small ones.

Any change in the limits to the statutory audit obligation may impact on the external accounting industry in as much as more auditors will apply for authorisation as external accountants. Firms that opt against having an audit will be able to obtain advisory services from external accountants to a greater degree 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. New regulations on risk management and internal control, which entered into force on 1 January 2009, also apply to external accounting firms. In addition to the increased risk involved in the use of ICT, the above development actualises the issue of business outsourcing by external accounting firms, and non-resident actors' access to the Norwegian market.

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. Checks to verify compliance with regulations on risk management and internal control will take place in 2010.

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 priority for Finanstilsynet. Guidelines for the collaboration with NARF have been drawn up. Off-site supervision in 2008 showed a rising number of authorised external accountants that are members of NARF. In that year 58.5 per cent of all authorised external accountants reported NARF membership. NARF's quality control report for 2009 is reproduced on page 81.

In addition to reports from NARF, Finanstilsynet's inspections are normally based on reports received from sources such as the Tax Administration, liquidators of bankruptcy estates, clients of external accountants and media coverage. Some checks are carried out without being prompted by suspicion of rule breaches. When external accountants are selected for inspection, a criterion employed is whether or not they are quality controlled by NARF. Finanstilsynet has a particular focus on the largest external accounting firms and groups.

Finanstilsynet processed a total of 69 supervisory cases in 2009, of which 62 were related to appointed external accountants and seven to external accounting firms. The agency'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

	2006	2007	2008	2009
External accountants, licences revoked	11	49	19	47
External accounting firms, licences revoked	1	19	0	47*
Suspension**	0	1	1	0

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

** Applies since 30 June 2006.

The number of licence revocations is higher every second year since failure to respond to Finanstilsynet's questionnaire in the off-site supervision normally leads to revocation of authorisation as an external accountant. In 2009 47 revocations were ordered for this reason, 36 of which referred to external accountants and 11 to external accounting firms. All authorised external accountants and external accounting firms are subject to such 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. The last round of such supervision was in autumn 2008 when reports were submitted via the Altinn internet portal. In spring 2009 Finanstilsynet presented a report subsequent to the off-site supervision programme which is available on the agency'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. In 2009 Finanstilsynet carried out a special follow up of external accounting firms in a negative equity capital position and of external accountants and external accounting firms who reported not having submitted their tax returns and accounts on time.

Seminars for external accountants

In 2009 Finanstilsynet gave presentations at ten 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. About 757 external accountants attended. Finanstilsynet gave further presentations at three seminars organised by Økonomiforbundet, attended by 200 persons.

Unlawful external accounting activity

Finanstilsynet investigates entities reported to be carrying on business in violation of the Authorisation of External Accountants Act. Nineteen written reports of unlawful accounting activities were received in 2009. After further investigations Finanstilsynet issued three orders to halt activities for which a licence was required.

The agency wrote to the Norwegian Agrarian Association and the Norwegian Fishermen's Association asking them to remind their members that the opportunity of associations in the primary industries to provide external accounting services no longer applies.

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 register, which is available on the agency's website.

Table 14: Unlawful external accounting activity

	2006	2007	2008	2009
Reports received	47	33	19	19
Activities suspended	18	9	7	3
Reports to the police	2	0	0	1

LICENSING

Standard application forms for external accountants and external accounting firms were put into use in 2009 to ensure more complete

applications, and thereby reduce processing time. The application form and guidance are available on Finanstilsynet's website.

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

	2006	2007	2008	31.12.2009	Licenses in 2009
External accountants	7,472	7,966	8,340	8,780	693
External accounting firms	2,652	2,691	2,676	2,693	183

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

In 2006 the Accounting Regulations were amended to require compliance with the continuing education requirement. According to transitional provisions the requirement must be complied with as from

31 December 2009. Finanstilsynet reminded all authorised external accountants of this requirement in June 2009. Lack of continuing education could prompt withdrawal of authorisation.

REGULATORY DEVELOPMENT

Finanstilsynet circulated for comment an amendment to the Accounting Regulations in January 2009. This was in response to the implementation of Directive 2005/36/EC on the recognition of professional qualifications, which superseded Directive 89/48/EEC on a general system for the recognition of higher-education diplomas. The agency's proposal continues the right of external accountants holding professional qualifications from other EEA states to achieve authorisation in Norway. It also allows external accountants holding professional qualifications from other EEA states who move to Norway to inform Finanstilsynet of their intention to operate as external accountants in Norway on a temporary basis. The amendments will be adopted and enter into force early in 2010.

Act of 19 June 2009 on Services (Services Act) entered into force on 28 December 2009. The act contains special rules for processing applications to engage in the provision of licensable services. At the request of the Ministry of Finance, Finanstilsynet examined the need for diverging rules in respect of applications for authorisation as an external accountant or external accounting firm. As recommended by Finanstilsynet, the legal basis needed to establish such rules is included in the Accounting Act. The amendment to that act entered into force on the same date as the Services Act. Draft regulations on application processing time and the effects of overstepping time limits were circulated for comment by the Ministry of Finance in October 2009. The amendments, which entered into force on 28 December 2009, have yet to be implemented.

Finanstilsynet
 Postboks 1187 Sentrum
 0107 Oslo

Oslo, 29 January 2010

NARF Quality Control – Annual Report 2009

The Norwegian Association of Authorised Accountants (NARF) conducted its quality control programme in 2009 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 2008. We hereby present an overview of controls conducted in 2009.

Number of controls

A total of 364 quality controls were conducted in 2009, of which 36 were follow-up controls. This is slightly fewer than in 2008 when the corresponding figures were 362 and 54 respectively.

Level of control and implementation

As part of a continuing aim to improve members' service quality, 10 quality control seminars were held in autumn 2009. The focus was on statutory requirements and good accounting practices. Finanstilsynet played a contributory role.

The control programme for 2009 was based on previous control programmes, but focused to a greater degree than previously on topical issues in connection with the financial crisis.

Twenty-eight controllers were engaged in the 2009 control programme, the great majority having attended a two-day seminar in advance. The seminar focused on ethical questions, 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 2009 quality control programme produced the following results:

	Ordinary controls				Follow-up controls			
	Individuals	%	Firms	%	Individuals	%	Firms	%
Approvals	520	87	264	81	55	82	24	69
Follow-up controls	81	13	62	19	12	18	11	31
Total	601	100	326	100	67	100	35	100
Control results yet to be processed	2		2		1		1	

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

Eight cases were referred to Finanstilsynet in 2009 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 and ordinary housing cooperatives' sale of cooperative flats. Firms, lawyers and housing cooperatives are checked for compliance with the requirements of the law and regulations, including observance of good estate agency practice. Finanstilsynet's responsibility for supervision of estate agency activities is accompanied by administrative, consultative and information tasks under the Estate Agency Act.

ESTATE AGENCY



TRENDS

Further decline in the number of estate agency firms

Many firms were compelled to close down for financial reasons as a result of the slump in the property market in 2008. The number of firms fell from 717 at the start of the year to 611 at year-end, i.e. by a net figure of 106. The marked decline continued in the first four months of 2009 up to the point where activity levels in the property market began to pick up early in summer 2009. Although new firms were established during the year, the total number of estate agency firms fell to 516 by end-2009, i.e. a net decline of 95 firms. The large decline in 2009 was due in part to 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 act by the end of 2009. A number of firms omitted to reapply for various reasons; see description under "Licensing".

Many estate agency firms have a significant branch network. At the end of 2009, 353 branches were registered, bringing the number of localities in Norway where estate agency services were offered under the auspices of specialised estate agency firms to 870 at the start of 2010. At the same point 14 housing cooperatives brokered sales of their own flats, and 1,308 lawyers had furnished the security needed to engage in estate agency.

SUPERVISION AND MONITORING

Inspections in 2009

Finanstilsynet conducted 29 on-site inspections of estate agency firms and lawyers in 2009. One additional IT inspection was carried out. The following themes were in focus:

- finances
- compliance with the duty to obtain and disclose information
- treatment of client assets and completion of the financial settlement
- compliance with the regulations on risk management and internal control
- compliance with the money laundering legislation

The slump in the property market has put a tight squeeze on the finances of many estate agencies. Two major factors have intensified the industry's problems in a sluggish market: a) over-establishment in some areas has led to price competition, substantially driving down estate agency fees, and b) the very low equity capital position and weak financial cushion of many agencies in the face of a contracting market. Estate agencies have substantial client assets under management which, particularly in a downturn, heightens the importance of Finanstilsynet's monitoring of client assets and of agencies' financial position, as was the case in 2009. Over the year a number of poorly capitalised agencies were subject to inspections and written approaches. This prompted some agencies to cease trading, while others had to supply capital in order to meet the statutory financial requirements.

