DNB Livsforsikring AS Pillar 3

A company in the DNB Group

Extract

2016

DNB

SOLVENCY AND FINANCIAL CONDITION REPORT 2016

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Introduction

DNB Livsforsikring AS (DNB Liv) does not present accounting information in English. This means that the company's Solvency and Financial Condition Report (SFCR) for 2016 is only available in Norwegian.

Due to the interest shown by international investors and analysts, an extract from the SFCR has been translated into English. The extract primarily includes parts of the quantitative aspects described in the SFCR. The description of the system for risk management and internal control is omitted in its entirety.

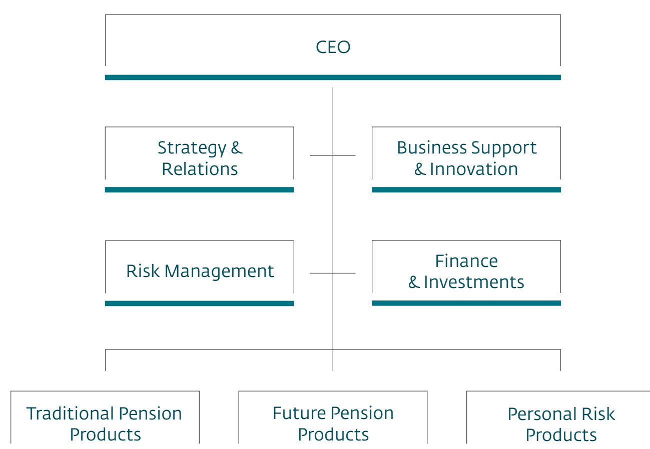
The translated extract from the SFCR does not replace the Norwegian version and does not fulfill the requirements which must be met by the SFCR.

DNB LIV – OPERATIONS AND PRODUCTS

A. DNB Liv – operations and products

DNB Liv has a licence to engage in life insurance operations. DNB Liv achieved profits after tax of NOK 1.3 billion in 2016. The company had total assets of NOK 299 billion as at 31 December 2016, an increase of NOK 9.9 billion from 2015.

DNB Liv is organised in three divisions based on the categories of products offered by the company. Including corporate functions, DNB Liv is organised as follows:



Traditional Pension Products
Traditional Pension Products is mainly responsible for the company's pension products that include guarantees in the form of agreed and defined benefits. This includes both guaranteed rates of return and life-long benefits. The three dominant products are defined-benefit pension in the private sector, paid-up policies and individual products with guaranteed rates of return. Further sales of these products have been stopped, primarily as a result of the risk and capital requirements related to the guaranteed rates of return. With respect to defined-benefit pensions, the annual premium thus refers to existing customers. New pension customers cannot transfer their defined-benefit pension scheme to DNB Liv. Paid-up policies are completely paid-up contracts which are issued when members are disenrolled from a defined-benefit pension scheme, either through a job change or if the employer partially or completely winds up a defined-benefit scheme. A number of employers have recently wound up their defined-benefit schemes, which has resulted in strong growth in the company's paid-up policy portfolio. DNB Liv no longer accepts paid-up policies from other life insurance companies and pension companies. Individual pension products are products established before 1 January 2008 which include a guaranteed rate of return and various guarantees regarding life expectancy. The authorities changed the product regulations for this type of products in 2008, though premiums are still paid on some contracts.

In DNB, Group Finance has organisational and functional responsibility for Traditional Pension Products. DNB Liv is responsible for legal and accounting aspects.

Future Pension Products
Future Pension Products is responsible for defined-contribution pensions, employer's liability insurance and individual pension products both with and without guaranteed rates of return. The company's new sales primarily encompass these products. The products are distributed mainly through the DNB Group's sales channels. The sales channels are organised as part of DNB Bank ASA. This includes physical service concepts and online sales solutions.

In DNB, Wealth Management has organisational and functional responsibility for Future Pension Products, while DNB Liv is responsible for legal and accounting aspects.

Personal Risk Products
Personal Risk Products are one-year risk products where insurance coverage is linked to health-related events such as accidents, sickness and death. These products are also distributed through DNB Bank ASA through both physical distribution and online sales.

In DNB, Personal Banking in DNB Bank has organisational and functional responsibility for Personal Risk Products, while DNB Liv is responsible for legal and accounting aspects.

