1927-2009

Kommunalbanken Norway Annual Report 2009

Kommunalbanken Norway

Miljøfyrtårn®

“The situation in financial markets developed quickly throughout the year and KBN successfully adapted its business and was able to benefit from the changing environment.”

CONTENTS

2009
- a year that will be hard to beat

Kommunalbanken Norway (KBN) ended 2009 by breaking three records, namely profit, lending growth and funding volume. I will comment on all three.

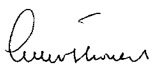
Towards the end of 2008 there was much uncertainty with regard to the future. The municipal sector sent a warning message to the authorities concerned with how Norwegian banks would be able to meet the loan demand from the municipalities. The bankruptcy of Lehman Brothers and the liquidity crisis that followed created a mood of extreme pessimism. KBN also felt the tremors of the crisis in financial markets but it became clear even before the end of 2008 that investors' flight to quality worldwide meant that interest for our bond issuance remained. This access to liquidity should in theory have meant that KBN could easily meet the increased lending to the municipalities. Capital, however, is a limiting factor in doing this. All financial institutions should have a sufficient level of core capital in respect of its lending volume or total balance sheet. To finance future growth, financial institutions either must increase capital levels through capital injection or through retained earnings.

In 2009, KBN financed the largest growth in the institution's history through earnings. However, these earnings were not the result of materially higher lending margins. The earnings came primarily from the buy-back of certain structured notes that KBN issued previously, the most part into Japan. Furthermore, KBN's liquidity portfolio was placed in short dated investments. As these investments matured the proceeds were re-invested at considerably higher margins. The liquidity portfolio is invested in such high quality names so that any change in its market value is marginal. Gains on the buy-back of KBN's own securities and on investments in the liquidity portfolio contributed to 65 per cent of total earnings.

Such returns normally can only be achieved through a considerable increase in the risk profile. This also implies a risk of experiencing equivalent losses. It is important to underline however that KBN benefited from a very special market situation, which gave us an opportunity to realise profit. As we reached the end of 2009, the level of buy-back enquiries returned to a pre-crisis level, and as such, the opportunity to repeat such extraordinary gains has gone.

Lending growth increased in 2009 by 28.2 per cent. At times KBN was the only financial institution offering loans. At some stages in 2009, the credit market was non-functioning. During these times KBN was the only choice. The lending growth would not have been as strong if we were not able to increase our earnings as we did. The markets which we employ to raise our funding functioned better and better throughout the year, in line with the return to stability in international financial markets.

All these factors are closely tied. Behind the growth in lending lay the extraordinary market situation that KBN was able to benefit from. The gains KBN could make from this situation made sure that the municipalities could benefit from new loans.



Petter Skouen
President & CEO

2009 - The year in brief

KBN's contribution to society increased due to the effects of the financial crisis.

In a White Paper to the Norwegian parliament discussing the government's ownership policy, KBN is classified as 'an institution with important sector political functions'.

Profit for the year increased by NOK 1.009 billion to NOK 1.399 billion.

Return on adjusted shareholders' equity increased from 27.2 per cent to 63.5 per cent.

Total return on assets increased from 0.22 per cent to 0.62 per cent.

KBN's total lending portfolio increased by NOK 33 billion to NOK 151 billion.

KBN advises its customers in connection with entering into ordinary banking agreements. In 2009, KBN assisted in the signing of 29 such agreements.

KBN's market share for loans to the local government sector increased from 40.8 per cent to 46.7 per cent.

The Board proposes to allocate profit of NOK 67 million to payment of dividends and NOK 200 million to payment of extraordinary dividends. NOK 1.132 billion of profit will be retained as equity capital.

Total funding volume raised in 2009 was NOK 116 billion and KBN had continued access to funding markets throughout the year.

Further to KLP's purchase of Kommunekreditt AS from Eksportfinans ASA, the central government purchased KLP's 20 per cent stake in KBN and became its sole owner.

KBN was certified by environmental management organisation The Eco-Lighthouse Foundation. Relocation to its new office building gives KBN the opportunity to make further energy saving measures.

KBN relocated to new premises in the autumn of 2009.

Summary financial figures

(Figures in NOK million)

	2009	**2008**
Net interest and commission income	1 032.9	507.7
Other income	0.9	0.8
Staff costs and other expenses	90.5	78.4
Profit before tax	1 946.3	543.0
Tax	547.1	153.1
Profit for the year	1 399.2	390.0

KBN facts

KBN was established by an act of Parliament in 1926 and reorganised pursuant to a conversion act in 1999 as a government funding agency.

KBN has an important public policy function of providing low cost loans to Norwegian municipalities and counties.

KBN is the largest lender to the local government sector in Norway with a market share of 46.7 per cent, including loans to municipally-owned companies.

KBN can only lend to municipalities and counties and to municipal enterprises and intermunicipal companies against a municipal guarantee.

KBN is 100 per cent owned by the central government. The state's ownership is managed by the Norwegian Ministry for Local Government and Regional Development.

KBN has been assigned the highest possible credit ratings, Aaa/AAA, by the credit rating agencies Moody's Investor Service and Standard and Poor's respectively.

KBN has total assets of NOK 232 billion.

How KBN works

KBN uses its triple-A credit rating to raise funds by issuing bonds in international capital markets.

KBN follows a diversified funding strategy and annual issuance volumes are determined by its 12 months net cash requirement including forecasted lending growth. No currency or interest rate risks are allowed. Swap agreements are used to hedge against movements in interest rates as well as currency fluctuations. Currency proceeds are eventually swapped to floating rate and Norwegian kroner and matched against KBN's lending portfolio.

With continued access to stable financing from bond markets globally, KBN is able to provide loans at competitive terms to Norwegian municipalities and counties. Under normal conditions, Norwegian local governments select their loan providers through a tender process, and by participating in the process, KBN contributes to setting the benchmark for pricing to the sector.

KBN's excess liquidity reserves are invested in a portfolio of highly rated short dated assets. Revenue generated from the liquidity portfolio has been satisfactory under current market conditions.

Key figures

(Figures in NOK million)

	2009	**2008**
Total lending 31.12.	151 275	118 060
Lending		
The year's approbations	46 393	28 221
Unsettled allocations	4 660	2 439
Disbursement during the year	43 158	28 253
Principal payments on loans	9 900	11 933
Borrowings		
Borrowings in foreign currencies	213 334	190 669
Domestic bond issues	11.083	11 527
Domestic note issues	0	0
Key figures		
Average total assets	224 084	179 331
Return on capital before tax	88.27 %	37.85 %
Dividend	267	44
Capital adequacy	11.05%	11.60 %
As percentage of average total assets		
Interest income	2.16	5.02
- Interest costs	1.69	4.72
= Net interest income	0.47	0.29
- Commission costs and costs of banking services	0.01	0.01
+ Net foreign exchange gains/losses	0.10	0.00
+ Gain from repurchase of issued securities	0.35	0.06
+ Other income	0.00	0.00
- Staff costs	0.02	0.03
- Other expenses	0.02	0.02
= Operating profit	0.87	0.30
Profit analysis (figures in NOK million)		
Interest income	4 847	8 998
- Interest expenses	3 794	8 473
= Net interest income	1 053	525
- Commission costs and costs of banking services	20	18
+ Net gain/(loss) on financial instruments at fair value	222	-2
+ Net gain/(loss) from repurchase of issued securities	781	115
+ Other income	1	1
- Staff costs	53	46
- Other expenses	38	32
= Profit before tax	1 946	543
Profit for the accounting period before tax	1 946	543

An update on the Norwegian economy

Economies in every corner of the world are starting to emerge from a sharp and severe economic slowdown. Despite positive signs from many developed economies across the world, capacity utilisation in advanced economies will remain very low for some years to come.

A recovery in financial markets has been visible since the middle of 2009 and with improved credit conditions and a pick-up in global trade, the chance of the world experiencing a "double dip" recession is receding.

Compared to its Scandinavian and European peers, Norway was in a better position than most countries to counteract the effects of the economic slowdown. The current account balance and government finances are solid, and Norway is projected to be the only OECD country to post a budget surplus in 2010. Furthermore, the Norwegian banking system is not large, and the financial position of Norwegian banks is sound.

The Norwegian government is a net creditor with substantial foreign assets and large fiscal surpluses, primarily originating from the oil and gas sector. The government's total net cash flow from the extraction of petroleum is transferred to the Government Pension Fund – Global, Norway's Sovereign Wealth Fund. This Fund is fully integrated into the National Budget which means the Government will cover the non-oil budget deficit by transfers from the fund according to the fiscal rule.

Norway is the world's fifth largest oil exporter and with a pick up in the oil price during 2009, activity related to the production of petroleum related goods and services have not been adversely affected by the economic situation. This acts as a stabilisation factor in the Norwegian economy compared to other export oriented countries.

As in many developed countries, Norway's financial stabilisation package helped to curb the slowdown in economic activity and stimulate domestic demand. Fiscal policy measures in 2009 equated in total to a stimulus of 3 per cent of GDP for mainland Norway. Combined with the measures towards the financial sector, these packages had a profound effect on the rate of the slowdown in the Norwegian economy.

According to Norges Bank, the Norwegian central bank, "the operational target of monetary policy in Norway is low and stable inflation, with annual consumer price inflation of close to 2.5 per cent over time". In recent years, inflation moved slightly above this target level and as such the key policy rate was raised accordingly. However, following the onset of the financial crisis, Norges Bank reduced the key policy rate considerably, continuing to cut further in 2009 to 1.25 per cent. Although projections for 2010 are uncertain, forecasts show a steady increase in rates going forward of up to and beyond 2 per cent.

Norway has been through a period of high GDP growth in recent years, peaking at 6.1 per cent for the mainland economy in 2007. After two quarters

The Norwegian local government sector

- An asset class of exceptional quality

Norwegian local government rests on strong pillars. The high credit quality of the sector is largely derived from several factors; the economic and legislative framework that protect local authorities' status, responsibilities and finances, the strong equalisation system between municipalities that ensures minimum revenues, a high degree of central government transfers and a comprehensive system for meticulous central government supervision and control on the local government budgetary process.

The combined strengths of the system are fundamental to the low risk associated with Norwegian local governments as an asset class. Norwegian municipalities play a crucial role in providing vital services to the Norwegian public and a stable economic framework with access to low cost financing is considered important by the central government. The central government has a strong incentive to provide for a stable economic environment for local government financing, as volatility could lead to uncertainty, increase municipal borrowing expenses and prevent local governments delivering essential services to the population.

KBN's public mandate of offering the local government sector access to low cost financing contributes to protecting the stability of this system.

The Nordic model

The public sector in the Nordic region is effectively comprised of central and local governments. In Norway, Sweden and Denmark, the local government sector is made up of two tiers: counties and municipalities.

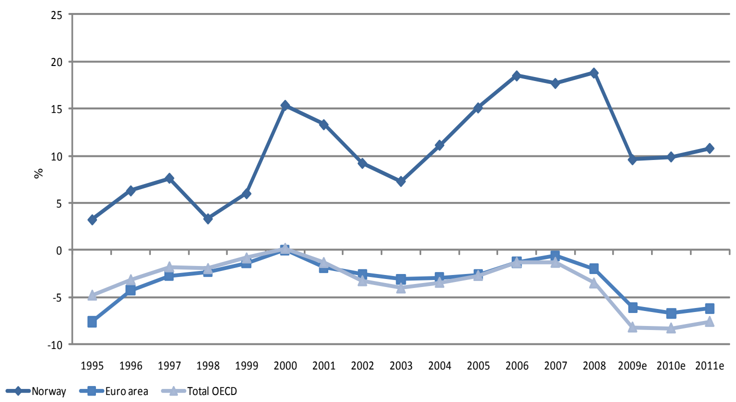
In Norway's case, the concept of municipal self-government is an important political principal, however in contrast to other Nordic and most European countries this self-government is not enshrined in the Norwegian constitution. The central government can at any time regulate the framework of municipal self-government and in principle this gives the national authorities great influence on the content of municipal activities.

The Norwegian local government sector has the responsibility for the provision of welfare state services. Municipalities' responsibilities cover education (primary schools), healthcare, care for the elderly, and the provision of drinking water and sewerage, while counties perform healthcare (county hospitals), secondary education, and some public transportation functions. The central government controls the transfer of funds through the public pension and social security system as well as controlling natural resources, defence, and of negative GDP growth, the economy rebounded in Q2 2009 and forecasts show an annualised GDP growth of approximately minus 1 per cent in 2009. However, growth is expected to bounce back sharply, with GDP growth in the region of 3 and 4 per cent in 2010 and 2011 respectively, considerably better than most other advanced economies.

Unemployment in Norway has not risen as sharply as in other developed countries. In October, the unemployment rate was 3.2 per cent, with projections pointing to a peak in 2010 of 3.75 per cent, tailing off to 3.5 per cent in 2011.

According to the National Budget for 2010, fiscal policy will provide further stimulus to the economy in 2010. As economic conditions normalise the government budget deficit should be reduced to about 4 per cent of the capital in the Government Pension Fund – Global, Norway's sovereign wealth fund.

General government financial balances (% of GDP)



Source: OECD

the police.
Norway is divided into 19 counties and 430 municipalities, both having equal standing in terms of the formal framework for their responsibilities.

Supervision and control

Local governments hold an important position, being responsible for more than two thirds of public expenditure. The framework for the activities of the local government sector is laid down by Parliament through legislation and decisions regarding local government financing. Parliament determines the division of functions between the different levels of government, i.e. central government, counties and municipalities. The government can only assign new functions to local government by means of legislation or decisions made by Parliament.

Although the average population of a Norwegian local government is 10,000 (and Norway's population is 4.8 million) and the difference in size of local governments is vast, there exists a comprehensive regional development policy which compensates for the economic disparities between local governments. It is an aim of the central government to offer citizens a high level of public services with equal standards, wherever they live in the country. Therefore there is a high degree of redistribution of income between municipalities and between counties. This is achieved through the General Purpose Grant Scheme. Redistribution of resources through the General Purpose Grant Scheme ensures both a fair distribution of income, and regional growth and development. This is essential to maintain an efficient and autonomous local government sector.

The local government sector relies on several sources of income, mainly taxes and central government transfers which account for 44 per cent and 34 per cent of revenues respectively. Municipalities collect most of their taxes from individual and corporate income and property tax. Counties on the other hand receive only income tax. The right of municipalities and counties to levy taxes is limited by maximum rates set annually by Parliament. Today, all municipalities and counties apply the maximum rate.

The legislative framework underlying the local government sector is laid out in the Local Government Act of 1992 which focuses on the key areas of monitoring and controlling local government budgets, regulating borrowing and the granting of guarantees, and provisions should a local government encounter financial difficulties.

Municipal budgets are regulated by the central government and each county or municipality's annual budget must be presented to the Ministry for Local Government and Regional Development.

Local government borrowing and granting of guarantees are regulated under the Local Government Act of September 1992 and municipalities are only permitted to raise debt for primary municipal investments, to convert existing debt and for temporary liquidity purposes.

Importantly, under the local government act, a local government cannot file for bankruptcy and cannot have bankruptcy proceedings filed against it.

If a local government does incur a budget deficit, the central government steps in to assure that the local government in question acts to provide a solution to correct its financial position. First, the local government is put on a publicly available 'watch-list'. The central government must then approve each of the local government's borrowings as well as a 'financial plan' for rectifying the problem within three years.

At all times the central government has the power to edit the budget and/or the 'financial plan' to ensure a timely recovery for the relevant municipality.

