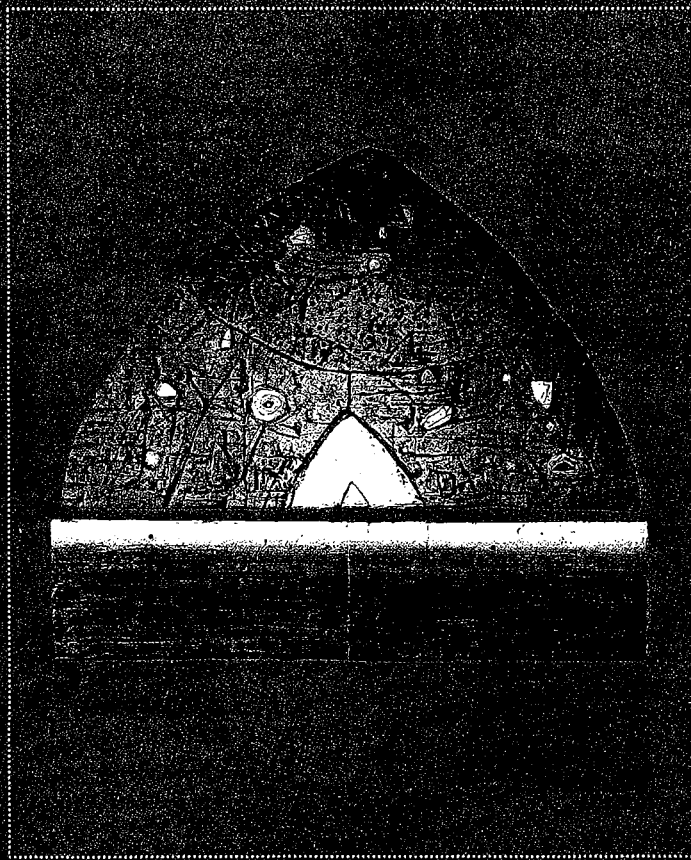




ANNUAL REPORT 1949



KREDITTILSYNET

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The objects depicted in the Annual Report are made by the ceramist Kari Christensen. She has had several extensive decoration jobs and her works of art are displayed in a multitude of Norwegian and international museums and collections, such as the Museums of Art in Oslo, Bergen and Trondheim, and in the Victoria and Albert Museum in London. Front cover : Natt, 62 x 80 cm, Photo: Blueline.

FOREWORD

The year 1994 may be described as a good year for the financial institutions and Kredittilsynet (The Banking, Insurance and Securities Commission of Norway).

For the financial industry, 1994 proves that the crisis years are over. We are again experiencing economic strength and freedom of action after a year marked by consolidation and normalisation of business. For the first time since 1987, we have experienced a year without serious crises within the financial institutions. Most institutions' own funds and solvency have been strengthened considerably so that they are better prepared to meet both domestic and international challenges.

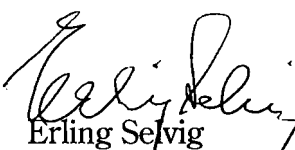
The interest rate and securities markets were marked by fluctuations which had a large impact on the value of the institutions' portfolio. This did not, however, create significant problems. For the life insurance companies, the fall in portfolio values was offset by reserves such as unrealised gains on share value and additional reserves which were established, inter alia by the government authorities' solvency measures in the autumn 1993. An explicit detailing in 1994 of the accounting rules regarding bonds also played a role.

Even though the securities markets to a large degree have functioned satisfactory during 1994, several incidents of unethical behaviour have been revealed, involving brokerage firms and securities trading. Unacceptable behaviour has also had ramifications into other branches. Økokrim (The National Authority for Investigation and Prosecution of Economic and Environmental Crime in Norway) and the Directorate of Taxes have become involved in cases where there have been founded suspicions of breach of statutory regulations. Kredittilsynet itself has been promoting the establishment of good ethical guidelines.

The EEA agreement came into force in 1994, and the majority of the laws and regulations intending to make Norway part of the single market have been adopted. Due to prior years' liberalisation of the financial markets, there has been a smooth transition in the regulatory framework for the financial industry. The international functions of Kredittilsynet have increased significantly, inter alia through closer co-operation with supervisory authorities in other EEA countries.

A lesser need for handling crises and better budgetary and personnel funding from the Government and Parliament, have enabled Kredittilsynet to emphasise long term duties. A new strategic plan emphasising preventive supervision has been adopted. The foundation has been laid for a better surveillance of macroeconomic factors which may create problems for the financial industry. The credit assessment routines in Norwegian banks has been analysed and compared with the standard in international banks. The practice of granting housing loans has been studied in order to prevent increased risk-taking. Extensive on-going supervisory duties have been carried on, and in certain areas, including pension funds, supervision has been intensified. The supervision of auditors and accountants has also been strengthened by the establishment of document based supervision and thematic supervision. Kredittilsynet's own organisation has been strengthened. We have a strong foundation for meeting new supervisory challenges.

Oslo, 18. January 1995


Erling Selvig
Chairman of the Board


Bjørn Skogstad Aamo
Director General

Important features and main challenges in the financial sector

1994 was marked by consolidation and normalisation of the financial institutions' situation. For the first time since 1987, no financial institution was wound up or experienced a crisis. The institutions' own funds have been strengthened and they are better prepared for the future