B

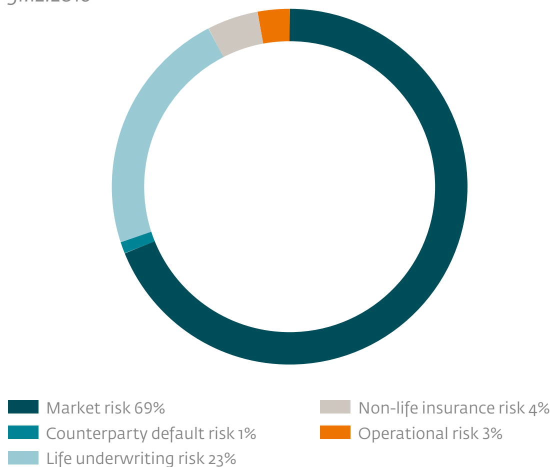
RISK PROFILE

7 Insurance risk
8 Market and credit risk

RISK PROFILE

The company's greatest risks are insurance risk, market risk and operational risk. The chart below shows the various risk factors' share of the gross capital requirement at year-end 2016:

RISK PROFILE
31.12.2016



The total gross capital requirement was NOK 41 billion. This was a reduction of NOK 2.5 billion compared with 31 December 2015. The reduction was due to lower market risk and life insurance risk, while non-life insurance risk increased. Operational risk was on the same level as at the beginning of the year. There were no significant changes in the various risk categories' relative shares.

INSURANCE RISK

The insurance risk in DNB Liv is in varying degrees divided between policyholders and the company. The risk result reflects differences in the results related to mortality, disability and settlement payments and the assumptions in the company's basis of calculation for premiums and provisions. The company is exposed to insurance risk related to non-life insurance products (employer's liability insurance), and for risk with a maximum one-year duration, disability pensions and dependant's pensions.

For group pension agreements and new individual pension and endowment insurance products, up to 50 per cent of a positive risk result can be transferred to the risk equalisation fund. This fund can be used during years with a negative risk result. The risk equalisation fund cannot exceed 150 per cent of the company's total risk premiums for the accounting year.

For existing contracts, the insurance risk is constantly monitored through analysis and follow-up of risk results within each product categories. The company also uses reassurance as an instrument to reduce insurance risk. The company currently has reassurance agreements covering disasters and major individual risks within group and individual insurance. The reassurance agreements entail that DNB' Liv is responsible for risk up to an agreed level, while the reassurer covers the excess risk up to an upper defined limit.

To reduce the insurance risk when policyholders take out insurance, a health assessment of the insured is carried out in connection with the sale of individual risk products. An individual health assessment is also carried out also for small-scale group schemes. In connection with the sale of disability pensions, customers will be categorised according to risk based on a concrete assessment of the risk related to the individual customer.

The tables below shows the risk result from last two years according to product:

RISK RESULTS

2016 NOK million	Risk premium	Risk contribution	Risk result
Defined benefit pension	447	341	106
Paid-up policies	1 592	1 433	159
Defined contribution pension with diability coverage	837	714	123
Group association pension	62	51	11
Individual endowment insurance	274	144	130
Individual pension insurance	453	364	89
Group Life policies	381	352	29
Non-life insurance	356	267	89
Total	**4 402**	**3 666**	**736**

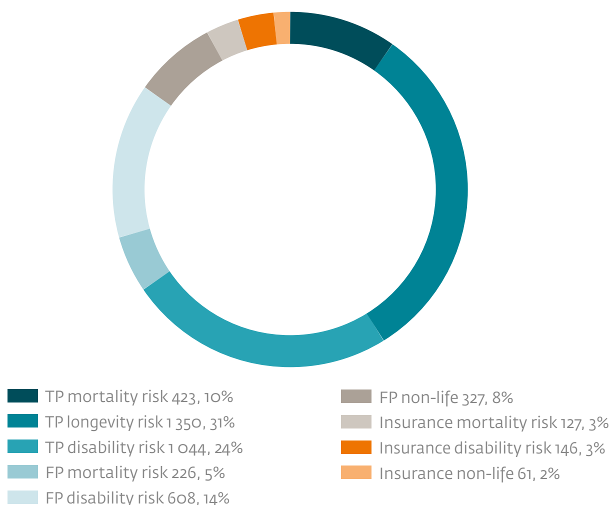
2015 NOK million	Risk premium	Risk contribution	Risk result
Defined benefit pension	886	639	247
Paid-up policies	1 194	1 195	(1)
Defined contribution pension with diability coverage	1 084	820	264
Group association pension	66	50	16
Individual endowment insurance	312	164	148
Individual pension insurance	466	367	99
Group Life policies	375	327	48
Non-life insurance	483	443	40
Total	**4 866**	**4 005**	**861**

In 2016, all product groups generated a positive risk result. The positive risk result for defined-benefit pension and paid-up policies is mainly due to good results related to disability pensions. This is particularly the case for paid-up policies, where there was a significant improvement from 2015. The reduced risk premium for defined-benefit pension is mainly due to the fact that large customers wound up their defined-benefit pension schemes during 2016, whereby paid-up policies have been issued. This is also the reason for the increase in the risk premium for paid-up policies. For risk products with no right to profit sharing (mainly disability pensions) there was a significant decline in business volume. This is due to the implementation of the new disability pension scheme, where new regulations result in a reduction in the sums insured.