Should the extremely unlikely situation arise that a local government does experience financial difficulties the central government appoints a supervisory board for the relevant local government and the board then approves all payments and the order in which any claims shall be met. However, it is a testament to the high level of control and supervision of the municipal sector that this measure has never had to be implemented.

The Board of Directors' Report

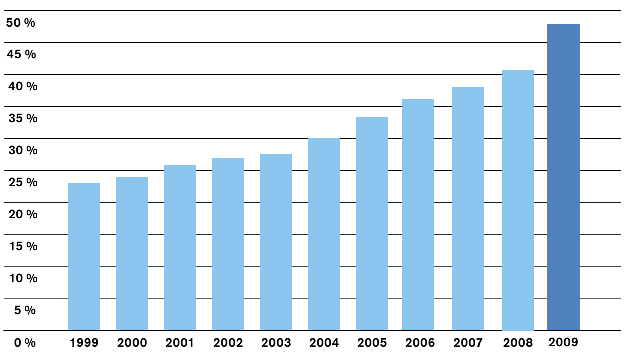
2009 has been an extraordinary year, which can neither be compared to previous years, nor set the benchmark for years to come. The situation in financial markets developed quickly throughout the year and KBN successfully adapted its business and was able to benefit from the changing environment.

For KBN, 2009 was marked by the following:
- Large profit
- Large one-off realised gains
- Strengthened market position.

KBN achieved a profit for the year of NOK 1.399 billion, compared with NOK 390 million in 2008. Strong lending, solid gains on the management of surplus liquidity and large extraordinary gains are the reason for this increase in profit. Of KBN's earnings in 2009, 21 per cent came from lending, 79 per cent from buy-back of KBN's own securities and liquidity management. Total return on assets increased from 0.22 per cent in 2008 to 0.62 per cent in 2009, while return on equity increased from 27.2 per cent in 2008 to 63.5 per cent in 2009.

KBN's total lending portfolio grew by NOK 33 billion, from NOK 118 billion at year end 2008, to NOK 151 billion at the end of 2009. In the same period, KBN's market share for the entire municipal sector, including municipal companies, increased from 40.8 per cent to 46.7 per cent. Lending demand has been large due to a considerable increase in project financing and also increased refinancing needs from the municipal sector. KBN is given special responsibilities from the central government. In order for KBN to take on these responsibilities in 2009, it has been important to offer financing to all those municipalities and counties who required financing, particularly at a time when financing opportunities from commercial entities have been extremely thin.

KBN's share of total market 1999-2009



The municipalities and counties increased their gross debt by NOK 27 billion from NOK 229 billion in 2008 to NOK 256 billion in 2009. This increase is NOK 4 billion greater than the previous year. KBN's lending volume directly to counties and municipalities grew by NOK 29 billion, or 27 per cent. During 2009, KBN placed loans to the sum of NOK 43 billion, compared with NOK 28 billion in 2008.

KBN has a policy of maintaining net cash balances equivalent to a minimum of 12 months' net debt redemptions. The liquidity portfolio of NOK 68 billion is carefully placed, adhering to a low-risk investment strategy. At year-end, notes issued by governments, states, regions and institutions with a government guarantee made up for 80 per cent of the portfolio. The majority of the liquidity portfolio has a maturity date of less than one year.

Further to KLP's purchase of Kommunekreditt AS from Eksportfinans ASA, the central government acquired KLP's stake in KBN and became its sole owner.

Through the increase in capital received at the end of 2008, and by means of the retained earnings generated in 2009, KBN has been in the position to fulfil its sector political function, as stated in the central government's ownership policy.

KBN's registered office is in Oslo.

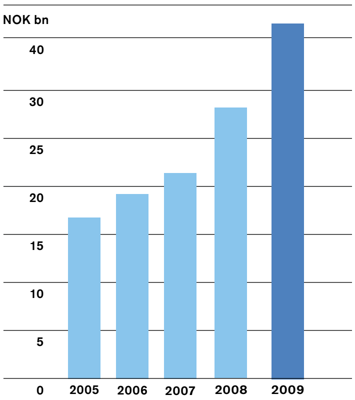
Annual accounts

The annual financial statements have been prepared on the basis of the going concern principle. It is the opinion of the Board that the Profit and Loss Statement and Balance Sheet, with their associated notes, as at 31 December 2009 provide an adequate description of the institution's financial position at year end. The annual accounts have been prepared in accordance with IFRS.

Net interest income after commission costs and costs of banking services amounted to NOK 1.033 billion in 2009, an increase of 103 per cent compared with 2008.

KBN had unhindered access to funding in 2009 and through a diversified funding strategy KBN's average cost of funds remained low, despite a marked increase in the cost of long-term financing in international markets. Furthermore, through favourable moves in basis swap levels, KBN was able to improve its funding cost in Norwegian kroner terms and thereby increase margins on its lending and liquidity management.

Loans granted 2005-2009



In 2009, net interest income from lending activities increased by NOK 188 million to NOK 391 million. This increase in income is due primarily to strong growth in the lending portfolio and favourable pricing when converting funding proceeds from USD to NOK.

There was a material increase in the contribution to net interest income from the management of surplus liquidity. This is due primarily to the increased premium for credit risk as a result of the financial crisis and an increase in volume of the liquidity portfolio.

KBN's financial results are marked by significant gains on the buy-back of KBN's own debt. The special circumstances in capital markets combined with continued access to funding made it possible for KBN to buy back a certain amount of its own debt with a realised gain of NOK 775 million. These buy-backs were primarily structured issues, and will not lead to increased costs going forward. The gain made on these buy-backs was as a result of an increase in the average remaining life of these issues due to a change in market conditions, and in light of the financial crisis, an increased credit risk premium.

Net unrealised gains on financial instruments at fair value and relating to hedging amounted to NOK 222 million. The value of KBN's liabilities has been written down by NOK 54 million as a result of interest rate changes and increased credit premiums on long dated funding. The value of the liquidity portfolio increased by NOK 201 million while the value of the lending portfolio at fair value was reduced by 98 million. Large movements in basis swap levels, predominately USD/NOK, led to an unrealised gain on KBN's outstanding basis swaps of NOK 65 million.

KEY FIGURES

(Figures in NOK 1 000 000)	2009	2008
PROFIT		
Net interest income	1 053	525
Pre-tax profit	1 946	543
Profit for the year	1 399	390
Return on equity after tax*	63.45%	27.20%
Total return on assets after tax*	0.62%	0.22%
LENDING		
The year's approbations	43 158	28 253
Total lending portfolio**	151 275	118 060
LIQUIDITY**	68 310	71 412
FUNDING		
Borrowings	116 263	67 961
Buy-back of own securities	6 832	4 753
Redemptions	58 135	33 550
Total outstanding debt**	224 418	202 197
TOTAL ASSETS	231 932	216 236
EQUITY CAPITAL		
Equity capital	3 561	2 205
Core capital ratio	9.25%	7.45%
Total capital ratio	11.05%	11.60%

*Annualised return
**Principal

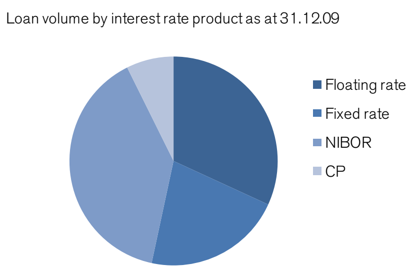
Operating costs amounted to NOK 91 million in 2009, compared with NOK 78 million in 2008. Personnel costs increased by NOK 6 million (or 14 per cent) as a result of an increase in employees, wage growth and increased pension costs. The increase in employees is due to KBN's growth in general and as a result of an increased reporting requirement from the authorities. KBN's relocation to new premises also led to an increase in costs as a result of installation and furnishing the new offices as well as vacating the previous offices. IT costs increased by NOK 2 million, primarily due to an upgrade of KBN's IT systems.

During 2009, KBN's assets increased by NOK 16 billion to NOK 232 billion.

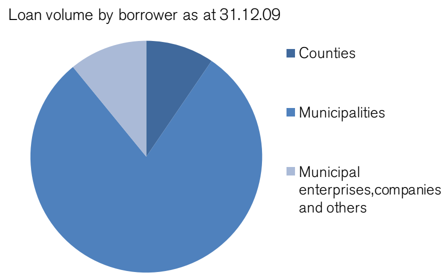
Total capital at year end amounted to NOK 3.973 billion, NOK 3.326 billion of which is core capital, an increase from NOK 2.251 billion in 2008. KBN's equity capital increased by NOK 1.075 billion in 2009. The capital ratio at year end was 11.05 per cent, and the core capital ratio was 9.25 per cent.

Lending

The total lending portfolio of NOK 151 billion is divided between NOK 120 billion for loans to municipalities, NOK 14 billion to counties and NOK 17 billion for loans to inter-municipal companies and other companies with municipal guarantees that perform primary municipal responsibilities. Of the total NOK 36 billion in new loan offerings, NOK 4 billion was offered to municipalities with less than 5000 inhabitants, and KBN was able to win NOK 3 billion of these loans.



71 per cent of the loan portfolio is floating rate with fixed rate loans making up the remaining 29 per cent. The percentage of loans linked to Nibor increased from 36 to 39 per cent in 2009 and short term loans increased from 4 to 7 per cent in the same period. The proportion of fixed rate loans decreased from 26 per cent in 2008 to 21 per cent in 2009.



All counties have loans with KBN. Of the 430 municipalities in Norway, only 5 do not have a loan with KBN. Furthermore, the majority of municipal and inter-municipal companies have loans with KBN. KBN is also experiencing an increase in demand from toll road companies and other companies involved in other core municipal services. These types of loan always require a municipal or county guarantee.

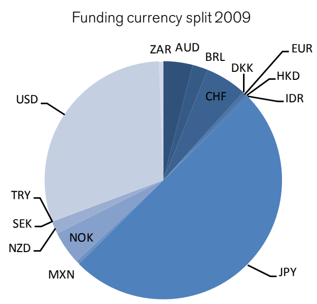
Most municipalities and counties take out a single loan annually to cover their annual investments. Investments in 2009 cover the entire range of primary municipal responsibilities.

As part of KBN's regular customer service, the institution advises customers on evaluating the interest rate climate, the choice of interest rate product and assistance in the management of their liability portfolio. Customers have direct access to online financial information and their own loan portfolio through the KBN website. KBN also arranges regional seminars which cover current topics in the municipal sector.

In accordance with the law on public acquisitions, the municipalities have to set a tender on banking agreements. KBN advises municipalities on entering into ordinary banking agreements and can offer advice to its customers as this is an area in which KBN does not operate. In 2009, KBN assisted in the signing of 29 banking agreements.

Funding

KBN raised a total of NOK 116 billion in 2009 via 15 different currencies, an increase of NOK 68 billion on the previous year.



In the first quarter of 2009 credit spreads of even triple-A rated institutions widened to record levels, only to tighten again markedly from April and onwards. Despite turbulent market conditions, KBN had continued good access to funding markets and the total annual issuance was the largest ever. KBN has benefited from a diversified funding strategy over the years and has focused on maintaining this through investor presentations in a variety of different countries in Europe, Asia and the Americas.

KBN follows a funding strategy established on four key segments:
- Benchmark funding

- Issuance in public niche markets
- Private placements to institutional investors
- Retail issues

Focusing on a variety of funding markets, KBN has secured stable access to funding markets on favourable terms and at the same time increased the institution's investor base. Japan continues to be KBN's largest source of funds, while other key markets included the rest of Asia and Europe.

In recent years, KBN has seen a substantial increase in the volume of funding raised in the Japanese "Uridashi" market. Uridashi loans are primarily sold direct to retail investors in Japan, where under Japanese regulations KBN qualifies as a sovereign borrower. Increased demand for KBN's name has meant that annual volume continued to grow in 2009.

KBN issued two successful benchmark bonds in 2009. Both issues were USD 1 billion in size, the first a three-year note launched in June, the second a five-year launched in October, extending KBN's curve in USD out to 2014. Credit spreads were wider than in 2008, but remained competitive, reflecting a general shift in levels for triple-A public sector issuers.

Continued access to funding markets can be attributable to the desire for investors to invest in high quality government related credits. In this regard, the credit quality of Norway and the Norwegian public sector stands out, which can be illustrated for example by the fact that Norway has the tightest sovereign credit default swap (CDS) spreads in the market.

KBN's total outstanding debt portfolio, including bonds, commercial paper and other funding instruments, increased from NOK 202 billion to NOK 224 billion in 2009.

KBN's international loan programme "The Programme for the Issuance of Debt Instruments" is a standardised loan documentation that not only simplifies but provides security for both lender and borrower. The Programme has an issuance limit of EUR 30 billion and will be increased to EUR 35 billion in 2010.

Liquidity management

KBN has a policy of maintaining net cash balances equivalent to a minimum of 12 months' net debt redemptions. This means that in a given situation KBN can cover all its debt obligations for the next 12 months without additional borrowing. Surplus liquidity is managed using a low risk investment policy, both in terms of credit and market risk, through investing in liquid securities issued by governments and financial institutions with a high credit rating. The majority of the portfolio has a maturity of less than one year. KBN is not exposed to any interest or currency risk, and the maturity profile of the liquidity portfolio is coordinated with underlying borrowing redemptions.

Risk management

Risk management and risk exposure are subject to a strict internal regulation to ensure that KBN maintains its credit rating and thus is able to access the most attractive funding markets. Credit and liquidity risk are generally low. KBN is not positioned for interest and currency risk. All risk limits and trading in new financial instruments must be approved by the Board. The financial guidelines are approved by the Board on an annual basis.

Credit risk represents KBN's single largest risk. Consequently the control and monitoring of KBN's credit exposure is given great focus and is done so on a continual basis.

Credit risk in the lending portfolio is confined to potential late payment of interest and instalments, not to potential failure of payment obligations. The provisions of the Local Government Act do not permit local and regional authorities to file for bankruptcy. There are also provisions in the Local Government Act relating to the procedures for late payment scenarios. According to these provisions, the state, in the form of the Ministry of Local Government and Regional Development, steps in to manage the financial obligations of the municipality should it be unable to meet these obligations. This gives loan providers protection against any loss of accumulated debt and accrued interest.

Credit risk arising from KBN's liquidity management and hedging operations is low due to strict policies on entering into financial contracts.

Trading in derivatives is subject to standard ISDA agreements, which involves netting of exposure that KBN faces on any particular counterparty should it file for bankruptcy. Furthermore, collateral agreements (CSA's) are in place with the majority of swap counterparties, whereby cash is deposited to match any derivative exposure over a predefined threshold.

Clear procedures and processes have been established for managing potential credit risk. All new lines of credit are established by the institution's finance committee and are reviewed regularly. Credit risk is managed on the basis of KBN's own credit risk models. The size of the credit limit is determined chiefly by available risk capital, the counterparty's rating, the type of financial instrument and its maturity.

Market risk consists mainly of interest and currency risk. KBN's financial policies only permit minimal exposure to interest rates and exchange rate risks. Interest rates and exchange rate risk is managed by ensuring that KBN's positions are hedged at all times.

Liquidity risk is minimised by ensuring that the liquidity portfolio is equivalent to a minimum of 12 months net debt redemptions. In addition, the liquidity portfolio is invested in liquid assets of high credit quality and short maturity.

Operational risk exists potentially throughout KBN's business. The institution seeks to minimise operational risk by focusing on good internal control, sound ethics and a high level of expertise among its employees.

Marketing, communication and corporate social responsibility

KBN collaborates with organisation within the local government sector, and co-organises several conferences within the local government financing field. KBN also participates in other municipal conferences in order to profile its services. The Board is focussed on maintaining regular contact with the government and other public figures to promote KBN's role.