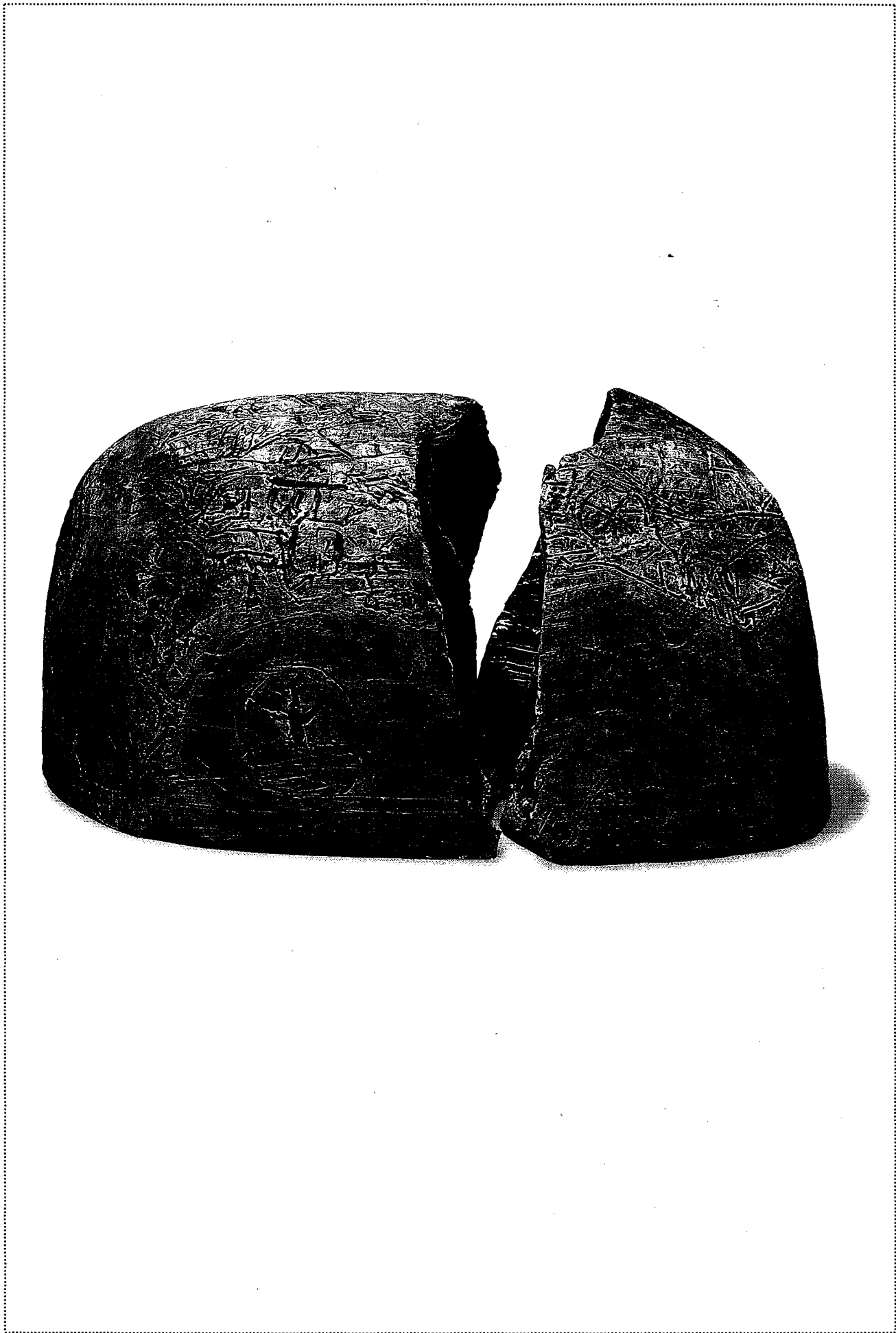
After prior years of crises, 1994 became a good year for most financial institutions, characterised by consolidation and a normalisation of the situation. No financial institutions experienced a crisis or winding up situation. The commercial banks, as a group, had larger profits than ever before. The savings banks, which already in 1993 had emerged from the crisis, also showed good results. Several life insurance companies will show relatively poor results in 1994. (One must bear in mind that the results in 1993 were exceptionally good). The non-life insurance companies have improved their insurance results while the financial revenue is relatively low.

The financing companies had relatively large profits while the mortgage institutions had moderate profits. In mid-March, Kredittilsynet will present its analysis of the 1994 year-end results in a quarterly report.

The commercial banks' results are particularly affected by the fact that excess loan loss provisions from previous years has been transferred back as revenue in the accounts. Kredittilsynet has researched the extent of the accounting for excess loan loss provisions in 1992, 1993 and up to the third quarter of 1994. During the first three quarters of 1994 the commercial banks transferred 1.8 billion NOK. Total transfers of loan loss provisions for the commercial banks from 1992 to the third quarter of 1994 amount to 3.3 billion NOK. This corresponds to 7.9% of the 41.4 billion NOK aggregate losses on books over the years 1990 to the third quarter of 1994. The 30 largest savings banks barely transferred 0.6 billion NOK during the first 3 quarter of 1994. Including 1992 and 1993, the aggregate figure for the period 1990 to the third quarter of 1994 was 1.3 bill NOK or 4.8% of the total loan losses on books during the same period. It ensues from the investigation that the transfer of prior loan loss provisions is moderate compared to the banks' aggregate losses in later years.

Economic outlook and requirements pertaining to financial institutions

After a period with no or little growth, the international economic boom which started in 1993 was boosted in 1994. The growth estimates for Norway for 1994 have been revised upward several times. In the Government's final budget bill for 1995, the GNP growth was estimated to be 5.5%, for continental Norway 3.5%. The desire to reduce the budget deficit and to induce lower interest rates has led to cost cutting measures, and the growth in 1995 in continental Norway is estimated to be around 2.3%.



GROTTE clay/stoneware, 38x60x30. Photo: Knud Larsen.

Banks and lenders experienced low losses in 1994, but must prepare for higher loss levels in the future than what they experienced in the 1980's

An important objective for the institutions and Kredittilsynet is to prevent that stronger growth and competition lead to weaker credit assessment norms

Falling interest rates and the economic boom in Norway contributed to improving the payment ability of households and of the commercial sector. This has again led to a boost in the property market and added loan security for the banks. Altogether, this has contributed to a strong reduction in losses for banks and other lenders. However, this low level of loan losses will not persist. The banks must prepare for higher losses than what they were used to before the liberalisation of the credit market in the 80's.

The adopted tightening measures will particularly apply to private and public expenditure. There are reasons to expect continued increase in housing investments and a sharp boom in other investments. This will probably lead to a larger increase in financial institution loans in 1995 than in 1994.