DNB Liv's total insurance risk is mainly generated by longevity risk and disability risk for defined-benefit pensions and paid-up policies. The diagram below shows mortality exposure, longevity, disability and health risk in terms of risk premiums for the three business areas of Traditional Pension Products (TPP), Future Pension Products (FPP) and Personal Risk Products (Insurance) at year-end 2016.

INSURANCE RISK - MEASURED BY RISK PREMIUM

31.12.2016, NOK million



- TP mortality risk 423, 10%
- TP longevity risk 1 350, 31%
- TP disability risk 1 044, 24%
- FP mortality risk 226, 5%
- FP disability risk 608, 14%
- FP non-life 327, 8%
- Insurance mortality risk 127, 3%
- Insurance disability risk 146, 3%
- Insurance non-life 61, 2%

MARKET AND CREDIT RISK

Asset management in DNB Liv is divided between three main investment portfolios: the common portfolio, the investment choice portfolio and the corporate portfolio. Policyholders' funds are managed in the first two portfolios, while the company's assets are managed in the corporate portfolio.

The table below shows exposures and returns in the common and corporate portfolios.

EXPOSURE AND RETURN

	2016		2015	
NOK million	**Exposure 31.12**	**Return in %**	**Exposure 31.12**	**Return in %**
Common portfolio				
Norwegian equities	1 228	15.2	987	6.1
International equities	13 463	8.6	18 229	0.4
Norwegian bonds	21 684	2.5	15 615	0.8
International bonds	7 131	5.6	4 267	1.4
Money market	28 802	1.8	40 268	1.1
Bonds and loans valued at amortized cost	114 961	4.4	108 872	4.6
Real estate	19 575	8.0	20 199	13.5
Others	1 438		555	
Total	**208 282**	**4.2**	**208 993**	**4.6**
Corporate portfolio				
Total	**29 989**	**2.4**	**27 713**	**2.5**

Net income from investments in the common portfolio and the corporate portfolio was NOK 8.8 billion and NOK 0.7 billion, respectively.

Asset management costs totalled NOK 213 million in 2016, corresponding to 0.1 percent of assets under management.

The table below shows the composition of the assets in sub-portfolios in the common and corporate portfolios.

ASSETS

NOK million	Norwegian Equities	Inter-national Equities	Norwegian bonds	Inter-national bonds	Money market	Held to maturity	Loans and receivables	Real estate	Other	Total
Common portfolio										
- low risk	38	595	1 162	315	3 084	3 566	2 572	782	90	12 203
- moderate risk	116	1 217	2 054	558	4 526	6 307	4 755	1 890	159	21 581
Individual savings with guarantee	166	1 459	2 016	902	1 900	4 524	2 808	1 588	52	15 416
Paid-Up policies	108	1 431	2 490	676	3 180	11 151	5 687	1 238	193	26 154
Paid-Up Policies (remaining long life provisions)	544	5 956	8 808	2 391	10 953	39 447	14 668	9 176	682	92 623
Disability coverage for defined contribution	6	132	425	221	1 257	1 089	670	0	0	3 801
Health insurance similar to non-life insurance	0	0	0	0	722	866	400	109	104	2 201
Defined benefit pension with guarantees for Private Market	250	2 673	4 730	2 068	3 180	12 588	3 864	4 791	158	34 303
Common portfolio	**1 228**	**13 463**	**21 684**	**7 131**	**28 802**	**79 537**	**35 423**	**19 575**	**1 438**	**208 282**
Corporate portfolio	1 013	3	0	0	23 270	3 120	1 857	6	720	29 989
Total	**2 241**	**13 466**	**21 684**	**7 131**	**52 072**	**82 657**	**37 280**	**19 581**	**2 158**	**238 270**

The investment choice portfolio includes all assets where customers themselves make investment decisions. The customer chooses investment profile among the options made available in DNB Liv's product solutions, and the customer him/herself is responsible for the market risk.