Flaws noted in property-for-sale descriptions and settlement procedure

The estate agent's duty to obtain, check and pass on information about a property is regulated in detail in the Estate Agency Act. An important part of Finanstilsynet's supervision is to check compliance with the legislation by scrutinising individual transactions at on-site inspections. Property-for-sale descriptions are often found to be deficient and to lack requisite information on the property.

Where financial settlement is concerned, cases of serious dereliction of the agent's obligations have been brought to light. These largely involve breaches of, in some cases non-statutory, rules for the correct exchange of performances between buyer and seller which may involve the agent, prior to transfer of property title, paying 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.

Gradual adjustment to new internal control requirements

Estate agency firms became subject to the Internal Control Regulations (Regulations on Risk Management and Internal Control) as from 2008 when the new Estate Agency Act entered into force. The agency management has overall responsibility for the establishment of proper control routines. A good internal control system, used proactively in the business, will be a hallmark of a serious firm and could prevent agents from committing serious errors likely to cause

ESTATE AGENCY

direct financial loss. There is a substantial gain to be made from not making mistakes and thereby avoiding negative media coverage and Finanstilsynet's sanctions. Thus far, supervisory experience indicates that firms are measuring up to the internal control requirement with varying success. Although some firms have procured comprehensive system descriptions in the form of manuals and the like, documentation of its active use in the day-to-day business is not always available.

Breaches of the money laundering legislation

A new Act on measures to combat money laundering and the financing of terrorism (Money Laundering Act) entered into force on 15 April 2009. Estate agencies and lawyers engaged in estate agency are reporting entities under the Money Laundering Act. The legislation requires reporting entities to maintain proper internal control and communication routines that ensure compliance with obligations under this Act. At on-site inspections in 2009 checks were made to ensure that estate agencies had such routines in place.

Some inspections revealed transactions which, based on objective criteria, appeared suspicious and should have been scrutinised and in the event reported to ØKOKRIM. In these cases Finanstilsynet did not, however, take a position on whether the transactions were in fact related to criminal offences. In one case Finanstilsynet opted to report the estate agency to the police for failure to investigate and report as required under the Money Laundering Act.

Revocation of the right to carry on estate agency

The licence of an agency or lawyer may be revoked in cases where it is inadvisable to allow the business to continue, for example where an agency or lawyer has grossly or repeatedly breached obligations pursuant to the rules. An estate agency certificate may be revoked where the holder is deemed unfit, for example where the individual has grossly or repeatedly breached his or her duties pursuant to law or regulations.

Three agency licences were revoked in 2009 due to breaches of the conduct-of-business rules. One licence was revoked due to serious breaches of the money laundering legislation, i.e. failure to report suspicious transactions to ØKOKRIM and because irregular transfers of large sums had been made from a client account to agency employees in a manner that concealed the true nature of the transactions. In this case, moreover, settlement had in one instance been paid without security being furnished, thereby exposing the buyers to substantial risk, and major deficiencies were noted in record keeping and estate agency routines. In the second case, serious settlement errors had been committed which had inflicted substantial loss on a client, and client asset reconciliation and record keeping were deficient. In the third case, the licence revocation was due to failure to comply with an order from Finanstilsynet to document that client assets were correctly handled and that the agency's finances were satisfactory, both being necessary to render it probable that the agency was a going concern.

The right of one lawyer to carry on estate agency was revoked principally because he had issued a guarantee in favour of the buyer's bank which he knew would not be called because, being the estate agent, he was aware that at the time the guarantee was issued the property had already been resold.

The estate agency certificates of three individuals at three different estate agencies were revoked because they, in their capacity as responsible for settlements, had executed transactions with client assets that entailed gross breaches of good estate agency practice. In so doing, they caused actual and substantial losses for clients in two cases and a risk of major losses in the third case.

In another case a lawyer's right to act as 'estate agent in charge' at an estate agency was revoked as a result of failure to attend to the control function attached to this position. Further violations of laws and regulations were noted, also prompting revocation of the agency's licence.

LICENSING

New licences awarded to all estate agencies

In connection with the entry into force of the Estate Agency Act of 29 June 2007, the Ministry of Finance issued regulations containing transitional rules that allowed all agencies holding a licence under the previous act to carry on their estate agency business without applying for a licence to engage in estate agency under the new act for up to two years after the act's entry into force, i.e. up to 1 January 2010.

In practice it turned out that a large majority of agencies opted to defer application for a new licence until autumn 2009. Finanstilsynet faced a large task in issuing the new licences, in particular because the requirements for obtaining a licence were substantially wider than under the old act. Good-repute requirements have been introduced for management board members and general manager that need to

be documented by police certificate. Moreover, the new act includes requirements on board members' and the general manager's competence, and a management board declaration that the agency has sufficient capital and that estate agency procedures have been prepared.

The process of awarding licences went off without problems of note, however, and virtually all agencies intending to continue their estate agency business after 1 January 2010 were awarded the requisite licence by the end of 2009. About 40 agencies omitted to apply for a new licence since their business was either minimal or had in practice ceased.

Licensing of 'transitional estate agents'

The new Estate Agency Act introduced in 2008 two new types of competence certificate for persons filling certain positions at estate agency firms. These certificates are in addition to the estate agency certificate held by persons who have the statutory training and experience and are fit and proper. The act requires estate agency firms to designate an estate agent responsible for each assignment who will perform the most essential agency functions. Only persons holding

an estate agency certificate or lawyers with the requisite experience and who are otherwise fit and proper may be a 'responsible estate agent'. Lawyers with estate agency experience may also be the 'estate agent in charge' at estate agency firms. Such authorisations were issued to 31 lawyers in 2009.

However, the requirement that a responsible estate agent should hold an estate agency certificate or be a lawyer will only apply as from 1 January 2011. In a three-year transitional period from the entry into force on the Act, persons with at least three years' practical experience of estate agency, and who in addition pass an examination approved by Finanstilsynet and otherwise meet the conditions for being issued with an estate agency certificate, will also qualify as responsible estate agents. Finanstilsynet issued just 417 such licences to 'transitional estate agents' in 2008 and 2009. In light of the fact that a very large number of persons have been operating as estate agents without the requisite training, a large increase in the number of applications can be expected in 2010 which is the final transitional year before the competence requirement for responsible estate agents comes into force.

REGULATORY DEVELOPMENT

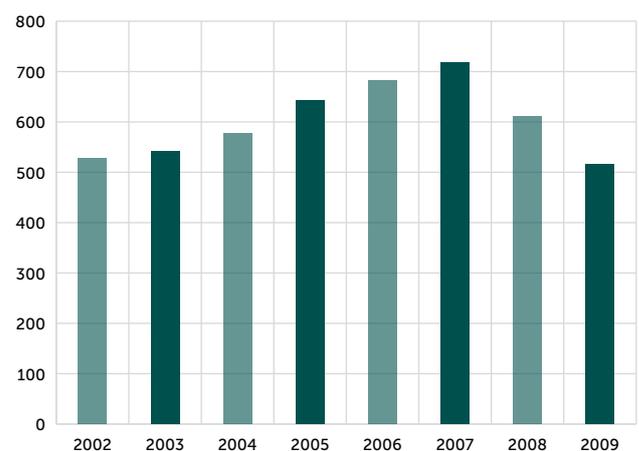
Draft regulations related to the quid-pro-quo principle

In the course of 2009 Finanstilsynet proposed to the Ministry of Finance certain amendments to the legislation in the estate agency sphere.

The fundamentally most important of the proposals is that funds paid in by the buyer to the estate agency to cover the purchase price for the property cannot be disposed over in favour of the seller before the buyer has acquired legal right to the property in the land register. This provision may inter alia be waived outside consumer purchases. Finanstilsynet bases the proposal on its impression that estate agencies' traditional practice of effecting final settlement after transfer of title deeds has been waived in recent years based on the assumption that the so-called guarantee bond provides sufficient protection against financial risk on the part of the buyer. However, Finanstilsynet doubts whether a proper risk assessment is feasible in the individual case. The proposal entails either that the estate agency fee must be paid by the principal on the due date or that the broker provides the principal with credit until the purchase sum can be

disposed over in favour of the seller, i.e. after transfer of title deeds, which takes somewhat longer.