The financial strength and capital adequacy of Norwegian banks has improved significantly in 1993 and 1994. The savings banks' average share of core capital has increased from 9.5% at the beginning of 1993 to 11.6% by the end of the third quarter 1994. For commercial banks where the government does not have a majority of the shares, the core capital has increased from 8.8% (beginning 1993) to 9.8% (3rd quarter 1994).

By the end of the third quarter 1994, Den norske Bank (DnB) and Christiania Bank & Kreditkasse (CBK) had a core capital of about 6% on a consolidated basis. No other Norwegian bank, except Fokus bank, have such a low core capital ratio. Compared to other banks, a large share of DnB and CBK's business is related to a highly competitive Norwegian commercial sector, a market in which they meet increased competition from foreign financial institutions. Hence, Kredittilsynet believes that in order to improve these banks' competitiveness in the long run, a clear goal should be to raise DnB's and CBK's core capital. The positive results from 1994 are to a large extent affected by the accounting of prior loan loss provisions and low loan loss provisioning on new loans. According to Kredittilsynet, rather than being distributed, a large part of the 1994 profits should be retained to strengthen the equity capital in order to enable the banks to meet future challenges.

As banks and other financial institutions get over their difficulties of the past few years, there is also a trend towards increased competition. Different Norwegian institutions fight to gain and keep shares of the loan market as well as the markets for savings and financial investments. There are reasons to believe that this trend will accelerate in 1995. In addition, there will be increased competition from branches of foreign financial institutions, though the total market share remains moderate. As more and more companies are issuing bonds directly to the public, the securities market will also become a real alternative to bank loans. On the financing side the unit trusts will provide a relevant alternative. Competition from Norwegian and foreign parties has led to the two largest Norwegian commercial banks losing market share in 1994.

Increased competition has reduced the financial institutions' interest rate margins. They could be expected to decline even further. An important task for Kredittilsynet and the financial institutions would be to prevent

that stronger growth and competition lead to lower credit assessment standards. With loan losses in 1995 at a reasonable level and expected reduction in transfer of excess loan loss provisions, the aggregate results, particularly at commercial banks, will not be as good as in 1994.

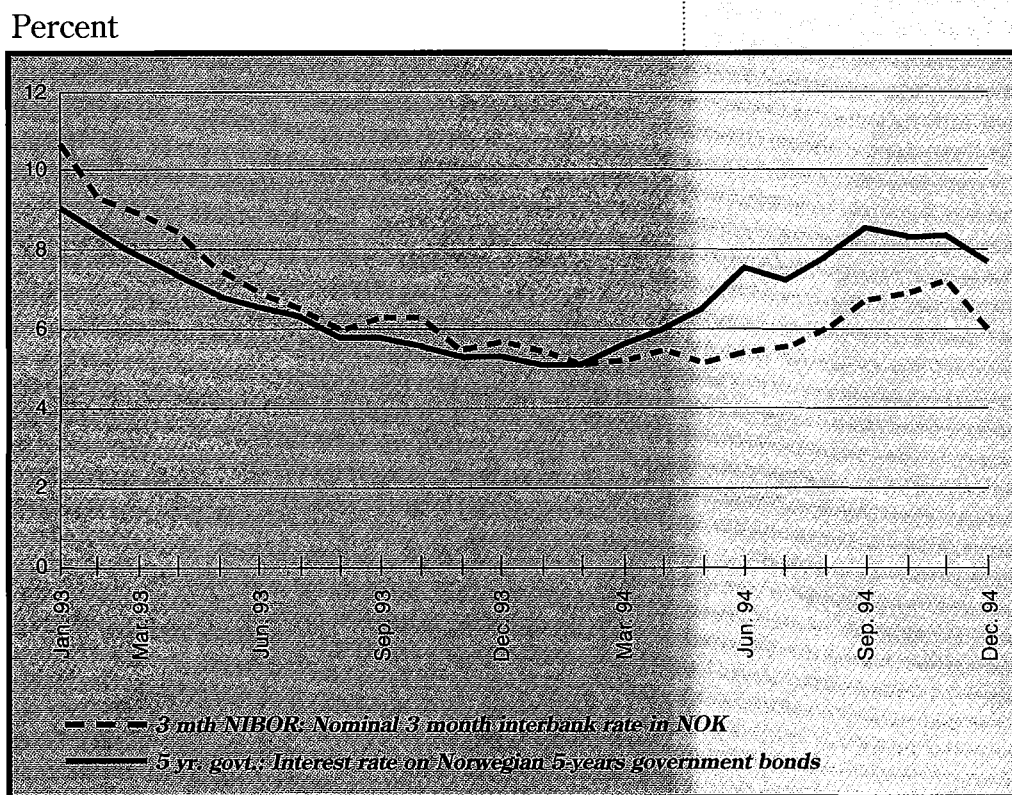
After a series of negative experiences abroad, 1995 seems to become the year when Norwegian institutions again find it reasonable to establish activities abroad. Kredittilsynet assumes that the institutions have learned a lot from their experiences in the 80's, nevertheless, it will keep an eye on these operations.

Consequences of wide fluctuations in interest rates

In the strategic plan of April 1994, Kredittilsynet sums up the economic forecast as follows: "The Norwegian economy may in general terms be marked by moderate growth, low inflation and low but unstable interest rates". Large fluctuations in interest rates have dominated the developments in the financial sector in 1993 as well as in 1994.

Due to the fall in interest rates in 1993, the financial institutions made large profits on their securities portfolios. This particularly applied to the life insurance companies with a large bond portfolio. Most of 1994 was characterised by rising interest rates even though there was a slight fall at the end of the year. A significant part of the profits from 1993 were eroded by losses on the securities portfolio as a result of the rising interest rates in 1994.