Customer portfolios at year-end 2016 are shown in the table below:

MARKET VALUES

NOK billion	2016
Common Portfolio	**204**
Corporate market	37
Defined benefit pension	33
Disability coverage for defined contribution pension	4
Private market	166
Defined benefit pension with guarantees for Private Market	35
Individual endowment insurance	15
Paid-Up policies	26
Paid-Up Policies (remaining longivitety provisions)	90
Non-life insurance	2

NOK billion	2016
Defined contribution with investment choice	**60**
Corporate market	49
Profile <=30	17
Profile 50	23
Profile >=80	8
Fond menu	1
Private market	11
Profile <=30	0
Profile 50	1
Profile >=80	1
Others	9

Expected return and guaranteed rate of return
DNB Liv carries the risk of fulfilling the company's commitments in contracts with policyholders. The return on financial assets must be sufficient to meet the guaranteed rate of return specified in insurance policies. Otherwise, inadequate returns will have to be covered by applying the market value adjustment reserve, additional statutory reserves, equity or subordinated loan capital. The guaranteed rate of return must be complied with on an annual basis. Measured in relation to policyholders' funds, the company's total guaranteed rate of return averages 3.1 per cent. The table below shows long-term developments in the guaranteed rate of return for product categories. In step with the payment of pensions, the guaranteed rate of return as a percentage of pension commitments will be somewhat reduced each year.

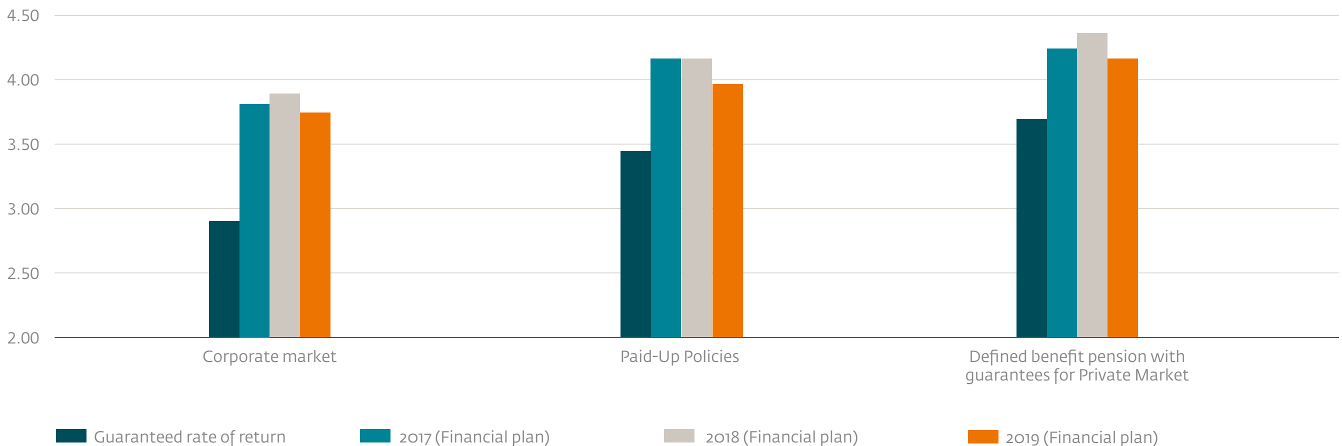
DEVELOPMENT OF THE GUARANTEED RATE OF RETURN

Per cent	2016	2015	2014	2013	2012
Group pension	3.1%	3.1%	3.2%	3.3%	3.4%
Individual endowment insurance	3.4%	3.4%	3.4%	3.4%	3.4%
Individual pension insurance	2.3%	2.3%	2.3%	2.6%	2.7%
Group associations pension	4.0%	4.0%	4.0%	4.1%	4.1%
Average	**3.1%**	**3.1%**	**3.2%**	**3.2%**	**3.3%**

Meeting the guaranteed rate of return is important for the company's value creation and developments in its solvency position. Based on normalised expected returns for the company's largest portfolios for the period 2017-2019, the chart below shows the guaranteed rate of return relative to the expected return.

GUARANTEED RATE OF RETURN AND EXPECTED RETURN.

