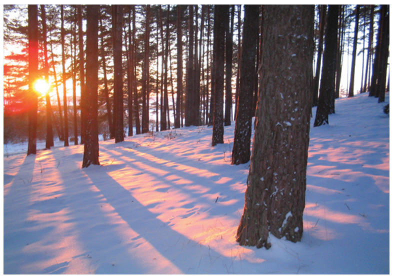
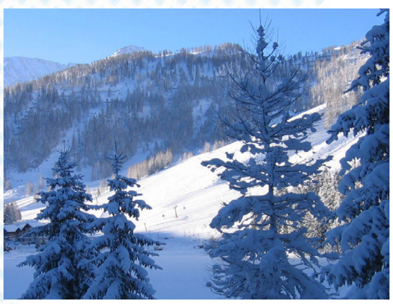




Kommunalbanken Norway
Annual Report
2011

KBN Kommunalbanken Norway

85 years
1927 - 2012

Key figures

(Amounts in NOK 1 000 000)

	2011	2010
RESULTS		
Net interest income	1 582	1 197
Core earnings [1]	1 138	808
Profit before tax	1 001	1 034
Profit for the year	724	741
Return on equity after tax [2]	18.33%	21.62%
Return on equity after tax (core earnings) [2]	28.80%	23.59%
Return on assets after tax [2]	0.22%	0.26%
Return on assets after tax (core earnings) [2]	0.34%	0.29%
LENDING		
New disbursements	46 921	49 933
Outstanding loans [3]	207 572	183 841
LIQUIDITY PORTFOLIO [3]	103 263	86 278
BORROWINGS		
New long-term borrowings	142 341	138 231
Repurchase of own debt	3 416	2 032
Redemptions	104 162	89 840
Total borrowings [3]	338 615	290 231
TOTAL ASSETS	366 901	315 491
EQUITY		
Equity	4 594	4 034
Core capital adequacy ratio	9.79%	9.15%
Total capital adequacy ratio	13.22%	9.86%

[1] Profit after tax adjusted for unrealised gains/losses on financial instruments
[2] Annualised return on equity and return on assets as percentage of average equity and average assets
[3] Principal amounts

The year of the rating agencies

We have left behind us a year with much turmoil in financial markets worldwide. The debt situation in some countries in the Euro Zone has been the subject of considerable attention, and a number of European banks and nations have had their credit rating reduced significantly in 2011.

Meanwhile, we are very fortunate in Norway. The Norwegian economy has good growth, unemployment is low and we are not affected by the problems the rest of Europe is experiencing. This has a positive impact in several areas for KBN.

Investors worldwide have looked upon Norway and KBN as one of the very few safe havens around. There has been considerable interest in our loans and access to capital through most of the year. The growing economy in the municipalities of Norway has resulted in a substantial demand for loans. KBN's growth in lending totalled at 13 per cent. Our market share is currently at 49.3 per cent.

In November 2011, the Norwegian government announced that they would create an export government-run financing scheme. The decision has had significant implications for Exportfinans which until now has had this role, and where the Norwegian state owns 15 per cent. The debt was significantly downgraded because rating agencies believed the risk of default increased as a result of the decision. However, in the wake of Exportfinans, we have found that many investors ask about our Government support. The support has been quickly confirmed by our owners, with the result that we still maintain our AAA rating.

In the future, we see many exciting opportunities for KBN. During 2012, the Government will finalize its work on the National Transport Plan for the period 2014 - 2023. It is already clear that new ways of financing Norwegian transportation will have a significant place in the plan. We would like to see KBN being a part of this solution, as there is no doubt that KBN currently possesses the skills and experience needed.

In the meantime we will continue to do what we can to be the best, most affordable municipal financial source for the welfare of all.

Petter Skouen
President & CEO

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 well over 49 per cent. KBN is also one of the largest financial institutions in Norway.

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 of 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 is regulated by the Norwegian FSA, or Finanstilsynet.

KBN's cost effective organisational structure and conservative management means that operating costs are kept low. KBN's operating costs as a percentage of total assets were 0.03 per cent in 2011.

Environmental management organisation The Eco-Lighthouse Foundation certified KBN's business practices as environmentally sustainable.

CONTENTS

2011 - 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'.

KBN achieved a profit for the year of NOK 724 million compared with NOK 741 million in 2010.

Return on adjusted shareholders' equity (after tax) decreased from 21.6 per cent in 2010 to 18.3 per cent.

Return on assets after tax decreased from 0.26 per cent in 2010 to 0.22 per cent.

The Board of Directors proposes that the profit of NOK 724m is to be transferred to retained earnings as a result of the requirement for a minimum of 9 per cent core equity capital before 30 June 2012.

KBN's total lending portfolio increased by NOK 23.7bn to NOK 207.6bn.

KBN's market share for loans to the local government sector increased from 48.7 per cent to 49.3 per cent.

KBN advises its customers in connection with entering into ordinary banking agreements. In 2011, KBN assisted in the signing of 36 such agreements.

Total funding volume raised in 2011 was NOK 142bn in a market with increasing turmoil in the Euro Zone.

In 2010 KBN was the first Norwegian financial institution to launch a "Green Lending Rate", whereby projects that promote a better environment qualify for an improved interest rate. As of 31 December 2011 loans granted under green lending rate conditions totalled NOK 6.4bn.

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

An update on the Norwegian economy

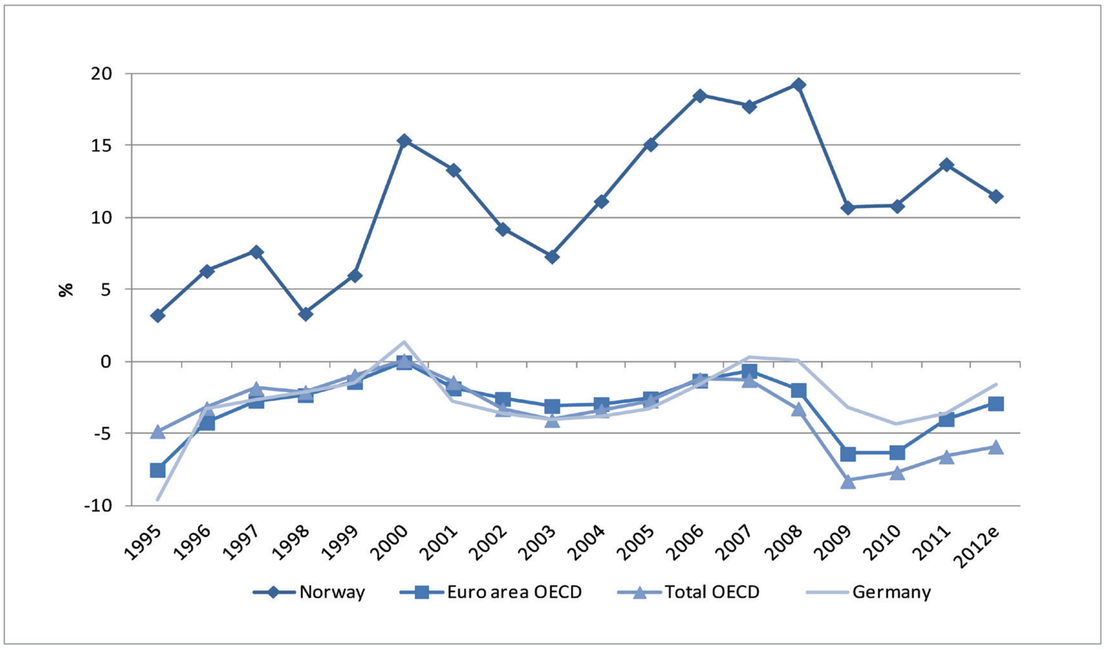
2011 has been plagued by the spiraling sovereign deficits in Europe and the uncertainty about the Euro-zone as a whole in addition to general imbalances and large budget deficits in advanced economies. Unemployment rates are increasing and further challenges in the Eurozone are likely to occur. Continued budget cuts and slow growth will mean low interest rates in the leading industrial countries for the short to medium term.

Compared to its peers in Europe, Norway is in a significantly better position than most countries to counteract the effects of a general economic slowdown. The current account balance and government finances are solid, and Norway is projected to post a surplus of 11.5 per cent of GDP in 2012. 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.

At the end of 2011, the Government Pension Fund – Global reached NOK 3.2 trillion in size, approximately USD 550 billion or 120% of GDP. The fund increased its share of equity investments to 60 percent from 40 percent between the summers of 2007 and 2009, reducing fixed-income investments to 40 percent. From March 2010, it also has a mandate on to invest as much as 5 per cent of its assets in real estate through a corresponding decrease in fixed-income investments.

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. With a bounce back in the economy from the second half of 2009, rates were increased steadily to the 2.25 per cent level by mid 2011 and then cut again to 1.75% in late 2011 due to increased uncertainty in the global economy. Projections for 2012 are uncertain, but despite solid domestic growth it's expected that Norges Bank



General government financial balances (% of GDP) *

will hesitate to increase rates before we see a marked increase in economic activity in Europe. Inflation is also back under 2 per cent and expected to stay between 1.0-1.5 per cent for the coming year.

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. Although Norway experienced two quarters of negative GDP growth in 2009, the economy rebounded in H2 2009 and according to the Ministry of Finance, the mainland economy showed only mild negative growth of 1.4 percent for the whole of 2009.

In 2010 and 2011, the economy bounced back, with increased consumer confidence, low interest rates and low unemployment leading to higher private consumption. GDP growth for mainland Norway reached 2.6 per cent in 2011. Despite a sluggish European economy Norway's GDP growth growth is expected to be around 3 per cent in 2012.

Unemployment in Norway has not risen as sharply as in other developed countries. Projections from the Ministry of Finance point to an unemployment rate of 3.2 per cent in 2012, a decrease of only 0.1 per cent compared with 2011. This is lower than the average of the past 20 years, approximately 4 per cent, and also very low compared with other developed economies.

* Source: OECD Economic Outlook No. 90, November 2011 , Ministry of Finance.

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 the police.

Norway is divided into 19 counties and 429 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 5.0 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 39 per cent and 42 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.


KBN Kommunalbanken

The Board of Directors' Annual Report 2011

The year has been marked by turmoil within the global financial markets and there has been considerable uncertainty around macroeconomic developments.

The municipal sectors in many countries have been directly affected by this critical period of financial crisis and significantly reduced budgets.

In Norway, the investment activity and need for municipality financing is still high. Well balanced growth and favourable margins in hedging instruments led to increased earnings for Kommunalbanken Norway (KBN), which had a positive effect on the annual profit. On the other hand, unrealised changes in the value of financial hedging instruments resulted in reduced profit.

KBN's profit after tax was NOK 724m compared to NOK 741m in 2010. Return on equity after tax was 18.3 per cent, compared to 21.6 per cent in 2010.
KBN's overall goal is to secure low cost financing to the municipal sector for the realization of local welfare. This is in accordance with KBN's sector policy role as defined by the Central Government. The role is fulfilled by passing on the favourable conditions KBN achieves in capital markets. KBN should also aim for a satisfactory return on equity.

KBN has continued its role as the main provider of loan capital to municipalities and counties. Initiated by government policy, the municipal sector gross debt has now reached a higher level. The annual growth in gross debt is almost four times higher than in 2005. Over the last two years there has been a growth of more than 10 per cent. Debt levels are mainly a consequence of the fact that municipalities are the main producers and suppliers of local welfare services. Investment levels are high in most service areas. The local government sector's gross debt at the end of 2011 was NOK 421bn, an increase of 12 per cent from 2010. Net debt is significantly lower and totalled NOK 183.8bn at year end.

KBN's total lending at year end were NOK 207.6bn, compared to NOK 183.8bn in the previous year, an increase of NOK 23.8bn or 13 per cent. KBN's market share increased from 48.7 per cent to 49.3 per cent.

KBN's borrowings in 2011 reached NOK 142.3bn in 17 currencies, compared to NOK 138.2bn in 2010.

During the first half of 2011, the funding markets were characterized by a continued normalization from 2010 compared with the turmoil in 2008 and 2009. However, following the 3rd quarter, there was increasing unrest in the Euro Zone, a trend which peaked in November-December.

KBN's liquidity policy aims to have liquidity over time equivalent to 12 months' net capital requirements. Total available liquidity at year end amounted to NOK 114.0bn, including collateral from counter parties amounting to NOK 10.8bn. Liquidity reserves are invested based on a low risk strategy. By year end securities issued by governments, regional governments and institutions with governmental guarantees amounted to more than 70 per cent of the portfolio.

The Central Government, represented by the Ministry for Local Government and Regional Development, is the sole owner of KBN. KBN's registered office is in Oslo.

Annual accounts

The Board of Directors confirms, in accordance with the Norwegian Accounting Act § 3-3a, that the Company's ability to continue as a going concern remains unchanged, and the financial statements for 2011 are prepared on a going concern basis. The Board of Directors considers that the financial statement, with notes of 31 December 2011, provide an adequate description of KBN's financial position at year end. The annual accounts have been prepared in accordance with International Financial Reporting Standards, IFRS, as adopted by the EU.

KBN's profit after tax in 2011 was NOK 724m compared with NOK 741m in 2010. Well-balanced growth and favourable margins in instruments contributed to increased earnings in 2011, while fair value changes on financial instruments in economic hedges reduced the result. KBN achieved a return on equity of 18.3 per cent after tax in 2011 against 21.6 per cent in 2010.

Net interest income amounted to NOK 1,582m, an increase of NOK 385m compared with 2010. Interest rates on KBN's loans, measured against 3-month's NIBOR nominal rate, remained stable throughout the year. However, net interest income from the lending portfolio increased, due to the fall in prices on the conversion of U.S. dollars to Norwegian kroner, which contributed to lower borrowing costs for KBN. Net interest income from management of excess liquidity increased as a result of a general credit spread related to the crisis in the Euro Zone. Favourable derivative margins on hedging instruments have also contributed to this result.