The Board assesses KBN's ethical standards for marketing communication and marketing activities on an ongoing basis. KBN's ethical guidelines establish a practice that means KBN's customers can feel safe that the institution has a proactive approach to ethical conduct.

Corporate governance

KBN complies with Norwegian recommendations for corporate governance. The purpose of the recommendations is that companies must have corporate governance that clarifies the distribution of roles between shareholders, the Board and the management, in addition to that specified in the applicable legislation. The recommendation is intended to strengthen confidence in companies and contribute to the greatest possible wealth creation over time, to the benefit of shareholders, customers, employees and other interested parties.

KBN's main objective is to ensure that the market for local government loans remains competitive, so that local governments benefit from the best possible borrowing terms. At the same time, KBN should aim for a return on equity set by the central government. This is done under Norwegian law, KBN's Articles of Association and its ethical guidelines.

KBN's central bodies are organised in accordance with the provisions of the Companies Act. KBN's bodies are: the General Assembly, the Supervisory Board, the Control Committee, the Audit Committee, internal and external auditors and the President & CEO. KBN is made up of three operating areas with staff and support functions.

The institution's internal audits are intended to ensure that risk analysis and monitoring is carried out, and that operations are conducted in accordance with approved policies and guidelines. Internal audits are also an integral part of the KBN's management and planning process. Risk analysis in the audit process is followed up at departmental level and is reported to the President & CEO and the Board of Directors.

At the General Assembly, Else Bugge Fougner was re-elected as Chairman of the Board. Kristin Marie Sørheim was elected as the new Vice Chairman. Svein Blix and Martha Takvam were re-elected as Board members. Åmund T. Lunde and Frode Berge were elected as new members of the Board. Other representatives are Nanna Egidius and Martin Spillum (the employee's representative). Tor Christian Hansen is the alternate employee representative.

Organisation and skills development

At year end there were 44 employees, occupying 42.5 full time equivalent positions. KBN's human resources plan has a three year time horizon and is evaluated annually. The plan ensures that KBN has sufficient personnel with the competence required for the tasks and ambitions established in KBN's planning and strategy policies.

In October 2009, KBN relocated to new premises on Haakon VIIs gate 5b. The new premises will allow for increased efficiency and the opportunity to expand. Modern and energy saving heat and ventilation systems are in place. The building does not impact the external environment.

Health, safety and diversity at KBN
KBN considers it of importance to recruit capable and proficient staff, including those with an international background. This helps to give the institution greater competence in the areas that are central to KBN's business. 14 per cent of the employees at senior management or specialist levels are of non-Nordic region origin, and comprise 3 women and 3 men.

The working environment survey undertaken in 2008 has been followed up through focus on continuity and improvements. Absence through illness has been reduced from 2 per cent in 2008 to 1.8 per cent in 2009, with 2.7 per cent among female staff and 0.9 per cent among male staff. No workplace injuries were reported in 2009. Five employees took parental leave, one woman and four men. One employee took sabbatical leave. All employees benefit from an annual health check and optional occupational therapy advice.

Social responsibility
Ethical guidelines have been adopted by the Board and apply to all employees and union officials. The guidelines are reviewed in an annual employee seminar, where working practices are also discussed. KBN emphasises communicating the content of the ethical guidelines to its customer groups.

The environment: KBN has been certified by the environmental management organisation The Eco-Lighthouse Foundation in connection with environmentally sustainable business practices, on the back of which guidelines for sorting of waste, waste reduction, and systems for reducing KBN's CO2 emissions, are already in place. Relocation to its new office building gives KBN the opportunity to make further energy saving measures

Public policy function: KBN has a primary objective of being a predictable and reliable provider of credit. The institution must be a guarantor for competition in the loan market for the local government sector, so that counties and municipalities receive the best possible loan terms.

Equality of opportunity
The institution does not discriminate on the basis of gender in areas such as salary, career development and recruitment. Of the institution's 44 employees, 22 are women and 22 are men.

The proportion of women on the Board is 50 per cent. The Chairman of the Board is a woman.

KBN's senior management consists of the President & CEO (male) and a Deputy CEO (female). Women comprise 33 per cent of the executive management level.

Through its salary and personnel policy, KBN strives to recruit and train highly qualified employees, based on its needs at any given time. The institution is strongly committed to the equal pay principal, which means equal pay for work of equal value.

Application of profits
The Board proposes that the profits of NOK 1.399 billion be applied as follows:

NOK 67 million to be applied to payment of dividends and NOK 200 million to be applied to the payment of an extraordinary dividend.

NOK 1.132 billion is to be transferred to other equity capital.

After this application of profits, KBN has distributable reserves of NOK 3.293 billion.

Future prospects
It is too early to declare that the financial crisis is over. Despite macro-economic indicators starting to show positive signs, there are still challenges ahead both at a national and international level. Central government counter-cyclical policies helped to stabilise both the financial markets and the real economy. Such policies will now be gradually phased out. In Norway, counter-cyclical policies meant that the amount of proceeds from the State Pension Fund – Global, or Norway's sovereign wealth fund, surpassed the government's four per cent fiscal rule.

This implies that the probability of tighter budgetary conditions in the future is higher. The municipal sector will continue to be an important part of the government's financial policy, but the general budgetary tightening will no doubt affect the municipal sector. It is quite possible that the municipalities and counties can expect tighter budgetary limits in the years to come.

The National Budget for 2010 plans for continued high activity in the municipal sector and this is expected to lead to a continued increase in demand for new loans. In 2009, the municipal sector was given an important role through the central government's financial stimulus package of maintaining activity and employment levels. Even with the withdrawal of financial stimulus, and most likely a tighter financial policy, there are still a considerable number of investment projects that need to be completed. The municipalities must therefore make important yet difficult decisions when determining their budgets.

KBN's lending growth will be determined by the competitive situation in the municipal lending market. Competition is important so that the municipalities and counties have the opportunity to finance public sector tenders at attractive levels. KBN's primary objective is, and will continue to be, to ensure that the local government sector has access to long term financing on the best possible loan terms. However the competitive situation develops, KBN will endeavour to offer loans at attractive terms.

KBN's floating lending rates were kept low throughout 2009. The majority of the municipalities' loans are in floating rate. An increase in interest rates of 1 per cent would translate to an increase of NOK 1 billion in interest rate charges for the local government sector.

One of the Board's most important objectives is to ensure that through KBN's status in international capital markets, by means of its high credit quality and its core competency, the municipalities and counties benefit by receiving continued low financing rates.


Else Bugge Fougner


Kristin Marie Sørheim


Frode Berge


Svein Blix


Nanna Egidius


Åmund T. Lunde


Martin Spillum


Martha Takvam

The solid earnings generated in 2009 made it possible for KBN to strengthen its capital base significantly. The Board considers it of great importance that KBN's capital is sufficiently large to facilitate continued lending growth and to meet new requirements for banks and financial institutions.

The capital markets have stabilised and this has led to lower credit risk premiums and a restoration of liquidity. Challenges can still remain in the form of growing government budget deficits and increased competition from sovereigns and government guaranteed issuers in the funding markets. It is therefore important for KBN to maintain its position in the public markets. The Board therefore expects continued high activity in the funding markets.

2009 has been an extraordinary year. KBN has emerged unaffected by the financial crisis. The institution has been able to fulfil its sector political function by making it possible for the municipalities and counties to finance public sector investments in a cost efficient way – unaffected by the financial crisis. The financial results are highly satisfactory.

The Board would like to thank the employees for a job well done.

The Board continues to emphasise that KBN pursues its operations in a way that KBN is perceived by the municipalities and counties as an important vehicle for the financing of the tasks that they have ahead of them.

Oslo, 31 December 2009
12 March 2010

The Board of Directors, Kommunalbanken AS

Else Bugge Fougner
Chairman of the Board

Kristin Marie Sørheim
Vice Chairman

Frode Berge
Member

Svein Blix
Member

Nanna Egidius
Member

Åmund T. Lunde
Member

Martin Spillum
Member

Martha Takvam
Member

Petter Skouen
CEO & President

INCOME STATEMENT

(Amounts in NOK 1 000 000)	Note	2009	2008
Interest income	7	4 847	8 998
Interest expenses	7	3 794	8 473
NET INTEREST INCOME	4	1 053	525
Commission expenses and expenses of banking services	8	20	17
Net gain/(loss) on financial instruments at fair value	3,6	222	(2)
Net gain/(loss) from repurchase of issued securities		781	115
Other income		1	1
TOTAL OTHER OPERATING INCOME		984	96
Salaries and administrative expenses	9,11	68	61
Depreciation on fixed assets		5	5
Other expenses		18	12
TOTAL OPERATING EXPENSES		91	78
PROFIT BEFORE TAX		1 946	543
Income tax	10	547	153
PROFIT FOR THE YEAR		1 399	390

STATEMENT OF COMPREHENSIVE INCOME

(Amounts in NOK 1 000 000)	Note	2009	2008
Profit for the year		1 399	390
Other comprehensive income		0	0
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		1 399	390

STATEMENT OF FINANCIAL POSITION

(Amounts in NOK 1 000 000)	Note	2009	2008
ASSETS			
Deposits with credit institutions	1,5,12	988	3 900
Instalment loans	1,2,5,13	153 040	120 935
Notes, bonds and other interest-bearing securities	1,2,5	69 649	73 018
Financial derivatives	1,5,16	8 241	18 369
Deferred tax assets	10	0	1
Other assets	15	14	12
TOTAL ASSETS		**231 932**	**216 236**
LIABILITIES AND EQUITY			
Loans from credit institutions	1,5	1 051	1 922
Senior securities issued	1,2,5,14	223 566	200 087
Financial derivatives	1,5,16	2 206	10 240
Other liabilities		512	179
Deferred tax liabilities	10	60	0
Pension liabilities	11	24	20
Subordinated debt	1,5,18	667	1 253
Hybrid Tier 1 capital instruments	1,5,18	285	329
TOTAL LIABILITIES		**228 371**	**214 031**
Share capital	25	1 221	1 221
Retained earnings		2 340	984
TOTAL EQUITY		**3 561**	**2 205**
TOTAL LIABILITIES AND EQUITY		**231 932**	**216 236**

Statement from the Board of Directors

We confirm that the annual report for 2009 is, to the best of our knowledge, prepared in accordance with International Financial Reporting Standards, IFRS, and that the information in the financial statements provides a fair overview of the Company's assets, debt, financial position and results. To the best of our knowledge, the annual report provides a fair overview of important events during the accounting period in question and their effects on the annual accounts, and also the material risk and uncertainties facing the Company during the next accounting period.

Oslo, 31 December 2009
12 March 2010
The Board of Directors, Kommunalbanken AS

Else Bugge Fougner
Chairman of the Board

Kristin Marie Sørheim
Vice Chairman

Frode Berge
Member

Svein Blix
Member

Nanna Egidius
Member

Åmund T. Lunde
Member

Martin Spillum
Member

Martha Takvam
Member

Petter Skouen
CEO & President

STATEMENT OF CHANGES IN EQUITY

(Amounts in NOK 1 000 000)

1 January—31 December 2009	Share capital	Retained earnings	Total equity
Equity as of 1 January 2009	1 221	984	2 205
Total comprehensive income for the year	0	1 399	1 399
Issue of share capital	0	0	0
Dividends	0	(44)	(44)
Equity as of 31 December 2009	**1 221**	**2 340**	**3 561**

1 January—31 December 2008	Share capital	Retained earnings	Total equity
Equity as of 1 January 2008	755	594	1 349
Total comprehensive income for the year	0	390	390
Issue of share capital	466	0	466
Dividends	0	0	0
Equity as of 31 December 2008	**1 221**	**984**	**2 205**

STATEMENT OF CASH FLOWS

(Amounts in NOK 1 000 000)	Note	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES			
Interest received		5 754	9 225
Interest paid		(4 748)	(8 437)
Fees and commissions paid		(19)	(17)
Receipts from repurchase of issued securities		781	115
Other income		1	24
Cash payments to employees and suppliers		(69)	(73)
Income taxes paid		(201)	(56)
		1 499	781
Net disbursement of loans to customers		(33 217)	(14 000)
Net (increase)/decrease in deposits with credit institutions		2 375	(3 044)
Net (increase)/decrease in notes, bonds and other interest-bearing securities		(6 416)	(23 025)
Net (increase)/decrease in other assets		62	(426)
Net increase/(decrease) in other liabilities		(25)	437
NET CASH FLOWS FROM OPERATING ACTIVITIES		(35 723)	(39 277)
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property and equipment		(8)	(1)
NET CASH FLOWS FROM INVESTING ACTIVITIES		(8)	(1)
CASH FLOWS FROM FINANCING ACTIVITIES			
Net proceeds from issuance of debt securities		50 886	24 216
Proceeds from other borrowed funds		0	0
Repayment of other borrowed funds		(612)	(481)
Proceeds from issuance of subordinated debt		0	102
Repayment of subordinated debt		0	(172)
Dividends paid		(44)	0
Issue of ordinary shares		0	466
NET CASH FLOWS FROM FINANCING ACTIVITIES		50 230	24 131
NET CHANGE IN CASH AND CASH EQUIVALENTS		14 499	(15 148)
Effect of foreign exchange differences		(14 476)	15 076
Cash and cash equivalents at 1 January		40	111
Net change in cash and cash equivalents		23	(72)
Cash and cash equivalents at 31 December		63	40
Cash and deposits with central banks		0	*0*
Deposits with credit institutions without agreed period of notice	12	63	*40*

ACCOUNTING POLICIES

Reporting entity

Kommunalbanken AS (”the Company”, or ”KBN”) is a limited company established for the purpose of providing loans to local authorities, regional authorities, inter-municipal companies and other companies that provide municipal services under a municipal guarantee or other security. The Company's registered office is in Haakon VIIs gate 5B, Oslo. The financial statements for the year ended 31 December 2009 were approved by the Board of Directors on 12 March 2010.

Basis for preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the EU. The Company presents its financial statements on a historical cost basis, except for:

- Financial instruments at fair value through profit and loss
- Financial instruments held for trading, which are measured at fair value
- Loans and receivables in fair value hedges, where hedged risk is measured at fair value

Foreign currency translation

The Company's functional and presentation currency is the Norwegian kroner (NOK). Assets and liabilities denominated in a foreign currency are translated into NOK at the exchange rate on the reporting date (31 December 2009). Revenues and expenses denominated in a foreign currency are translated into NOK at the exchange rate at the transaction date.

Estimates and critical accounting judgements

Preparation of financial statements in accordance with IFRS requires management to exercise judgement and estimates which can affect carrying values of assets and liabilities, and revenues and expenses. Estimates and accounting judgements are based on historical experience and expectations of future trends. Actual results may deviate from those estimates.

<u>Fair value of financial instruments</u>

The fair value of financial instruments that are not traded in an active market, or do not have available quoted prices at the reporting date, is determined using valuation techniques. The valuation requires the management to make assumptions and use estimates when considering credit risk and liquidity risk. Even if the assumptions and estimates are based to the greatest possible extent on actual market conditions prevailing at the reporting date, they involve judgement and may add to the degree of uncertainty in valuations. Items in the financial statements that can be impacted by management's assumptions include:

- Bonds and notes measured at fair value, where market quotes are not available and fair value needs to be established using valuation techniques
- Loans to customers measured at fair value
- Financial liabilities in the form of issued securities measured at fair value
- OTC-derivatives which do not have available market quotes and fair value needs to be established using valuation techniques

<u>Pension liabilities</u>

The value of pension liabilities is determined using actuarial valuation, which involves making assumptions about variables, which affect the cost of obligation, i.e. discount rates, expected return on assets, future salary increases, mortality rates and future pension increases. Changes in the estimates impact the value of pension liabilities and pension costs. The Company complies with the actuarial and economic estimates prepared and updated by the Norwegian Accounting Standards Board (Norsk Regnskapsstiftelse).