Per cent

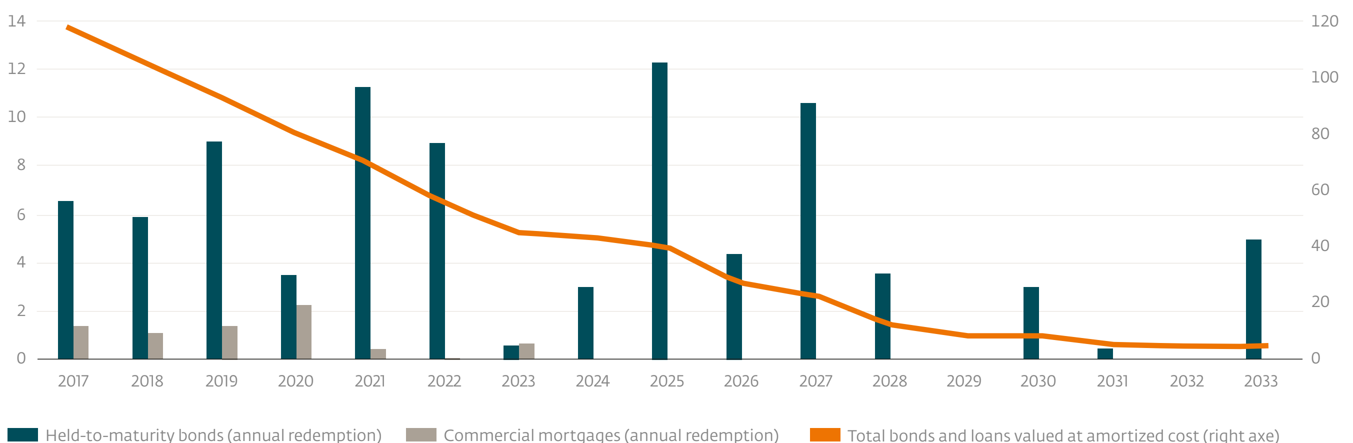


As shown in the chart, the expected return is well above the guaranteed rate of return. The smallest margin refers to defined-benefit pensions with the highest guaranteed rate of return.

Development in fixed-income instruments

DNB Liv aims to be an active and responsible asset manager which ensures an adequate return on policyholders' funds and an acceptable return on the company's invested capital through good diversification and consistent management of market risk. The current low interest rate level makes it demanding to achieve a high return for policyholders. The existing held-to-maturity portfolio, which generates a return of approximately 4.4 per cent, makes it possible to achieve a return that is higher than the guaranteed rate of return. In 2017, some NOK 6.6 billion of this portfolio will become due, and the interest rate level for new investments of similar credit quality is significantly lower. In 2016, DNB Liv purchased commercial mortgages from DNB Bank/DNB Næringskreditt for a total value of NOK 7.1 billion. The table below shows the annual redemption of held-to-maturity bonds and commercial mortgages. The total portfolio of held-to-maturity bonds and loans carried at amortised cost represented NOK 119 billion. This also includes home mortgages.

ANNUAL REDEMPTION AND TOTAL BONDS



Fixed-income instruments are essential in making the company meet the guaranteed rate of return over the coming years.

TECHNICAL PROVISIONS, SOLVENCY II

C. Technical provisions, solvency II

Technical provisions (TP) affect the company's solvency capital and solvency capital requirements. The difference between the company's assets and TP represents the company's solvency capital.

TP equals the sum of the best estimate (BE) and the risk margin (RM). The next table shows the provisions as at 1 January 2016 and at year-end 2016:

TECHNICAL PROVISIONS

NOK million	Insurance with guarantee		Index-linked and unit-linked insurance without guarantee	Non-life insurance	Total
	With profit sharing	Without profit sharing			
01.01.2016					
Best estimate	161 649	53 980	46 208	6 050	267 886
Risk margin	4 238	748	1 241	234	6 461
Technical provisions	165 887	54 727	47 449	6 284	274 347
31.12.2016					
Best estimate	166 169	46 007	56 592	6 187	274 954
Risk margin	3 155	600	1 114	224	5 093
Technical provisions	169 324	46 606	57 706	6 411	280 048

Comparable provisions in the accounts totalled NOK 281 billion on 1 January 2016 and NOK 285 billion on 31 December 2016.

Life insurance products with profit sharing include paid-up policies and individual products with guaranteed rates of return sold prior to 1 January 2008. Life insurance products without profit sharing include defined-benefit pensions and individual products sold after 1 January 2008. Unit linked insurance policies with no guarantee are defined-contribution pensions and unit linked products in the personal market segment.

Technical provisions increased by approximately NOK 6 billion during the year. The increase refers to unit linked insurance policies with no guaranteed rate of return, where the entire increase stems from defined-contribution pensions. The increase in defined-contribution pensions related to both new premiums and returns on policyholders' funds. Premium income for unit linked insurance policies with no guaranteed rate of return came to approximately NOK 8 billion in 2016. Technical provisions for products with a guaranteed rate of return was down NOK 4.7 billion. A major cause of this is that the commitments have been reduced as a result of a slightly higher discount rate at year-end 2016.

The risk margin is quantified through a separate model for this purpose. In the models, developments in the capital requirement for insurance risk (life and non-life insurance) are projected. The risk margin is 6 per cent multiplied by the present value of all future capital requirements for insurance risk. The discount rate applied is based on the supervisory authorities' market rate curve on the calculation date. In the projection, it is assumed that for most products, the insurance risk is proportionate to the development in the best estimate for the cash flow.