The turmoil in the credit markets and uncertainty in macroeconomic development lead to increased volatility on the market value of bank assets and liabilities and derivative financial instruments used in economic hedges. Net unrealised fair value change on financial instruments was minus NOK 575m in 2011. Value changes are largely due to the special situation on the swap market, where a sharp increase in demand for U.S. dollars resulted in an increase of a USD-NOK and a USD-EUR basis spread.

The basis swap is an essential element of KBN's business model, which is based on low-cost foreign currency borrowings in international capital markets and lending in Norwegian kroner to the local government sector. KBN uses basis swaps to convert borrowings in foreign currency into Norwegian kroner, and to hedge the currency risk in financial investments.

Through the use of basis swaps, with the same maturity as the underlying assets and liabilities, KBN is expected to achieve stable margins and predictable earnings in the future. The market value of the basis swaps can change considerably during the term, as the prices on basis swaps reflect the demand for U.S. dollars and may show significant fluctuations during periods of market turmoil. Value changes affect KBN's income statement and balance sheet, and contribute to increased volatility of capital adequacy. Since basis swaps are used exclusively as hedging transactions and held to maturity, their fair value changes are recognised in the income statement and core capital will be reversed when the contracts mature.

KBN was the first Norwegian financial institution to launch a "Green Lending Rate", whereby projects that promote a better environment qualify for an improved interest rate. Photo: Samfoto.

Operating expenses were NOK 96m in 2011 compared to NOK 97m in 2010. Operating expenses account for 0.03 per cent of total assets.

Total assets in 2011 increased NOK 51.4bn to NOK 366.9bn. The loan portfolio increased by NOK 23.7bn in 2011 and as of 31 December 2011 was NOK 207.6bn. Excess liquidity increased by NOK 21.1bn to NOK 114.0bn.

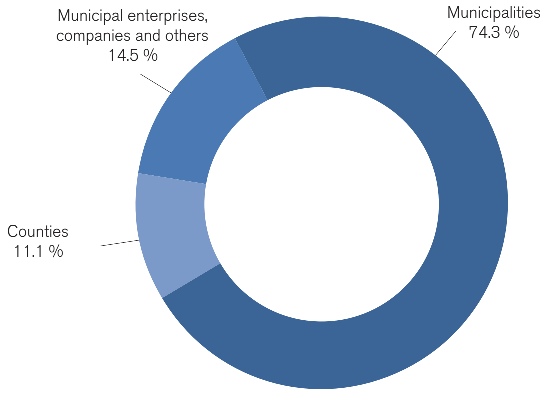
The total capital at year end was NOK 7,150m, of which eligible core capital amounted to NOK 5,295m. The core capital ratio at year end was 9.8 per cent, while total capital ratio was 13.2 per cent.

Lending

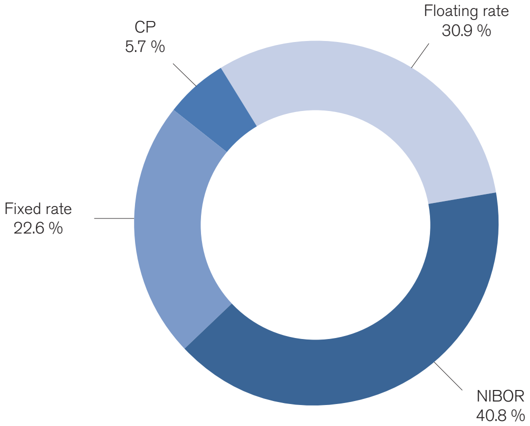
At the end of 2011 KBN total loans amounted to NOK 207.6bn. Municipalities, as a group of borrowers, account for NOK 154.3bn (74 per cent) and counties for NOK 23.1bn (11 per cent), while local companies, inter-municipal companies and other companies operating under a full municipal guarantee, which perform public duties, have total loans of NOK 30.2bn (15 per cent). This is partly because the counties have taken over the responsibility for much of the national road network. Within the infrastructure area, several projects are organized into separate companies with guarantees.

KBN shall ensure that the local governments have access to affordable loans, and is offering the same interest rates to small and large municipalities. Out of a lending growth of NOK 23.7bn in 2011, NOK 4.6bn went to municipalities with less than 5,000 inhabitants, based on the demand for loans of NOK 5.8bn (79 per cent accepted KBN's offer). The acceptance

Loan volume by borrower
as at 31.12.2011



Loan volume by interest rate product
as at 31.12.2011



rates for loans to larger municipalities were somewhat lower, mainly due to competition from the domestic capital market.

At the beginning of 2012, all counties, 423 of the country's 429 municipalities, including Longyearbyen's local council, have loans with KBN. The same applies to most municipally owned enterprises and inter-municipal companies, in addition to toll road companies and companies that perform other municipal services. Loans to companies with limited liability require municipal or county guarantee, mainly unconditional guarantee.

KBN is the largest lender in the long-term debt market with pt-rate, NIBOR-rate and fixed rate. KBN operates in a competitive market, and competitors are found mainly in the domestic capital markets.

After a turbulent second half year in the financial markets, with a fall in long term interest rates, there has been an increased demand for KBN's fixed rate loans. Approximately 23 per cent of the loan portfolio at the end of 2011 were fixed rate loans, an increase of one percentage point from previous year. Loans with commercial paper terms increased from 5 per cent to just under 6 per cent in the period. The other loan categories shows only minor changes from 2010. In November, KBN decided to reduce the loan offering with short term note condition to limit loan growth, partly due to new and stricter capital adequacy requirements.

As part of its regular customer service, KBN is a discussion partner on issues relating to the composition of loan portfolios and the evaluation and selection of interest rate alterations. KBN provides updated online financial information and offers the municipalities access to their own loan portfolio via KBN's website. In 2011, KBN also continued its increased emphasis on building customer relationship through activities such as customer meetings and regional conferences with relevant topics for the sector.

According to The Public Procurement Act, the municipalities must tender major banking agreements. KBN will, as a neutral party, assist local authorities to invite tenders for payment services. In 2011 KBN assisted in 36 such negotiations.

Infrastructure projects are an important area for KBN. Due to the administrative reform in 2010, an essential part of the national road network, including ferry services, were transferred from the state to counties. A large part of the new road projects are to be financed by toll road collection. The Public Roads Administration has estimated that toll road financing will total NOK 140bn over a 30 year period. This allows for a stronger commitment from KBN. As of 31 December 2011 KBN had granted loans for road financing of NOK 22.5bn, an increase of 6.5bn from 2010.

In 2010, KBN was the first Norwegian financial institution to launch a Green Lending Rate Scheme to help municipalities reduce energy consumption and greenhouse gas emissions. Major investments must be implemented in the municipalities to achieve local and national climate goals. KBN would like to contribute so that such projects are financially viable through more favourable financing. The green lending rate is lower than the ordinary rate currently at KBN. As of 31 December 2011 loans granted under green lending rate conditions totalled NOK 6.4bn.

KBN has not had losses on loans to customers in 2011. There were no fraud or payment problems experienced by customers which might lead to expected losses in 2012.

Funding

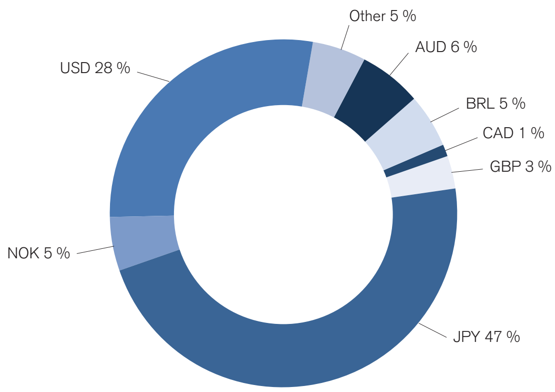
KBN divides its funding activities across four areas: USD benchmark issuance, issuance in public niche markets, private placements to institutional investors and retail issuance. Focusing on a variety of funding markets, KBN has secured stable access to funding markets on favourable terms and at the same time increased the institution's investor base. Japan continues to be KBN's largest source of funds, while other major markets included the United States, Europe and the rest of Asia.

In recent years, KBN has increased issuance in the Japanese Uridashi bond market. Uridashi bonds are primarily aimed at private investors in Japan, where KBN, in accordance with the Japanese authorities' definition, is a state borrower. Altogether 278 transactions were done in this market in 2011, which amounted to NOK 67bn or almost 50 per cent of the total borrowing.

To finance the green lending rate, KBN has established a green funding program for the Japanese retail market, earmarked for climate and environmental projects.

In 2011, borrowing was made in 17 different currencies and KBN benefits from this diversified funding strategy. KBN issued two USD benchmark loans in 2011. The loans were well received and both loans were oversubscribed. Demand for these deals was especially strong from the United States and investors from this region made up the largest proportion of investors. The 5 year bond issue in January 2011 was KBN's largest, totalling USD 2bn.

Funding currency split 2011



KBN has an AAA rating and KBN's bonds are perceived as attractive investments. This is due to Norway's strong financial position, KBN's ownership and special role as lender to Norwegian municipalities. High demand from international investors for these types of securities continues to provide KBN with good access to the financial markets.

KBN's total volume of bonds, commercial papers and other funding instruments rose in 2011 from NOK 290.2bn to NOK 338.6bn.

KBN's international lending program "Program for the Issuance of Debt Instruments" is mainly aimed at international borrowing. This is a standardized loan documentation that simplifies and secures the loan processing, for both lender and borrower. The program has no maximum limit from 2011 onwards.

In the fourth quarter there was some market turmoil related to the downgrading of the Norwegian Eksportfinans. KBN appreciated that the Central Government as owner of KBN quickly confirmed unchanged support.

Liquidity management

In line with KBN's financial policies the liquidity level should be, over time, equivalent to 12 months' net capital requirements, including lending growth. This means that KBN in any given situation is able to meet all obligations over the next 12 months without any new borrowing. Excess liquidity is managed with a low-risk investment strategy, both in terms of credit and market risk. The liquidity reserve is invested in liquid fixed income securities issued by governments, states, regional governments, multilateral development banks and financial institutions, with high credit ratings. The average maturity is 16 months, of which about half is due within 12 months. There is no interest rate or currency risk and the maturity profile is reconciled against the underlying borrowings.

Risk management

Risk management and risk exposure within KBN will ensure KBN's credit rating and access to the most attractive financial markets. Credit and liquidity risk is overall low. KBN has no position-related exposure to interest rate and currency risk. All risk limits and trading of new financial instruments are approved by the Board of Directors. The financial policies and guidelines for lending to local authorities are considered by the Board of Directors annually.

Credit risk represents the biggest risk factor on KBN's asset side. Management, monitoring and credit ratings of KBN's engagements are continuously evaluated.

Credit risk for lending is limited to the payment deferment when payment obligation cannot be eliminated. The Local Government Act states that municipalities and counties cannot be declared bankrupt. The Local Government Act also provides the procedures to be followed if payment deferral must be implemented. Following these rules the Ministry for Local Government and Regional Development takes over the management of a municipality if the municipality fails to fulfil its payment obligations. This ensures the lender against loss of accumulated debt and accrued interest.

Credit risk for liquidity management and related hedging deals is low in accordance with KBN's guidelines for entering into financial agreements. The framework for liquidity management approved by the Board of Directors, includes requirements for amongst other things, a rating of at least A2 / A from the rating institutes Moody's and Standard and Poor's, maturity, instrument type, type of counterparty and the counterparty's home country.

Derivative trading is documented, using the ISDA Master Agreements and the establishment of collateral agreements, which include cash collateral with derivative counterparties.

Procedures and processing for managing credit risk are established. All counterparties are reviewed regularly and the Board of Directors is kept informed about KBN's counterparty risk. An extended market update is given quarterly.

Market risk consists primarily of interest rate and currency risk. KBN's policy allows minimal exposure to interest rate and currency fluctuations. Management of interest rate and currency risk is done by ensuring that KBN's assets and liabilities are balanced at any time.

Liquidity risk is minimized by the fact that the liquidity portfolio over time will equal 12-month net capital requirements. Moreover, the portfolio is invested in liquid securities of high credit quality and short duration.

Operational risk is present in all parts of KBN's activities. KBN minimizes operational risk through a continuous effort to ensure good internal controls and good ethical behaviour and competence of the individual employee. The Board of Directors is regularly informed about KBN's operational risk.

Communication, media and public relations
KBN works with many organizations in the municipal sector in order to improve the understanding of KBN's socially beneficial function through the financing of public welfare tasks. Emphasis is placed on good contact with the authorities and other public bodies.

Cooperation with Husbanken (The State Housing Bank) has been prolonged so that KBN may use Husbanken's regional offices as regional hubs for customer contact.

The Board of Directors established the framework for KBN's ethical standards when it comes to marketing communications and marketing activities. The customers must have assurance that KBN operations are ethical and cautious.

Corporate governance
KBN is subject to Norwegian recommendation for corporate governance in the areas that are relevant, taking account of KBN's organizational form and ownership structure. The purpose of the recommendation is for companies to practice corporate governance that regulates the division of roles between shareholders, board and management, in addition to those required by legislation. Recommendation will strengthen confidence in companies and contribute to the greatest possible value creation over time, to the best interests of shareholders, customers, employees and other stakeholders.

KBN's central bodies are organized in accordance with the provisions of the Companies Act. KBN's bodies are: The General Assembly, the Supervisory Board, the Board of Directors, the Control Committee, internal and external auditors and the chief executive officer. The administration is organized into three business areas, in addition to staff and support functions.