Chart 7: Number of estate agencies as at 31.12.



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

Substantial increase in the number of debt collection cases

About 2,759,000 new cases were referred to debt collection agencies in the first half of 2009, an increase of about 24 per cent or 531,000 cases over the same period of 2008. This is the largest number of new cases ever referred to debt collection agencies in the course of a half-year period.

Debt collection agencies had 3,239,000 cases in process as at 30 June 2009, representing claims for recovery totalling NOK 58.7 billion, including interest and debt collection expenses. This was an increase of about 339,000 cases and NOK 9.5 billion in claims for recovery compared with the same point in 2008.

Of the total debt collection cases that were brought to completion in the first half of 2009 – numbering 2,603,000 – as many as 740,000 were closed before dispatch of a demand for payment, i.e. before it was necessary to initiate further debt collection measures entailing higher extrajudicial costs for the debtors.

Stable industry structure

The structure of the debt collection industry has remained virtually unchanged over the past ten years. 110 ordinary debt collection agencies were registered at the end of 2009 compared with 116 at the start of the year. Just a few of these are sizeable actors. As at mid-year eight agencies accounted for about 70 per cent of ongoing cases, while just six accounted for almost 80 per cent of claims for recovery. The largest actors are Lindorff AS / Lindorff Obligations AS, Aktiv Kapital Norge AS, Kredinor and Intrum Justitia AS. For most of these agencies the debt collection market can probably be

characterised as good in the sense that the supply of business has been increasing at the same time as the resolution ratio has been high. A high resolution ratio and that fact that a large proportion of debt collection cases is resolved at an early stage of the recovery process suggests that a laxer attitude to timely payment rather than a poor ability to pay on the part of debtors has made itself felt in many instances.

Of firms that purchase overdue debt and collect it themselves under a special licence, only six were left at the end of 2009. These firms hold a portfolio of overdue payments worth NOK 1.5 billion. However, such activity is also engaged in by a number of finance and mortgage companies that do not need a debt collection licence since they hold a special financial services licence.

Steep reduction in debt collection fees

Given the rules governing debt collection fees up to and including 2009, and the steadily increasing supply of payment defaults referred for debt recovery, debt collection agencies' business has by and large previously provided a satisfactory return. However, as a result of the Ministry of Justice and the Police's decision in autumn 2009, the debt collection industry faces a substantial challenge as from 1 January 2010 when debtors' liability for debt collection expenses is reduced by between 20 and 50 per cent depending on the size of the claim. Whether all agencies will survive such a steep reduction fees/earnings is a moot point. Much depends on whether the agencies can obtain full or partial compensation for the revenue reduction by renegotiating agreements with principals so that the creditor pays parts of the recovery costs. The creditors' alternative is to take back the assignments and collect their claims themselves.

SUPERVISION AND MONITORING

Inspections in 2009

Finanstilsynet conducted 11 on-site inspections at ordinary debt collection agencies and a number of limited, document-based investigations based on correspondence with the agencies concerned to look into debtors' allegations of flawed debt collection procedures. One IT inspection was conducted.

The on-site inspections revealed a number of cases of flawed assignment agreements between debt collectors and their clients; use of deficient debt collection notices, demands for payment and other

claim letters; and instances where debt collection notices were sent prematurely. Finanstilsynet also made a number of comments on agencies' routines for client asset treatment, including routines for reconciliation of client funds against client liability, and some comments on agencies' compliance with the regulations governing ICT systems at banks etc.

Finanstilsynet also investigated agencies' compliance with regulations on risk management and internal control, and some agencies were found to be unfamiliar, or non-compliant, with these regulations.

DEBT COLLECTION

Revocation of licences

Two personal debt collection licences were revoked as a result of findings made during on-site inspections, in both cases because the individuals concerned, in their capacity as de facto manager, had for some

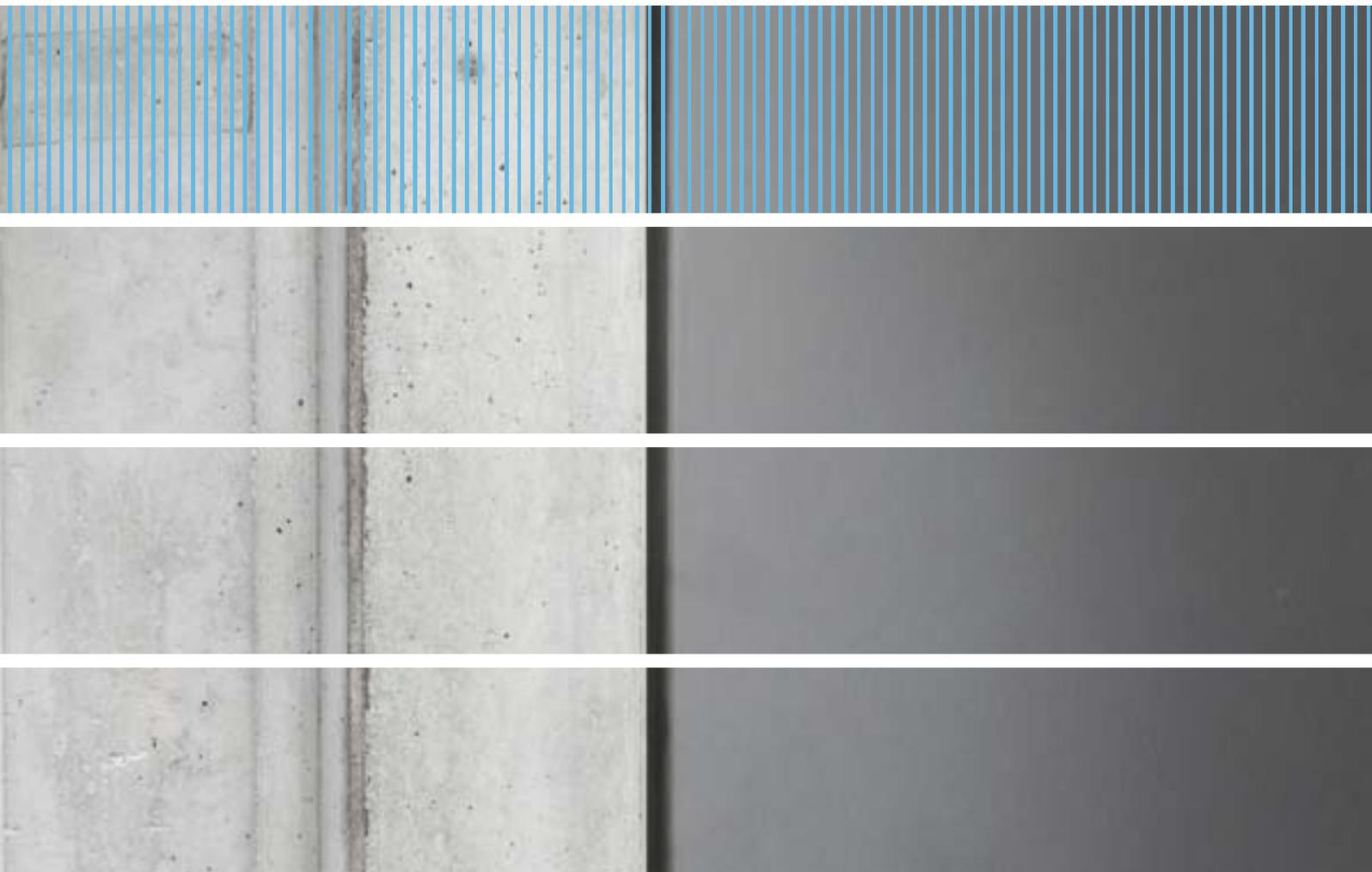
time maintained poor control over the debt collection business, as reflected in a number of serious and protracted procedural errors of substantial proportions.

LICENSING

Complaints/approaches related to the requirement as to good debt collection practice

Finanstilsynet received 214 written complaints/approaches concerning firms licensed to carry on debt collection in 2009 compared with 291 the previous year. About three out of four complainants were consumers, the remainder businesses. The complaints targeted

numerous and diverse circumstances, but most related to debt collectors' treatment of objections and their calculation of debt collection fees. Businesses complained above all about being registered by debt collectors on the debtors list, and not being expunged from that list, as well as about debt collectors' handling of objections.