Financial instruments

<u>Fair Value Option</u>

The Company manages interest and FX-risk by hedging all exposure to changes in exchange rates and interest rate levels using financial derivatives. In order to achieve corresponding treatment between the derivatives, which are recognised at fair value through profit and loss, and the hedged items, the Company applies the Fair Value Option for financial liabilities and assets, where such treatment is appropriate and significantly reduces “accounting mismatch” that would otherwise arise from measuring assets and liabilities on a different basis.

<u>Classification and measurement</u>

Classification of financial instruments takes place on initial recognition and determines the subsequent measurements according to IAS 39. Financial instruments are classified into the following categories (in accordance with IAS 39):

1. Financial assets designated at fair value through profit and loss (FVO)

Financial assets classified in this category include selected bonds and notes in the liquidity portfolio, fixed rate loans and NIBOR-indexed loans to customers, which are hedged with interest rate and/or cross-currency derivatives. Application of the Fair Value Option to these assets helps to achieve consistent treatment with associated derivatives or financial liabilities which are measured at fair value through profit and loss.

2. Financial assets held for trading

Included in this classification are bonds and notes in the trading portfolio. Financial derivatives, with the exception of contracts designated as hedging instruments, are classified as financial assets or liabilities held for trading. Debt certificates issued by municipalities with a maturity of less than 1 year and traded in an active market are classified as financial assets held for trading. Financial assets held for trading are measured at fair value through profit and loss.

3. Financial assets held to maturity

Financial assets in this category are primarily asset-backed securities that have been acquired with the intention of being held to maturity and selected securities that became illiquid as a result of the financial crisis in 2008 and had been reclassified from “Held for trading” to “Held to maturity”-category as of 1 July 2008. Financial assets held to maturity are measured at amortised cost using the effective interest rate method.

4. Loans and receivables

Included in this category are loans and advances to customers, and bonds and notes not quoted in an active market. Financial assets classified as Loans and receivables are measured at amortised cost using the effective interest rate method.

Hedge accounting may apply to bonds and notes classified as Loans and receivables when interest rate and cross-currency swaps are used to manage corresponding risks in securities. When the criteria for fair value hedge are met, the change in the fair value that is attributable to the risk hedged is recorded as a part of carrying value under "Notes, bonds and other interest-bearing securities", and is also recognised in the income statement as "Net gain/(loss) on financial instruments at fair value".

5. Financial liabilities designated at fair value through profit and loss (FVO)

Fair Value Option is applied to the majority of issued debt, where market risk exposure is hedged with derivative contracts. The financial liabilities and corresponding derivative contracts are evaluated on a fair value basis and managed in accordance with the Company's risk management policy that allows only limited exposure to interest rate and FX-risk in liabilities.

6. Financial liabilities at amortised cost

Financial liabilities measured at amortised cost are public benchmark loans, that are designated as hedged items and meet criteria for fair value hedges. Changes in fair value of these loans that are attributable to the risk hedged are recorded as a part of the carrying value under "Senior securities issued" and are recognised in the income statement as "Net gain/(loss) on financial instruments at fair value".

Determination of fair value

When a financial instrument is recognised initially, it is measured at its fair value plus, in the case of financial instruments not at fair value through profit and loss, transaction costs that are directly attributable to the acquisition or issue of the instrument.

After initial recognition, the fair value of financial instruments is determined using available market data and valuation methods. Determination of fair value follows IFRS 7 Fair value hierarchy:

Level 1

Securities traded in an active market are recorded at quoted prices in active markets at the reporting date. Quoted prices are provided by international vendors (Reuters/ Bloomberg), and management assesses those prices with regard to methodology and liquidity of the market in which the financial assets are traded. Quoted prices provided by vendors are classified as Level 1-inputs when they represent actual market transactions. Basis swap prices on USD-NOK, EUR-NOK and EUR-USD basis swaps, that are quoted in an active market are classified as Level 1-inputs.

Level 2

Level 2 includes financial instruments that are not traded in an active market and fair value can be determined using quoted prices on identical or similar instruments, or using valuation methods where significant inputs are based on observable market data. Level 2-inputs might include:

- Observable interest rate yield curves, FX-rates, equity indexes and commodity indexes
- Quoted prices and credit spreads at the reporting date for similar instruments issued by the same issuer but with a different tenor, so that an adjustment for maturity is necessary
- Quoted prices and credit spreads at the reporting date for similar instruments issued by the same issuer but denominated in a different currency, so that an adjustment for currency is necessary
- Actual market transactions in identical instruments before or after reporting date, so that an adjustment for events between the date of transaction and the reporting date is necessary
- More liquid instruments issued by the same issuer with identical maturity, but an adjustment for liquidity risk is necessary
- Prices on potential new issues in similar instruments from the same issuer

Level 3

Level 3 includes financial instruments that are not traded in an active market. Fair value of these instruments is determined using valuation methods where significant inputs are not based on observable market data. Financial instruments classified as Level 3 include notes and bonds with low liquidity, fixed-rate loans to customers, issued bond debt not traded in an active market and most OTC-derivatives. Notes and bonds issued by Norwegian issuers are valued using consensus prices calculated by the Norwegian Securities Dealers Association ("Norges Fondsmeglerforbund"), and classified as Level 3.

The same input might be used to determine fair value of notes and bonds classified as Level 2 and Level 3. In these cases classification depends on whether adjustments that are done to the observable market data are considered to be significant (Level 3) or not (Level 2). Other inputs used in determination of fair value might include:

- Indicative prices and estimates for similar instruments provided by other market participants
- Market indices, both bonds and credit default swap indices, for similar instruments
- Non-binding price quotes from different sources
- Historical or implied volatilities

Recognition and derecognition

Recognition and derecognition of financial instruments in the Statement of Financial Position takes place at time of settlement. On initial recognition all financial assets and liabilities are measured at fair value. For financial assets that are not carried at fair value through profit and loss, the value at initial recognition includes transaction costs that are directly attributable to acquisition.

For regular way purchase of financial assets, the value changes of the asset to be received during the period between the trade date and settlement date are recognised in the same way as the asset acquired, i.e. the change in value is not recognised for financial assets carried at amortised cost; it is recognised in profit and loss for assets carried at fair value or classified as held for trading.

Financial assets are derecognised when the contractual rights to the cash flows expire or are transferred. Repurchase agreements (repo) involve transfer of assets while the Company retains practically all risk and reward, and therefore does not qualify for derecognition. Securities sold subject to repurchase agreements ('repos') are not derecognised from the Statement of Financial Position, and a corresponding counterparty liability is recognised.
Financial liabilities are derecognised when the contractual obligation has been discharged, cancelled or expired. Buy-backs of issued bond debt result in derecognition of financial liabilities. Any difference between settlement amount and carrying value of the liability is recognised in the income statement as gain or loss at the date of transaction.

<u>Offsetting of financial assets and liabilities</u>
Financial assets and financial liabilities are offset and the net amount is presented in the Statement of Financial Position when the Company has a legally enforceable right to offset these items and intends to realise the asset and settle the liability simultaneously.

<u>Impairment of financial assets</u>
Financial instruments classified as Loans and receivables or Held to maturity are measured in accordance with IAS 39. When there is objective evidence of value loss, the assets are impaired.
Individual impairments
If there is objective evidence that a loss has been incurred, the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows. The loss is recognised in profit and loss. When commitments are assessed for individual impairments, the following loss events may be taken into consideration:

- Significant financial difficulty of the issuer or obligor
- Payment default or breach of contract
- Delinquency in interest or principal payments or renegotiation of loan terms as a result of debtors' financial problems

Group impairments
Financial assets are tested for impairment at a group level, based on the division of the assets into groups with similar risk characteristics. Assets are impaired if the observable data indicates a reduction in future cash flows from the group as a result of negative changes to debtors' creditworthiness and/or changes in economic environment that correlate with defaults in the group. Loans to customers are assessed as a uniform group, based on the provisions of the Local Government Act that rates all Norwegian municipalities equally with regard to risk to the lender. Securities carried at amortised cost are split into groups according to the issuer's risk, underlying exposure and geographical spread. The impairment loss is calculated per risk group, based on expectations to the macroeconomic conditions that can impact on the counterparty's ability to pay, and the loss history for the various risk groups.
Under current legislation limiting the municipalities' possibility of going bankrupt, the Company does not expect any impairments on its loan portfolio.

Hedge accounting
Interest rate swaps and cross currency swaps are used to manage market risk in the portfolio of notes and bonds classified as Loans and receivables. Hedge relationship between a bond and a swap is treated as fair value hedge. Hedge relationship is established and documented at a transaction level, and hedge effectiveness is measured on an on-going basis using Dollar-Offset method. Ineffective part of hedge is recognised in the income statement.
Hedging instruments are measured at fair value through profit and loss, and carrying amounts are adjusted accordingly. Change in fair value on the hedged items, that is attributable to the risk hedged, is recorded as a part of carrying value of the item and is recognised in the income statement as "Net gain/(loss) on financial instruments at fair value".

Statement of Cash Flows
Statement of Cash Flows is prepared using the direct method and presents cash flows classified by activity. Cash and cash equivalents include cash on hand, demand deposits and short-term deposits with credit institutions that are readily convertible to cash.

Recognition of income and expenses
Interest and commissions are recognised in profit and loss as they are earned or accrue. Unrealised gains and losses on financial instruments at fair value are recognised in profit and loss under "Net gains/(losses) on financial instruments at fair value". Interest income for assets and liabilities carried at amortised cost is recognised in profit and loss using the effective interest method.
Unrealised gains and losses on financial instruments at fair value and value changes on hedged items under hedge accounting are recognised in profit and loss under "Net gains/(losses) on financial instruments at fair value".
Commission costs on government guaranteed funding are accrued over the lifetime of the transaction. Other commission costs and charges are recognised as expenses in the period when the service is provided.

Fixed assets
Fixed assets are carried at cost with the deduction of accumulated depreciation and write-downs. Ordinary depreciation, based on cost price, is calculated using a straight line method over the estimated useful life, and the disposal value of the assets is assumed to be zero.

Intangible assets
A domain name is defined as an intangible fixed asset with an indefinite useful life and is not depreciated. Assets are tested for impairment annually. If there is an indication that the assets are impaired, the value of the assets is written down, and the difference between the carrying amount and the recoverable amount is recognised in profit and loss.

Pensions
The Company has an employee pension scheme. The pension scheme is treated as a defined benefit plan. The traditional earning profile and expected final salary are used to determine entitlements. The net pension cost for the period is included in "Salaries and administrative expenses" and consists of the sum of the period's pension accumulation,

interest costs on the calculated liability and expected return on the pension assets.
The Company has pension commitments for salaries that exceed 12 times the National Insurance base amount, which is not administered through a life insurance company.
Value of net pension liabilities is calculated based on economic and actuarial assumptions. Estimate deviations in excess of 10 % of the higher of gross pension liabilities and gross pension assets at the beginning of the year (the corridor) are recorded in the income statement.

Tax and deferred tax
Taxes are recognised as they accrue, i.e. the tax cost is based on the pre-tax accounting profit or loss. It is adjusted for temporary and permanent differences before the year's tax base for tax payable is calculated. Deferred tax and the deferred tax asset are calculated on the basis of temporary differences between the accounting and tax values at the financial year end. The nominal tax rate is used for calculation. Tax increasing and tax-reducing differences within the same period are offset.
Income tax consist of tax payable (tax on the taxable profit or loss for the year), changes in net deferred tax and insufficient/ excess provision for payable tax allocated in previous years.

Equity
The Company's equity consists of share capital and retained earnings.
Dividends are classified as equity until approval by the Annual General Meeting.

Segment information
The Company has one operating segment: lending to the Norwegian municipalities and municipal companies. The Company does not provide separate segment reporting other that disclosures on lending portfolio and business as a whole.

New accounting standards in 2009
Following the amendments to IAS 1, the Company presents a new set of financial statements from 1 January 2009. The new set includes Statement of Comprehensive Income, that shows items recognised directly in equity. The Company had no such items in 2008 and 2009.
IFRS 7 has been amended and come into effect from 1 January 2009. The amendments require enhanced disclosures about fair value measurement and liquidity risk.

Issued standards, that have not come into effect
IFRS 9 *Financial instruments*
IFRS 9 replaces classification and measurement rules in *IAS 39 - Financial instruments-Recognition and measurement.* In the new IFRS 9 financial instruments with basic loan features and managed on a contractual cash flow basis should be recorded at amortised cost, unless fair value option is applied. Other financial instruments should be measured at fair value. Effective date for IFRS 9 is scheduled to be 1 January 2013, but the standard is still not approved by the EU. The measurement principles used in the Company's accounts are retained in the new standard, and IFRS 9 is not expected to have any substantial impact on the Company's statement of financial position and income statement. The new standard is expected to be implemented from 1 January 2013.
Changes in IAS 32 *Financial instruments – presentation - Classification of Rights Issues*
According to the amended IAS 32, rights, options or warrants to acquire a fixed number of the entity's own equity instruments for a fixed amount of any currency are considered as equity instruments. The amendment is to be applied to annual periods beginning on or after 1 February 2010. The Company will implement the amendment from 1 January 2011 and does not expect it to have any substantial impact on statement of financial position or income statement.
Changes in IAS 39 *Financial instruments – recognition and measurement - Eligible Hedged Items*
Changes in IAS 39 aim to clarify what is a qualifying portion of fair value or cash flows. The amendments clarify application of hedge accounting to hedge of inflation risk and hedging with options. The amendments also make clear that hedged risk should be separately identifiable and reliably measurable to qualify for hedge accounting. The amendments are effective for annual periods beginning on and after 1 July 2009. The Company will implement the amendments from 1 January 2010 and does not expect any substantial changes as a result of implementation.
No other issued standards, that have not come into effect, or changes in the accounting standards resulting from IASB's improvement project, are considered to be relevant for the Company.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1

Classification of financial instruments

(Amounts in NOK 1 000 000)

At 31 December 2009	Total	At fair value through profit and loss			Held to	Loans and	Other
		FVO	Held for trading	Fair value hedge	maturity	receivables	liabilities
Deposits with credit institutions	**988**	925	0	0	0	63	0
Instalment loans	**153 040**	78 862	11 162	0	0	63 017	0
Notes, bonds and other interest-bearing securities	**69 649**	34 595	16 140	0	1 481	17 432	0
Financial derivatives	**8 241**	0	8 195	46	0	0	0
Total financial assets	**231 918**	**114 382**	**35 497**	**46**	**1 481**	**80 512**	**0**
Loans from credit institutions	**1 051**	1 051	0	0	0	0	0
Senior securities issued	**223 566**	215 520	0	0	0	0	8 046
Financial derivatives	**2 206**	0	201	2 005	0	0	0
Subordinated debt	**667**	667	0	0	0	0	0
Hybrid Tier 1 capital instruments	**285**	285	0	0	0	0	0
Total financial liabilities	**227 775**	**217 523**	**201**	**2 005**	**0**	**0**	**8 046**

At 31 December 2008	Total	At fair value through profit and loss			Held to	Loans and	Other
		FVO	Held for trading	Fair value hedge	maturity	receivables	liabilities
Deposits with credit institutions	**3 900**	3 680	180	0	0	0	40
Instalment loans	**120 935**	58 798	4 999	0	0	57 138	0
Notes, bonds and other interest-bearing securities	**73 019**	31 619	32 138	0	2 388	6 874	0
Financial derivatives	**18 369**	0	18 324	45	0	0	0
Total financial assets	**216 223**	**94 097**	**55 641**	**45**	**2 388**	**64 012**	**40**
Loans from credit institutions	**1 922**	1 922	0	0	0	0	0
Senior securities issued	**200 087**	200 087	0	0	0	0	0
Financial derivatives	**10 240**	0	10 240	0	0	0	0
Subordinated debt	**1 253**	1 253	0	0	0	0	0
Hybrid Tier 1 capital instruments	**329**	329	0	0	0	0	0
Total financial liabilities	**213 832**	**203 592**	**10 240**	**0**	**0**	**0**	**0**

NOTE 2

Financial instruments measured at amortised cost

(Amounts in NOK 1 000 000)

At 31 December 2009	Carrying amount	Fair value
Instalment loans	63 017	62 979
Notes, bonds and other interest-bearing securities classified as Loans and receivables	17 432	17 555
Notes, bonds and other interest-bearing securities classified as Held to maturity	1 481	1 461
Total financial assets at amortised cost	**81 930**	**81 995**
Senior securities issued	8 046	8 061
Total financial liabilities at amortised cost	**8 046**	**8 061**

At 31 December 2008	Carrying amount	Fair value
Instalment loans	57 138	57 145
Notes, bonds and other interest-bearing securities classified as Loans and receivables	6 874	6 854
Notes, bonds and other interest-bearing securities classified as Held to maturity	2 388	2 320
Total financial assets at amortised cost	**66 400**	**66 319**
Senior securities issued	0	0
Total financial liabilities at amortised cost	**0**	**0**

Fair value of financial instruments recorded at amortised cost is determined using the same principles, as financial instruments carried at fair value. Calculation of fair value is based on the same market rates, estimates and assumptions, and uses the same valuation techniques for all financial instruments, regardless of classification.