KBN 's internal control function will ensure the implementation of risk analysis and risk monitoring, and that business is conducted in accordance with adopted strategies and policies. Internal control is an integral part of the management and planning process at KBN. Status and the risk control process is monitored at department level and reported to the CEO and the Board of Directors.

The Board of Directors is elected by the General Assembly in accordance with the laws § 16, cf. § 8. The Board of Directors shall consist of 5-9 members. Two of the Board of Directors' elected members must be elected by and from among the employees. For these members personal deputies must be selected to attend and speak on the Board of Directors. The other members are elected for two year terms, so that at least two are up for election each year, with a maximum of three of the elected members.

Regulations §§ 6 and 7 state that the acquisition of shares is conditional upon the consent of the Board of Directors. Consent can only be refused if there are reasonable grounds to do so. The pre-emption rights that a shareholder has under the Company's Act § 4-19 can also be applied to shares that have changed hands.

Chairman Else Bugge Fougner and board member Åmund Lunde were re-elected at the general meeting. Nils R. Sandal was elected as the new vice chairman of the Board of Directors and Rune Sollie as a new board member. Employee representation on the Board of Directors was extended with one member, to two members.

The Board of Directors has thereafter the following composition: Else Bugge Fougner (Chairman), Nils R. Sandal (Vice Chairman), Åmund T. Lunde, Frode Berge, Nanna Egidius, Martha Takvam, Rune Sollie, Ellen E. Scavenius (employee representative, with Thomas Mathisen as personal deputy) and Roald Fischer (employee representative, with Lise Bakken as personal deputy).

The Board of Directors has established two sub-committees, the Audit Committee and the Compensation Committee.

Organization and skills development

By the end of the year there were 50 permanent employees at KBN, occupying 48 full time equivalent positions, compared with 48 permanent employees occupying 46.8 full time equivalent positions the previous year. This increase is a consequence of KBN's growth, new government requirements and the need to strengthen expertise in strategically important areas. KBN's human resources plan has a three-year perspective and is evaluated annually. The plan ensures that KBN has sufficient personnel with appropriate expertise, in relation to its goals and ambitions, as laid down in planning and strategy documents.

The Board of Directors has started the process recruiting a new CEO in KBN as a result of Mr. Petter Skouen retiring in November 2012.

Health, safety and diversity at KBN

KBN is committed to recruiting high skilled employees, including employees with an international background and experience. This provides KBN with competence that is of importance for KBN's operation. 8 per cent of the employees are of non-Nordic origin, 3 women and 2 men. These are also represented in management and among the field specialists.

The 2010 work environment survey was followed up, including an ergonomic review of the work space. KBN is actively working on measures that can contribute to a better working environment.

Sick leave is at 2.6 per cent, compared to 2.5 per cent in 2010, distributed by 4.1 per cent among women and 0.9 per cent among men. There were no reports of injuries in 2011. 7 employees have had parental leave, 4 women and 3 men. All employees are offered an annual health check.

The KBN headquarters are satisfactory. The building does not impact on the external environment.

Ethics and social responsibility

Ethical guidelines that apply to employees and officers have been revised and clarified. The guidelines are reviewed and discussed regularly. Work has systematically taken place to ensure that each employee has knowledge and an awareness of the guidelines. KBN is committed to communicating the content of KBN's ethical guidelines to customer groups.

Environment. In 2009, KBN was certified as an eco-business, and will be re-certified in 2012. Implementing measures as recycling, waste reduction, and systems resulting in reduced CO^2 emissions continue. The offices provide good opportunities for energy efficiency.

Sector Policy function. It is a priority for KBN to be a predictable and reliable supplier of credit to the municipal sector. KBN is a guarantor of the municipalities to achieve the best possible loan terms.

Equality of opportunity

KBN is focused on providing women and men the same opportunities for professional and personal development, salary, promotion and recruitment. KBN has flexible schemes that make it easier to combine career and family life. Of KBN's workforce of 50, 25 are women and 25 are men.

The proportion of women on the Board of Directors is 44.4 per cent. The Chairman of the Board of Directors is a woman.

Top management consists of the CEO (male) and Vice President (female). Of the entire management team, 60 per cent consisted of women in 2011.

Through its salary and employer policy, KBN strives to recruit and develop talented staff, based on the needs of KBN at any time. Great emphasis is placed on following the equal pay principle, so that jobs of equal value are remunerated equally.

Application of profits

As a result of the requirement for a minimum of 9 per cent core equity capital before 30 June 2012, the Board of Directors proposes that the profit of NOK 724m is to be transferred to retained earnings. Unrestricted equity after appropriation of profit is thus NOK 3,373m and total capital amounts to NOK 7,150m.

Future prospects

Norway is in a different economic situation than most countries in Europe. Norway has for many years had budget surpluses. These surpluses are among the highest of all countries in Europe. This means that Norway is in a better position to choose its own future economic policies.

Economic activity in Norway is held up by strong demands from households and high activity in the oil and gas industry. It is expected that Norwegian exporters will face reduced demand, especially from the European market. It is expected that investment and employment in traditional industries will also drop. With this scenario in mind, continued growth is still foreseen in local government revenues. The increase in local government gross investment is expected to decrease somewhat in 2012, with the result that growth in local government debt will decline. A consequence of this being that growth in local loan volume will decrease.

The financing of infrastructure projects is expected to take up a relatively large proportion of new loans from the sector. The same applies to the development of nursing and care services, in the wake of the coordination reform in the Norwegian health sector.

KBN will continue its differentiated borrowing strategy in 2012. Total borrowing in 2012 is expected to be reduced by about NOK 10-20bn compared to 2011, provided that the market allows for longer maturities of funding, without this raising capital costs significantly. According to plan, the Japanese capital market will continue to be KBN's most important funding market. The number of benchmark loans will increase compared to last year. Other markets that are characterized by longer maturities will also be given priority. In recent years, KBN took up relatively few loans in the domestic Norwegian market. Work is undertaken to try to find solutions that may increase KBN's domestic borrowings.

An important milestone will be to satisfy the requirement for a minimum of 9 per cent core equity capital as of 30 June 2012. The report is released on condition that the difference between the level of core equity capital at the end of the 3rd quarter of 2011 and the requirement of core equity capital at the end of the 2nd quarter of 2012 will be covered through a capital increase. New capital adequacy requirements (CRD IV) are scheduled to be implemented in early 2013. KBN can meet these requirements. KBN is in dialogue with the owner, the Kingdom of Norway, about the consequences of a possible introduction of unweighted debt-equity ratio in 2019. This may require additional capital.

The accounts for 2011 show satisfactory results. KBN has handled a challenging year in

The members of the Board of Directors, from left to right,
Else Bugge Fougner, Nils R. Sandal, Frode Berge, Nanna Egidius, Roald Fischer, Åmund T. Lunde, Ellen E. Scavenius, Rune Sollie and Martha Takvam.







a satisfactory way and is well positioned for the future. This is the condition for continuing KBN's main function: financing local welfare.

The Board of Directors would like to thank KBN's employees for a job well done.

Oslo, 31 December 2011
16 March 2012

The Board of Directors of Kommunalbanken Norway

Else Bugge Fougner
Chairman of the Board

Nils R. Sandal
Vice Chairman

Frode Berge
Board Member

Nanna Egidius
Board Member

Roald Fischer
Board Member

Åmund T. Lunde
Board Member

Ellen E. Scavenius
Board Member

Rune Sollie
Board Member

Martha Takvam
Board Member

Petter Skouen
President & CEO

INCOME STATEMENT

(Amounts in NOK 1 000 000)	**Note**	**2011**	**2010**
Interest income		6 730	5 034
Interest expense		5 148	3 837
NET INTEREST INCOME	**1**	**1 582**	**1 197**
Fees and commission expenses	**2**	19	18
Net unrealised gain/(loss) on financial instruments	**3,12**	(575)	(89)
Net trading income	**4**	109	41
TOTAL OTHER OPERATING INCOME		**(485)**	**(66)**
Salaries and administrative expenses	**5,6,7**	77	75
Depreciation on fixed assets		4	5
Other expenses		15	17
TOTAL OPERATING EXPENSES		**96**	**97**
PROFIT BEFORE TAX		**1 001**	**1 034**
Income tax	**8**	276	293
PROFIT FOR THE YEAR		**724**	**741**

STATEMENT OF COMPREHENSIVE INCOME

(Amounts in NOK 1 000 000)	**Note**	**2011**	**2010**
Profit for the year		724	741
Other comprehensive income		0	0
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		**724**	**741**

STATEMENT OF FINANCIAL POSITION

(Amounts in NOK 1 000 000)	**Note**	**2011**	**2010**
ASSETS			
Deposits with credit institutions	**9,11,13,20**	3 151	8 030
Instalment loans	**9,10,11,14**	210 189	185 679
Notes, bonds and other interest-bearing securities	**9,10,11,12,15**	116 657	95 610
Financial derivatives	**9,11,12,19**	36 889	26 155
Other assets	**16**	15	17
TOTAL ASSETS		**366 901**	**315 491**
LIABILITIES AND EQUITY			
Loans from credit institutions	**9,11,17,20**	11 915	8 814
Senior securities issued	**9,10,11,12,18**	336 942	288 093
Financial derivatives	**9,11,12,19**	10 165	13 067
Other liabilities		53	37
Current tax liabilities	**8**	445	259
Deferred tax liabilities	**8**	14	182
Pension liabilities	**7**	30	25
Subordinated debt	**9, 11, 21**	2 080	306
Hybrid Tier 1 capital instruments	**9, 11, 21**	663	672
TOTAL LIABILITIES		**362 307**	**311 456**
Share capital	**22**	1 221	1 221
Retained earnings		3 373	2 814
TOTAL EQUITY		**4 594**	**4 034**
TOTAL LIABILITIES AND EQUITY		**366 901**	**315 491**

STATEMENT OF CHANGES IN EQUITY

			2011	
(Amounts in NOK 1 000 000)	**Note**	**Share capital**	**Retained earnings**	**Total equity**
Equity as of 1 January 2011		1 221	2 814	4 034
Total comprehensive income for the year		0	724	724
Dividends		0	(165)	(165)
Equity as of 31 December 2011	**22**	**1 221**	**3 373**	**4 594**

			2010	
(Amounts in NOK 1 000 000)	**Note**	**Share capital**	**Retained earnings**	**Total equity**
Equity as of 1 January 2010		1 221	2 340	3 561
Total comprehensive income for the year		0	741	741
Dividends		0	(267)	(267)
Equity as of 31 December 2010	**22**	**1 221**	**2 814**	**4 034**

STATEMENT OF CASH FLOWS

(Amounts in NOK 1 000 000)	Note	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES			
Interest received		6 396	4 853
Interest paid		(5 091)	(3 846)
Fees and commissions paid		(21)	(18)
Receipts from repurchase of issued securities		111	41
Cash payments to employees and suppliers		(92)	(92)
Income taxes paid		(260)	(400)
		1 044	**537**
Net disbursement of loans to customers		(23 734)	(32 566)
Net (increase)/decrease in deposits with credit institutions		8 835	112
Net (increase)/decrease in notes, bonds and other interest-bearing securities		(21 489)	(23 921)
Net (increase)/decrease in other assets		0	(2)
Net increase/(decrease) in other liabilities		21	14
NET CASH FLOWS FROM OPERATING ACTIVITIES		**(35 324)**	**(55 825)**
CASH FLOWS FROM INVESTING ACTIVITIES			
Purchase of property and equipment		(2)	(7)
NET CASH FLOWS FROM INVESTING ACTIVITIES		**(2)**	**(7)**
CASH FLOWS FROM FINANCING ACTIVITIES			
Proceeds from issuance of commercial paper		14 417	2 646
Repayment of commercial paper		(14 385)	(2 575)
Proceeds from issuance of debt securities		142 374	137 857
Repayment of debt securities		(107 659)	(91 936)
Proceeds from other borrowed funds		0	0
Repayment of other borrowed funds		(487)	0
Proceeds from issuance of subordinated debt		1 565	400
Repayment of subordinated debt		0	(351)
Dividends paid		(165)	(267)
Paid in share capital		0	0
NET CASH FLOWS FROM FINANCING ACTIVITIES		**35 661**	**45 773**
NET CHANGE IN CASH AND CASH EQUIVALENTS		**335**	**(10 059)**
Effects of foreign exchange differences		(264)	10 075
Cash and cash equivalents at 1 January		78	63
Net change in cash and cash equivalents		72	15
Cash and cash equivalents at 31 December		**150**	**78**
Deposits with credit institutions without agreed period of notice	**13**	*150*	*78*

ACCOUNTING POLICIES

REPORTING ENTITY

Kommunalbanken AS (”the Company” or ”KBN”) is a limited company providing loans to counties, municipalities, intermunicipal companies and other companies that carry out local government tasks under a municipal guarantee or other security. KBN’s registered office is in Haakon VIIs gate 5B, Oslo. The financial statements for the year ended 31 December 2011 were approved by the Board of Directors on 16 March 2012.

BASIS OF PREPARATION

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

- Financial instruments at fair value through profit or loss
- Financial instruments held for trading
- Financial instruments classified as Loans and receivables or Other liabilities that are hedged items in fair value hedges and the carrying value is adjusted for fair value changes attributable to the risks that are being hedged.

FOREIGN CURRENCY TRANSLATION

The Company’s functional and presentational 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. Revenues and expenses denominated in a foreign currency are translated into NOK at the exchange rate at the transaction date. The financial statements are presented in NOK and rounded to the nearest million kroner.

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. The most significant uses of judgement and estimates are as follows:

Fair value of financial instruments

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. Assumptions and judgements may apply to the classification of financial instruments measured at fair value in the IFRS 7 hierarchy.