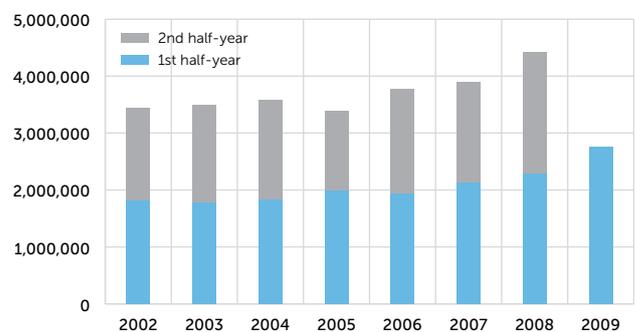


REGULATORY DEVELOPMENT

As mentioned above, debt collection fees were substantially reduced by the decision of the Ministry of Justice and the Police to amend regulations in September 2009 which affects all claims falling due on 1 January 2010 and later.

In November 2009 the Ministry of Justice and the Police circulated for comment draft amendments to the Debt Collection Regulations that were needed to bring the regulations into line with the Directive on the recognition of professional qualifications and the Services Directive, both of which are binding on Norway by virtue of the EEA Agreement. The amendments will if adopted entitle service providers established in another EEA state to engage in debt collection in Norway on a temporary basis without obtaining a debt collection licence or registering their business.

Chart 8: Number of debt collection cases received



Source: Finanstilsynet



SUPERVISION OF IT AND PAYMENT SERVICES 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 services systems, to ensure that payment services are performed in a sound, coordinated and rational manner. The regime includes checking that institutions operate in a satisfactory manner and in compliance with the ICT regulations and other bodies of rules.



TRENDS

ICT solutions in the financial sector have long made use of functions geared to a mass market, for example Microsoft Office products and security products such as Symantec, Norman and F-secur. Developments in this area and new business process areas within the same distribution and management structure proceed largely via the internet. ICT-related tasks have evolved outside Norway, which works well so long as the reception system adapts to the situation. A new situation has now arisen with the substantial volume of outsourcing in evidence in the operations area as elsewhere, in the first instance to other Nordic countries. In 2009 there were also signs that important ICT-related operations may be moved out of the Nordic region and out of our cultural and geographical proximity. If this development continues, it will over time pose significant challenges for the financial sector in Norway in terms of risk management and preparedness.

There is a growing tendency for organised crime in areas where the internet is used as a platform to attack solutions in use in the financial sector and where the internet is built into client solutions in the financial sector. Such crime, cybercrime, affects internet bank solutions and internet commerce. Attacks come in waves, interspersed

with long periods without attack or periods where the attacks are stopped by the sector's own countermeasures. Through its participation in international cooperation in this field Finanstilsynet keeps abreast of the situation and developments in other countries. This heightens the ability to put in place countermeasures to prevent or weaken new attacks. Finanstilsynet considers it important to give this area sufficient priority and to try to stay a step ahead of the solutions used by criminal groups.

In 2009 Norwegian point of sale terminals for card payments were exposed to serious attack, skimming, through illegal capture of the content of the cardholder's magnetic strip. The national debit card solution, BankAxept, is thus corrupted. Since this standard has been shown to provide inadequate protection, the solution needs to be reconsidered in light of events and the development of the PCI standard, the international parallel to the Norwegian standard. In retail trade, debit and credit cards are widely used in conjunction with the banks' payment systems, a fact of major social significance for the country. That is why it is important to secure the confidence of the general public in the solutions, and a challenge to find effective ways to counter this type of attack.

SUPERVISION AND MONITORING

IT inspections

In 2009 Finanstilsynet conducted 22 IT inspections and inspections of payment service systems at banks, insurers, finance companies, mortgage companies, securities institutions, real estate agencies and external accounting firms. Inspections were also carried out at IT service providers under the ICT Regulations section 12 on the outsourcing of ICT operations. A further 18 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 importance to the nation and were otherwise based on a risk assessment in which priority was given inter alia to electronic payment solutions. The following concerns received most attention in 2009:

- Inadequate solutions for catastrophe back-up and absence of testing
- Deficiencies related to management and control of ICT activity
- Incomplete implementation of risk and vulnerability (RAV) analyses
- Inadequate control in connection with the installation and maintenance of security solutions related to firewalls and virus checking
- Vulnerabilities in digital distribution solutions to clients

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 2009 Finanstilsynet received six such notifications. Since this provided insufficient information to undertake an overall assessment of risk, a project was set in train, continuing in 2010, to examine and evaluate functions in payment service systems related to logging on, authentication, security and authorisation solutions. The object is to ensure that the solutions in use conform to the applicable rules and that the level of risk inherent in them is acceptable. Finanstilsynet works closely with Norges Bank in the payment systems field. This ensures reciprocal information and coordination in cases where this is expedient.

Risk and vulnerability (RAV) analysis

Early in 2010, repeating previous practice, Finanstilsynet is to publish an RAV analysis of ICT use in the financial sector in 2009. Based on in-house analyses and data sources available to the agency, Finanstilsynet has prioritised specific risk areas requiring further follow-up and concrete action. Finanstilsynet's RAV analysis for 2009 gives a detailed account.

The financial industry is part of society's critical infrastructure, of which ICT is a critical element. A survey of ICT infrastructure in the financial sector, initiated by Finanstilsynet and completed in 2009, covered both logical and physical infrastructure. Based on the survey, an analysis was undertaken to identify possible vulnerable areas and any deficiencies in the management and control of the infrastructure.

Outsourcing of ICT services from Norway is identified as a risk area. For that reason a study was set in train to ascertain risk factors and recommend relevant measures. It includes reviewing Norwegian legislation and identifying international recommendations that provide guidance on risk management in this area.

Event reporting

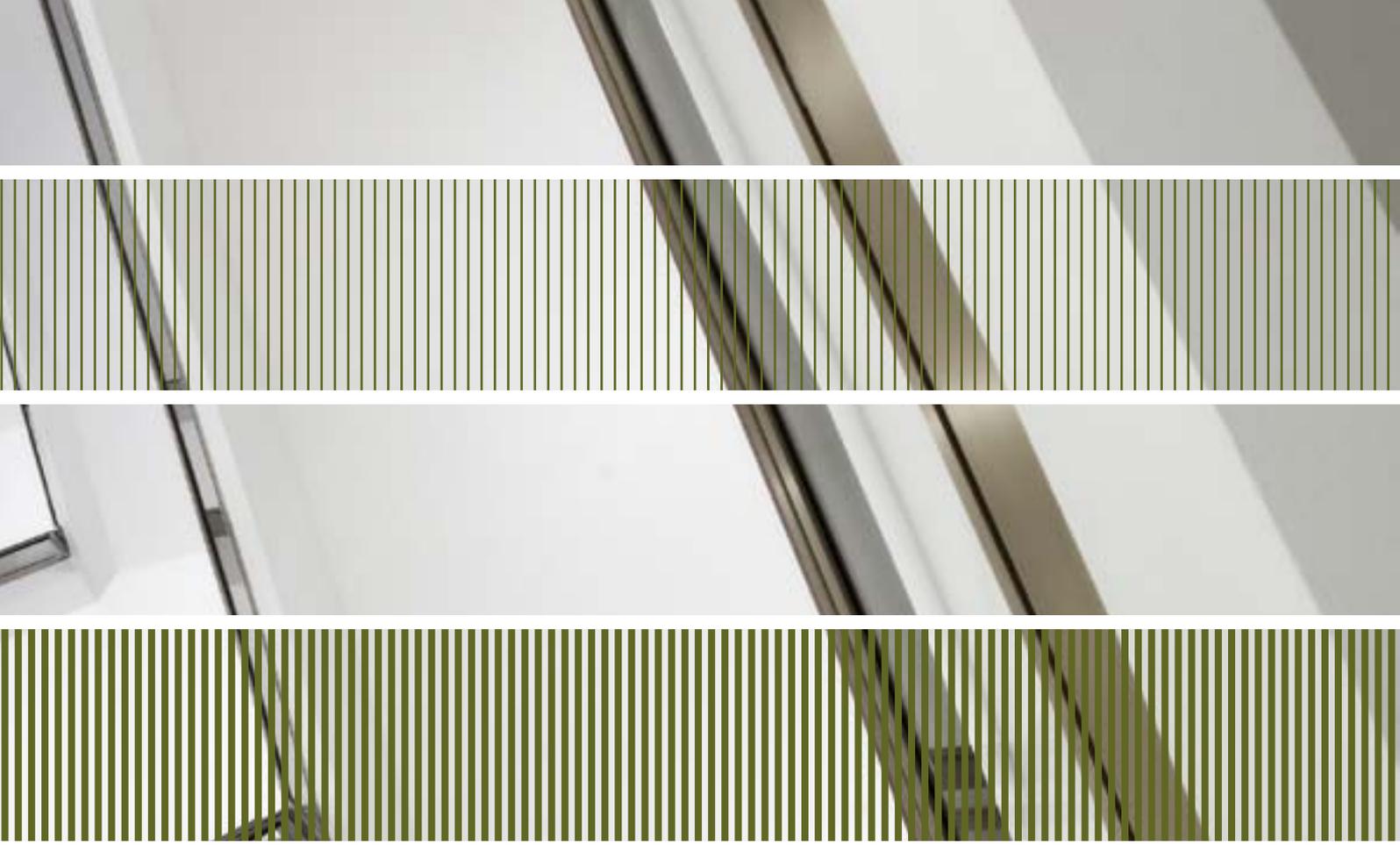
In 2007 a trial arrangement was set up for event reporting to Finanstilsynet. The conclusion drawn was that this was a useful means of ensuring timely and correct information on serious ICT events in the financial sector. The arrangement also encourages individual firms to make active use of events in their own work on assuring sufficient quality and acceptable risk. The data provided by event reporting are used in the RAV analysis and as a basis for raising current issues directly with the institutions concerned.