NOTE 3

Net gain/(loss) on financial instruments at fair value

(Amounts in NOK 1 000 000)

Unrealised gain/(loss) on financial instruments at fair value	2009					
	Total	At fair value through profit and loss			Loans and	Other
		FVO	Held for trading	Fair value hedge	receivables	liabilities
Instalment loans	**(552)**	(536)	(16)	0	0	0
Notes, bonds and other interest-bearing securities*	**385**	46	(7)	0	346	0
Financial derivatives	**1 875**	0	2 148	(273)	0	0
Loans from credit institutions	**10**	10	0	0	0	0
Senior securities issued*	**(1 529)**	(1 425)	0	0	0	(104)
Subordinated debt and Hybrid Tier 1 capital instruments	**33**	33	0	0	0	0
Net unrealised gain/(loss) on financial instruments at fair value	**222**	**(1 872)**	**2 125**	**(273)**	**346**	**(104)**

*Financial derivatives in fair value hedges are measured at fair value through profit and loss. Hedged items in fair value hedges include NOK 17.7 billion in notes and bonds, and NOK 7.8 billion in senior securities issued, that are measured at amortised cost. Changes in fair value in hedged items that are attributable to hedged risk are recorded as a part of carrying value of corresponding assets and liabilities, and are recognised in the income statement as "Net unrealised gain/(loss) on financial instruments at fair value". The effect of fair value hedges on the income statement is described in Note 6.

Unrealised gain/(loss) on financial instruments at fair value	2008					
	Total	At fair value through profit and loss			Loans and	Other
		FVO	Held for trading	Fair value hedge	receivables	liabilities
Instalment loans	**1 885**	1 867	18	0	0	0
Notes, bonds and other interest-bearing securities	**347**	353	9	0	(15)	0
Financial derivatives	**(2 513)**	0	(2 556)	43	0	0
Loans from credit institutions	**(11)**	(11)	0	0	0	0
Senior securities issued*	**351**	351	0	0	0	0
Subordinated debt and Hybrid Tier 1 capital instruments	**(60)**	(60)	0	0	0	0
Net unrealised gain/(loss) on financial instruments at fair value	**(2)**	**2 499**	**(2 529)**	**43**	**(15)**	**0**

Realised gains on financial instruments are a result of market transactions, such as the repurchase of issued debt and trading activities in the liquidity portfolio. Realised gains on financial instruments recorded in the income statement are presented in the table below:

	2009		2008	
	Amount	Gain/(loss)	Amount	Gain/(loss)
Repurchase of issued debt	6 832	775	4 753	115
Trading activities	3 268	6	0	0
Total	**10 100**	**781**	**4 753**	**115**

NOTE 4

Reclassifications

(Amounts in NOK 1 000 000)

No financial instruments have been reclassified from or to fair value-category during 2009.

Due to the shortage of liquidity and credit availability in the markets in 2008, the level of market activity for some asset classes was reduced. Following the amendment of IAS 39 in 2008, the company re-assessed its Held for trading-portfolio and reclassified some instruments to Held to maturity. Reclassification was made at fair value as of 1 July 2008.

	31 December 2009	31 December 2008
Carrying value	325	440
Fair value	325	433

Total fair value loss at 1 July 2008 amounted to NOK 5.2 million. NOK 2.8 million of this amount has been amortised in Net interest income in 2008, and NOK 1.9 million—in 2009. If the assets had not been reclassified, an unrealised gain of NOK 6.0 million would have been recognised in the income statement in 2009. There are no losses expected on the reclassified assets during their remaining lifetime.

NOTE 5

Fair value of financial instruments

(Amounts in NOK 1 000 000)

At 31 December 2009	Level 1	Level 2	Level 3	Total
Deposits with credit institutions	0	925	0	**925**
Instalment loans	0	56 427	33 596	**90 023**
Notes, bonds and other interest-bearing securities	4 463	30 467	15 806	**50 736**
Financial derivatives	865	6 782	594	**8 241**
Total financial assets at fair value	**5 328**	**94 601**	**49 996**	**149 925**
Loans from credit institutions	0	1 051	0	**1 051**
Senior securities issued	30 649	19 342	165 529	**215 520**
Financial derivatives	65	1 400	741	**2 206**
Subordinated debt	0	0	667	**667**
Hybrid Tier 1 capital instruments	0	0	285	**285**
Total financial liabilities at fair value	**30 714**	**21 793**	**167 222**	**219 729**

At 31 December 2008	Level 1	Level 2	Level 3	Total
Deposits with credit institutions	0	3 860	0	**3 860**
Instalment loans	0	0	63 797	**63 797**
Notes, bonds and other interest-bearing securities	5 097	48 851	9 808	**63 756**
Financial derivatives	0	18 369	0	**18 369**
Total financial assets at fair value	**5 097**	**71 080**	**73 605**	**149 782**
Loans from credit institutions	0	0	1 922	**1 922**
Senior securities issued	0	0	200 087	**200 087**
Financial derivatives	0	10 240	0	**10 240**
Subordinated debt	0	0	1 253	**1 253**
Hybrid Tier 1 capital instruments	0	0	329	**329**
Total financial liabilities at fair value	**0**	**10 240**	**203 592**	**213 831**

Certain financial instruments have been transferred from one level into another during 2009. The transfers are a result of improved liquidity in the credit markets, and the amendments to IFRS 7 with a clarification on fair value hierarchy. Transfers from level 3 to level 1 include NOK 30.6 billion in senior securities issued, primarily large public benchmark loans where fair value was based on observable market quotes at 31 December 2009.

Reconciliation of movements in Level 3

	2008	Purchase	Sale	Gain/(loss)	Transfers	2009
Instalment loans	63 797	4 195	(8 255)	43	(26 184)	33 596
Notes, bonds and other interest-bearing securities	9 808	9 807	(908)	(30)	(2 871)	15 806
Financial derivatives	0	425	0	48	121	594
Total financial assets in level 3	**73 605**	**14 427**	**(9 163)**	**61**	**(28 934)**	**49 996**
Loans from credit institutions	1 922	0	(1 922)	0	0	0
Senior securities issued	200 087	67 723	(36 304)	1 017	(66 994)	165 529
Financial derivatives	0	45	0	1	695	741
Subordinated debt	1 253	0	(605)	19	0	667
Hybrid Tier 1 capital instruments	329	0	(58)	14	0	285
Total financial liabilities in level 3	**203 592**	**67 768**	**(38 889)**	**1 051**	**(66 299)**	**167 222**

Fair value of financial instruments

Determination of fair value at level 1 requires use of quoted market prices. Inputs that can be classified as level 1 are described in detail in "Accounting policies".

Fair value of financial instruments in level 2 and 3 is determined mainly using discounted cash flow method, where future cashflows are discounted with relevant money market interest rates plus an adjustment for credit and liquidity risk. Financial instruments with embedded option elements are valued using option pricing models that use both inputs observable in the market and estimated inputs as parameters. All changes in fair value are recorded as part of carrying value of assets and liabilities, and recognised in the income statement.

<u>Deposits with credit institutions</u>

Deposits with credit institutions that are carried at fair value include cash time deposits with other credit institutions. Because of their short-term nature the fair value of these instruments is approximately equal to the notional amount.

<u>Instalment loans</u>

Level 2 includes Short-term debt certificates issued by municipalities and loans with floating Nibor-indexed interest rate. The customers have more flexibility in refinancing these types of loans with other lenders should market conditions change. As a result, these types of loans are subject to greater competition from lenders and have observable prices that can be used as Level 2 input when the fair value is determined.

Level 3 includes fixed rate loans to customers that are not traded in an active market and do not have observable market prices after initial recognition. A significant valuation input for fixed rate loans is credit value adjustment, that is estimated at each reporting date. Credit risk is considered to be the same for all municipalities. As observable market data for credit risk is not available, the management has to make assumptions and estimate relevant adjustments for credit risk based on current lending levels and any additional loan security.

<u>Notes and bonds</u>

The best estimate of fair value is price quotations in an active market with many willing buyers and sellers at a reporting date. Level 1 inputs for notes and bonds include quoted prices provided by international vendors (Reuters/Bloomberg). The price quotes used in valuation represent actual transactions in an active market. Securities issued by Norwegian issuers are recorded at prices calculated by the Norwegian Securities Dealers Association ("Norges Fondsmeglerforbund"), that are non-binding and are therefore considered as Level 3 input.

Fair value of notes and bonds that do not have available market quotes at the reporting date is calculated using the discounted cashflow method, where discount rates are derived from current interest rate yield curves. Discount rates are adjusted for credit risk and liquidity risk of the issuer, based on observable market data. When applying credit/liquidity value adjustments to discount rates, the assets are grouped based on the issuer's credit rating, currency, time to maturity, underlying exposure and geographic position. For more detailed description of inputs in fair value determination, see "Accounting principles".

<u>Senior securities issued</u>

The funding portfolio is split into four main groups, based on the funding product and loan documentation used. The four main categories are benchmark loans, loans in public niche markets, private placements and retail loans. The two first groups are characterised by public syndicated loans in various currencies, where the size of the loan forms the primary difference between the two groups. Fair value of these loans is based on quoted prices of existing issues, prices on new issues and price information obtained from different sources. When those prices represent actual market transactions sufficiently close to the reporting date, they will be classified as Level 1 input in fair value hierarchy.

If such prices are unavailable, the discount cashflow method is used to determine fair value of the loans. The inputs used in the valuation are based on observable market data (Level 2), i.e. current interest rate yield curves and prices on similar instruments adjusted for differences in currency, time to maturity and size. The Company also uses non-binding quotes provided by other market participants. When such quotes are not supported by actual market transactions and make a significant input in valuation, they are classified as Level 3.

Group three is private placements and is characterised by non-public loans where the loan terms are specially adapted for a single investor. The final main group is retail loans, i.e. loans sold to retail investors. These loans are normally not traded in the secondary market and don't have available price quotes. The portfolio is therefore classified as Level 3 in fair value hierarchy. The choice of valuation models and input depends on the structure of each loan. The fair value of the bonds without embedded options is determined using the discounted cashflow method with inputs based on current interest rate yield curves and credit spreads estimated from prices on new issues. The fair value of structured bonds with option elements is calculated using option pricing models that use both interest rates, FX-rates and historical volatilities as parameters.

Financial derivatives

All financial derivatives are OTC-contracts used only in economic hedges. Basis swaps (USD-NOK, USD-EUR and EUR-NOK) are recorded at market prices quoted in an active market. The fair value of plain vanilla interest rate– and cross currency swaps is determined using the discounted cashflow method with discount rates derived from observable swap interest rates. Equity and commodity linked derivatives with embedded options are valued using the same valuation models as corresponding loans and are classified as Level 3.

The table below shows impact of 1 basis point change in estimated credit spreads on fair value of financial instruments at Level 3.

	1 bp change in credit spread
Instalment loans	9
Notes, bonds and other interest-bearing securities	(1)
Financial derivatives	(58)
Senior securities issued	29
Subordinated debt and Hybrid Tier 1 capital instruments	0
Total	**(21)**

NOTE 6

Hedge accounting

(Amount in NOK 1 000 000)

Fair value hedge is applied to transactions used to manage exposures to interest rates and FX-rates in assets and liabilities.

Exposure to interest rate risk and FX-risk in notes and bonds classified as Loans and receivables is hedged with interest rate swaps and cross currency swaps. Hedge relationship is established at transaction level and hedge effectiveness is measured using Dollar-Offset method on a regular basis. Fair value hedge is also used for selected issued bonds. The risks hedged in liabilities include interest rate risk and FX-risk, and are hedged with interest rate swaps and cross currency swaps.