Pension liabilities

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

RECOGNITION AND DERECOGNITION

Recognition and derecognition of financial instruments in the Statement of Financial Position takes place at the settlement date. 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 or 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 are recognised from the trade date.

Financial assets are derecognised when the contractual rights to the cash flows expire or are transferred. Financial liabilities are derecognised when the contractual obligation has been discharged, cancelled or expired. Repurchases 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.

FINANCIAL INSTRUMENTS—CLASSIFICATION AND MEASUREMENT

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

Financial assets designated at fair value through profit or 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 or loss.

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 or loss.

Financial assets held to maturity

Financial assets in this category are primarily investments of equity capital in senior bonds, and 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.

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 the hedged 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 unrealised gain/(loss) on financial instruments".

Financial liabilities designated at fair value through profit or 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.

Financial liabilities at amortised cost
Financial liabilities measured at amortised cost are public benchmark loans issued in the second quarter of 2009 and onwards 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 unrealised gain/(loss) on financial instruments".

Financial derivatives
Financial derivatives are classified as Held for trading, with the exception of contracts designated as hedging instruments in fair value hedges. All financial derivatives are measured at fair value through profit or loss and are presented as assets when the value is positive, and as liabilities—when the value is negative.

FINANCIAL INSTRUMENTS—DETERMINATION OF FAIR VALUE

Level 1
Securities traded in an active market with frequent market observations are recorded at quoted prices in active markets at the reporting date. Quoted prices are provided by international vendors (Reuters/Bloomberg). 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 where fair value can be determined using quoted prices on identical or similar instruments, or using valuation techniques 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 techniques 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.

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

OFFSETTING OF FINANCIAL ASSETS AND LIABILITIES

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. Standard master netting agreements do not qualify for offsetting, therefore, the related assets and liabilities are presented gross in the Statement of Financial Position. Cash collateral received or pledged as additional security for derivative exposure is subject to ISDA-agreements that give right to offsetting of assets and liabilities in event of default, but do not qualify for offsetting under IAS 32. Cash collateral is presented gross in the Statement of Financial Position.

IMPAIRMENT OF FINANCIAL ASSETS

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 the income statement. 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 distress

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 instalment loans.

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 and senior securities issued classified as Other liabilities. 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 or 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 unrealised gain/(loss) on financial instruments".

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 the income statement as they are earned or accrue. Interest income for assets and liabilities carried at amortised cost is recognised in the income statement 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 income statement under "Net unrealised gain/(loss) on financial instruments".

Commission expenses on government guaranteed funding are accrued over the lifetime of the transaction. Other commission expenses 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 classified as an intangible 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 or loss.

PENSIONS

The Company has an employee pension scheme. The pension scheme is treated as a defined benefit plan. A standard profile of benefits earned 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 service costs, interest costs on the calculated liability and expected return on the pension assets. Value of net pension liabilities is calculated based on economic and actuarial assumptions. Actuarial gains and losses 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.

TAXES

Taxes are recognised as they accrue, i.e. the income tax is based on the profit before tax. It is adjusted for temporary and permanent differences before the year's tax base for current taxes is calculated. Deferred tax liabilities and deferred tax assets 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 this calculation. Tax increasing and tax-reducing differences within the same period are offset. Income tax consists of current taxes (tax on the taxable profit or loss for the year), changes in net deferred tax and adjustment to taxes payable in respect of previous years.

EQUITY

The Company's equity consists of share capital and retained earnings. Dividends are classified as equity until approved 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 than disclosures on the lending portfolio and the business as a whole.

NEW ACCOUNTING STANDARDS IN 2011

The accounting standards applied in 2011 are consistent with previous years. There are no new accounting standards that affect KBN's financial statements.

Standards issued or changed but not yet effective:

•IFRS 7 Financial instruments—Disclosure
•IFRS 9 - Financial instruments
•IAS 1 Presentation of financial statements
•IAS 19 Employee benefits

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 one opts to measure these assets at fair value. Other financial instruments should be measured at fair value. Effective date for IFRS 9 is postponed to 1 January 2015, but the standard is still not approved by the EU. IFRS 9 is expected to affect the Company's presentation of financial liabilities.

The proposed changes in IAS 19 eliminate the use of the "corridor" approach and instead mandate all remeasurement impacts to be recognised in OCI. Effective date for the amendments is expected to be 1 January 2013. The proposed change will not have any significant impact on KBN's financial statements.

The other standards are not expected to have any material effect on the Company's financial statements.

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1 NET INTEREST INCOME

(Amounts in NOK 1 000 000)

	2011						
	Total	At fair value through profit or loss			Held to	Loans and	Other
		FVO	Held for trading	Fair value hedge	maturity	receivables	liabilities
Deposits with credit institutions	**45**	45	0	0	0	0	0
Instalment loans	**6 271**	3 718	310	0	0	2 243	0
Notes, bonds and other interest-bearing securities	**2 588**	1 508	288	0	147	645	0
Financial derivatives	**(2 173)**	0	(1 596)	(578)	0	0	0
Total interest income	**6 730**	**5 271**	**(998)**	**(578)**	**147**	**2 889**	**0**
Loans from credit institutions	**12**	12	0	0	0	0	0
Senior securities issued	**10 049**	8 796	0	0	0	0	1 254
Financial derivatives	**(4 960)**	0	(3 970)	(990)	0	0	0
Subordinated debt and Hybrid Tier 1 capital instruments	**48**	48	0	0	0	0	0
Total interest expenses	**5 148**	**8 855**	**(3 970)**	**(990)**	**0**	**0**	**1 254**
Net interest income	**1 582**	**(3 584)**	**2 972**	**412**	**147**	**2 889**	**(1 254)**

	2010						
	Total	At fair value through profit or loss			Held to	Loans and	Other
		FVO	Held for trading	Fair value hedge	maturity	receivables	liabilities
Deposits with credit institutions	**28**	28	0	0	0	0	0
Instalment loans	**4 910**	2 933	316	0	0	1 662	0
Notes, bonds and other interest-bearing securities	**2 481**	1 128	437	0	53	863	0
Financial derivatives	**(2 385)**	0	(1 633)	(751)	0	0	0
Total interest income	**5 034**	**4 088**	**(880)**	**(751)**	**53**	**2 525**	**0**
Loans from credit institutions	**13**	13	0	0	0	0	0
Senior securities issued	**9 395**	8 623	0	0	0	0	772
Financial derivatives	**(5 589)**	0	(5 018)	(571)	0	0	0
Subordinated debt and Hybrid Tier 1 capital instruments	**19**	19	0	0	0	0	0
Total interest expenses	**3 837**	**8 655**	**(5 018)**	**(571)**	**0**	**0**	**772**
Net interest income	**1 197**	**(4 567)**	**4 138**	**(180)**	**53**	**2 525**	**(772)**

NOTE 2 FEES AND COMMISSION EXPENSES

(Amounts in NOK 1 000 000)

	2011	2010
Expenses of banking services	12	12
Other transaction costs	9	8
Other income	2	1
Total fees and commission expenses	**19**	**18**

NOTE 3 NET UNREALISED GAIN/(LOSS) ON FINANCIAL INSTRUMENTS

(Amounts in NOK 1 000 000)

	2011					
	Total	At fair value through profit or loss			Loans and	Other
		FVO	Held for trading	Fair value hedge	receivables	liabilities
Instalment loans	**525**	522	3	0	0	0
Notes, bonds and other interest-bearing securities	**(168)**	(85)	16	0	(98)	0
Financial derivatives	**(252)**	0	(1 656)	1 404	0	0
Loans from credit institutions	**(3)**	(3)	0	0	0	0
Senior securities issued	**(544)**	855	0	0	0	(1 399)
Subordinated debt and Hybrid Tier 1 capital instruments	**(132)**	(132)	0	0	0	0
Net unrealised gain/(loss) on financial instruments	**(575)**	**1 156**	**(1 637)**	**1 404**	**(98)**	**(1 399)**

	2010					
	Total	At fair value through profit or loss			Loans and	Other
		FVO	Held for trading	Fair value hedge	receivables	liabilities
Instalment loans	**(186)**	(186)	0	0	0	0
Notes, bonds and other interest-bearing securities	**174**	29	(21)	0	166	0
Financial derivatives	**(1 468)**	0	(1 975)	507	0	0
Loans from credit institutions	**1**	1	0	0	0	0
Senior securities issued	**1 370**	2 040	0	0	0	(670)
Subordinated debt and Hybrid Tier 1 capital instruments	**21**	21	0	0	0	0
Net unrealised gain/(loss) on financial instruments	**(89)**	**1 905**	**(1 995)**	**507**	**166**	**(670)**

Unrealised gain/(loss) on financial instruments includes value changes on financial instruments classified as at fair value through profit or loss, as well as fair value adjustments on financial instruments in fair value hedges.

Changes in fair value arise from changes in market prices, interest rates, exchange rates, credit spreads and basis swap spreads and are reflected in the carrying values of financial instruments and in the income statement. Unrealised gains/(losses) are reversed over contracts' remaining lifetime when the instruments are held to maturity and are settled at contract terms. If the instruments are redeemed before maturity and any gain or loss is realised, the amount is reclassified to "Net trading income".

Financial derivatives in fair value hedges are measured at fair value through profit or loss. The hedged items include NOK 13.6 billion in Notes, bonds and other interest-bearing securities, and NOK 58.7 billion in Senior securities issued, that are classified as Loans and receivables and Other liabilities and are measured at amortised cost. Changes in fair value attributable to the risk hedged are recorded as part of the carrying value of the hedged items and are also recognised in the income statement as "Net unrealised gain/(loss) on financial instruments".

NOTE 4 NET TRADING INCOME

(*Amounts in NOK 1 000 000)*

	2011	2010
Gain/(loss) from repurchase of securities issued	121	41
Gain/(loss) from sale of notes and bonds	(12)	0
Net trading income	**109**	**41**

NOTE 5 SALARIES AND ADMINISTRATIVE EXPENSES

(Amounts in NOK 1 000 000)

	2011	2010
Salaries	40	46
Employer contributions	6	7
Pension costs	9	4
Other personnel benefits	3	1
Administrative expenses	18	16
Total salaries and administrative expenses	**77**	**75**
Average number of employees	*47.7*	*44.7*

NOTE 6 REMUNERATION

(Amounts in NOK 1 000)

The Company's remuneration policy is designed in accordance with the Regulation on remuneration in the financial service industry, and State's guidelines on remuneration for senior executives in state-owned companies. The aim of the remuneration policy is to attract and retain talented professionals, encourage better performance and reward further development and good results. The Board of Directors evaluates and approves remuneration policy annually. The Board in KBN has established a compensation committee, that prepares matters concerning remuneration for the Board's consideration.

Total remuneration consists of fixed salary, variable salary, pension benefit plans and other benefits. KBN has no share-based or option-based programs for the employees.

The remuneration policy supports the Company's strategy for attracting and retaining professional with high level of expertise, necessary to manage a total capital of approximately NOK 350 billion. The remuneration policy is underpinned by KBN's goal to provide public sector financing in the competitive environment, which is achieved through high level of competence and efficiency in all operational functions.

KBN maintains competitive salary level, but is not leading as compared with similar private sector companies. The main element in the total remuneration is fixed salary, reflecting an employee's role, experience and individual performance.

KBN has a variable salary scheme for the employees. Variable salary paid out in 2011 is based on performance and goal achievement in 2010. The Board has evaluated the variable salary scheme with respect to the new regulations becoming effective from 1 January 2011, and decided to replace performance-based variable salary with a profit sharing scheme. The profit sharing requires the achievement of the Company's overall financial targets in 2011. The profit sharing scheme includes all employees and gives an additional 1.5 month of the base salary. The total amount for profit sharing in 2011 was NOK 4.5 million.

	2011			
Remuneration to senior executives	**Fixed salary**	**Variable salary**	**Other benefits**	**Pension costs**
Petter Skouen (President & CEO)	1 968	461	175	729
Siv F. Galligani (Deputy CEO)	1 589	399	98	462
Martin Spillum (CFO)	1 764	937	17	430
Anette Berg (Head of Lending) (from 01.01.2011)	1 181	0	11	345
Karina Folvik (Head of Accounting and Financial Reporting)	1 287	741	19	295
Total remuneration to senior executives	**7 789**	**2 538**	**320**	**2 261**
Total remuneration to employees whose professional activities affect the risk positions of the institution	**17 423**	**3 388**	**455**	**2 468**
Total remuneration to the employees in the independent control functions	**5 480**	**1 733**	**150**	**702**

	2010			
Remuneration to senior executives	**Fixed salary**	**Variable salary**	**Other benefits**	**Pension costs**
Petter Skouen (President & CEO)	1 940	393	167	436
Siv F. Galligani (Deputy CEO)	1 479	264	93	292
Martin Spillum (CFO)	1 544	300	6	267
Anette Berg (Head of Lending) (from 01.01.2011)	0	0	0	0
Karina Folvik (Head of Accounting and Financial Reporting)	1 145	251	19	203
Total remuneration to senior executives	**6 108**	**1 208**	**285**	**1 198**
Total remuneration to employees whose professional activities affect the risk positions of the institution	**16 386**	**2 577**	**152**	**2 307**
Total remuneration to the employees in the independent control functions	**4 746**	**485**	**33**	**560**

The President & CEO has a termination benefit agreement of one year salary following termination of employment. Other senior executives have a period of notice of three months and no termination benefit following termination. The President & CEO has the same pension plan as the other employees with a benefit level of 66 per cent without a limitation to 12xNational insurance base amount. Pension costs include the cost of the defined benefit plan and provisions for contributions covering salary over 12x base amount.