Crisis preparedness

Work on ensuring sufficient preparedness in the ICT area in the financial sector is continuing through close cooperation with the Financial Infrastructure Crisis Preparedness Committee (BFI). The work builds on experience gained from the nationwide exercise ICT-08, held under the auspices of the Directorate for Civil Protection and Emergency Planning (DSB), in which Finanstilsynet played a coordinating role for the financial sector.

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). Cooperation has been established with Norges Bank (on payment systems), the National Security Authority (NSM) (inter alia on event reporting), the Norwegian Post and Telecommunications Authority, the Data Inspectorate and trade organisations. The agency participates in an international supervisory collaboration, Information Technology Supervisors Group (ITSG), and in the development of international standards through groups working on banking and security standards, electronic signature standards (ETSI ESI) and the committee dealing with security issues under the International Federation for Information Processing



(IFIP). Finanstilsynet is Norway's representative in the European Security Research and Innovation Forum (ESRIF).

Finanstilsynet participates in an inter-European project focusing on internet security and notification (Communication Middleware for

Monitoring Financial Infrastructures). The project, financed partly 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.

REGULATORY DEVELOPMENT

Requirements for reporting serious and critical ICT events were established through an amendment to the ICT Regulations of 1 December 2009. Work has started on guides to key sections of the

ICT Regulations. Some guides were completed in 2009, and more will follow in 2010.



The financial crisis continued to impact on Finanstilsynet's international activities in 2009. There has been strong pressure from political quarters, consumers, international organisations and EU bodies to implement new rules and other measures to mitigate the effects of the crisis. International activity has been intense, and financial supervisors and regulators have rarely come in for as much attention as in the past two years. Steps were rapidly taken both globally and within the EU to strengthen international supervisory cooperation: the Financial Stability Board was established, the Basel Committee on Banking Supervision broadened its membership, and a new EU supervisory structure was proposed.

INTERNATIONAL ACTIVITIES



GLOBAL MEASURES TO STRENGTHEN REGULATION AND SUPERVISION

The financial crisis has highlighted the need for stronger international coordination of regulatory development and supervision. The financial crisis and regulation and supervision of the financial sector have featured on the agenda for G-20 summits since 2008, and the G-20 countries have drawn up common principles for reform of the financial markets. Steps were rapidly taken, including the establishment of the Financial Stability Board (FSB) and broadening of the Basel Committee on Banking Supervision, and a reform of the EU financial supervisory structure was proposed. The International Monetary Fund (IMF) acquired greater international coordinating responsibility. Responsibility for concretising the international reforms recommended by the G-20, the IMF and the FSB is assigned to international organisations such as the Basel Committee, the IAIS and IOSCO and the EU institutions and the EU's supervisory committees.

A wide-ranging international effort is under way in a number of forums to improve the regulation and supervision of financial institutions and markets. A particular call is being made to supplement the supervision of individual institutions with macroeconomic analyses of the state of and developments in the markets, i.e. a macroprudential approach. The financial crisis pressed home the need for better communication and coordination between governments, supervisors and central banks both at the national level and across borders, and work is in progress to strengthen and harmonise the rules and practice of crisis management.

Much political pressure is being applied to put in place a common rule book for large cross-border financial groups, and supervisory colleges responsible for coordinating supervision of such groups are to be established for all border-crossing financial institutions.

SUPERVISORY STRUCTURE OF SEVERAL COUNTRIES TO BE REORGANISED AS A RESULT OF THE FINANCIAL CRISIS

As a consequence of the financial crisis and ensuing criticism of the supervisory regime, a number of countries have opted to reorganise their national financial supervision structure. Several, for varying reasons, advocate a twin-peaks model which separates prudential supervision of banks, insurers and investment firms, from the supervision of market conduct and investor protection. This model seems to be gaining support in Austria, Belgium, France, Germany and Portugal, while Finland and Switzerland are among those countries

which have moved towards an integrated supervisory model akin to Norway's. Direct criticism of supervisory priorities in the United Kingdom and Ireland has had and will have consequences for the organisation of the supervisory authorities in these countries. In several countries there is a need to avoid conflicts between protection of investor and consumer interests on the one hand and safeguarding financial institutions' solvency (prudential supervision) on the other.

COOPERATION BETWEEN INTEGRATED SUPERVISORS

The integrated supervision model entails joint supervision of banks, insurance companies and securities businesses. Finanstilsynet was the first integrated supervisory body to be established in Europe, in 1986. The United Kingdom's setting up of the Financial Services Authority (FSA) in 1997, in particular, boosted international support for the model. Finland, the last Nordic country to do so, merged its supervisory authorities in the financial sector on 1 January 2009. Switzerland did likewise on the same date.

Since 1999 a number of supervisory authorities with an integrated approach to supervision have met informally each year, at the Integrated Financial Supervisors Conference, to discuss

administrative and technical matters of common interest. In 2009 the Dutch financial supervisor hosted the conference which was attended by representative of supervisory authorities from 16 countries including, for the first time, the Swiss supervisor FINMA. Topics discussed included follow-up of the financial crisis, crisis management, the role of government in financial institutions, financial conglomerates and practical issues with respect to supervisory colleges.

Reform of the EU's supervisory structure

Based on the de Larosière report, the EU Commission agreed on 27 May 2009 on a new supervisory structure at the European level. After a brief and intense round of consultation last summer, the

Commission adopted concrete legislative proposals on 23 September. The Ministry of Finance, Finanstilsynet and Norges Bank delivered a joint consultative response.