	2009	2008
Net gain/(loss) on financial derivatives in fair value hedges	(273)	43
Net gain/(loss) on notes and bonds in fair value hedges	346	(15)
Net gain/(loss) on issued bonds in fair value hedges	(104)	0
Net gain/(loss) on fair value hedges recognised in income statement	**(31)**	**28**

NOTE 7

Net interest income

(Amounts in NOK 1 000 000)

	2009					
	At fair value through profit and loss			Held to maturity	Loans and receivables	Other liabilities
	FVO	Held for trading	Fair value hedge			
Interest income from deposits with credit institutions	32	0.1	0	0	0.3	0
Interest income from instalment loans	2 543	173	0	0	1 681	0
Interest income from notes, bonds and other interest-bearing securities	668	767	0	25	1 153	0
Interest income from financial derivatives	0	(999)	(1 198)	0	0	0
Other interest income	0	0	0	0	1	0
Total interest income	**3 243**	**(60)**	**(1 198)**	**25**	**2 836**	**0**
Interest expenses on loans from credit institutions	24	0	0	0	0	0
Interest expenses on senior securities issued	7 449	0	0	0	0	160
Interest expenses on subordinated debt	37	0	0	0	0	0
Interest expenses on financial derivatives	0	(3 668)	(199)	0	0	0
Other interest expenses	0	0	0	0	0	(9)
Total interest expenses	**7 510**	**(3 668)**	**(199)**	**0**	**0**	**151**

	2008					
	At fair value through profit and loss			Held to maturity	Loans and receivables	Other liabilities
	FVO	Held for trading	Fair value hedge			
Interest income from deposits with credit institutions	103	0	0	0	2	0
Interest income from instalment loans	2 660	349	0	0	3 393	0
Interest income from notes, bonds and other interest-bearing securities	755	1 114	0	242	244	0
Interest income from financial derivatives	0	376	(241)	0	0	0
Other interest income	0	0	0	0	2	0
Total interest income	**3 518**	**1 839**	**(241)**	**242**	**3 640**	**0**
Interest expenses on loans from credit institutions	90	0	0	0	0	0
Interest expenses on senior securities issued	6 095	0	0	0	0	0
Interest expenses on subordinated debt	70	0	0	0	0	0
Interest expenses on financial derivatives	0	2 254	0	0	0	0
Other interest expenses	0	0	0	0	0	(36)
Total interest expenses	**6 255**	**2 254**	**0**	**0**	**0**	**(36)**

NOTE 8

Commission expenses and expenses of banking services

(Amounts in NOK 1 000 000)

	2009	2008
Guarantee fee to the State of Norway	1	3
Expenses of banking services	11	8
Other transaction costs	8	6
Total commission expenses and expenses of banking services	**20**	**17**

NOTE 9

Salaries and other remuneration

(Amounts in NOK 1 000)

Salaries	2009	2008
Salaries	38 786	35 642
Employer's contributions	5 102	4 782
Pension costs	7 854	6 796
Other benefits	1 197	955
Total salaries	**52 939**	**48 175**

Average labour years	43,5	40,1

	2009			2008		
Compensation for senior employees	Salaries	Remuneration/ Bonus	Pension costs	Salaries	Remuneration/ Bonus	Pension costs
President & CEO	1 792	567	473	1 629	305	459
Deputy CEO	1 247	286	311	921	196	270

The President & CEO has termination benefit agreement of one year salary following termination of employment. Other senior management have a period of notice of three months and no termination benefit following termination. The mandatory retirement age for President & CEO is 65. The pension scheme for the President & CEO is the same as for the other employees with a benefit level of 66 per cent without a limitation to 12 x Base amount. Pension costs include pension costs in the collective pension scheme and provision for pension commitment covering salary over 12 base amounts.
The Company has an incentive programme for the employees. The incentive programme is re-evaluated and approved by the Board annually. The programme includes all employees, regardless of position and area of responsibility. The incentive programme is aiming at stimulating better performance and long-term profit-making, and supports the company's ability to attract and develop motivated and competent employees.
The remuneration approach is based on a set of quantitative criteria and reflects goal achievement in the areas critical for the Company's long-term value creation and sustainability. The incentive programme consists of the following elements:

- **Variable salary** gives compensation for performance and value creation beyond a normal level.
- **Bonus to key personnel** is offered to selected key employees when the risk and cost of replacement is especially high. 50 % of the bonus is deferred in 1 year.

The employees may receive both variable salary and bonus, but the total remuneration under the incentive programme (including vacation pay and employer's contribution), cannot exceed 25 % of total annual salary costs or 3 month salary to each employee.
The provision made for the remuneration payments in 2009 amounts to NOK 7 056 444 and is recognised under "Salaries" in the income statement. Bonus to the President & CEO for 2008 amounted to NOK 400 000, and NOK 180 744 to the Deputy CEO. Approved bonus for 2009 includes NOK 547 480 in bonus to the President & CEO, and NOK 376 319 to the Deputy CEO.
Based on the extraordinary results achieved by the Company in 2009, the Board approved a separate bonus to a few employees, who had a particular influence on the goal achievement in 2009. The bonus is to be paid over a 2-years period. Total variable remuneration to the employees (including vacation pay and employer's contribution) is limited to 50 % of the fixed salary.
In addition to the incentive programme the Company in 2008 has offered a one-time compensation to four employees who were identified as essential to the future development of the Company. The agreement matures in 2011 and requires continuous employment through the whole period.

Remuneration to the Board of Directors, Control Committee and Supervisory Board

Board of Directors	2009	2008
Chairman Else Bugge Fougner	190	172
Vice chairman Per N. Hagen	48	95
Vice chairman Kristin Marie Sørheim	50	0
Board member Frode Berge	45	0
Board member Svein Blix	90	86
Board member Nanna Egidius	90	86
Board member Åmund T. Lunde	45	0
Board member Iver Lund	0	35
Board member Martha Takvam	90	86
Board member Sverre Thornes	43	43
Board member, employee representative Martin Spillum	90	86
Total Board of Directors	**780**	**689**

Control Committee	2009	2008
Chaiman Brit Lund	47	46
Committee member Kristine Stray Ryssdal	30	29
Committee member Kjell Inge Skaldebø	30	29
Alternate member Kristina Nilssen	0	0
Alternate member Roy Jevard	12	9
Total Control Committee	**118**	**113**

The remuneration to alternate member is NOK 3 000 per appearance.

Supervisory Board	2009	2008
Chairman Oddvar Flæte	9	17
Chairman Elin Eidsvik	11	5
Members	57	46
Total Supervisory Board	**77**	**68**

Loans to employees	31 December 2009	31 December 2008
Short-term loans to senior employees	25	62
Short-term loans to other employees	570	793
Home mortgages to senior employees	3 120	3 336
Home mortgages to other employees	32 571	29 970
Total loans to employees	**36 286**	**34 161**
Interest subsidies in the period	434	374

The President & CEO's mortgage had a balance of NOK 2.383 million with an interest rate of 2.36 per cent as at 31 December 2009. The mortgage repayment period is 20 years. The loan must be repaid within 6 months of leaving the Company.

Fees to the statutory auditor	2009	2008
Statutory auditing services	630	590
Other financial audit and attestation services	945	787
Tax support	0	25
Other services not related to audit	146	165
Total fees excl. VAT	**1 721**	**1 567**

NOTE 10

Tax

(Amounts in NOK 1 000)

Tax expense	2009	2008
Tax payable	485 879	153 539
Changes in deferred tax	61 258	(456)
Total tax expense	**547 137**	**153 083**
Current tax payable	485 879	153 539
Withholding tax	0	0
Total tax payable	**485 879**	**153 539**

Reconciliation of effective income tax rate	2009	2008
Profit before tax	1 946 307	543 033
Calculated income tax (28 %)	544 966	152 049
Non-deductible expenses	7 755	3 691
Non-taxable revenue	0	0
Tax expense	**547 137**	**153 083**
Effective income tax rate	28,1%	28,2%

Deferred tax liability/(asset)	2009	2008
Deferred tax liability/(asset) at 1 January	(1 056)	(600)
Change in deferred tax	61 257	(456)
Deferred tax liability/(asset) at 31 December	**60 201**	**(1 056)**

Temporary differences	31 December 2009	31 December 2008
Fixed assets	(670)	(1 591)
Hedging instruments	0	0
Pensions	(24 144)	(19 915)
Provisions	(850)	(800)
Fair value changes	240 668	18 534
Total	**215 004**	**(3 772)**
Deferred tax liability/(asset) 28%	**60 201**	**(1 056)**

NOTE 11

Pensions

(Amounts in NOK 1 000)

The Company has a defined benefit plan for all employees administrated through Kommunal Landspensjonskasse (KLP). The pension benefits include retirement pension, disability pension, spouse and child pension, and are coordinated with the National Insurance Scheme. The defined benefit plan complies with the requirements of the Norwegian Mandatory Service Pension Act.
Full pension benefit requires a service period of 30 years and gives the right to a retirement pension of 66 per cent of salary, including the National Insurance Scheme. KBN also has a scheme linked to the contractually agreed early retirement pension scheme (AFP). The scheme is included in the calculation of pension liabilities. Pension commitment for salaries over 12 x Base amount is expensed when incurred.
Pension costs and commitments recognised in the Statement of Financial Position include employer's contributions.
The defined benefit plan is administrated through a public sector occupational pension scheme and asset composition cannot be specified.

Economic estimates used in calculation of pension costs and commitments:

	2009	2008
Discount rate	4,50%	4,50%
Estimated wage growth	4,50%	4,50%
Expected growth in Base amount	4,25%	4,25%
Expected return on assets	5,70%	5,50%

Collective scheme		Pension commitment	Salaries over 12xBase amount	
2009	2008		2009	2008
46 803	38 001	Defined benefit obligation	6 347	2 961
25 856	20 653	Plan assets	0	0
(1 578)	(393)	Unrecognised actuarial gains/(losses)	(1 572)	0
19 368	**16 955**	**Net pension commitment**	**4 775**	**2 961**

Collective scheme		Pension costs	Salaries over 12xBase amount	
2009	2008		2009	2008
5 553	4 733	Fair value of pension earnings for the year	1 065	860
1 775	1 636	Interest costs on pension commitment	277	108
(1 195)	(975)	Expected return on plan assets	0	0
273	149	Service costs	0	0
129	0	Actuarial gains/losses recognised in income	472	95
6 536	**5 543**	**Net pension costs**	**1 814**	**1 063**

Changes in pension commitment

	Collective scheme	Salaries over 12XBase amount
Pension commitment at 1 January	16 955	2 961
Net pension costs	6 536	1 814
Pensions paid	(4 122)	0
Pension commitment at 31 December	19 368	4 775

NOTE 12

Deposits with credit institutions

(Amounts in NOK 1 000 000)

	31 December 2009	31 December 2008
Deposits with credit institutions without agreed lifetime	63	40
Deposits with credit institutions with agreed lifetime	925	3 861
Total Deposits with credit institutions	**988**	**3 901**

NOTE 13

Instalment loans

(Amounts in NOK 1 000 000)

	31 December 2009	31 December 2008
Principal amount	151 275	118 060
Accrued interest	817	1 377
Adjustment for fair value*	908	1 460
Loans to customers	**153 000**	**120 897**
Other loans	40	38
Total instalment loans	**153 040**	**120 935**

*Changes in fair value attributable to changes in credit risk of the lending portfolio are close to zero.

Geographic distribution	31 December 2009	31 December 2008
Østfold	8 623	7 265
Akershus	17 622	13 660
Oslo	1 364	1 004
Hedmark	6 198	5 003
Oppland	5 233	4 144
Buskerud	8 924	7 179
Vestfold	6 134	4 854
Telemark	6 170	5 616
Aust-Agder	4 277	3 617
Vest-Agder	7 796	5 855
Rogaland	10 824	8 245
Hordaland	14 707	9 199
Sogn og Fjordane	5 120	3 970
Møre og Romsdal	10 718	6 799
Sør-Trøndelag	9 889	8 539
Nord-Trøndelag	5 783	5 295
Nordland	9 774	7 796
Troms	8 038	6 581
Finnmark	4 037	3 418
Svalbard	45	21
Total loans to customers	**151 275**	**118 060**

Past due interest and instalment payments amount to NOK 21.7 million at 31 December 2009, and NOK 65.5 million—at 31 December 2008.

NOTE 14

Senior securities issued

(Amounts in NOK 1 000 000)

	2009	2008
Senior securities issued (nominal amounts) at 1 January	202 197	136 272
New issuance	116 263	62 733
Redemptions	(64 967)	(38 302)
Amortisation	(26)	109
Translation differences	(29 048)	41 385
Senior securities issued (nominal amounts) at 31 December	224 418	202 197
Accrued interest	2 662	2 932
Adjustment for fair value	(3 514)	(5 042)
Total senior securities issued	**223 566**	**200 087**
Adjustment for fair value as a result of change in credit risk	*350*	*247*

Change in fair value attributed to changes in credit risk is calculated as a difference between market value and net present value of the portfolio based on risk-free interest rates.

There is no breach of debt covenants as at 31 December 2009.

NOTE 15

Other assets

(Amounts in NOK 1 000)

Other assets	2009	2008
Intangible assets	512	512
Fixed assets	11 600	8 449
Other assets	774	1 229
Prepaid, non-accrued expenses and accrued income	768	1 454
Total other assets	**13 654**	**11 644**

NOTE 16

Financial derivatives

(Amounts in NOK 1 000 000)

The Company uses financial derivatives to hedge against interest and currency risks that arise as a result of the Company's activities. The Company enters into swap contracts with counterparties which have high credit ratings and all derivative exposure is subject to risk limits set by the Board. The Company's funding in foreign currency is hedged by interest rate and currency derivatives, so that it only has exposure to changes in 3-month money market interest rates in NOK, USD and EUR.
Funding in foreign currency is converted to NOK using basis swaps (mostly USD-NOK), where the Company receives interest payments in currency and pays interest in NOK.
Interest rate risk arising from fixed rate lending is hedged by interest rate swaps and FRAs. Interest rate and currency swaps are also used to hedge against market risk in the liquidity portfolio.
The Company has no credit derivatives in its portfolio.

Interest rate derivatives:

- Interest rate swaps, with exchange of interest terms for an agreed amount over an agreed period.
- Forward rate agreements (FRA), that fix the interest rate for a nominal amount for a future period.

Currency derivatives:

- Cross currency swaps, with exchange of currency amounts at an agreed rate over an agreed period.
- FX-forwards, which are purchase and sales of a currency amount at a fixed rate at a future point of time.

Equity-related derivatives:

- Derivatives that have equity instruments as underlying instruments, or that are related to the price of specific equity instruments or equity indexes.

Commodity-related derivatives:

- Derivatives with commodity indexes as underlying instruments.

Counterparty risk arising from derivative portfolio is measured continuously. Counterparty risk is mitigated by using standard ISDA-agreements that give the right to offset all liabilities in the case of default. In addition the Company enters into collateral agreements with most swap counterparties. The agreements require collateral in form of cash to be posted for all net exposures over a predefined threshold.

	31 December 2009			31 December 2008		
	Nominal value*	Assets	Liabilities	Nominal value*	Assets	Liabilities
Held for trading:						
Interest rate derivatives	123 092	1 014	111	119 856	1 347	495
Currency derivatives	286 626	5 218	624	262 883	16 754	9 649
Equity-related derivatives	49 872	1 946	(542)	30 896	223	50
Commodity-related derivatives	2 710	17	7	946	0	45
	462 299	**8 195**	**200**	**414 581**	**18 324**	**10 240**
Fair value hedges:						
Interest rate derivatives	3 696	50	(3)	0	0	0
Currency derivatives	1 838	(4)	2 009	0	45	0
	5 534	**46**	**2 006**	**0**	**45**	**0**
Total financial derivatives	**467 833**	**8 241**	**2 206**	**414 581**	**18 369**	**10 240**

* Nominal value reported in the capital adequacy statement

Pursuant to the requirements in the Company's financial policy, all derivative contracts can be used in economic hedges only. Most of the derivatives are classified as Held for trading (IAS 39), with the exception of derivatives designated as hedging instruments in fair value hedges. All financial derivatives are recorded at fair value through profit and loss.

NOTE 17
Collateral
(Amounts in NOK 1 000 000)

	31 December 2009	31 December 2008
Cash collateral received	2 836	11 360
Cash collateral posted	(1 733)	(1 277)
Total cash collateral	**1 104**	**10 083**

Collateral agreements cover most of the swap counterparties and shall provide additional security against loss in case of default. All collateral agreements follow standard CSA-terms and allow only use of cash collateral (USD and EUR). Collateral assets are provided by full transfer of ownership (title transfer) from collateral provider to collateral taker.

NOTE 18
Subordinated debt
(Amounts in NOK 1 000 000)

Subordinated debt (nominal amounts)	Redemption right	Interest	31 December 2009	31 December 2008
Perpetual subordinated loan capital (NOK 7.5 mill)		3,20%	8	8
Perpetual subordinated loan capital (EUR 45 mill)		6,95%	373	439
Perpetual subordinated loan capital (JPY 3 bn)		1,61%	186	232
Ordinary subordinated loan capital (EUR 20 mill) *	2012	6,29%	166	195
Ordinary subordinated loan capital (NOK 102 mill) (Interest rate is adjusted every 3 months)*	2019	3,02%	102	102
Ordinary subordinated loan capital (NOK 80 mill) (Interest rate is adjusted every 3 months)	2017	2,17%	80	80
Ordinary subordinated loan capital (USD 65 mill) (Interest rate is adjusted every 3 months)	2014		0	456
Total subordinated debt			**915**	**1 511**

*Hybrid Tier 1 Capital instruments are capital instruments approved as an element in the core capital within a limit of 15 per cent of total Tier 1 capital.