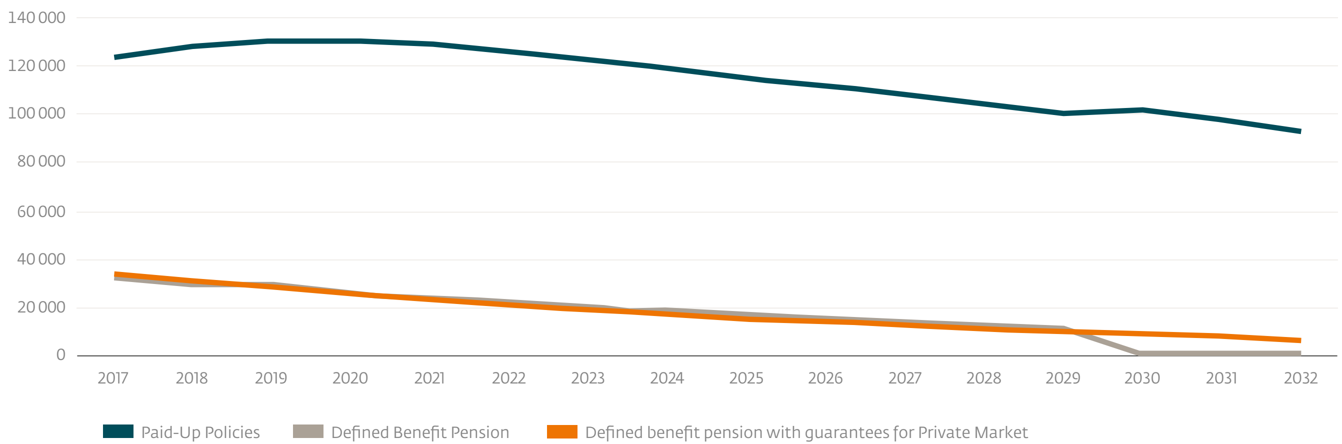
DNB Liv has applied to Finanstilsynet (the Financial Supervisory Authority of Norway) and been given permission to use the transitional rules for technical provisions. At year-end 2016, this had a positive effect on solvency capital of NOK 8.8 billion after tax.

When calculating technical provisions, a volatility adjustment (VA) of the interest rate curve is applied. The adjustment is intended to prevent artificial volatility in the company's solvency position as a result of changes in the market spread on the company's bond portfolio, among other things to reduce pro-cyclical behaviour. The VA is calculated using a reference portfolio based on assets in Norwegian life insurance companies, and represented a 29 basis point increase in the interest rate curve at year-end 2016. Without the VA, the provisions (TP), without the transitional rules, would have been approximately NOK 4 billion higher and reduced the solvency margin by 27 percentage points.

Based on the expected termination of defined-benefit pension schemes and the issue of paid-up policies, a projection has been made of insurance liabilities (TP) with guaranteed rates of return up to 2032, which is the end of the transitional period for the valuation of technical provisions. Products with a guaranteed rate of return are expected to be reduced from NOK 188 billion in 2017 to about NOK 99 billion in 2032.

DEVELOPMENT - TECHNICAL PROVISIONS

NOK million



A reduction in technical provisions with a guaranteed rate of return and longevity risk combined with an increase in products without such guarantees will contribute to strengthening the company's solvency position in the coming years.

D

CAPITAL MANAGEMENT

16 Solvency capital
17 Solvency capital requirement and minimum capital requirement
18 Violations of the solvency capital requirement and the minimum capital requirement

DNB's long-term financial ambition towards 2019 is that the Group will achieve a return on equity above 12 per cent, a long-term common equity Tier 1 capital ratio of approximately 16 per cent and a dividend payout ratio of minimum 50 per cent of the Group's profit provided that the capital adequacy ratio is satisfactory. For DNB Liv, the aim is to achieve a 6-8 per cent return on equity, a solvency margin above 150 per cent including transitional rules, and a dividend payout ratio of minimum 50 per cent. DNB Liv's self-assessment of risk and capital concludes that the company is sufficiently capitalised in the period up to 2019 and that there is a balance between risk and capital. This is conditional on a 50 per cent dividend payout ratio . The targeted solvency margin, rules for the level of Tier 1 capital and dividends as well as the composition of the buffer capital and own funds are under review.