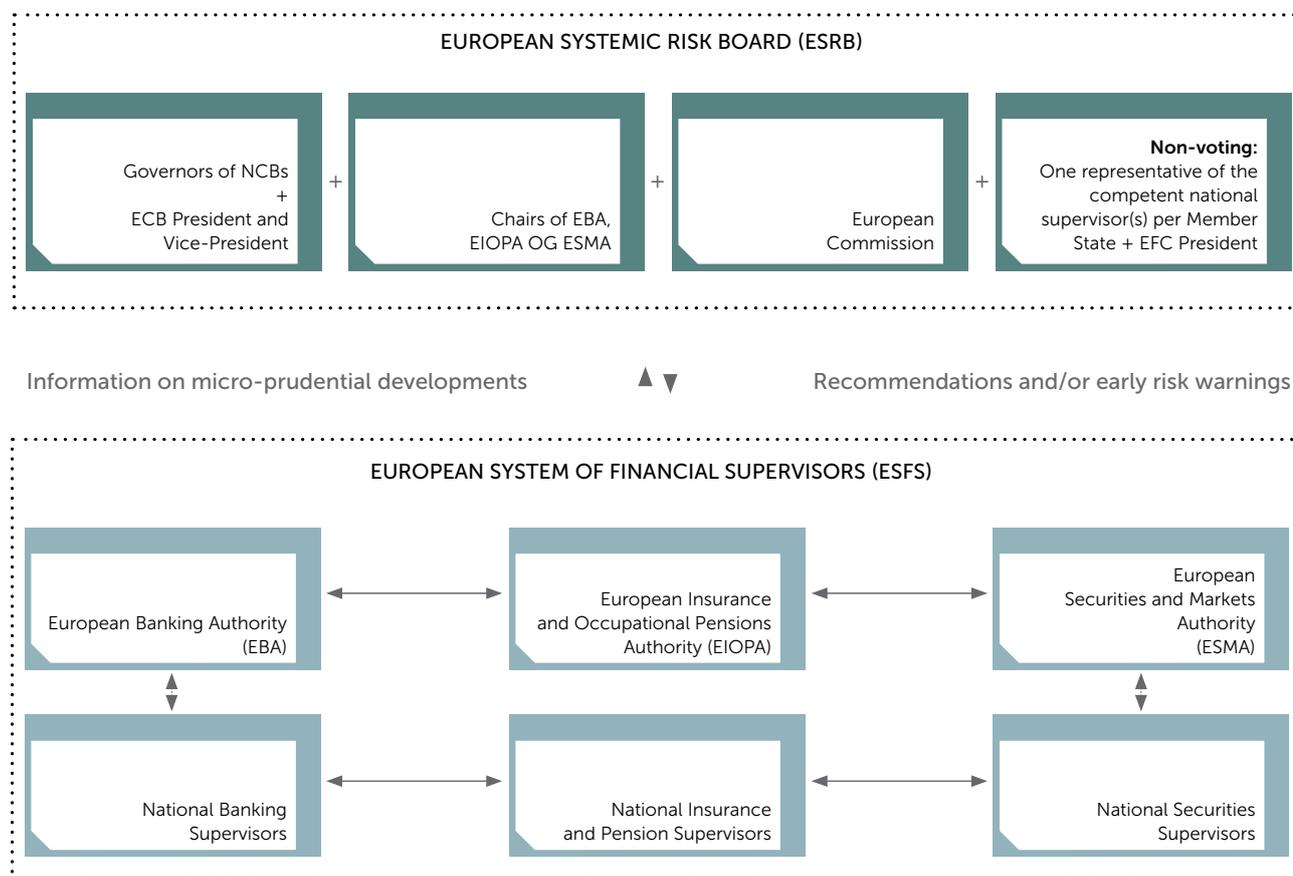
The Commission proposes the creation of a European System of Financial Supervisors (ESFS) with overall responsibility for supervision of individual financial institutions (“micro-prudential supervision”). In this system the existing supervisory committees, whose role in regulatory development is merely advisory, will be replaced by three European supervisory authorities empowered to adopt decisions across national jurisdictions. Supervisory colleges will be set up for cross-border financial institutions. The main responsibility for the day-to-day supervision will remain with the national supervisors. The new European supervisors – the European Banking Authority, the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority – will draw up and adopt joint supervisory standards which will become binding when adopted as regulations by the Commission. The European supervisory authorities will also be assigned legally binding mediation powers to settle disputes between national supervisors. They will, moreover, be empowered to apply binding decisions to national supervisors and

to issue direct orders to individual institutions. Under the proposal, coordination between these three bodies be formalised through a joint committee with specific responsibility for issues related to the regulation and supervision of financial conglomerates. Finanstilsynet will have observer status in these new European supervisory authorities.

The Commission also proposes the creation of a European Systemic Risk Board (ESRB) with overall responsibility for macro-prudential supervision, in which the chairs of the new European supervisory authorities and the Commission will participate in addition to the central banks and the European Central Bank (ECB). The ECB will also act as secretariat to the ESRB. National supervisors will be able to attend as observers. A proposal from the Swedish presidency has paved the way for Norwegian observer status on the ESRB on an ad hoc basis.

The Commission tabled concrete legislative proposals in the matter on 23 September 2009. The proposals were considered by the EU Council which adopted amendments on 2 December. The proposals are now being considered by the EU Parliament, and the new supervisory structure is expected to be introduced as from 2011.

Chart 9: Proposed new EU supervisory structure



SECURITIES MARKET

Finanstilsynet is a member of the International Organization of Securities Commissions (IOSCO) and attends the European Regional Committee and the IOSCO Commodity Futures Task Force. Finanstilsynet opted not to attend the annual meeting held in Tel Aviv in June 2009. IOSCO has drawn up a Multilateral Memorandum of Understanding (MMoU) concerning consultation and cooperation and the exchange of information to which Finanstilsynet acceded in 2006.

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

At the EU/EEA level Finanstilsynet participates in the Committee of European Securities Regulators (CESR). CESR acts as an advisory group to the European Securities Committee (ESC) and the EU Commission and works to ensure consistent supervision and

enforcement of community legislation in member countries. In 2009 CESR focused on measures related to the financial crisis and phase-in of rules governing the supervision of credit rating agencies.

Finanstilsynet plays an active part in several CESR working groups. It participates in CESR's Review Panel which in 2009 focused on reporting on the implementation of CESR's Standards No. 1 and 2 on financial information and the UCITS Directive (passporting). Much resources have been expended on mapping the MiFID Directive's and the Transparency Directive's implementations. The administrative sanctions available under the Market Abuse Directive were reviewed, and a major review was conducted of the Prospectus Directive. In 2009 an initiative was taken to reform CESR's working structure which, with its 70 subgroups, has been unwieldy and demanding.

In May 2009 Finanstilsynet hosted a meeting of CESR's European Enforcers Coordination Session (EECS) which seeks to harmonise and coordinate the enforcement of international accounting standards in the EEA.

BANKS AND FINANCIAL INSTITUTIONS

Government leaders and authorities have been concerned with reforming rules and supervisory structure in the wake of the financial crisis, and in international forums and EU bodies an intense effort is under way to develop a robust body of rules able to prevent future crises.

The Basel Committee on Banking Supervision under the Bank for International Settlements (BIS) adopts international standards for banking supervision and coordinates the global collaboration on banking supervision. Although Norway is not a member of the Basel Committee, Finanstilsynet receives relevant documents from the Committee and is invited to comment on them, and to take part in some of the Committee's activities. Every second year the Basel Committee organises an international conference for banking supervisors (International Conference of Banking Supervisors – ICBS). No conference was held in 2009.

Finanstilsynet attends, as an observer, meetings of the European Central Bank's Banking Supervision Committee and attends bilateral meetings with ECB representatives.

Finanstilsynet attends all meetings of the Committee of European Banking Supervisors (CEBS) and most meetings of CEBS' subgroups,

including Groupe de Contact (the main working group under CEBS). Work is in progress on proposals for amending the capital adequacy framework, including revised requirements on the quality of own funds through the application of maximum limits to hybrid capital and general requirements on characteristics of hybrid and tier 1 capital. CEBS has worked on guidelines to elaborate these requirements. Attention has also been given to liquidity risk management routines and to supervision of liquidity risk, to strengthening securitisation regulations, to tightening rules governing large exposures, to a common European reporting format and further harmonisation of capital adequacy reporting.

Strict requirements are imposed (both globally and at the EU/EEA level) with regard to creating supervisory colleges for all cross-border banking groups. The division of responsibilities between home country and host country is to be clarified. Work under CEBS' auspices is coordinated with the Basel Committee; see the account in the report *The Financial Market in Norway 2009: Risk Outlook*.

Within Groupe de Contact banking supervisors regularly exchange information on problems in the banking sector, and map and seek to coordinate supervisory methods in EEA countries. A networking group has also been specifically set up to coordinate operational

supervision of cross-border banking groups. CEBS and Groupe de Contact have played an important coordinating role in connection with the financial crisis, and in 2009 worked on a proposal to reform

and supplement the capital adequacy framework with a view to preventing future crises.