NOTE 19
Risk management
KBN has AAA/Aaa rating from S&P and Moody's, which requires the Company to adhere to a low risk profile. The company's risk limits are set so that the Company has a 0.01 percent (or lower) probability of bankruptcy. This is implicitly presumed by the company's AAA-rating. The company's risk is managed according to its overall goal of achieving stable and predictable results and a return required by its shareholders. KBN follows a conservative investment policy. All interest, currency risk and structured risk in assets and liabilities is hedged on an ongoing basis using derivative contracts. The Company's financial policy permits derivatives only to be used for hedging purposes. Risk associated with company's assets is low. Its client base is the local government sector, which has high creditworthiness with a good geographic diversification. Liquidity portfolio consists of bonds issued by sovereigns (0 % risk weighting) and highly rated financial institutions (20 % risk weighting). Lending to the local and regional authorities, inter-municipal companies and other companies with a municipal guarantee carries a very low level of risk. The Local Government Act states that a municipality cannot go bankrupt. Should a municipality face payment difficulties, the central government would assume control of the municipality until it is able to meet its payment obligations. On no occasion has the government had to apply Sections 56-58 of the Local Government Act to take over management of a municipality. The lender is protected against loss of principal and interest. Management of the company's liquidity portfolio is subject to conservative guidelines. In a normal situation, the liquidity portfolio should make up a maximum of 30% of the company's assets. For shorter periods, the liquidity portfolio can constitute up to 35 % of the total capital, although the part of the portfolio that exceeds 25 % of the total capital result must be invested in sovereigns or sovereign-guaranteed securities. The guidelines for the liquidity portfolio combine the requirement for high credit quality and a short maturity profile, which contributes to lowering the default risk in the portfolio.

NOTE 20
Interest rate risk
(Amounts in NOK 1 000 000)

Interest rate risk occurs as a result of the differences in the interest rate periods for assets and liabilities, and the fact that incoming and outgoing payments are due at different times. As part of interest risk management, the Company actively buys and sells securities issued by financial institutions and sovereigns and enters into derivative contracts.
The Company has maintained its strategy of adapting funding activities to the various types of loans it offers, which has resulted in its funding and lending activities having approximately identical interest periods. Interest risk is managed by matching duration of the funding portfolios with that of the loan portfolios. Maturity differences are monitored on a continuous basis.
The Company's assets and liabilities are denominated in several currencies, but all interest risk is hedged perfectly at a transaction level for all currencies except NOK, USD and EUR. The interest risk in these three currencies is hedged using interest rate swaps, so that the company only has exposure to changes in 3 month money market interest rates.
Interest rate sensitivity is measured as a change in fair value of assets and liabilities at 1 per cent change in interest rate level (parallel shift).
Interest rate sensitivity in NOK depends on the opportunity to adjust floating interest rates on the lending portfolio. The Board has adopted a total limit for interest rate risk of NOK 12 million. The interest rate sensitivity is measured in the interval of 40, 45 and 50 days to an adjustment of the floating rate on the lending portfolio, and the lowest value is reported. The interest rate sensitivity in the main currencies is shown in the table below:

	1% interest rate change
NOK	9,5
USD	(4,9)
EUR	2,5
Total	**7,1**

Interest rate sensitivity can affect the income statement during the next three month period.
The calculation is based on the total assets and liabilities at 31 December 2009, and a 45-day period to the adjustment of the floating rate on the lending portfolio.

NOTE 21

Currency risk

(Amounts in NOK 1 000)

Currency risk is defined as the risk of loss in market value as a result of fluctuations in FX-rates. The currency risk occurs as a result of the Company's funding mainly being in foreign currency, while lending is provided in NOK. The Company's risk policy requires hedging of all currency risk in the assets and liabilities. However, short-term net positions in the P/L items may occur in EUR and USD. The currency risk is hedged both at transaction level and portfolio level. The limit for currency risk is set to NOK 6 million for a 10 per cent absolute change in all currencies.

	31 December 2009		31 December 2008	
Currency	Net position	10%-change in FX -rate	Net position	10%-change in FX -rate
USD	(35 431)	3 543	28 228	2 823
EUR	2 698	270	28 331	2 833
AUD	(1 859)	186	186	19
CAD	37	4	72	7
CHF	882	88	1 413	141
CZK	0	0	0	0
DKK	91	9	106	11
GBP	693	69	832	83
HKD	10	1	13	1
HUF	30	3	36	4
ISK	0	0	13	1
JPY	1 828	183	(325)	33
MXN	15	1	15	1
NZD	81	8	(283)	28
PLN	0	0	30	3
SEK	696	70	221	22
THB	0	0	0	0
TRY	150	15	368	37
ZAR	(22)	2	(119)	12
Total	**(30 101)**	**4 452**	**59 137**	**6 058**

The table above shows an absolute effect on the income statement of a 10 per cent change in FX—rates relative to NOK. The amount is calculated based on assets and liabilities denominated in foreign currencies at 31 December 2009. Sensitivity analysis does not take into account correlation between FX-rates and other market risk factors.

NOTE 22

Credit risk

(Amounts in NOK 1 000 000)

The Company has exposure to the municipal sector, as well as financial institutions and sovereigns within the OECD. Loans given to municipalities may have maturities of up to 50 years, and the credit limits are regulated by Large Exposure regulation. Credit exposures on financials must have a rating of A/A-1 or above.
General limits for credit risk are set by the Board and evaluated at least annually.
KBN grants loans to public sector entities that carry out work for local and regional authorities. The conditions for such loans are that local or regional authorities provide guarantees that have been approved by the government, represented by the County Governor or the Ministry of Local Government and Regional Development. In addition, the loans are secured by collateral in the entities' assets. Loans secured by collateral amount to NOK 1.57 billion.

Amounts in the table below represent maximum credit exposure

	Exposure at 31 December 2009								
Maturity	< 1 year				> 1 year				
Risk class	A-3	A-2	A-1/A-1+	Not rated	A	AA	AAA	Not rated	Total
Sovereigns and central banks	0	0	10 692	0	0	1 512	2 249	0	**14 453**
Regional authorities*	0	0	9 329	15 867	607	10 002	5 247	122 623	**163 675**
Public sector entities	0	0	0	2	0	0	0	16 547	**16 549**
Multilateral development banks	0	0	7 834	0	0	0	8 803	0	**16 637**
Financial institutions	0	179	7 104	0	2 160	952	494	0	**10 889**
Securitisation	0	0	180	0	0	0	306	0	**486**
Total	**0**	**179**	**35 139**	**15 869**	**2 767**	**12 466**	**17 099**	**139 170**	**222 689**

*Include loans to municipal sector of NOK 153 billion.

Credit risk by country

	Exposure at 31 December 2009								
Maturity	< 1 year				> 1 year				
Risk class	A-3	A-2	A-1/A-1+	Not rated	A	AA	AAA	Not rated	Total
Australia	0	0	483	0	0	202	9	0	**694**
Belgium	0	0	115	0	249	0	0	0	**364**
Canada	0	0	859	0	761	269	0	0	**1 889**
Denmark	0	0	3 630	0	80	0	2 885	0	**6 594**
Finland	0	0	219	0	0	0	1 314	0	**1 533**
France	0	0	-33	0	459	220	618	0	**1 265**
Ireland	0	0	2 855	0	66	0	0	0	**2 922**
Italy	0	0	0	0	0	0	0	0	**0**
Japan	0	0	432	0	0	515	0	0	**947**
Luxembourg	0	0	0	0	0	0	0	0	**0**
The Netherlands	0	0	1 866	0	83	0	220	0	**2 169**
New Zealand	0	0	17	0	0	0	0	0	**17**
Norway	0	0	1 030	15 869	133	0	0	139 170	**156 202**
Portugal	0	0	0	0	0	0	0	0	**0**
Spain	0	179	370	0	369	1 163	26	0	**2 107**
Supranational	0	0	7 780	0	0	0	8 090	0	**15 869**
Switzerland	0	0	175	0	82	0	0	0	**257**
Sweden	0	0	993	0	0	0	747	0	**1 740**
Germany	0	0	9 983	0	0	9 961	2 646	0	**22 591**
UK	0	0	2 388	0	485	12	544	0	**3 428**
USA	0	0	704	0	0	124	0	0	**828**
Austria	0	0	1 273	0	0	0	0	0	**1 273**
Total	**0**	**179**	**35 139**	**15 869**	**2 767**	**12 466**	**17 099**	**139 170**	**222 689**

NOTE 23
Liquidity risk
(Amounts in NOK 1 000 000)

Liquidity risk is defined as a risk for the Company not being able to meet its commitments and/or finance lending demand without significant extra costs being incurred in the form of value loss in assets that have to be sold, or in the form of more expensive funding.
Liquidity risk is monitored and managed through internal control and financial policy. KBN's financial policy requires to maintain net cash balances equivalent to a minimum 12 months' net debt redemptions. This means that in any given situation the Company can cover all its debt obligations for the next 12 months without new borrowing.
The liquidity portfolio is managed using a conservative investment policy to keep both credit risk and market risk low. Surplus liquidity is invested in notes and bonds issued by sovereigns, sub-sovereigns, regional authorities, multilateral development banks and financials with a high credit rating. Most of the portfolio matures within 12 months. Liquidity risk is further reduced by matching maturities on assets and liabilities. The Company also has a short-term funding programme and a credit line with DnB NOR to manage short-term liquidity.

Principal amounts split by tenor	Total principal	< 1 month	1-3 months	3-12 months	1-5 years	>5 years	Without maturity
Deposits with credit institutions	**988**	988	0	0	0	0	0
Instalment loans	**153 041**	2 825	6 631	6 374	10 661	126 547	3
Notes, bonds and other interest-bearing securities	**67 997**	8 743	6 217	19 820	27 663	5 554	0
Other assets	**14**	0	0	1	0	0	13
Total assets	**222 040**	**12 556**	**12 848**	**26 195**	**38 324**	**132 101**	**16**
Loans from credit institutions	**1 051**	1 051	0	0	0	0	0
Senior securities issued	**224 942**	8 101	3 913	34 613	106 495	71 821	0
Other liabilities	**524**	3	8	489	0	0	24
Subordinated debt	**646**	0	0	372	194	80	0
Hybrid Tier 1 capital instruments	**266**	0	0	0	165	101	0
Equity	**3 561**	0	0	267	0	0	3 294
Total liabilities	**230 990**	**9 155**	**3 921**	**35 740**	**106 854**	**72 002**	**3 317**
Financial derivatives	**10 213**	**586**	**469**	**(354)**	**2 722**	**6 790**	**0**
Net liquidity exposure		**3 987**	**9 396**	**(9 900)**	**(65 807)**	**66 889**	**(3 301)**

Principal amounts split by interest rate reset	Total principal	< 1 month	1-3 months	3-12 months	1-5 years	>5 years	Without maturity
Deposits with credit institutions	**988**	988	0	0	0	0	0
Instalment loans	**153 041**	51 126	43 191	31 483	21 902	5 335	3
Notes, bonds and other interest-bearing securities	**67 997**	11 638	18 598	16 845	15 850	5 066	0
Other assets	**14**	0	0	1	0	0	13
Total assets	**222 040**	**63 752**	**61 789**	**48 330**	**37 753**	**10 400**	**16**
Loans from credit institutions	1 051	1 051	0	0	0	0	0
Senior securities issued	224 942	34 663	50 242	54 962	74 274	10 801	0
Other liabilities	524	3	8	489	0	0	24
Subordinated debt	646	80	8	373	186	0	0
Hybrid Tier 1 capital instruments	266	101	0	0	165	0	0
Equity	3 561	3 561	0	0	0	0	0
Total liabilities	**230 990**	**39 458**	**50 257**	**55 823**	**74 625**	**10 801**	**24**
Financial derivatives	**10 231**	**3 497**	**(38 624)**	**8 158**	**37 496**	**(313)**	**0**
Net interest rate exposure		**27 790**	**(27 093)**	**664**	**623**	**(714)**	**(8)**

NOTE 24

Capital adequacy and capital management

(Amounts in NOK 1 000 000)

The Company's capital consists of share capital, retained earnings, Hybrid Tier 1 capital and subordinated capital. A healthy capital level is regarded as essential to maintain the company's AAA rating and ensure efficient market competition. The Board assesses the capital situation on an ongoing basis and approves KBN's principles for capital management.
The Company is subject to Capital Adequacy Requirements and shall have a sufficient capital level for its risk profile and current market situation. Capital level is measured as core capital ratio and total capital ratio relative to the risk-weighted assets. KBN's capital situation is assessed in relation to risk in day-to-day market conditions and through stress tests.
In order to maintain a sufficient capital level the Company can, depending on the market situation, reduce or increase its total assets or enter into a dialog with the shareholder to change the Company's capital structure through dividend policy or share capital.

	31 December 2009			31 December 2008		
	Book value	Risk-weighted assets	Minimum capital requirement	Book value	Risk-weighted assets	Minimum capital requirement
Credit risk						
Sovereigns and central banks	7 582	0	0	4 646	0	0
Regional governments and local authorities	167 916	28 322	2 266	136 800	23 322	1 866
Of which are Norwegian municipalities	*145 150*	*28 312*	*2 265*	*116 702*	*23 322*	*1 866*
Public sector entities	3 371	0	0	2 671	0	0
Multilateral development banks	16 651	0	0	9 743	0	0
Financial institutions	19 525	3 401	272	14 192	2 838	227
Of which counterparty exposure on derivatives	*19 328*	*3 362*	*267*	*7 585*	*1 517*	*121*
Corporates	496	99	8	749	150	12
Claims secured by residential property	1 584	575	46	1 720	629	50
Covered bonds	400	40	3	34	3	0
Other assets	12	12	1	9	9	0
Total credit risk	**217 536**	**32 449**	**2 596**	**170 566**	**26 953**	**2 156**
Market risk*	**27 471**	**2 388**	**191**	**37 355**	**2 555**	**204**
Operational risk—Basic Indicator Approach		**1 132**	**91**		**694**	**55**
Minimum Capital requirement		**35 970**	**2 878**		**30 202**	**2 416**
Total capital ratio			**11,05%**			**11,60%**
Core capital ratio			**9,25%**			**7,45%**

**KBN has no settlement, currency and commodity risk.*

Supplementary capital cannot exceed 100 per cent of Tier 1 capital. KBN's capital satisfies the capital adequacy requirements. KBN's capital comprises the following elements:

	31 December 2009	31 December 2008
Core capital:		
Share capital	1 221	1 221
Retained earnings	2 340	984
Total equity	**3 561**	**2 205**
Hybrid Tier 1 capital instruments	285	329
Deferred tax asset	0	-1
Goodwill	-1	-1
Allocated to dividend	-267	-44
Unrealised gains on issued debt attributable to changes in credit risk	-252	-247
Actuarial gains/losses recognised at the date of transition to IFRS	0	9
Total Tier 1 capital	**3 326**	**2 251**
Supplementary capital:		
Subordinated debt	80	552
Perpetual subordinated debt	567	701
Total supplementary capital	**647**	**1 253**
Total capital	**3 973**	**3 504**

Subordinated capital has been calculated pursuant to The Regulation governing calculation of subordinated capital for financial institutions.

NOTE 25

Share capital

	31 December 2009		31 December 2008	
	Number of shares	Share in %	Number of shares	Share in %
The Kingdom of Norway	1 220 625	100 %	976 500	80 %
KLP	0	0%	244 125	20 %
Total	**1 220 625**		**1 220 625**	

KBN's share capital amounts to NOK 1 220 625 000 as of 31 December 2009. Share capital is divided into 1 220 625 shares of NOK 1 000. A dividend of NOK 267 200 000 (NOK 219 per share) has been proposed for 2009. Dividend paid for the fiscal year 2008 amounted to NOK 43 750 000 (NOK 35,8 per share).