Interest rates in 1993 and 1994



Wide interest rate fluctuations influenced the development at the financial institutions in both 1993 and in 1994. There are reasons to believe that this will also be the case in the years to come

There are reasons to believe that there may still be wide fluctuations in interest rates and in the securities market in the years to come. Several institutions seem to have anticipated such trends by emphasising investments in short-term securities rather than long-term securities. Because of the importance to society and to the commercial sector of long-term investments in securities, institutions with long-term liabilities should also in practice have opportunities to make long-term investments. This represents an important challenge to the individual institutions as well as to the regulatory and supervisory authorities.

Kredittilsynet faced this trend inter alia in fall 1993 by contributing to the solvency measures for life insurance companies. The introduction of a

Source: Norges Bank

Profit on securities and estimated profits (losses) in 1994				
	Figures on books 1993	Bill. NOK 1994	Adjusted fig. 1993	Bill. NOK 1994
Commercial banks	2.4	-0.6	2.9	-0.4
Savings bank	2.1	-0.5	2.6	-1.3
Norges Postbank	0.1	0.0	3.3	-1.2
Non-life insurance	1.3	-0.2	2.0	-1.1
Life insurance	9.1	1.4	17.7	-8.5

The estimates for the branches have been made by "blowing up" figures from the four largest commercial banks, the ten largest savings banks, the six largest non-life insurance companies, while figures for all the life insurance companies have been included.

Large unrealised gains and additional reserves helped the life insurance companies weather the fall in the securities market without major problems

The EEA agreement has not brought about major changes for the financial institutions or the financial market. The competition from foreign institutions has been moderate, and has mostly been targeted toward more sophisticated services

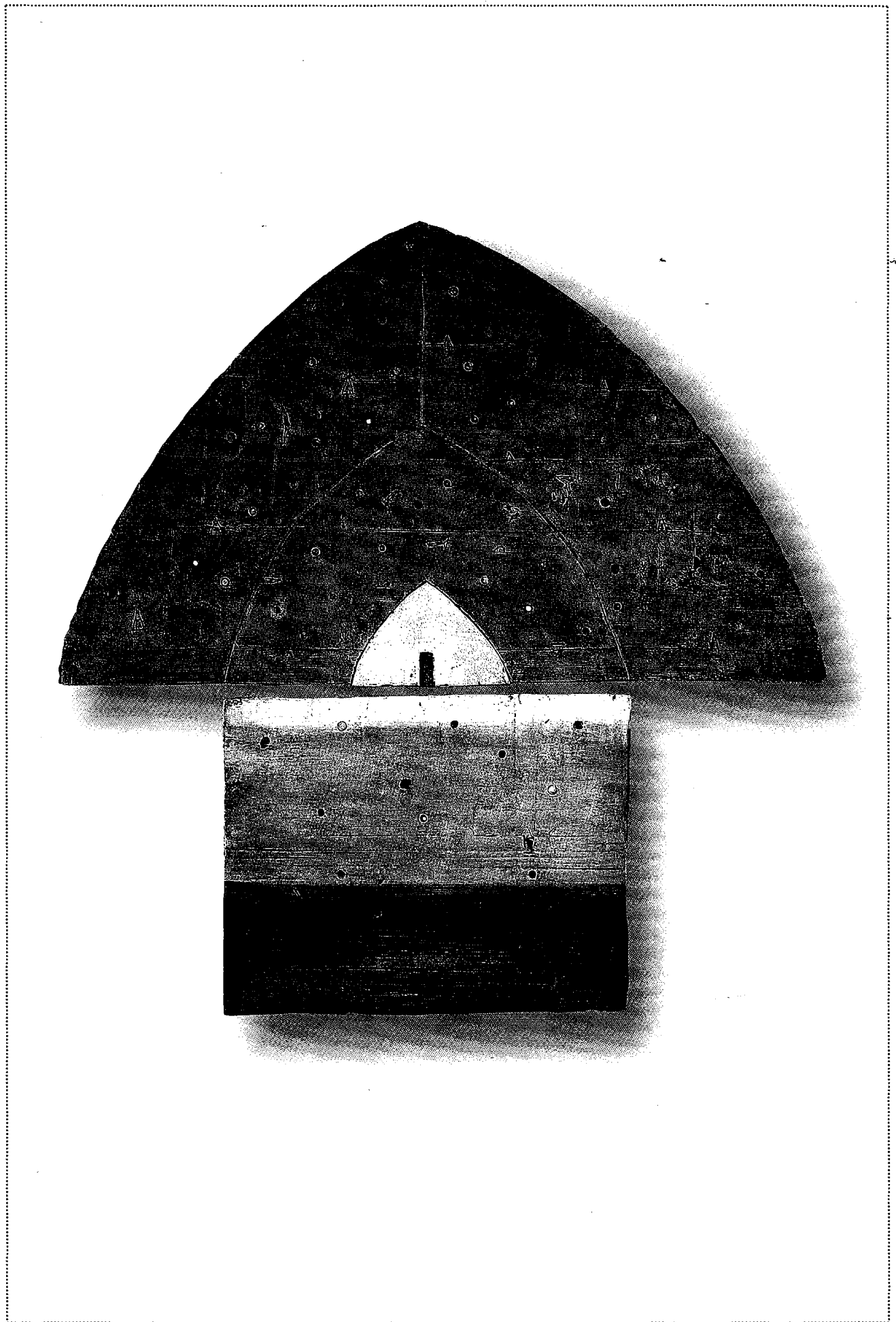
"buffer" in terms of additional reserve requirements, and the decision that unrealised gains no longer be irreversibly allocated to the policyholders, were major factors preventing that the fall in the bond and equity markets in 1994 created significant problems for the life insurance companies. The measures also helped to prevent disturbances in the investments of the life insurance companies. Furthermore Kredittilsynet's explicit detailing of the accounting regulations regarding bonds in fall 1994 has been important for several companies. Provided bonds are «kept until maturity», they may be accounted for as long-term assets and thus not be depreciated in accordance with the fall in the market value, which otherwise is the case. These rules have also had a positive effect on the bond market.

There are also uncertainties regarding the forecast interest rate level for 1995. Even if the real interest rate level is relatively high, the economic boom makes a significant decline in interest rates not very probable. The life insurance companies should in their annual balance of accounts endeavour to set aside further additional reserves.