Lending to employees has the same terms for senior executives as for the other employees. The President & CEO's mortgage as of 31 December 2011 had a balance of NOK 2.2 million at 3.45 per cent. The mortgage repayment period is 20 years.

Board of Directors	2011	2010
Chairman Else Bugge Fougner[1]	215	215
Vice-chairman Kristin Marie Sørheim[1] (until 22.06.11)	58	122
Vice-chairman Nils R Sandal[1] (from 22.06.11)	60	0
Board member Frode Berge	98	92
Board member Svein Blix (until 22.06.11)	48	92
Board member Nanna Egidius[2]	147	116
Board member Åmund T. Lunde[1,2]	205	155
Board member Martha Takvam[2]	147	116
Board member Rune Sollie[2] (from 22.06.11)	75	0
Board member employees' representative Ellen Eskedal Scavenius	98	47
Board member employees' representative Martin Spillum	0	45
Board member employees' representative Roald Fischer (from 22.06.11)	50	0
Total Board of Directors	**1 198**	**1 000**

[1]Member of compensation committee

[2]Member of audit committee

Control Committee	2011	2010
Chairman Brit Lund	51	49
Committee member Kristine Stray Ryssdal	0	15
Committee member Kjell Inge Skaldebø	32	31
Committee member Anne-Ma Tostrup Smith	32	15
Committee alternate member Roy Jevard[1]	7	13
Total Control Committee	**122**	**123**

[1]Remuneration to the alternate member is NOK 3 500 per meeting

Supervisory Board	2011	2010
Chairman Elin Eidsvik	21	19
Members	55	47
Total Supervisory Board	**75**	**66**

Fees to the statutory auditor	2011	2010
Statutory audit fees	791	701
Other financial audit and attestation services	837	854
Tax services	0	0
Other services not related to audit	29	53
Total fees excl. VAT	**1 657**	**1 607**

NOTE 7 PENSIONS

(Amounts in NOK 1 000)

KBN has a defined benefit plan that covers all employees and is administered through Kommunal Landspensjonskasse (KLP). The pension benefits cover retirement benefits, disability and death and survivor pensions. Pension benefits complement benefits from the National Insurance Scheme. The defined benefit plan is compliant 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 base salary including the National Insurance Scheme. KBN also has a contractual pension plan (AFP). The plan is included in the calculation of pension liabilities. Pension liabilities for salaries over 12xBase amount is expensed when incurred. Following the amendments of the guidelines on remuneration for senior executives in state-owned companies from 1 April 2011, the pension plan covering salaries over 12xBase amount has been closed.

The employer contributions to the defined benefit plan are recognised as expense.

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 defined benefit obligation

	31 December 2011	31 December 2010
Discount rate	2.60%	4.00%
Estimated wage growth	3.50%	4.00%
Expected growth in Base amount	3.25%	3.75%
Expected growth in benefit levels	2.48%	3.00%
Expected return on assets	4.10%	5.40%

Pension costs in 2011 are calculated based on economic estimates as of 31 December 2010. Pension liabilities as of 31 December 2011 is calculated based on economic estimates as of 31 December 2011.

Pension costs	**Funded plan**		**Unfunded plan**	
	2011	**2010**	**2011**	**2010**
Net periodic pension cost	6 100	5 452	1 348	827
Interest cost	2 102	1 964	411	288
Expected return on plan assets	(1 627)	(1 401)	0	0
Service cost	225	204	0	0
Actuarial (gain)/loss recognised in profit or loss	0	0	212	68
(Gain)/loss of change in pension plan	0	(3 180)	0	0
Employer contributions	959	877	248	157
Net pension costs	**7 758**	**3 916**	**2 219**	**1 340**

Pension liabilities	**Funded plan**		**Unfunded plan**	
	2011	**2010**	**2011**	**2010**
Defined benefit obligation	61 278	46 602	10 748	8 926
Plan assets	(32 643)	(28 242)	0	0
Unrecognised actuarial gain/(loss)	(9 873)	(2 075)	(3 444)	(3 566)
Employer contributions	2 645	2 296	1 030	756
Net pension liabilities	**21 407**	**18 581**	**8 334**	**6 115**

Movement in pension liabilities	**Funded plan**		**Unfunded plan**	
	2011	**2010**	**2011**	**2010**
Net pension liabilities as of 1 January	18 581	19 368	6 115	4 775
Net pension costs	7 758	3 916	2 219	1 340
Contribution to the pension scheme	(4 932)	(4 703)	0	0
Net pension liabilities as of 31 December	**21 407**	**18 581**	**8 334**	**6 115**

Movement in the fair value of plan assets	Funded plan	
	2011	**2010**
Fair value of plan assets as of 1 January	28 242	22 661
Expected return on plan assets	1 627	1 401
Actuarial gain/(loss)	(1 002)	328
Service cost	(225)	(204)
Contribution to the pension scheme incl. employer contribution	4 323	4 122
Benefits paid	(322)	(67)
Fair value of plan assets as of 31 December	**32 643**	**28 242**

NOTE 8 TAX

(Amounts in NOK 1 000 000)

	2011	2010
Current taxes	445	257
Changes in deferred taxes	(169)	36
Total income tax	**276**	**293**

Current taxes	2011	2010
Current tax payable	445	257
Withholding tax	0	0
Total current taxes	**445**	**257**

Reconciliation of effective income tax rate	2011	2010
Profit before tax	1 001	1 034
Calculated income tax (28 %)	280	290
Non-deductible expenses	0	12
Non-taxable revenue	(4)	0
Tax expense	**276**	**293**
Effective income tax rate	27.6%	28.3%

Deferred tax liability/(asset)	2011	2010
Deferred tax liability/(asset) as of 1 January	182	146
Changes in deferred tax	(169)	36
Deferred tax liability/(asset) as of 31 December	**14**	**182**

Temporary differences	2011	2010
Fixed assets	0	0
Pension liabilities	(30)	(25)
Provisions	(1)	(1)
Financial derivatives	503	526
Fair value changes	(423)	152
Total temporary differences	**49**	**652**
Deferred tax liability/(asset) (28 %)	**14**	**182**

NOTE 9 CLASSIFICATION OF FINANCIAL INSTRUMENTS

(Amounts in NOK 1 000 000)

2011	Total	At fair value through profit or loss			Held to	Loans and	Other
		FVO	Held for trading	Fair value hedge	maturity	receivables	liabilities
Deposits with credit institutions	**3 151**	2 350	0	0	0	801	0
Instalment loans	**210 189**	115 635	11 910	0	0	82 643	0
Notes, bonds and other interest-bearing securities	**116 657**	84 801	13 679	0	4 532	13 645	0
Financial derivatives	**36 889**	0	34 283	2 606	0	0	0
Total financial assets	**366 885**	**202 786**	**59 872**	**2 606**	**4 532**	**97 089**	**0**
Loans from credit institutions	**11 915**	510	0	0	0	0	11 405
Senior securities issued	**336 942**	278 251	0	0	0	0	58 692
Financial derivatives	**10 165**	0	9 047	1 118	0	0	0
Subordinated debt	**2 080**	2 080	0	0	0	0	0
Hybrid Tier 1 capital instruments	**663**	663	0	0	0	0	0
Total financial liabilities	**361 766**	**281 504**	**9 047**	**1 118**	**0**	**0**	**70 097**

2010	Total	At fair value through profit or loss			Held to	Loans and	Other
		FVO	Held for trading	Fair value hedge	maturity	receivables	liabilities
Deposits with credit institutions	**8 030**	6 779	0	0	0	1 251	0
Instalment loans	**185 679**	103 879	8 375	0	0	73 424	0
Notes, bonds and other interest-bearing securities	**95 610**	58 853	24 562	0	3 155	9 041	0
Financial derivatives	**26 155**	0	25 096	1 059	0	0	0
Total financial assets	**315 473**	**169 511**	**58 032**	**1 059**	**3 155**	**83 716**	**0**
Loans from credit institutions	**8 814**	989	0	0	0	0	7 825
Senior securities issued	**288 093**	252 697	0	0	0	0	35 396
Financial derivatives	**13 067**	0	11 121	1 947	0	0	0
Subordinated debt	**306**	306	0	0	0	0	0
Hybrid Tier 1 capital instruments	**672**	672	0	0	0	0	0
Total financial liabilities	**310 954**	**254 665**	**11 121**	**1 947**	**0**	**0**	**43 221**

NOTE 10 FINANCIAL INSTRUMENTS MEASURED AT AMORTISED COST

(Amounts in NOK 1 000 000)

	2011		2010	
	Carrying amount	Fair value	Carrying amount	Fair value
Instalment loans	82 643	82 689	73 425	73 346
Notes, bonds and other interest-bearing securities classified as Loans and receivables	13 645	13 669	9 041	9 157
Notes, bonds and other interest-bearing securities classifies as Held to maturity	4 532	4 564	3 155	3 131
Total financial assets measured at amortised cost	**100 820**	**100 922**	**85 621**	**85 634**
Senior securities issued	58 692	58 037	35 396	35 446
Total financial liabilities measured at amortised cost	**58 692**	**58 037**	**35 396**	**35 446**

NOTE 11 FAIR VALUE OF FINANCIAL INSTRUMENTS
(Amounts in NOK 1 000 000)

	2011			
	Level 1	**Level 2**	**Level 3**	**Total**
Deposits with credit institutions	0	2 350	0	2 350
Instalment loans	0	79 036	48 510	127 545
Notes, bonds and other interest-bearing securities	24 492	56 859	17 129	98 480
Financial derivatives	5 713	24 629	6 548	36 889
Total financial assets at fair value	**30 205**	**162 873**	**72 187**	**265 264**
Loans from credit institutions	0	510	0	**510**
Senior securities issued	0	0	278 251	**278 251**
Financial derivatives	384	5 094	4 686	**10 165**
Subordinated debt	0	0	2 080	**2 080**
Hybrid Tier 1 capital instruments	0	0	663	**663**
Total financial liabilities at fair value	**384**	**5 604**	**285 680**	**291 670**

	2010			
	Level 1	**Level 2**	**Level 3**	**Total**
Deposits with credit institutions	0	6 779	0	**6 779**
Instalment loans	0	70 690	41 564	**112 255**
Notes, bonds and other interest-bearing securities	3 836	63 453	16 126	**83 415**
Financial derivatives	784	19 315	6 056	**26 155**
Total financial assets at fair value	**4 620**	**160 237**	**63 746**	**228 603**
Loans from credit institutions	0	989	0	**989**
Senior securities issued	24 520	0	228 177	**252 697**
Financial derivatives	2 699	7 802	2 566	**13 067**
Subordinated debt	0	0	306	**306**
Hybrid Tier 1 capital instruments	0	0	672	**672**
Total financial liabilities at fair value	**27 219**	**8 792**	**231 722**	**267 732**

Reconciliation of movements in Level 3

	2010	**Purchase**	**Redemption**	**Gain/(loss)[2]**	**Transfers**	**2011**
Instalment loans	41 564	12 969	(4 349)	(921)	(754)	48 510
Notes, bonds and other interest-bearing securities	16 126	9 903	(10 460)	66	1 495	17 129
Financial derivatives	6 056	1 660	(2 955)	1 968	(181)	6 548
Total financial assets at fair value in Level 3	**63 746**	**24 531**	**(17 764)**	**1 113**	**560**	**72 187**
Senior securities issued[1]	228 177	131 463	(94 903)	7 222	6 292	278 251
Financial derivatives	2 566	3 569	(378)	(1 069)	(3)	4 686
Subordinated debt	306	1 565	0	209	0	2 080
Hybrid Tier 1 capital instruments	672	0	0	(9)	0	663
Total financial liabilities at fair value in Level 3	**231 722**	**136 597**	**(95 281)**	**6 353**	**6 289**	**285 680**

[1] Increase in bond debt classified as Level 3 is mainly due to the lack of observable market transactions in late 2011 and the uncertainty associated with indicative pricing of outstanding bond debt as of 31 December 2011

[2] Gain and loss include unrealised changes in fair value on the instruments carried as of 31 December 2011

	2009	**Purchase**	**Redemption**	**Gain/(loss)**	**Transfers**	**2010**
Instalment loans	33 596	13 070	(4 496)	0	(605)	41 564
Notes, bonds and other interest-bearing securities	15 806	9 164	(6 809)	309	(2 345)	16 126
Financial derivatives	594	3 326	(557)	2 679	14	6 056
Total financial assets at fair value in Level 3	**49 996**	**25 560**	**(11 862)**	**2 989**	**(2 937)**	**63 746**
Senior securities issued	165 529	108 574	(70 749)	8 893	15 930	228 177
Financial derivatives	741	1 765	(41)	99	2	2 566
Subordinated debt	667	0	(389)	28	0	306
Hybrid Tier 1 capital instruments	285	402	0	(15)	0	672
Total financial liabilities at fair value in Level 3	**167 222**	**110 742**	**(71 179)**	**9 004**	**15 932**	**231 722**

Level 3 sensitivity	10 bp change in credit spread
Instalment loans	(156)
Notes, bonds and other interest-bearing securities	(2)
Financial derivatives	(419)
Senior securities issued	369
Subordinated debt	7
Hybrid Tier 1 capital instruments	0
Total	**(201)**

Determination of fair value at Level 1 requires use of quoted market prices. The criteria for Level 1 inputs are described in "Accounting policies."

Fair value of financial instruments in Level 2 and 3 is determined mainly using discounted cash flow method, where future cash flows 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.

Deposits with credit institutions

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.

Instalment loans

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 when 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.

Notes and bonds

The best estimate of fair value is price quotations in an active market with many willing buyers and sellers at the 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.