The solvency margin represents the degree to which the company's own funds meet the capital requirement stipulated in the solvency regulations. The solvency margin is calculated in two ways, with and without the transitional rules. When introducing Solvency II, the Norwegian authorities opened up for a gradual implementation of the regulations by allowing companies to value their insurance liabilities in accordance with the liabilities recorded in the accounts for a transitional period. This is expressed through the solvency margin with transitional rules. DNB Liv has been given permission to use the transitional rules, to be phased out gradually over a 16-year period. At year-end 2016, the solvency margin was 211 per cent. This means that the company's capital is more than double the capital requirement. Without the transitional rules, DNB Liv had a solvency margin of 152 per cent. The company's solvency capital and solvency capital requirements (SCR) are shown in the table below:

SOLVENCY CAPITAL AND SOLVENCY CAPITAL REQUIREMENT

NOK million	1.1.2016	31.12.2016
With transitional rules		
Available Solvency Capital	36 734	34 779
Solvency Capital Requirement	19 095	16 518
Solvency Margin	192%	211%
Without transitional rules		
Available Solvency Capital	22 565	25 981
Solvency Capital Requirement	19 886	17 116
Solvency Margin	113%	152%

The solvency capital requirement was reduced by approximately NOK 2.5 billion through 2016. A reduced equity exposure has contributed to reducing the solvency capital requirement. In addition, the company's technical provisions were strengthened through 2016, which reduced insurance risk through greater risk-absorbing capacity. The improved solvency capital without transitional rules is mainly due to higher interest rates and a strengthening of the company's equity through the generation of profits and retained profits. No dividends were paid for the 2016 accounting year.

When using the transitional rules, the company's solvency capital was higher than the solvency capital requirement throughout 2016. At year-end 2016, the company had good margins to the solvency capital requirements and was well capitalised. This also implies that the company will meet the solvency requirements if the interest rate level is lower than current market rates. Based on a normalised return over the coming two to three years, the solvency margin without transitional rules will improve by just over 10 percentage points per year, reflecting returns and profit generation.

SOLVENCY CAPITAL

At year-end 2016, the company's own funds were composed as shown in the table below:

SOLVENCY CAPITAL

NOK million	1.1.2016	31.12.2016
Own funds group 1		
Ordinary share capital	1 750	1 750
Surplus fund	6 016	6 016
Reconciliation reserve	23 251	21 106
Impact of transitional rules	*18 273*	*8 798*
Total basic own funds group 1 - SCR and MCR [1]	**31 017**	**28 872**
Own funds group 2		
Subordinated liabilities	5 500	5 500
Risk Equalisation Fund	319	407
Total basic own funds group 2 – SCR	**5 819**	**5 907**
Total basic own funds group 2 – MCR	**1 620**	**1 471**
Own funds group 3		
Deferred tax	(102)	(0,0)
Total basic own funds group 3 - SCR and MCR	**(102)**	**(0,0)**
Total available own funds to meet the SCR	**36 734**	**34 779**
Total available own funds to meet the MCR	**32 637**	**30 343**
Total available own funds to meet the SCR without transitional rules [2]	**18 461**	**25 981**

1) MCR is minimum capital requirement

2) The solvency capital requiment without transitional rules was NOK 17,1 billion at year-end 2016

Total recorded equity and subordinated loans amounted to NOK 28.5 billion, while solvency capital calculated according to Solvency II and the transitional rules was approximately NOK 35 billion. The reconciliation reserve in the above table includes other equity of NOK 13.5 billion and NOK 14.8 billion, respectively, for 2015 and 2016. This corresponds to the figures in the accounts. The transitional rules permit the use of Solvency I provisions rather than Solvency II provisions. This gave a reconciliation reserve of NOK 9.7 billion and NOK 6.3 billion, respectively, for 2015 and 2016, so that the reconciliation reserve totalled NOK 23.2 billion for 2015 and NOK 21.1 billion for 2016. Recorded equity and subordinated loans plus the reconciliation reserve thus sum up to total own funds in solvency margin calculations.

Subordinated loans under own funds group 2 consist of a perpetual subordinated loan of NOK 3 billion and a dated loan of NOK 2.5 billion falling due in 2025 with possible accelerated prepayment in 2020. The perpetual loan can be repaid in 2025. Both loans are internal loans in the DNB Group. There is a limitation on how much of the own funds group 2 can be used to meet the MCR requirement, and funds in this category are reduced. Funds included in group 3 cannot be used to meet the MCR requirement.

Based on the transitional rules, total own funds have increased by NOK 0.8 billion. In the course of 2016, the reconciliation reserve was increased by NOK 0.7 billion. This is due to a combination of retained earnings and the fact that use of the transitional rules reduces the reconciliation reserve. In addition, the risk equalisation fund increased by just under NOK 100 million.