In its supervisory functions, Kredittilsynet will emphasise the individual institution's ability to handle interest rate fluctuations. New capital adequacy rules for market risk, ensuing from an EU Council Directive, will strengthen the institutions' ability to withstand interest rate fluctuations. It may, in the future, also be necessary to assess the need for other amendments or clarifications of regulations, aimed at enabling institutions with long term commitments to make long term investments.

The European regulatory framework

The EEA agreement came into force in 1994, and Norway became a part of the single market, also for financial services. Within the end of 1994, eight foreign financial institutions had notified Kredittilsynet that they wished to establish a branch in Norway according to the new regulations. According to these regulations, a bank from an EEA country may establish a branch in another EEA country, without establishing a new joint stock company. Four of these institutions are banks. Foreign banks may after a while get a strong foothold through their branches, particularly in the market for sophisticated banking services. Notifications regarding cross-border provision of banking and insurance services have been received, but the extent of actual services is probably minimal. So far the participation in the single market for financial services has not created any disturbances in the Norwegian market, although there is a wider array of services offered to households and to the commercial sector.



TIDLIG MORGEN clay/stoneware, 80x80 cm. Photo: BLUELINE.

Norwegian financial institutions both can and will make an effort to meet the competition. The increased competition may lead to improved and cheaper financial services

With less urgent problems at individual institutions and increased availability of resources, Kredittilsynet may turn more of its attention toward long term responsibilities

It may be noted that the effect of the EEA agreement on the financial market in 1994 has neither been significant nor dramatic. This is to a large extent due to the fact that Norwegian authorities, even before the drafting of the agreement, had an open attitude towards foreign countries and was paying attention to regulations in other European countries when shaping the Norwegian laws and regulations.

Even though Norway is not a member of the European Union, Norwegian financial institutions and financial markets in 1995 and beyond, will be bound by regulations which have been, and will be, developed by the countries in the European Union. The EEA agreement and its amendment (the "additional package") formally bind Norway to the regulations which have already been implemented. When it comes to new regulations, Norway is formally able to make independent decisions to deviate from these regulations. Such deviation will in practice be contingent upon strong argumentation.

The confidence in Norwegian financial institutions and financial markets would be strengthened if Norwegian regulations have requirements regarding solvency etc. which are at least as stringent as the EU regulations. Good follow-up and application of the regulations will be important. One would expect that Norway, as the only significant financial market within the EEA and outside the EU, will be scrutinised by the actors in the market, the media and surveillance authorities when it comes to abiding by the rules.

During 1994 Kredittilsynet has actively participated in a long range of committees, conferences and working groups within the EU and the EEA system. In addition, bilateral communication with supervisory authorities in many EU-countries has been established. Norway will not participate in the central policy-making committees for government officials (the banking advisory committee and the insurance committee) nor in the decision-making political bodies which draw the guidelines for the development of regulations in the financial sector. The EEA agreement provides the Norwegian authorities with consultation rights and it will be important to take advantage of these rights. Emphasis must be placed on systematic and well prepared participation in the expert groups that draft new regulations and oversee current regulations. Kredittilsynet must also emphasise good bilateral relationships with the EU countries, including Sweden, Finland and Denmark. The Nordic co-operation may become of great importance and has to be given high priority. Therefore, Kredittilsynet believes that the development of skills and capacity in international issues should be emphasised as if we were members of the European Union.

Supervisory functions in 1995

Kredittilsynet will make use of the strategic plan of 1994 when setting priorities in 1995. The projects which, according to the strategic plan, have been initiated for macroeconomic surveillance, better credit rating systems, improved documentary (off-site) supervision and supervision of IT (Information Technology) operations, will be prioritised. At the same time, we will emphasise the improvement of quality control in the case processing routines and in the on-going supervision. The case

processing time and the number of unfinished cases have been reduced in 1994 and these efforts will continue in 1995. According to what we have mentioned above, we will emphasise continued contact with the EU countries and follow up the regulatory work in the EU institutions. The measures to further develop the organisation of Kredittilsynet will be followed up.

1994 has proved that there is a particular need for pursuing ethical issues and for being conducive to a safer use of derivatives. These will be important tasks in 1995. The implementation of the EU directive on capital adequacy requirements for market risk and preparations for supervision ensuing from these regulations, will also present a particular challenge for Kredittilsynet in 1995.

Strategy and preventive measures

STRATEGIES AND PRIORITIES

Kredittilsynet shall be a competent, efficient and independent institution which in its supervisory function, shall help the financial system to fulfil its obligations to society in an appropriate and safe manner according to laws and regulations.

Main goal

The main goal of Kredittilsynet is to induce trust in the financial system by seeking to promote:

- adequate solvency, risk awareness, and management and control in the financial institutions
- contingency plans and routines for preventing the development of situations which may threaten the stability of the financial system
- conformity to laws, regulations and ethical norms within the financial market
- an up to date and appropriate regulatory framework leading to well functioning markets, for the supervised institutions as well as for the users of their services.

Choice of strategy

In April 1994, the board of Kredittilsynet adopted a new strategic plan which includes analyses of challenges, main objectives, means and priorities for the next years.

The Storting (the Norwegian parliament) passed a resolution in 1992 that Kredittilsynet shall remain an independent and strengthened commission. Kredittilsynet has been awarded better resources from 1993 to 1995. The number of positions has been increased by 32. If the main characteristics of the supervisory functions do not change, the resources will not increase significantly more. Internationalisation, turbulence tied to commercial and macroeconomic factors, economic crime and a higher degree of complexity in the supervisory functions, will increase the challenges and the work load in the years to come.

Kredittilsynet will meet these challenges by:

- Increasing efforts to predict trends which may affect the financial institutions
- giving higher priority to preventive measures in order to face possible threats against a sound and stable development
- achieving a higher impetus by actively promoting internal co-ordination, rationalisation and systematisation of the tasks.