INSURANCE AND PENSIONS

Finanstilsynet is a member of the International Association of Insurance Supervisors (IAIS) and plays a part in developing international principles for supervision of insurance business. Finanstilsynet attends the IAIS annual conference and is represented on the technical committee, which has overarching responsibility for standard setting. The IAIS held its sixteenth annual conference in October 2009 in Rio de Janeiro where several standards and guidelines were adopted, including a Standard paper and Guidance paper on the structure of capital resources for solvency purposes, a Guidance paper on the use of supervisory colleges in group-wide supervision, an Issues paper on corporate governance and an Issues paper on relationship between the actuary and the external auditor in the preparation and audit of financial reports.

Finanstilsynet is also a member of the International Organization of Pensions Supervisors (IOPS) and attended IOPS' annual conference in 2009, also held in Rio de Janeiro. IOPS is developing standards for the regulation and supervision of private pensions.

At the EU/EEA level Finanstilsynet attends the meetings of the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS), and also participates in most of CEIOPS' working groups and committees. The bulk of CEIOPS' work in 2009 consisted in preparing advice to the European Commission on the reform of EU solvency rules (Solvency II). The proposal for a new insurance directive (the Solvency II directive) was adopted in 2009, and CEIOPS continued its drafting of technical implementing measures for the Commission in a number of areas. See the CEIOPS website at www.ceiops.eu and the chapter *Insurance and pensions*, page 53–54.

In 2009 Finanstilsynet was invited to chair a CEIOPS sub-committee, the Task Force on Insurance Guarantee Schemes (TF-IGS), which in 2009 prepared a report and drafted recommendations which CEIOPS submitted to the EU Commission concerning possible future harmonisation of insurance guarantee schemes in the EU. In 2009 Finanstilsynet hosted a meeting of CEIOPS' Insurance Groups Supervision Committee.

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 with regard to regulation and supervision of auditors. In addition to providing a forum for contacts between audit regulators, IFIAR promotes the sharing of knowledge on the industry, on regulatory and supervisory experience and other matters. The head of Accounting and Auditing Supervision Department at Finanstilsynet is a member of IFIAR's Advisory Council, which assists and advises IFIAR's officers in their duties. Other countries represented on the Advisory Council are the US, Japan, Germany, Singapore and France. IFIAR normally holds two main meetings each year.

Norwegian audit firms involved in the audit of issuers listed in the US must be registered with the Public Company Accounting Oversight Board (PCAOB). Finanstilsynet attaches importance to good supervisory collaboration with PCAOB, and there was frequent contact between the two bodies in 2008 and 2009, above all in connection with the planning of possible joint inspections of audit firms in Norway. See the account in the chapter on *Auditing*, page 72. Joint inspections were not possible in 2009 due to lack of reciprocity agreements between the US and the EU.

Regulatory development in the EU in the accounting and audit field follows the comitology system. Finanstilsynet and the Ministry of



Finance attend meetings of the Accounting Regulatory Committee (ARC) which is assessing new International Financial Reporting Standards (IFRS) and advising on their implementation in the EU. Finanstilsynet plays an active role in the European Enforcers Coordination Sessions (EECS) under CESR, which seeks to harmonise and coordinate the enforcement of IFRS in the EEA. The group meets regularly with the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC) to ensure that IFRS standards are consistently applied across the EEA.

Finanstilsynet plays an active part in the EU's development of accounting rules and standards for auditors, and in supervisory collaboration, including in the role of adviser to the Ministry of Finance on the Audit Regulatory Committee (AuRC). The agency 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. This includes 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 and infrastructures standardisation (ETSI ESI), and in the IT security working group

under the International Federation for Information Processing (IFIP). Finanstilsynet hosted the ITSG's 3rd Pan-European Conference in Oslo in September 2009. Finanstilsynet is Norway's representative in the European Security Research and Innovation Forum (ESRIF), an EU body working on security. The agency also participates in an EU-sponsored project to develop measures to enhance the ability to discover and respond to security events 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 is developing 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. Finanstilsynet did not participate in the EU's Committee on the

Prevention of Money Laundering and Terrorist Financing in 2009, but provided input to this committee via the EU supervisory committees. The European supervisory committees, CESR, CEBS and CEIOPS, have jointly set up an overview of practice followed by national supervisors in their implementation of the Third Money Laundering Directive.

EFTA COOPERATION

Finanstilsynet currently chairs 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 capital movements

and company law areas (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. The Working Group on Financial Services, which meets three times annually, has coordinated joint inputs from the EEA-EFTA countries to the Commission consultation on the creation of the new EU supervisory authorities.

NORDIC COOPERATION

Nordic cooperation remains a high priority, and Finanstilsynet attaches importance to good dialogue, both formal and informal, with its Nordic colleagues. The Nordic supervisors have concluded an overarching cooperation agreement, and the Norwegian supervisor has also signed individual cooperation agreements on the supervision of specific financial groups. In addition to the annual meeting of Nordic financial supervisors at director general level (in 2009 held in Stockholm), regular meetings are being held within the various sectors and at the administrative level, in addition to ad hoc meetings. In 2009 Finanstilsynet hosted the meeting of Nordic insurance supervisory authorities and the meeting of Nordic banking supervisory authorities. Finanstilsynet attended a number of meetings with

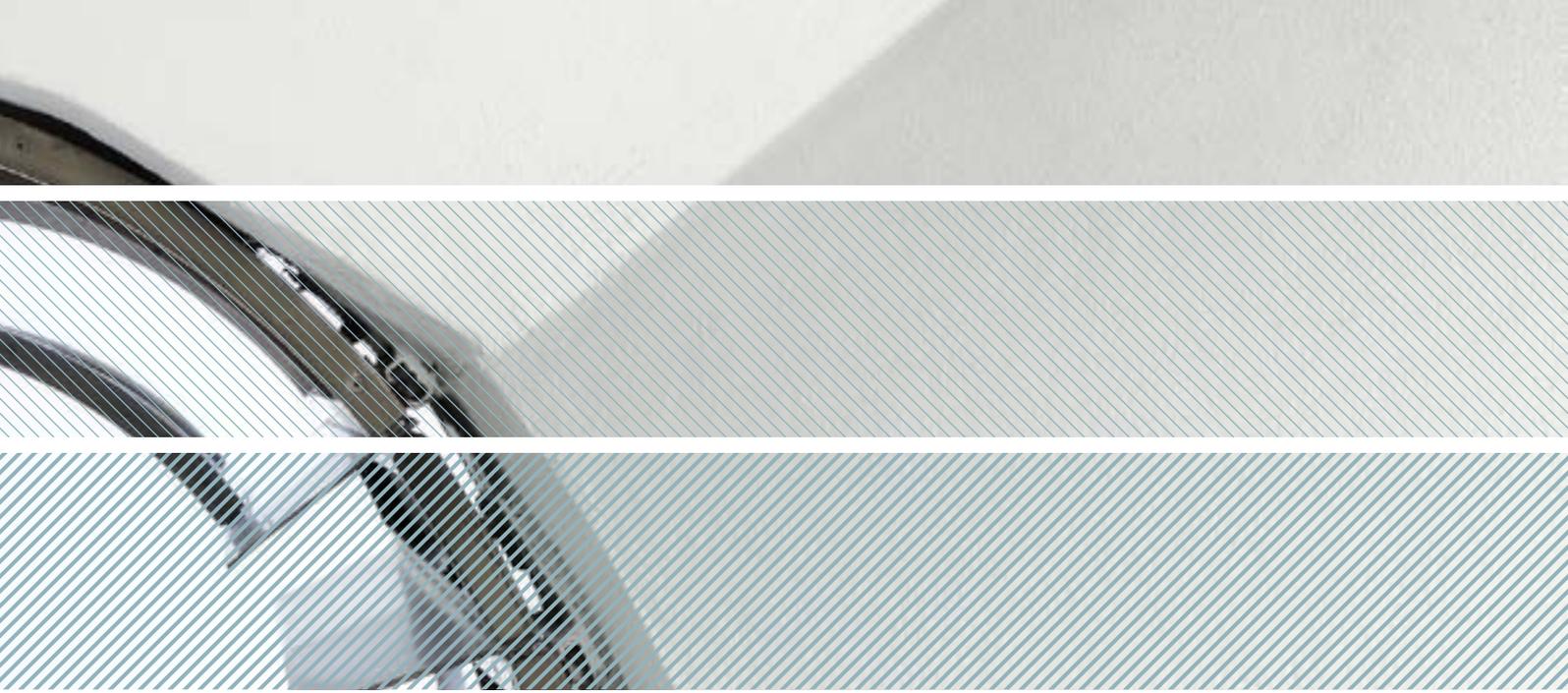
Nordic counterparts focusing on supervision of Nordic financial groups, and several joint on-site inspections were carried out at such groups. Further, the heads of the Nordic supervisory authorities and Nordic central bank governors met in Helsinki to discuss Nordic participation in the new EU supervisory authorities and the European Systemic Risk Board.