Fair value of notes and bonds that do not have available market quotes at the reporting date is calculated using the discounted cash flow 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 policies."

Senior securities issued

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.

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 do not 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 cash flow 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 financial 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 cash flow 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.

NOTE 12 HEDGE ACCOUNTING

(Amounts in NOK 1 000 000)

KBN applies fair value hedge to transactions in economic hedges of interest rate and cross-currency risk, that meet specified criteria. Fair value hedge is applied at individual transaction level where hedging instrument is explicitly linked to the hedged item (”micro hedge”). Hedge effectiveness is measured on an ongoing basis and all ineffectiveness is recognised under ”Net unrealised gain/(loss) on financial instruments”.

Carrying value of financial instruments in fair value hedges

	2011	2010
Notes, bonds and other interest-bearing securities	13 645	9 041
Senior securities issued	58 692	35 396
Financial derivatives	1 488	(888)
Total	**73 824**	**43 550**

Fair value changes on financial instruments in fair value hedges

	2011	2010
Notes, bonds and other interest-bearing securities	(98)	166
Senior securities issued	(1 399)	(670)
Financial derivatives	1 404	507
Total	**(94)**	**3**

Fair value changes on financial instruments in fair value hedges are mainly due to the changes in interest rates and basis swap spreads.

NOTE 13 DEPOSITS WITH CREDIT INSTITUTIONS

(Amounts in NOK 1 000 000)

	2011	2010
Deposits with credit institutions without agreed period of notice	150	78
Deposits with credit institutions with agreed period of notice	2 350	6 779
Cash collateral pledged	651	1 172
Total deposits with credit institutions	**3 151**	**8 030**

Deposits with credit institutions include cash collateral pledged as additional security for derivative exposure. Cash collateral was previously recognised under ”Notes, bonds and other interest-bearing securities”. Collateral posted is derecognised from the balance sheet as cash and recognised as an asset under ”Deposits with credit institutions”.

NOTE 14 INSTALMENT LOANS

(Amounts in NOK 1 000 000)

	2011	2010
Principal amount	207 572	183 841
Accrued interest	1 327	1 076
Adjustment for fair value	1 247	722
Total loans to customers	**210 146**	**185 639**
Other loans	43	40
Total instalment loans	**210 189**	**185 679**

Geographic distribution

	2011	2010
Østfold	11 476	11 199
Akershus	18 986	19 934
Oslo	4 481	4 224
Hedmark	7 469	6 684
Oppland	6 714	6 000
Buskerud	14 606	11 864
Vestfold	7 753	6 889
Telemark	8 522	7 163
Aust-Agder	4 766	5 220
Vest-Agder	10 982	9 581
Rogaland	17 021	12 508
Hordaland	25 807	19 011
Sogn og Fjordane	6 396	5 884
Møre og Romsdal	14 111	12 882
Sør-Trøndelag	12 180	10 996
Nord-Trøndelag	10 042	8 525
Nordland	12 464	11 645
Troms	8 486	8 636
Finnmark	5 263	4 956
Svalbard	48	42
Loans to customers	**207 572**	**183 841**

NOTE 15 NOTES, BONDS AND OTHER INTEREST-BEARING SECURITIES

(Amounts in NOK 1 000 000)

Assets by issuer

	2011	2010
Domestic		
Issued by public bodies[1]	0	2 552
Issued by other borrowers	2 080	1 940
Non-domestic		
Issued by public bodies[1]	85 035	66 328
Issued by other borrowers	29 542	24 792
Total notes, bonds and other interest-bearing securities	**116 657**	**95 610**

[1]Issued by or guaranteed by sovereigns, central banks, regional authorities and multilateral development banks.

Assets by maturity

	2011	2010
Under 1 year	53 818	46 006
1-5 year	60 911	45 701
Over 5 year	1 927	3 903
Total notes, bonds and other interest-bearing securities	**116 657**	**95 610**

NOTE 16 OTHER ASSETS

(Amounts in NOK 1 000 000)

Other assets	2011	2010
Intangible assets	1	1
Fixed assets	11	14
Other assets	1	1
Prepaid, non-accrued expenses and accrued income	2	2
Total other assets	**15**	**17**

NOTE 17 LOANS FROM CREDIT INSTITUTIONS

(Amounts in NOK 1 000 000)

	2011	2010
Loans from credit institutions without agreed period of notice	0	0
Loans from credit institutions with agreed period of notice	510	989
Cash collateral received	11 405	7 825
Total loans from credit institutions	**11 915**	**8 814**

Loans from credit institutions include cash collateral received as additional security for derivative exposure. Cash collateral was previously recognised under ”Notes, bonds and other interest-bearing securities”. Collateral received is recognised on the balance sheet as cash and a liability to the counterparty under ”Loans from credit institutions”.

NOTE 18 SENIOR SECURITIES ISSUED

(Amounts in NOK 1 000 000)

	2011	2010
Senior securities issued (nominal amounts) at 1 January	**290 231**	**224 418**
New issuance	142 341	138 231
Redemptions	(107 578)	(91 872)
Amortisation	(81)	(374)
Translation differences	13 702	19 828
Senior securities issued (nominal amounts) at 31 December	**338 615**	**290 231**
Accrued interest	2 667	2 746
Adjustment for fair value	(4 340)	(4 884)
Total senior securities issued	**336 942**	**288 093**
Gain from adjustment for fair value as a result of change in credit risk	*381*	*302*

There is no breach in debt covenants as at 31 December 2011.

Adjustments to fair value as a result of the Company’s credit risk is a part of the change in fair value not attributable to changes in parameters associated with market risk. It is assumed that the market risk in senior securities issued is limited to changes in observable money market interest rates. Changes in fair value attributable to changes in credit risk in senior securities issued are calculated as the difference between the discounted values applying:

a) Relevant money market interest rates at the reporting date adjusted for the credit risk at time of recognition; and
b) Relevant money market interest rates at the reporting date adjusted for the credit risk at the reporting date.

NOTE 19 FINANCIAL DERIVATIVES

(Amounts in NOK 1 000 000)

KBN uses financial derivatives solely for hedging against exposure to interest rate and currency risks arising in the Company’s business activities. KBN enters into swap contracts with counterparties with high credit rating and all derivative exposure is subject to risk limits approved by the Board. Bond debt denominated in foreign currency is hedged with interest rate and cross-currency swaps so that KBN only has limited exposure against changes in 3-month money market interest rates in NOK, USD and EUR. Swap contracts linked to the commodity index or equity index are used to hedge risk in borrowing where the return is linked to such indexes.

Borrowings in foreign currency are converted to Norwegian kroner through basis swaps in which KBN receives interest payments in foreign currency and pays the interest in Norwegian kroner. Interest rate risk arising from fixed interest rate on loans to customers is hedged with interest rate swaps and FRA. Interest rate and currency swaps are also used to hedge against market risk in the liquidity portfolio. The Company has no credit derivatives in the portfolio.

Counterparty risk arising from derivative contracts is mitigated by using standard ISDA-agreements that give the right to offset liabilities and assets in the case of default. In addition, the Company enters into collateral agreements with all new swap counterparties. Derivative exposure is monitored on an ongoing basis.

	2011			2010		
	Nominal value	Assets	Liabilities	Nominal value	Assets	Liabilities
Held for trading:						
Interest rate derivatives	102 404	848	1 525	119 755	1 708	1 515
Currency derivatives	410 817	23 111	7 347	351 936	13 356	9 454
Equity-related derivatives	86 393	10 291	159	67 862	9 951	150
Commodity-related derivatives	1 436	33	16	2 417	81	3
	601 050	**34 283**	**9 047**	**541 971**	**25 096**	**11 121**
Fair value hedges:						
Interest rate derivatives	51 461	1 661	32	26 720	808	156
Currency derivatives	17 843	944	1 086	7 010	251	1 790
	69 304	**2 606**	**1 118**	**33 731**	**1 059**	**1 947**
Total financial derivatives	**670 354**	**36 889**	**10 165**	**575 702**	**26 155**	**13 067**

Most financial derivatives are accounted for as ”Held for trading”, with the exception of contracts designated as hedging instruments in fair value hedges. As standard master netting agreements do not give a currently enforceable legal right to offset the recognised amounts, the financial derivatives are presented gross in statement of financial position. All financial derivatives are measured at fair value through profit or loss.

NOTE 20 COLLATERAL

(Amounts in NOK 1 000 000)

	2011	2010
Cash collateral received	11 405	7 825
Cash collateral pledged	(651)	(1 172)
Total cash collateral	**10 754**	**6 652**

Cash collateral received or pledged as additional security for derivative exposure is presented as cash received or cash paid respectively, with a relevant liability or asset item. Cash collateral is a part of the Company’s liquidity management and was previously presented under “Notes, bonds and other interest-bearing securities”.

NOTE 21 SUBORDINATED DEBT

(Amounts in NOK 1 000 000)

	Currency	Nominal amount in CCY	Redemption right	Interest rate	2011	2010
Perpetual subordinated loan capital[1]	NOK	400 million	2020	5.60%[2]	400	400
Perpetual subordinated loan capital[1]	NOK	102 million	2019	4.01%[2]	102	102
Perpetual subordinated loan capital[1]	EUR	20 million	2012	6.29%	155	156
Perpetual subordinated loan capital	NOK	8 million		4.38%[2]	8	8
Perpetual subordinated loan capital	JPY	3 billion	2012	1.61%	233	215
Ordinary subordinated loan capital	CAD	275 million	2016	3.74%	1 617	0
Ordinary subordinated loan capital	NOK	80 million	2012	3.19%[2]	80	80
Total subordinated debt					**2 594**	**961**

[1] Hybrid Tier 1 capital instruments

[2] Interest rate is adjusted every 3 months

NOTE 22 SHARE CAPITAL

	2011		2010	
	Number of shares	Share in %	Number of shares	Share in %
The Kingdom of Norway	1 220 625	100	1 220 625	100
Total	**1 220 625**		**1 220 625**	

NOTE 23 RISK MANAGEMENT

Organisation of risk management

Board of Directors. The Board of Directors in KBN determines the long-term risk strategy through a sustainable risk policy, predefined risk limits and delegation of authority. All risks are subject to internal limits.

Delegation of authority. General authorisation defines the authority to approve loans to customers, and take risk positions in all financial operations.

Responsibility. The President & CEO has an overall responsibility for risk taking and risk management in the Company.

Risk management. The Board of Directors determines the risk policies and limits, including transactions in new products. The Board reviews financial risk policy at least twice a year. Lending policies are reviewed at least annually. The Board assesses the capital situation and approves KBN's principles for capital management annually.

Risk controlling. Risk controlling entities are independent from the operational departments: Lending, Funding and Treasury. KBN portfolio and risk management system is Adaptiv360 delivered by Sungard. Internal audit is performed by KPMG, and statutory audit is performed by Ernst & Young.

Risk exposure

All material risks of the Company are identified and monitored to ensure that they are within the conservative internal risk framework aiming to ensure KBN's credit rating and access to the interbank markets. Credit risk and liquidity risk are generally low. The Company takes no open risk positions in interest rates or foreign currencies.

The following risk factors are identified as the most important for KBN's goal achievement:

- Credit risk and counterparty risk
  - Loss on loans granted to customers
  - Counterparty default – derivative transactions
  - Counterparty default – liquidity portfolio
  - Spread risk
- Market risk
  - Interest rate risk and cross currency risk
- Capital level
- Liquidity risk
- Operational risk

Credit risk

KBN's assets consist of loans to municipalities and a liquidity portfolio of bonds and notes issued by or guaranteed by sovereigns, regional authorities, multilateral development banks, covered bonds and financial institutions with high credit rating.

Framework for credit risk management. The credit risk in loans granted is based on the economic assessment of municipalities. The analysis takes into account quantitative and qualitative key performance indicators, including operating conditions, regulatory framework, financial standing, debt profile, management and an overall economic assessment of the geographic region. The rating estimates based on the internal credit ranking corresponds to the range between AA- and AA+.

All financial transactions in bonds, notes and derivatives are subject to the conservative risk policy. The lowest acceptable rating for investments in bonds and notes is A2/A from Moody's and Standard and Poor's.

The credit risk in derivative transactions is managed by using standard ISDA agreements. In addition, KBN enters into collateral agreements with all new swap counterparties.

Credit risk management consists of a set of tasks and processes aimed to monitor and control credit risk on an ongoing basis. The management assesses and approves all new limits and counterparties, based on KBN's internal credit risk models, available risk capital, counterparties' external ratings, types of financial instruments and tenor. The Board of Directors annually approves the credit policy for municipal lending, and all special exposures are assessed by the management.

Credit risk assessment. KBN's client base is the local government sector, which has high creditworthiness. The credit risk in loans granted is limited to payment delays. 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's able to meet its payment obligations.

KBN enters into derivative transactions with financial institutions to hedge exposure to interest rates and FX-rates. All new transactions are subject to strict rating requirements and also require an ISDA agreement and a collateral agreement with the counterparty.

Credit risk related to the liquidity portfolio is low. An average rating of the portfolio is AA+ (based on the lowest of S&P and Moody's), and 73 per cent of the portfolio is invested into securities with a BIS-weight of 0 per cent. Average maturity of the portfolio was 1.2 years as of 31 December 2011. The spread risk in the portfolio is managed at a counterparty level and is limited due to the portfolio's short maturity.

Market risk

Market risk occurs in the form of interest rate risk and currency risk. KBN's risk policy allows only low exposure to changes in interest rates and FX-rates. The interest rate and currency risk are managed through matching of assets and liabilities as well as through economic hedges with derivative instruments.