The new strategic plan of Kredittilsynet emphasises preventive measures



PLANET raku, diam. 38 cm, Kecskemét Museum, Ungarn

After several years of support measures and rescue operations, Kredittilsynet may now to a larger extent concentrate on preventive tasks and direct the supervision towards measures which may improve the general standard of the financial institutions

PREVENTIVE MEASURES AS A SUPERVISORY STRATEGY

Kredittilsynet's tasks at the end of the 1980's and the beginning of the 1990's were characterised by support measures and rescue operations. Concurrently with a major increase in numbers of on-site inspections and measures related to individual institutions, a significant amount of resources was spent developing regulations and supervisory methods.

The resources of the supervisory authority will be devoted to preventive supervision and measures to increase the standard at the supervised institutions. It is important to gain knowledge about what occurred before and during the banking crisis in order to prevent similar problems as those which characterised the 1980's. Organisational issues in the supervised institutions have proven to be important for a satisfactory management of the operations. Several issues led to the banking crisis. It is important to learn from the past, but it is equally important to keep an eye on other aspects and new trends and challenges which may threaten the solvency of an institution or disturb the stability of the financial system. This would improve Kredittilsynet's ability to implement measures on time and thereby play an active role in preventing new crises.

The preventive role of Kredittilsynet is two-tiered:

- at the micro-level Kredittilsynet shall stimulate the financial institutions to be as prepared as possible to meet difficult times which may put a strain on the profitability and solvency of the institution,
- at the macro-level Kredittilsynet shall follow the developments in the different sectors of the financial market and in the macroeconomy in general, in order to be able to uncover trends which may threaten the stability of the financial system and to help implement the necessary measures.

In accordance with the strategic plan, Kredittilsynet has increased the emphasis on preventive measures. The first step is the establishment of a macroeconomic surveillance program.

A macroeconomic surveillance program

Experiences from a number of countries have disclosed the importance of macroeconomic factors for understanding how crises may develop in financial institutions.

In order to be prepared for such crises in the future, Kredittilsynet has initiated the establishment of a macroeconomic surveillance program. This program will be used in the supervision of the financial institutions and the financial market. Norges Bank (the Central Bank) and Statistics Norway participate in the project.

The objective of the program is to uncover macroeconomic trends and features which under certain circumstances may weaken the capital base and threaten the solvency of an institution or a financial sector. The purpose is not to conduct a general economic surveillance, nor to develop broad economic models or major empirical analyses. The objective is to gain just enough information, so to recognise, before it is too late, situations which may threaten the capital or solvency of an institution or a sector. An on-going dialogue with other government bodies and economic experts in Norway

and on the international arena is essential. Other foreign supervisory authorities' systems for macroeconomic surveillance have been examined. When choosing indicators, it is necessary to build on past experience. In order to gather some experience from previous crises, an international expert conference was organised in Oslo as part of the project "Macroeconomic surveillance aiming to detect potential or emerging financial crises". A conference report is available in English and Norwegian.

The macroeconomic program is based on the following three elements:

- regular surveillance based on a set of economic indicators and analyses,
- research and examination of specific trends and issues,
- on the basis of the two elements above, worst-case scenarios are drawn up to study the financial institutions' sensitivity to changes in the economic climate.

Four groups of factors are being watched on a regular basis: indicators for financial fragility in the financial sector, indicators for financial fragility in the non-financial sector, indicators for structural changes in the financial markets, and indicators for macroeconomic uncertainty. A major issue in the program is to search for possible negative trends which may not be captured by indicators based on past experience.

Internal control routines at banks

Kredittilsynet has, partly as a consequence of the banking crisis, gained skills and expertise in management and control systems. The experience has proved useful in the further development of on-site supervision methods. In January, Kredittilsynet implemented a regulation regarding the banks' responsibility for control, documentation and confirmation of internal control. During 1994, every bank should have established internal control routines. The regulation has led to an active involvement from the banks. Several banks have initiated projects to improve the control, with an examination of the risks and control measures.

Study of the housing financing

In spring 1994, Kredittilsynet examined the financial institutions' practice and risk profile in housing financing. The reason was signs of higher loan to value ratios and a fear that this again might be used for competitive purposes in such a manner that the institutions may take on too much risk in the event of a fall in real estate prices. The survey included 50 financial institutions, including the largest banks, insurance companies and mortgage institutions, Postbanken and a selection of smaller banks with increasing residential loan portfolio.

According to the responses to the survey, the institutions are not taking high risks in granting residential loans.

Mortgage loans were usually given within 80% of the value of the residence and the interest rate usually reflected the mortgage ratio. Most institutions had formal credit limits related to the customer's income in addition to reviewing the person's ability to service the loan.

Only a few institutions were using safety margins reflecting a possible increase in interest rates when assessing the customer's payment ability. Institutions with poor routines are being followed-up.

The macroeconomic surveillance program will lead to increased knowledge about trends capable of threatening the stability in the financial system, and thus increase the ability to introduce necessary measures at an early point of time

A survey of housing loans has been conducted to prevent higher risks in the property market

Credit assessment norms in Norwegian banks have been surveyed and compared with those of international banks

Credit assessment project

In the autumn of 1993, a working group was established to examine the banks' credit assessment routines. The reason is that large Norwegian banks should be able to improve the quality of their credit assessment routines and their monitoring of large claims.

The working group visited eight leading international banks, the four largest Norwegian banks and four large savings banks and mapped international and Norwegian practice in this area.

The working group presented its report to Kredittilsynet in December 1994. The report is published at the same time as the annual report.

The conclusion is that the credit assessment practice at Norwegian banks generally speaking does not seem to be poorer than at the international banks. There is still room for improvement, however, in most banks. Most banks have already started reviewing their credit assessment routines.

Kredittilsynet will send the report to all the banks and pursue the matter in its supervisory work and by offering advice on sound credit assessment systems.

Supervision of the use of information technology (IT)

In the business plan for 1994, it was decided that the supervision of the financial institutions' use of information technology should be emphasised. An IT-adviser has been hired to take care of this. Kredittilsynet has made and tested own programs to be used in controlling the institutions' information technology. The programs start functioning 1 January 1995.