Since 2005 regular meetings have been held between the auditor supervisory authorities of Sweden, Denmark, Finland and Norway. The meetings show the value of closer contact and cooperation in the audit area, as elsewhere, not least in order to discuss issues associated with interpretation and follow up of the EU's 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 which integrates independently developed national econometric models into a global econometric model to provide consistent forecasts for the world economy. It also performs model-based quantitative macroeconomic analyses.

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 supervisors. 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

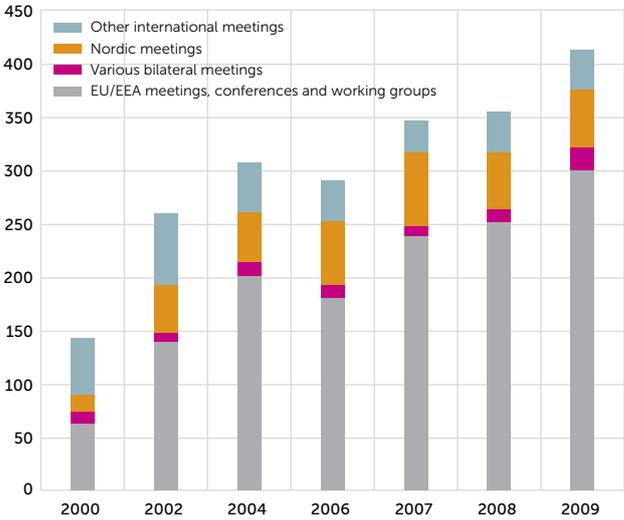


has also acceded to IOSCO's multilateral MoU for securities market supervision.

Finanstilsynet meets each year with representatives of the US Federal Reserve Bank and the European Central Bank. In 2009 Finanstilsynet had visitors from the IMF, OECD, delegations from Japan, Malawi, India and several delegations from China.

Finanstilsynet is in the process of revising its strategy for the coming years, and decided to visit international organisations and some supervisory authorities to hear their assessments of the developments in the financial markets and in financial market regulation and supervision in light of the financial crisis. In 2009 meetings were held with Australia's central bank and prudential regulator. Further visits are planned early in 2010, inter alia to Finland, Canada, Switzerland and the international organisations in Basel.

Chart 10: International meetings attended by Finanstilsynet



Source: 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 on Financial Conglomerates (JCFC) – Level 3
- Nordic supervisory meetings
- Various 3L3 working groups (cross-sectoral working groups under the EU supervisory committees)

Banking/finance

- International Conference of Banking Supervisors, held every two years
- OECD Financial Markets Committee
- European Banking Committee (EBC) – Level 2 – and various working groups under the EU Commission and the EBC
- Committee of European Banking Supervisors (CEBS) and Groupe de Contact (the main working group under CEBS) – www.c-ebs.org
- Nordic supervisory meetings

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 the EIOPC and the EU Commission
- Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) – www.ceiops.eu
- Nordic supervisory meetings

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
- Committee of European Securities Regulators (CESR) – www.cesr.eu
- Nordic meetings

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 (EGAOB)
- Nordic meetings

Money laundering and terrorist financing

- Financial Action Task Force (FATF) – www.fatf-gafi.org
- Committee on the Prevention of Money Laundering and Terrorist Financing (CPMLTF)
- Nordic meetings

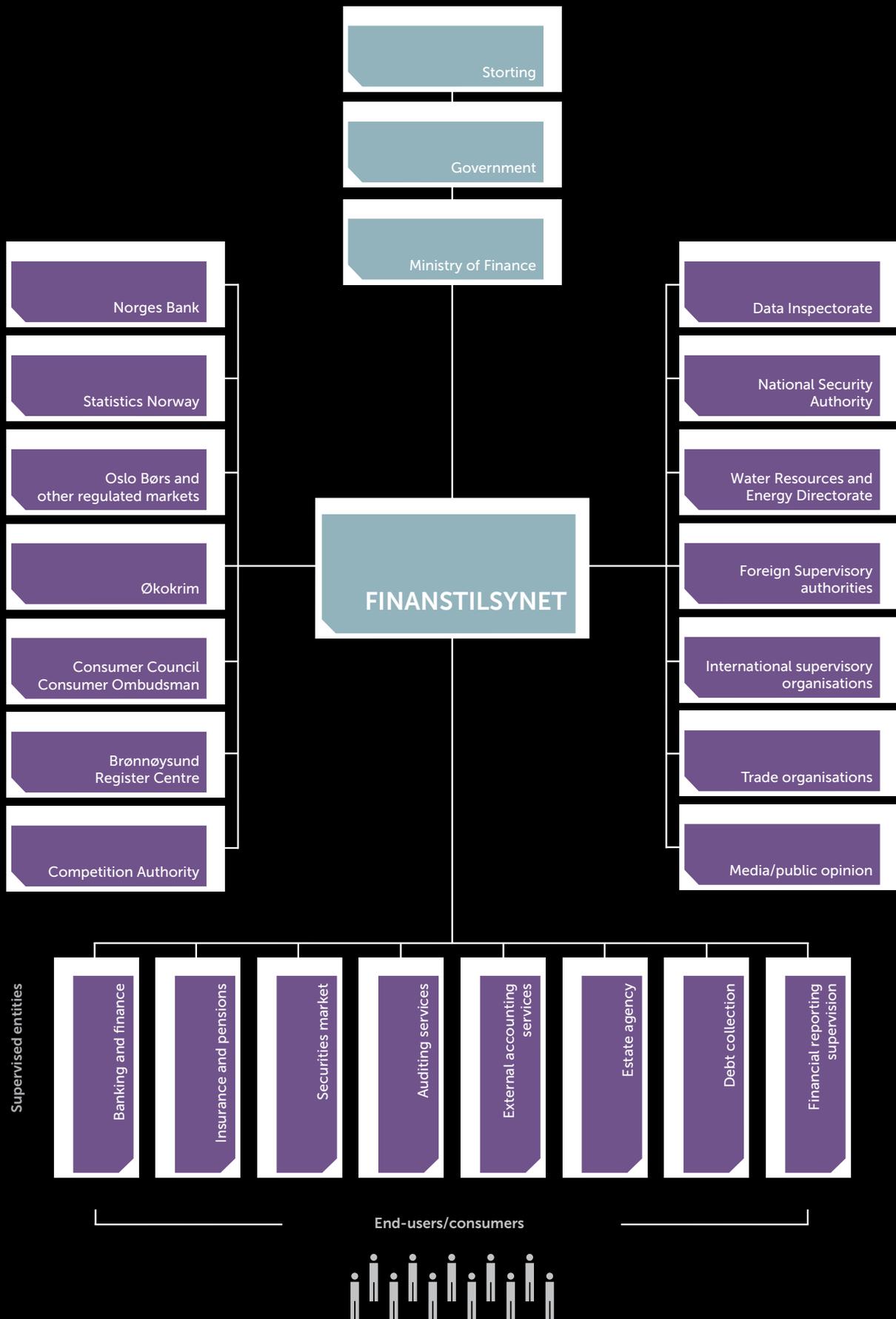
IT supervision

- European Security Research and Innovation Forum (ESRIF)
- Information Technology Supervision Group (ITSG)
- Nordic IT supervisory meetings
- Security working group under the International Federation for Information Processing (IFIP)
- ETSI ESI – Groups working on international standardisation in banking and security and on 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 (includes accounting and auditing)

FINANSTILSYNET'S KEY RELATIONS



THE FINANCIAL MARKET IN NORWAY 2009: RISK OUTLOOK

Since 1994 Finanstilsynet 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 in the light of general developments in the international and Norwegian economy, and assesses risks facing banks and other institutions in the Norwegian financial market.

The report is available in electronic form at www.finanstilsynet.no.
Printed version can be ordered from Finanstilsynet.

FINANSTILSYNET

Revierstredet 3
P.O. BOX 1187 Sentrum
NO-0107 Oslo

Tel. +47 22 93 98 00
Fax +47 22 63 02 26
post@finanstilsynet.no
www.finanstilsynet.no