Capital management

KBN is subject to the Capital Adequacy requirements and minimum standards for regulatory capital. In addition the Company assesses its capital level taking into account all substantial risks the Company is exposed to. The Board of Directors discusses the capital level and assesses all the risks annually to ensure that the Company's capital level is sufficient based on the actual and expected risk exposure.

In the process of capital assessment, the management identifies and measures all the risks the Company may be exposed to and estimates the capital level necessary to cover all external and internal risks. The following risks are assessed separately: credit risk, market risk, liquidity risk and operational risk. In addition the management considers concentration risk, key personnel risk, strategic risk, business risk, reputation risk, risk of changes in regulatory framework and compliance risk.

The Board pays special attention to the risk of changes in regulatory framework. The impending changes to CRD IV and to the national capital requirements increase the Company's capital charge. KBN aims to increase the core capital ratio to minimum 9 per cent by 30 June 2012.

Liquidity risk

Liquidity risk is managed by maintaining a liquidity portfolio which over time equals a minimum of 12 months' net debt redemptions. Surplus liquidity is invested in liquid bonds and notes with high credit rating and short time to maturity. Liquidity reserves should constitute between 25 and 35 per cent of total assets. KBN also aims to have duration of the liabilities equal or exceeding that of the assets.

Operational risk

Operational risk arises from all functions and is minimised by effective internal control, high professional level and focus on ethical behaviour. The management reports to the Board on the operational risk and loss or near-loss events.

NOTE 24 CREDIT RISK

(*Amounts in NOK 1 000 000)*

KBN has exposure to municipal sector, as well as sovereigns, financial institutions, local authorities, multilateral development banks and covered bonds 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 to financials must have a rating of A/A-1 or above.

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. KBN has had no losses on loans to customers in 2011. There is no evidence of impairment as at 31 December 2011.

KBN does not issue financial guarantees.

Amounts in the table below represent actual credit exposure

	2011								
Maturity		**< 1 year**				**> 1 year**			
Risk class	**A-2**	**A-1/A-1+**	**Not rated**	**A-**	**A**	**AA**	**AAA**	**Not rated**	**Total**
Sovereigns and central banks	0	7 421	0	0	0	1 115	5 136	0	**13 673**
Regional authorities *	0	18 273	18 869	0	674	21 207	12 837	189 604	**261 464**
Multilateral development banks	0	7 909	0	0	0	0	12 135	0	**20 044**
Financial institutions	230	14 175	1 474	0	1 188	195	184	0	**17 446**
Securitisation	0	279	0	0	0	0	0	0	**279**
Covered bond	0	4 057	0	0	0	0	9 840	0	**13 897**
Total	**230**	**52 114**	**20 343**	**0**	**1 862**	**22 517**	**40 132**	**189 604**	**326 802**

* Including loans to municipal sector of NOK 210.1 billion.

Credit exposure by country

	2011								
Maturity	**< 1 year**			**> 1 year**					
Risk class	**A-2**	**A-1/A-1+**	**Not rated**	**A-**	**A**	**AA**	**AAA**	**Not rated**	**Total**
Australia	0	1 085	0	0	0	84	0	0	1 169
Belgium	0	196	0	0	0	619	0	0	815
Canada	0	218	0	0	674	124	0	0	1 017
Denmark	37	9 590	0	0	0	0	557	0	10 183
Finland	0	598	0	0	0	0	498	423	1 519
France	0	7 768	0	0	0	0	2 799	0	10 567
Japan	0	0	0	0	0	166	0	0	166
Netherlands	0	2 452	0	0	0	111	266	0	2 829
Norway	0	893	18 869	0	1 188	0	3 037	188 239	212 226
Spain	0	572	0	0	0	638	0	0	1 210
United Kingdom	193	1 586	0	0	0	0	6 325	0	8 105
Supranational	0	7 909	0	0	0	0	11 964	0	19 873
Switzerland	0	958	0	0	0	0	0	0	958
Sweden	0	706	0	0	0	360	3 311	941	5 319
Germany	0	17 243	1 474	0	0	20 415	11 328	0	50 461
Austria	0	340	0	0	0	0	47	0	387
Total	**230**	**52 114**	**20 343**	**0**	**1 862**	**22 517**	**40 132**	**189 604**	**326 802**

NOTE 25 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'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 with 100 basis points change in interest rates (parallel shift).

The Board has adopted a total limit for interest rate risk of NOK 24 million. The interest rate sensitivity is measured assuming 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:

	100 bp change in interest rate
NOK	(16)
USD	(6)
EUR	18
Total	**(4)**

Interest rate sensitivity can affect the income statement during the next three month period.

NOTE 26 CURRENCY RISK

(Amounts in NOK 1 000 000)

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 income statement 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.

	2011		**2010**	
Currency	**Net position**	**10% change in FX-rate**	**Net position**	**10% change in FX-rate**
USD	(39)	4	(90)	9
EUR	(4)	0	3	0
Other currencies	1	1	4	0
Total	**(42)**	**5**	**(84)**	**10**

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 2011. Sensitivity analysis does not take into account correlation between FX-rates and other market risk factors.

NOTE 27 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 to manage short-term liquidity.

Exposure by maturity	Total	< 1 month	1-3 months	3-12 months	1-5 years	>5 years	Without maturity
Deposits with credit institutions	**3 151**	3 001	0	0	0	0	150
Instalment loans	**210 189**	3 839	4 493	10 745	19 441	171 671	0
Notes, bonds and other interest-bearing securities	**116 657**	15 835	1 927	12 428	86 467	0	0
Total assets	**329 997**	**22 674**	**6 420**	**23 173**	**105 907**	**171 671**	**150**
Loans from credit institutions	**11 915**	11 405	0	510	0	0	0
Senior securities issued	**336 942**	4 213	13 465	46 538	212 451	60 277	0
Other liabilities	**542**	29	18	452	14	0	30
Subordinated debt	**2 080**	0	0	80	1 759	0	241
Hybrid Tier 1 capital instruments	**663**	0	0	0	0	0	663
Total liabilities	**352 143**	**15 647**	**13 482**	**47 580**	**214 224**	**60 277**	**934**
Financial derivatives	**26 725**	**(149)**	**3 049**	**3 226**	**15 547**	**5 051**	**0**
Net liquidity exposure	**4 578**	**6 878**	**(4 013)**	**(21 180)**	**(92 769)**	**116 446**	**(784)**

Exposure by interest rate reset	Total	< 1 month	1-3 months	3-12 months	1-5 years	>5 years	Without maturity
Deposits with credit institutions	**3 151**	3 001	0	0	0	0	150
Instalment loans	**210 189**	69 086	52 303	46 713	34 379	7 708	0
Notes, bonds and other interest-bearing securities	**116 657**	20 141	28 131	19 716	46 784	1 885	0
Total assets	**329 997**	**92 229**	**80 434**	**66 429**	**81 163**	**9 592**	**150**
Loans from credit institutions	**11 915**	11 405	0	510	0	0	0
Senior securities issued	**336 942**	25 424	89 469	72 574	130 699	18 777	0
Other liabilities	**542**	29	18	452	14	0	30
Subordinated debt	**2 080**	80	7	234	1 759	0	0
Hybrid Tier 1 capital instruments	**663**	102	402	159	0	0	0
Total liabilities	**352 143**	**37 040**	**89 896**	**73 928**	**132 472**	**18 777**	**30**
Financial derivatives	**26 725**	**(1 116)**	**(48 830)**	**11 801**	**55 451**	**9 419**	**0**
Net liquidity exposure	**4 578**	**54 073**	**(58 293)**	**4 301**	**4 142**	**235**	**121**

NOTE 28 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 supplementary 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.

	2011			2010		
	Book value	**Risk-weighted assets**	**Minimum capital requirement**	**Book value**	**Risk-weighted assets**	**Minimum capital requirement**
Credit risk						
Sovereigns and central banks	6 390	238	19	7 652	0	0
Regional governments and local authorities	265 591	43 806	3 505	219 264	35 523	2 842
Of which are Norwegian municipalities	*208 782*	*43 778*	*3 502*	*175 414*	*35 083*	*2 807*
Public sector entities	9 761	0	0	3 601	0	0
Multilateral development banks	20 043	0	0	15 000	0	0
Financial institutions	31 090	4 260	341	32 060	6 412	513
Of which counterparty exposure on derivatives	*22 929*	*2 628*	*210*	*26 580*	*5 316*	*425*
Corporates	0	0	0	415	83	7
Claims secured by residential property	1 407	1 407	113	1 514	549	44
Covered bonds	13 897	1 390	111	4 217	422	34
Other assets	15	15	1	14	14	1
Securitisation	279	70	6	0	0	0
Total credit risk	**348 472**	**51 185**	**4 095**	**268 738**	**43 002**	**3 440**
Market risk	**13 687**	**539**	**43**	**32 883**	**2 799**	**224**
Operational risk—Basic Indicator Approach		**2 373**	**190**		**1 132**	**91**
Minimum capital requirement		**54 097**	**4 328**		**46 934**	**3 755**
Total capital ratio			**13.22 %**			**9.86 %**
Core capital ratio			**9.79 %**			**9.15 %**

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:

	2011	2010
Core capital:		
Share capital	1 221	1 221
Retained earnings	3 373	2 813
Total equity	**4 594**	**4 034**
Hybrid Tier 1 capital instruments	666	644
Deferred tax asset	0	0
Goodwill	(1)	(1)
Allocated to dividend	0	(165)
Unrealised gains on liabilities attributable to changes in own credit risk	36	(217)
Total Tier 1 capital	**5 295**	**4 296**
Supplementary capital:		
Ordinary subordinated debt	1 651	80
Perpetual subordinated debt	204	254
Total supplementary capital	**1 855**	**334**
Total capital	**7 150**	**4 630**

Subordinated capital has been calculated pursuant to The Regulation governing calculation of subordinated capital for financial institutions. Unrealised gain/loss on liabilities that are due to changes in own credit risk include both non-derivative and derivative liabilities.

Statement from the Board of Directors

Pursuant to §5-5 of the Securities Trading Act

We confirm that the financial statements for 2011 are, 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 true and fair view of the Company's assets, liabilities, financial position and profit or loss.

To the best of our knowledge, the financial statements provide a true and fair view of important events during the accounting period in question and their effects on the financial statements, and also the principal risks and uncertainties facing the Company in the next accounting period.

Oslo, 31 December 2011
16 March 2012
The Board of Directors
Kommunalbanken AS

Else Bugge Fougner Chairman	Nils R. Sandal Vice Chairman	Frode Berge Member	Nanna Egidius Member
Roald Fischer Member	Åmund T. Lunde Member	Ellen Eskedal Scavenius Member	Rune Sollie Member

Martha Takvam
Member

Petter Skouen
President & CEO

To the Annual Shareholders' Meeting in Kommunalbanken AS

AUDITOR'S REPORT

Report on the financial statements

We have audited the accompanying financial statements of Kommunalbanken AS, which comprise the statement of financial position as at 31 December 2011, the statements of income, comprehensive income, cash flows and changes in equity for the year then ended and a summary of significant accounting policies and other explanatory information.

The Board of Directors' and President & CEO's responsibility for the financial statements

The Board of Directors and President & CEO are responsible for the preparation and fair presentation of these financial statements in accordance with the International Financial Reporting Standards as adopted by the EU, and for such internal control as the Board of Directors and President & CEO determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with laws, regulations, and auditing standards and practices generally accepted in Norway, including International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements of Kommunalbanken AS 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 2011 and its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards as adopted by the EU.

Report on other legal and regulatory requirements

Opinion on the Board of Directors' report and the statement on corporate governance

Based on our audit of the financial statements as described above, it is our opinion that the information presented in the Directors' report and the statement on corporate governance concerning the financial statements, the going concern assumption and the proposal for the allocation of the result is consistent with the financial statements and complies with the law and regulations.

Opinion on registration and documentation

Based on our audit of the financial statements as described above, and control procedures we have considered necessary in accordance with the International Standard on Assurance Engagements (ISAE) 3000, "Assurance Engagements Other than Audits or Reviews of Historical Financial Information", it is our opinion that the Board of Directors and President & CEO have fulfilled their duty to ensure that the Company's accounting information is properly recorded and documented as required by law and generally accepted bookkeeping practice in Norway.

Oslo, 16 March 2012
Ernst & Young AS

Eirik Tandrevold
State Authorised Public Accountant (Norway)

(This translation from Norwegian has been made 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 2011.

The Control Committee recommends that the annual report and accounts presented be approved as Kommunalbanken's accounts for 2011 and that the application of profits is adopted by the Annual Shareholders' Meeting in accordance with the Board of Directors' proposals.

Oslo, 21 March 2012
Control Committee for Kommunalbanken AS

Britt Lund
Chairman

Anne-Ma Tostrup Smith

Kjell Inge Skaldebø
Vice Chairman

Supervisory Board's statement

To the Annual Shareholder's Meeting of Kommunalbanken AS

In accordance with § 15 in Kommunalbanken's Articles of Association, the annual accounts and report for 2011 have been examined by the Supervisory Board.

The Supervisory Board recommends that the Board of Directors' proposals for the operating statement and balance sheet as well as the application of profit, NOK 724 000 000, is adopted by the Annual Shareholders' Meeting.

Oslo, 19 April 2012
Supervisory Board for Kommunalbanken AS

Elin Eidsvik
Chairman

KBN and social responsibility

KBN's social responsibility role is described in the Ownership Report, No. 13 (2010-2011):
"The Bank's sector policy function as a reliable supplier of credit to local government with the best possible loan terms, is the core of the bank's social responsibility."

At the same time KBN shall contribute to sustainable development and long-term value creation through responsible business practices that protect the environment while furthering ethical and social issues.

With nearly 50 percent share in the market for loans to the local government sector, KBN is a significant player in society. KBN provides funding so that municipalities, counties and municipal corporations can realize their projects.