The profit per share is calculated as follows (amounts in NOK)):

	2009	2008
Profit for the year	1 399 169 358	389 953 000
Number of shares	1 220 625	1 220 625
Earnings per share	**1 146**	**319**

Auditor's report

To the Annual Shareholders' Meeting of Kommunalbanken AS

We have audited the annual financial statements of Kommunalbanken AS as of 31 December 2009, showing a profit of NOK 1,399,000,000. We have also audited the information in the Directors' report concerning the financial statements, the going concern assumption, and the proposal for the allocation of the profit. The financial statements comprise the statements of income, comprehensive income, financial position, cash flows and changes in equity as well as the accompanying notes. IFRSs as adopted by the EU have been applied in the preparation of the financial statements. These financial statements and the Directors' report are the responsibility of the Company's Board of Directors and President & Chief Executive Officer. Our responsibility is to express an opinion on these financial statements and on other information according to the requirements of the Norwegian Act on Auditing and Auditors.

We conducted our audit in accordance with laws, regulations and auditing standards and practices generally accepted in Norway, including the auditing standards adopted by the Norwegian Institute of Public Accountants. Those standards and practices require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. To the extent required by law and auditing standards, an audit also comprises a review of the management of the Company's financial affairs and its accounting and internal control systems. We believe that our audit provides a reasonable basis for our opinion.

In our opinion,

- the financial statements have been prepared in accordance with laws and regulations and present fairly, in all material respects the financial position of the Company as of 31 December 2009, and the results of its operations, cash flows and changes in equity for the year then ended, in accordance with IFRSs as adopted by the EU
- the Company's management has fulfilled its duty to properly record and document the Company's accounting information as required by law and generally accepted bookkeeping practice in Norway
- the information in the Directors' report concerning the financial statements, the going concern assumption, and the proposal for the allocation of the profit is consistent with the financial statements and comply with law and regulations.

Oslo, 12 March 2010
Ernst & Young AS

Eirik Tandrevold
State Authorised Public Accountant (Norway)
(sign.)

Note: The translation to English has been prepared for information purposes only.

Control Committee's statement

The Control Committee has examined Kommunalbanken AS' annual report and accounts as well as the Auditor's report for 2009.

The Control Committee recommends that the annual report and accounts presented be approved as Kommunalbanken's accounts for 2009 and that the application of profits is adopted by the Annual Shareholders' Meeting in accordancw with the Board's proposals.

Oslo, 18 March 2010
Control Committee for Kommunalbanken AS

Britt Lund
Chairman

Kjell Inge Skaldebø

Kristine E. Stray Ryssdal

Roy Jevard

Supervisory Committee's statement

In accordance with § 15 in Kommunalbanken's Articles of Association, the annual accounts and report for 2009 have been examined by the Supervisory Committee.

The Supervisory Committee recommends that the Board of Directors' proposals for the operating statement and balance sheet as well as the application of profit, NOK 1 399 000 000, is adopted by the Annual Shareholders' Meeting.

Oslo, 22 April 2010
Audit Committee for Kommunalbanken AS

Elin Eidsvik
Chairman

Articles of Association of Kommunalbanken AS

Chapter I - Company, objectives, registered office
§ 1 The Company's name is Kommunalbanken AS.

§ 2 The Company is a direct continuation of the enterprise carried out by the government administrative body, Norges Kommunalbank.

§ 3 The Company's objectives are to provide loans to local governments, counties, intermunicipal companies and other companies that carry out local government tasks against either a municipal guarantee, government guarantee, or other satisfactory security. The Company can also undertake other tasks appropriate to the Company's business.

§ 4 The Company's registered office is to be situated in Oslo.

Chapter II - Equity and subordinated loan capital – shares
§ 5 The Company's share capital is NOK 1,220,625,000 (one billion, two hundred and twenty million, six hundred and twenty five thousand Norwegian kroner) divided into 1,220,625 shares of NOK 1,000 (one thousand Norwegian kroner) each.

§ 6 The acquisition of shares is conditional on the consent of the Company's Board of Directors. Consent can only be withheld on grounds of fact.

§ 7 Pre-emption rights given to shareholders under section 4-19 of the Norwegian Companies Act can also be claimed for shares which have changed owner.

Chapter III - Board of Directors
§ 8 The Company's Board of Directors shall number not more than eight (8) but need not exceed five (5). One (1) of the elected members of the Board shall be elected by and from amongst the Company's employees. For this member one (1) personal deputy shall be elected with the right to be present and to speak at board meetings.

The other members shall be elected by the Annual General Meeting for two-year terms, so that at least two (2) shall be elected annually, but no more than three (3) of the elected members. At least half the elected members shall retire at the end of the first year after the drawing of lots, and the remaining members shall retire at the end of the second year.

The Annual General Meeting shall elect the chairman and vice-chairman of the Board of Directors.

§ 9 The chairman of the Board shall ensure that the Board holds meetings as often as the Company's business necessitates, or when a member calls for a meeting to be held.

The Board constitutes a quorum if more than half the members are present. Valid resolutions are those for which the majority of the members present have voted, although a proposal which implies an alteration or amendment requires more than one-third of all board members. If the votes on each side are equal, the chairman of the meeting shall have the casting vote.

§ 10 The Board is responsible for managing the Company's business and shall therefore inter alia:

1. Lay down guidelines for the conduct of the Company's business and check that they are followed
2.Grant loans and delegate authority
3. Make decisions and grant authority for new loans raised
4. Grant special powers and authorisation to sign on behalf of the company per procurationem
5. Present the annual accounts and directors' report to the Annual General Meeting
6. Make recommendations to the Annual General Meeting with respect to alterations to the Articles of Association
7. Appoint the managing director
8. Fix the managing director's salary

§ 11 The chairman of the Board, the managing director or two members of the Board jointly shall sign for the Company.

§ 12 The managing director shall be responsible for the day-to-day management of the Company and its business in accordance with the instructions laid down by the Board and approved by the Supervisory Board.

Chapter IV - Supervisory Board
§ 13 The Supervisory Board shall consist of twelve members and four deputy members. The Supervisory Board should be composed of as broad a range of members as possible, so as to ensure that the various districts and interest groups affected by the Company's business are fairly represented. A member of the Board of Directors cannot also be a member of the Supervisory Board.

One (1) of the members of the Supervisory Board shall be elected by and from amongst the Company's employees. For this member shall be elected one (1) personal deputy. The remaining members and deputy members shall be elected by the Annual General Meeting.

The members of the Supervisory Board shall be elected for two-year terms. One third of the members shall retire each year. Members elected by the shareholders shall be elected for two years. A minimum of one third of the members shall be elected annually. Following the first year one third of the members shall be up for election by drawing lots. The Supervisory Board shall elect a chairman and vice-chairman from amongst its members to serve for a term of one year.

§ 14 The Supervisory Board shall be convened by the chairman and meet at least once a year or as often as the chairman finds necessary or when called for by the Board of Directors, the Audit Committee or at least two of the members of the Supervisory Board. The notice of the meeting shall set out the business to be considered.

The Board of Directors, the Audit Committee and the Company's auditor shall be called to attend the meetings of the Supervisory Board. Unless otherwise determined by the Supervisory Board in individual instances, the Board of Directors and members of the Audit Committee are entitled to be present at the meetings of the Supervisory Board with the right to speak and the right of initiative.

The Supervisory Board constitutes a quorum when at least 2/3 of its members or deputy members are present. If the requisite number of members is not present, a new meeting of the Supervisory Board shall be called. The new meeting will constitute a quorum if more than half the members are present.

Valid resolutions of the Supervisory Board are those for which the majority of the members present have voted, although a resolution can only be passed if voted for by more than one third of all members. If the votes on each side are equal, the chairman of the meeting shall have the casting vote.

§ 15 The Supervisory Board shall supervise the Company's business to ensure that the Company's objectives are being promoted in accordance with law, regulation, memorandum and articles of association, and the resolutions of the Annual General Meeting and the Supervisory Board.
The Supervisory Board shall:
1. Approve the instructions for the managing director as laid down by the Board
2. Elect a state-authorised public accountant to act as auditor
3. Provide a statement to the Annual General Meeting in respect of the Board of Directors' proposals for the profit and loss account and balance sheet, including any consolidated profit and loss account and

consolidated balance sheet, and the Board's proposals for the application of profit or covering of loss for the year
4. Scrutinise the directors' report, the auditor's report and the Control Committee's report
5. Adopt instructions for the Control Committee
6. Give an opinion on matters concerning the Company which are brought before the Supervisory Board by the Board of Directors or Control Committee.

Chapter V - Annual General Meeting
§ 16 The ordinary Annual General Meeting shall be held before the end of June.

An extraordinary General Meeting shall be held if called for by shareholders representing minimum a tenth of the share capital, two members of the Supervisory Board, the Board of Directors, the Control Committee or the Company's auditor.

The Board of Directors shall call the Annual General Meeting.

The Annual General Meeting shall transact the following business:
1. The consideration and adoption of the Company's annual report and accounts, including the application of profit or covering of loss for the year, and the declaration of dividend.
2. The fixing of remuneration of the members of the Supervisory Board and the Board of Directors, the members of the Control Committee and the auditor.
3. Elections of members and deputy members of the Control Committee in accordance with § 17 of the Articles of Association.
4. Other business refered to in the notice of the meeting or which by law or Articles of Association falls under the Annual General Meeting.

Chapter VI - Control Committee
§ 17 The Control Committee shall consist of three members and one deputy member who shall be elected by the Annual General Meeting. One member shall satisfy the requirements to be fulfilled by judges under section 54, second subsection of the Norwegian Courts of Justice Act of 13 August 1915. The election of this member must be approved by the Banking, Insurance and Securities Commission.

No member or deputy member of the Board of Directors, auditor or employee of the Company can be elected as a member or deputy member of the Control Committee. Nor can any person become a member who is under a legal disability or in a relationship of collaboration, subordinacy or dependency to, or married to, or related by marriage or blood in the direct ascending or descending line or the first collateral line to a member of the Board of Directors, auditor or officer of the Company. No person may be elected as a member whose estate is in bankruptcy, under debt settlement proceedings or private administration. Should circumstances arise which render a person no longer eligible for election, he shall retire from the Control Committee.

Members of the Control Committee shall be elected for two-year terms. The Control Committee shall elect a chairman and vice-chairman from amongst its members.

The Control Committee shall supervise the business of the Company, including the transactions of the Board of Directors, and ensure inter alia that the business is run in accordance with law and the Articles of Association.

The Control Committee shall meet as often as may be considered necessary in order to ensure effective supervision. It shall keep such a record of its proceedings as is authorised by the Banking, Insurance and Securities Commission, and shall annually deliver a report on its work to the Supervisory Board, the Annual General Meeting and the Banking, Insurance and Securities Commission.

Chapter VII - Auditor
§ 18 The Company's auditor shall be a state-authorised public accountant and shall be elected by the Supervisory Board.

The auditor's report shall be delivered at least two weeks prior to the meeting of the Supervisory Board which shall consider the accounts.

Chapter VIII
§ 19 The Company shall raise funds for lending by issuing bonds, certificates or other form of loan notes or by entering into loan agreements.

§ 20 Loans can only be granted to municipalities, counties, intermunicipal companies and other companies which carry out local government tasks against either a municipal guarantee, government guarantee or other satisfactory security. The Company can also undertake other tasks appropriate to the Company's business.

§ 21 The Board of Directors shall fix all lending terms and conditions as may be in force at any time.

§ 22 The Company's capitalisation and financial administration shall be satisfactory in relation to the Company's business and consistent with the Company's aims of maintaining highest possible creditworthiness.

Chapter IX - Annual Report and Accounts
§ 23 The Company's financial year shall follow the calendar year.

The Board of Directors shall deliver annual accounts and an annual report for each financial year.

The annual accounts shall be placed at the disposal of the auditor at least one month prior to the ordinary Annual General Meeting. The audited annual report and accounts shall be scrutinised by the Audit Committee and Supervisory Board before being laid before the Annual General Meeting.

The Annual General Meeting shall adopt the annual report and accounts no later than the end of June.

The Board of Directors shall publish the annual report and accounts no later than one week after they have been adopted by the Annual General Meeting.

Chapter X - Age of retirement
§ 24 The age of retirement for the Company's Managing Director is 65 years.

Chapter XI - Entry into force
§ 25 These Articles of Association shall enter into force on the day on which they are Approved by the King.

Chapter XII - Alterations to the Articles of Association
§ 26 The Articles of Association cannot be altered save with the approval of the King.

The Articles of Association were adopted at the meeting of the Company's foundation on 1 November 1999.

Governing bodies (as at 1 March 2010)

The Board of Directors

- Else Bugge Fougner, Chairman, Barrister-at-law (Supreme Court)
- Kristin Marie Sørheim, special advisor, Tingvoll municipality, Vice Chairman
- Frode Berge, Head, Stavanger Regional Business Development
- Svein Blix, CEO, Bodø municipality
- Nanna Egidius, Director of Strategic Planning and Development, Lillehammer municipality
- Åmund T. Lunde, CEO of Oslo Municipality Pension Fund
- Martha Takvam, CEO of Telenor Real Estate
- Martin Spillum, Head of Treasury, employee representative

Alternate to the Employee Representative

- Tor Chr. Hansen, Loan Manager

Supervisory Board

- Elin Eidsvik, CEO, Hamarøy municipality, Chairman
- Svein Ludvigsen, fylkesmann, Troms, Vice Chairman
- Hanne Braathen, Mayor, Storfjord municipality
- Thor Bernstrøm, Assistant Director General, Ministry of Local Government and Regional Development
- Svein Skaaraas, CEO, Hamar municipality
- Tore Sirnes, CEO, Sandnes municipality
- Berit Flåmo, Head of Strategic Development, Trondheim Harbour
- Anita Orlund, Mayor, Skedsmo municipality
- Karen Marie Hjelmeseter, Municipal board representative, Sogndal municipality
- Knut Wille, CEO, Skien municipality
- Arne Johansen, CEO, Harstad municipality
- Ellen E. Scavenius, Portfolio manager, employee representative

Alternates to the supervisory board

- Anne Nafstad Lyftingsmo, Deputy Secretary, Ministry of Local Government and Regional Development
- Nils R. Sandal, CEO, Sogn og Fjordane county
- Rune Øygard, Mayor, Vågå municipality
- Gøril Bertheussen, CEO, Tromsø municipality

Alternate to the employee representative

- Christin Holmbø Kanden, Loan Manager

Control Committee

- Britt Lund, Chairman
- Kjell Inge Skaldebø, CEO, Åfjord municipality, Vice Chairman
- Kristine E. Stray Ryssdal, lawyer, REC ASA

Deputy member

- Roy Jevard, CEO, Melhus municipality

Auditor

- Ernst & Young AS

Eirik Tandrevold, State Authorised Public Accountant

Internal auditor

- KPMG AS

Stein-Ragnar Noreng, State Authorised Public Accountant

Management

Directors

Petter Skouen
President & CEO

Siv F. Galligani
Deputy CEO

Section heads

Marit Ødegård, Lending

Thomas Møller, Funding

Kjell Pettersen, Corporate Communication & Organization

Karina Folvik, Accounting

Knut Andresen, Middle Office & IT

Annette Nielsen, Back Office

Martin Spillum, Treasury

Frank Øvrebø, Credit Analysis

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