Sensitivities

The company's solvency position is vulnerable to changes in assumptions and the interest rate level. Sensitivities have been prepared in connection with the calculation of the solvency margin at year-end 2016. These are shown in the table below:

SENSITIVITIES

NOK million	Solvency margin
Solvency margin per 31.12.2016	152%
Interest rate up 50 bp.	177%
Interest rate down 50 bp.	126%
Increase of mortality by 10%	160%
Decrease of mortality by 10%	138%
Increase of disability by 10%	149%
Decrease of disability by 10%	154%
Decrease in value of equities by 25%	145%
Increase of spread by 50 bp. combined by increase in VA +15 bp.	150%
Decrease of ultimate forward rate (UFR) to 3.7 per cent	142%

The sensitivity analysis shows that the company's biggest risk relates to falling interest rates. If interest rates decline by 50 basis points, the solvency margin will be reduced from 152 per cent to 126 per cent. Changes in the mortality rate will also have a material effect on the company's solvency position. In the analysis, mortality is assumed to decline by 10 per cent, which corresponds to a 1-2 year increase in life expectancy. This reduces the solvency margin to 138 per cent. In April 2017, EIOPA adopted new rules for the calculation of the UFR (Ultimate Forward Rate). It has been decided that the UFR can be reduced by up to 15 basis points per year, for the first time on 1 January 2018. As of 1 January 2018, the UFR will thus be reduced from 4.20 per cent to 4.05 per cent. The sensitivity analysis shows that if the future interest rate level measured through the UFR is reduced from 4.2 per cent to 3.7 per cent, the solvency margin will be reduced to 142 per cent. The 15 basis point reduction in the UFR as of 1 January 2018 will thus have little effect on the solvency margin. The remaining sensitivities will have a limited effect on the solvency margin. The effect including the transitional rules is at the same level as shown above with one exception. Changes in interest rates are compensated for through the transitional rules, and interest rate changes have little effect on the company's solvency position when the transitional rules are applied. Based on calculations made as at 31 December 2016, the company will have a solvency margin of more than 190 per cent for all sensitivities when using the transition rules.

SOLVENCY CAPITAL REQUIREMENT AND MINIMUM CAPITAL REQUIREMENT

The table below provides an overview of developments in the solvency capital requirement without the transitional rules and the minimum capital requirement in 2016 in total and distributed over the main modules in the standard model.

SOLVENCY CAPITAL REQUIREMENT AND MINIMUM CAPITAL REQUIREMENT

NOK million	01.01.2016	31.12.2016
Market risk	17 689	14 765
Counterparty default risk	282	185
Life underwriting risk	5 579	4 868
Non-life insurance underwriting risk	921	984
Operational risk	1 158	1 147
Deferred tax	(5 743)	(4 833)
SCR	**19 886**	**17 116**
MCR	**8 102**	**7 702**

Through the year, the premium reserve was strengthened relative to the best estimate for the premium reserve, which gives a higher positive margin for the best estimate for the liabilities. This margin absorbs insurance stress and thus reduced life insurance risk in 2016. The reason for the strengthened recorded premium reserve relative to liabilities is the build-up of reserves for higher life expectancy and an expected lower probability of disability in the assumptions for 4Q16 than in 4Q15.

The increase in non-life insurance risk through the year was due to volume growth.

Interest rates increased from year-end 2015 to 2016, which reduced the interest rate risk for the liabilities. That is the main reason for the reduced market risk in the period. The equity risk has also helped to reduce the market risk, but have largely been offset by higher spread risk.

The calculation of the minimum capital requirement is based on the rates for best estimate provisions under Solvency II for life insurance products and non-life insurance products. In the calculation,

there is a lower and an upper limit for the requirement of minimum 25 per cent and maximum 45 per cent of the estimated solvency capital requirement. The minimum requirement as at 31 December 2016 is dominated by requirements for the company's life insurance operations (95 per cent). The remaining 5 per cent represents non-life insurance products. As at 31 December 2016, the minimum requirement was within the limitations of minimum 25 per cent and maximum 45 per cent.

During 2016, the minimum requirement was reduced by NOK 0.8 billion. The main reason for this is that the best estimate for provisions without the transitional rules was used as at 31 December 2015. Based on feedback from Finanstilsynet, this has been adjusted to provisions calculated according to the transitional rules. If the calculation as at 31 December 2015 had been based on the best estimate for provisions with transitional rules, the minimum requirement would have been NOK 7.3 billion. This means that in real terms, there was a marginal increase in the minimum requirement of NOK 22 million in 2016.

VIOLATIONS OF SOLVENCY CAPITAL REQUIREMENT AND THE MINIMUM CAPITAL REQUIREMENT

DNB Liv has reported its capital requirement to Finanstilsynet as from 1 January 2016 and for each quarter in 2016. The company fulfilled the solvency capital requirements throughout this period.