Lower interest on environmental projects

To ensure that municipalities can realize their energy and climate plans, KBN decided in 2010 to provide a separate interest rate product for climate-friendly investments. Our green floating rate is lower than the ordinary interest rate and can be used for projects that are rooted in local plans for the environment and climate. They may be investments in the areas of energy efficiency, renewable energy, waste management, recycling, pedestrian and bicycle paths, water quality, environmental-friendly means of transport and facilities for active outdoor life. As of 31 December 2011 loans totalling NOK 6.4bn were granted at the green floating interest rate.

Skill enhancement

KBN aims to enhance the expertise of municipal staff in the economic and finance sectors. KBN would like to work on a broad basis with organizations that are central within local government. KBN contributes financially with expertise and technical assistance where events are concerned. Detailed annual agreements are entered into with major partners.

The AF Kommunepartner works to make financial information available to local government through learning materials, teaching, courses, seminars / workshops and general advice. KBN is a partner in AF Kommunepartner.

In order to encourage and enhance skills, KBN has also instituted the annual "Local Municipal Economist" prize and a student scholarship.

Environmentally friendly management of KBN

The office facilities provide good opportunities for energy efficiency. Energy consumption is monitored by a network of sensors for power, cooling, and heating. The detailed survey and monitoring of energy consumption provides a unique opportunity to control and do something about KBN's own consumption. Implementation of surveys on recycling, waste reduction and systems, resulting in reduced energy consumption will continue.

Due to the nature of the activity, KBN's direct effect on total greenhouse gas emissions and environmental impact is minimal. An annual environmental report is created, which shows trends within the various criteria KBN measures. The carbon footprint is based on a climate calculator for businesses.

Suppliers

Environmental criteria are set for purchases, and environmentally-certified suppliers are selected in the place of suppliers who are unable to document environmentally friendly operations. The number of environmentally friendly products used by KBN has doubled since the survey began in 2009.

Miljøfyrtårn®

Articles of Association of Kommunalbanken AS

The Articles of Association were last changed by the Annual General Meeting 22 June 2011, and approved by the Financial Supervisory Authority of Norway 20 July 2011

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 Kommunal-bank.

The State's shares may be assigned to municipalities, counties, intermunicipal companies and municipal pension funds. Such assignment will be done in accordance with the Company's aim of maintaining highest possible creditworthiness.

§ 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 comprise of between five (5) and nine (9) members. Two (2) of the elected members of the Board shall be elected by and from amongst the Company's employees. For these members two (2) personal deputies 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
9. Prepare statements on remuneration policy.

§ 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 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 Control 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 Control 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 Control Committee are entitled to be present at the meetings of the Supervisory Board with the right to speak and the right of initiative. The Ministry of Local Government and Regional Development can participate in the Supervisory Board meeting with up to two observers.

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 income statement and balance sheet, including any consolidated income statement 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 Ministry of Local Government and Regional Development 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 to the Board of Directors in accordance with § 8 of the Articles of Association.

4. Elections of members and deputy members of the Control Committee in accordance with § 17 of the Articles of Association.

5. The Board of Director's statement on remuneration policy.

6. Other business referred 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 Financial Supervisory Authority of Norway ("Finanstilsynet").

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 Financial Supervisory Authority of Norway ("Finanstilsynet"), and shall annually deliver a report on its work to the Supervisory Board, the Annual General Meeting and The Financial Supervisory Authority of Norway ("Finanstilsynet")

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 Control 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 67 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.

Governing bodies

The Board of Directors

Else Bugge Fougner, Barrister-at-law (Supreme Court), Chairman
Nils R. Sandal, County mayor of Sogn og Fjordane, Vice Chairman
Frode Berge, Head of Stavanger Regional Business Development
Nanna Egidius, Director of Strategic Planning, Lillehammer municipality
Åmund T. Lunde, CEO of Oslo Municipality Pension Fund
Rune Sollie, Chief AFC at Statoil Fuel & Retail
Martha Takvam, CEO of Telenor Real Estate
Ellen E. Scavenius, Head of Treasury, employee representative
Roald Fischer, Head of Documentation, employee representative

Alternates to the Employee Representatives
Thomas Mathisen for E. E. Scavenius
Lise Bakken for R. Fischer

Supervisory Board

Elin Eidsvik, CEO of Hamarøy municipality, Chairman
Bjørn Arild Gram, mayor of Steinkjer municipality, Vice Chairman
Svein Ludvigsen, County Governor of Troms
Hanne Braathen, member of Storfjord municipal council
Svein Skaaraas, CEO of Hamar municipality
Tore Sirnes, CEO of Sandnes municipality
Berit Flåmo, Mayor of Frøya municipality
Karen Marie Hjelmeseter, County Chairman of the Centre Party, Sogn og Fjordane county
Knut Wille, CEO of Skien municipality
Anita Orlund, member of the Skedsmo municipal council
Arne Johansen, retired CEO of Harstad municipality
Bjørn Ove Nyvik, Chief Accountant, employee representative

Alternates to the supervisory board
Berit Koht, Chief Accountant of Troms county
Hans Seierstad, Mayor of Østre Toten municipality
Mona Skanke, member of Porsanger municipal council
Rune Øygard, Mayor of Vågå municipality

Observers to the supervisory board
Erik Kjeldstadli, Deputy Secretary, The Ministry of Local Government and Regional Development
Thor Bernstrøm, Assistant Director General, Ministry of Local Government and Regional Development

Control Committee

Britt Lund, Chairman
Kjell Inge Skaldebø, CEO of Åfjord municipality, Vice Chairman
Anne-Ma Tostrup Smith, lawyer, Statoil ASA

Deputy member
Roy Jevard, CEO of Melhus municipality

Auditor

Ernst & Young AS
Eirik Tandrevold, State Authorised Public Accountant

Internal auditor

KPMG AS
Are Jansrud, State Authorised Public Accountant

Management

Directors

Petter Skouen
President & CEO

Siv F. Galligani
Deputy CEO

Section heads

Martin Spillum, CFO

Karina Folvik, Accounting & Financial Reporting

Anette Berg, Lending

Thomas Møller, Capital Markets & Funding

Ellen Eskedal Scavenius, Treasury

Knut Andresen, MO - IT & Compliance

Frank Øvrebø, MO - Credit Analysis & Risk Management

Hilde Jordfald, HR

Tor Ole Steinsland, Corporate Communication

Kommunalbanken Norway finances local solutions

If KBN put up a sign saying that this day care centre, school, nursing home, swimming pool or cultural centre was funded by KBN, such signs would be seen all over Norway. Through our involvement over the years, many great projects have seen the light, and KBN is proud every time we are able to finance projects with favourable interest rates - often with our green lending rates. Here are some examples from 2011.

Ranemsletta barnehage

The "Green" day care centre in the Overhalla municipality was officially opened in 2011. It is a large and modern day care centre, with a budget of NOK 25 million. Thirty employees and 85 children spend their days here. KBN was invited to the opening and recorded a high approval, as far as the building was concerned, from the municipality's management to the day care center's staff and especially the children. The kindergarten is built to Passive House Standards and thus qualifies for KBN's green lending rate.

Hardangerbrua – Norway's longest suspension bridge

is a strategic hub and will be of great importance for two major transport routes running through inner Hordaland district. KBN is the lender providing NOK 1bn towards this gigantic project.

The benefits are great for the local community, the region, and the country as a whole when the bridge is completed in June 2013, says Einar Lutro, Executive Chairman of the bridge company, Hardangerbrua AS. The cost is estimated at NOK 2.3 bn.

Mr. Lutro says that KBN offered the most favorable terms of financing. It was the main reason they chose KBN when Hardangerbrua AS was bidding for loans.

Nordmørsterminalen

In Kristiansund, the Nordmøre terminal is ideally located between the bus station and fast ferry. In addition to offices the building contains a waiting room for travelers on a round-the-clock basis. The terminal has many clever solutions with regard to environmental and energy consumption. They include replacing the oil-fired boiler with a gas-fired boiler. A seawater pump cools the air, and new technologies for controlling light and ventilation have been installed. The building was financed with a green lending rate- an interest rate that is 0.10 percentage points lower than the ordinary rate. The building is part of the municipality's energy and climate plan.

Nordlysbadet

Alta's residents have a water theme park of which they can be proud. After three years of construction, the huge hole in the city's heart has become a beautiful oasis. The world's northernmost water theme park, located in the centre of Alta. Nordlysbadet cost a total of NOK 240 million, of which KBN is the largest lender. The theme park is meant to meet the needs of the inhabitants, but it also provides a positive effect on local businesses.

Banking agreements

There is much to be gained by placing the main bank agreement to tender, says Chief Financial Officer Knut Thiblin with Akershus County Council. They have just completed their tendering process and the result was a new bank connection and much better conditions. KBN had an important role in this process, says the CFO.

Most municipalities and counties have focused on measures that can reduce their operating and financial expenses. On the financial side, it has become more common to place their main bank contract to tender as an important measure in order to reduce expenses. Outsourcing of main banking agreements, to which the Public Procurement Act and related regulations are required by law, shall take place every four years.
All municipalities have many payment transactions and large deposits during the year. This means that smaller municipalities have as much to save as large municipalities, seen in relation to each other's cost levels. Municipalities and counties are attractive customers for banks, and it gives the municipality significant bargaining power. It is simply a matter of exploiting this potential as a possible customer, says KBN's Torger M. Jonasen.

KBN has a great deal of experience and expertise being advisor for municipalities and counties concerning competing outsourcing of financial institutions. The tender process is very extensive and time consuming. A lot must be defined in advance and all the data must be available.

The procedure for obtaining a new main bank agreement

KBN is happy to assist with advice on main bank agreements. KBN provides advice on everything from A to Z, through the following services:

- review of existing bank agreements, account organization and payment
- advice in connection with the municipality's bank relationships
- assistance with establishing a new banking agreement
- preparation of tenders
- implementation of the EEA announcement necessary or a Doffin Investment announcement
- implementation of competitive bidding or "competition with bargaining"
- evaluation of tenders / offers with a total recommendation
- assistance with negotiations at the "competition with negotiation"
- assistance with contract
- participating in information meetings with the banks.

Solør renovasjon (SOR)

Every day, tons of domestic food waste gets thrown away - a natural resource that is not utilized well enough. Solør Waste Management Authority (SOR) saw possibilities here and has done something about the issue. SOR has used Kildal composting for many years and the agreement was to be renewed. SOR had an opportunity to take over the entire plant. This would secure jobs and businesses in the community. General manager Marit Gundersen says that the purchase of Kildal Composting cost NOK 4 million, and even more enjoyable was the fact that SOR got a loan with a green rate. This is a loan that is granted only when it will be utilized for climate and environment related projects.

Infrastructure projects - KBN is an active participant

Anyone driving around the country will notice that the road network needs to be renewed and maintained. KBN is a major funding partner in various toll road projects. Infrastructure projects have become an important funding area for us, and today we are funding 22 projects in the order of NOK 22.5 bn.

The projects are spread all over the country; for example, the E6, the E18 motorways, tunnels and several national highways, including gigantic bridge projects such as the Hardanger suspension bridge. The need to upgrade our roads is huge and KBN takes their share of the future funding requirements.

As the Government has conveyed responsibility for parts of the national highway network to the county authorities, KBN has the opportunity to participate as a financing agent. When the county is building or expanding the road network to a toll road project, KBN will be one of many alternative lenders.

85 years of municipal lending

by professor Sverre Knutsen, Norwegian Business School*

The Norwegian municipal bank, Norges Kommunalbank (NKB), began operations in September 1927, after Parliament had adopted the Norges Kommunalbank Act in the winter of 1926. NKB was established as a state bank with its own board, appointed by the government and Parliament. NKB started with a basic capital of NOK 20 million and a reserve of NOK 3 million. NKB had no government guarantee for its deposits when it was established, but this changed in 1929.

Norges Kommunalbank started during a very turbulent time for the Norwegian economy and society. Norway entered into a strong, credit-driven boom during the First World War. Shipping and industry experienced a tremendous and largely speculative, debt-financed investment growth. A galloping inflation hit the economy. The price bubble in the stock market punctured early in the autumn of 1918, a few months before the war ended. In the autumn of 1920 a powerful, global deflation crisis struck in the Norwegian economy and hit the Norwegian export industry hard. Prices fell, exports fell and so did investments. Businesses had built up huge debts during the war boom, which they were no longer able to service. Many of the investments from the war boom period proved unprofitable and unsustainable.

Due to accelerating loan losses, the banks began to fail. In addition, the municipalities had incurred significant debt increases in relation to the large-scale development of hydroelectric power plants during and immediately after the war. These plants were also mostly financed with expensive and short-term loans from commercial and savings banks. In 1925, municipal debt had risen to NOK 1.6 billion - equivalent to approx. NOK 33 billion in today's money - of which a large part was the so-called short-term "debt soar". But then the value of the kroner began to rise and in 1928 the kroner was attached to gold reserves, and it returned to its pre-war level after a new severe deflationary period. The debt burden was a heavy burden for the municipalities to carry.

The authorities found it necessary to appoint a debt commission to deal with these debt problems in the municipalities, and in line with the commission's recommendation of 1928, NKB became an important tool in debt reform, including helping to refinance municipal debt. From 1928 to 1939 NKB paid out more than NOK 387 million in loans. Of these, 76 percent went to the conversion of municipal debt, while 24 percent went to local initiatives, mainly electricity development. Right from the beginning KBN was a municipal bank.

85 years
1927 - 2012

* Professor Sverre Knutsen, the Norwegian Business School, is writing Kommunalbanken Norway's history to be published this coming fall (2012).

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