A better control of payment transfer systems has been initiated. Inadequacies in the agreements between the users and providers of these systems will be followed up. Questions on risk and responsibility in connection with transactions in the payment system have to be clarified and taken into consideration in the agreements. These issues are being studied by the Financial Law Commission. Norges Bank has a centralised responsibility for payment transfer systems and Kredittilsynet will co-operate with Norges Bank in this field of supervision.

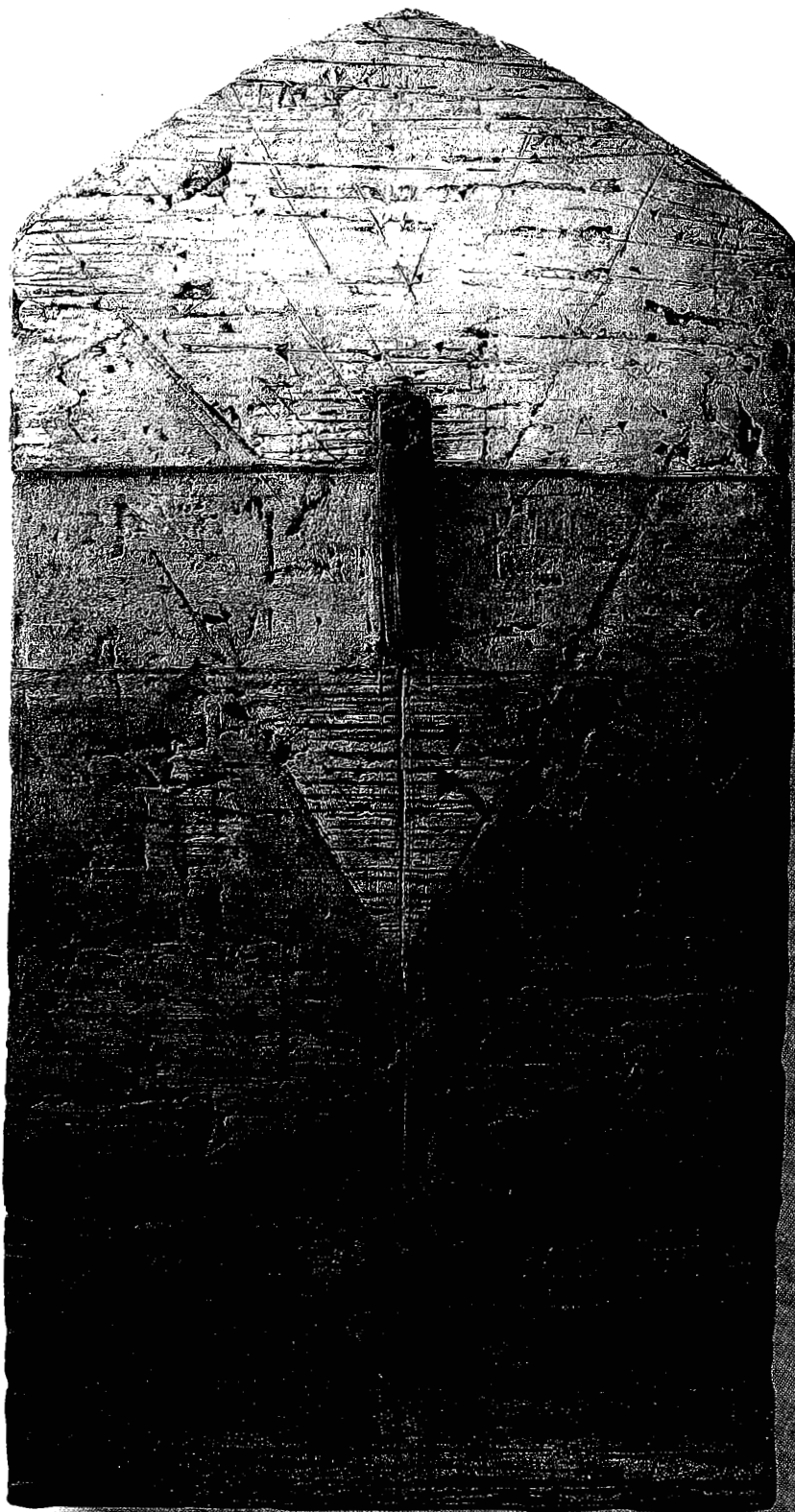
Measures against money laundering

Most institutions are working hard at adapting to the new regulations regarding measures against money laundering. The amendments in the Financial Service Act came into force on 1 January 1994, and a regulation regarding identification requirements and measures against money laundering came into force on 15 February 1994. The Act on the Supervision of Banks, Insurance companies and Securities trading etc. (Kredittilsynet) was amended to include a provision on reporting requirements to Økokrim¹ upon suspicions of money laundering.

The institutions have reported over 150 suspicious transactions to Økokrim. In the autumn of 1994, the Ministry of Finance requested comments on its proposed legislation expanding the scope of the money laundering regulations to more institutions, including Norges Bank, Postbanken, securities brokers, real estate agents, management companies, and other institutions and companies which may be used for money laundering purposes.

¹ The National Authority for Investigation and Prosecution of Economic and Environmental Crime in Norway

Measures against money laundering have shown results. The Ministry of Finance has suggested that the regulations be applicable to a wider range of institutions



STILLHET clay/stoneware, 55 x 104 cm. Photo: BLUELINE.

Closer internal cooperation and better co-ordination of Kredittilsynet's competence and resources have shown good results in 1994

Several cases concerning breach of rules and regulations have been sent to Økokrim

SYNERGY OPPORTUNITIES

Kredittilsynet is one of the few supervisory authorities with a common responsibility for most sectors of the financial system. In addition, Kredittilsynet has the supervisory responsibility for debt collection agencies, real estate agents and auditors. Kredittilsynet is also responsible for overseeing the accounting regulations.

This wide scope of supervision offers great synergy opportunities. A great challenge and one of the main goals in the strategic plan, is to take advantage of these synergy opportunities.

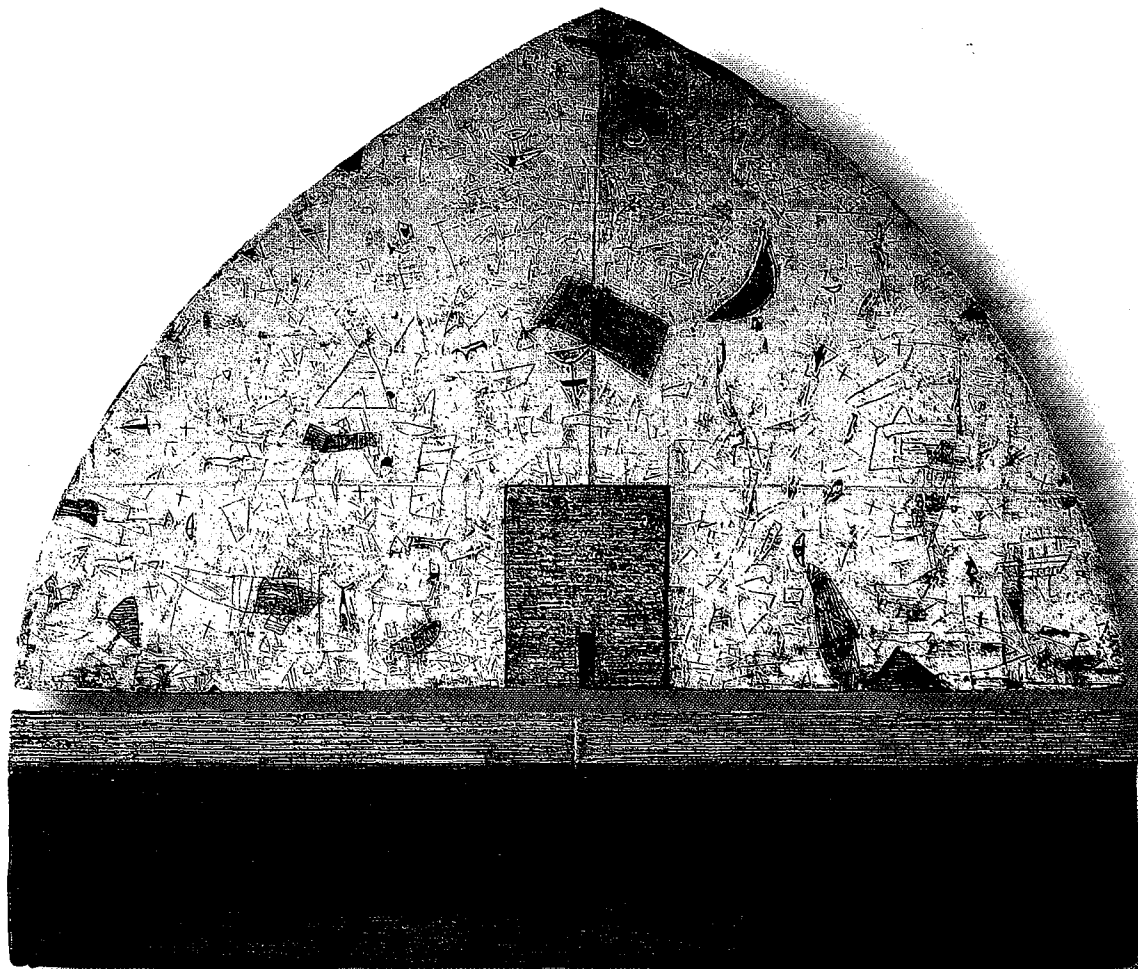
Throughout the year, many cases have been discovered and solved due to communication and co-operation between the different divisions in Kredittilsynet, e.g. at on-site inspections.

These cases prove how valuable a combined supervision may be and how important it is to have a close co-operation and effective co-ordination of the work in the different divisions of Kredittilsynet.

CASES FOR THE PROSECUTION

We have seen an increase in cases which have been sent to the prosecution for an evaluation of possible criminal charges.

Such cases have required significant efforts and resources. Kredittilsynet has altogether sent eight cases to the public prosecutor and to Økokrim. Most cases regard matters which have been revealed during on-site inspections in securities brokerage firms and pension funds. In addition, the Investigating Committee has reported three cases.



TEGN clay/stoneware, gold-leaf 62x80 cm, Kunstindustrimuseet i Oslo.

Photo: BLUELINE

Banking, finance and insurance

DEVELOPMENT OVER THE PAST YEAR AND SOME MAIN CHALLENGES

The commercial banks experienced a record surplus in 1994, while the savings banks showed good results. Loan losses were lower than expected. The interest rate trend led to weaker operating results by life insurance companies. Non-life insurance companies experienced lower claims and expenses, but also lower financial revenues

In 1993 the financial institutions improved their situation significantly, particularly as a result of lower interest rates throughout the year. The results for 1994 are affected by the latest rise in interest rates, which led to falling prices in the securities market. Loan losses have decreased more than expected, while costs still seem to be under control. All in all, this leads to relatively good results for the banks and financing institutions in 1994. Regarding life insurance companies, the interest rate development in 1994 led to significantly weaker operating results. Due to the solvency measures and Kredittilsynet's detailing of the accounting rules, the rise in interest rates will not cause significant problems for the life insurance companies, despite large inventories of fixed rate securities.

Despite the boom in the Norwegian economy, the aggregate credit growth remains small. Nevertheless, increased competition for borrowers leads to significant restructuring in the credit market. Savings banks and financing companies are increasing their market share, while the large commercial banks, life insurance companies and mortgage institutions show a decrease in loan volume.

For Kredittilsynet, a main challenge is to help prevent that losses on loans and guarantees threaten the solvency of the financial institutions and cause crises in the financial market. Therefore, preventive measures will still be emphasised, particularly aiming at improving the institutions' own management and control standards. International co-operation between supervisory authorities and harmonisation of regulations will remain important in the future. In order to protect the quality of the institutions' equity and subordinated capital, Kredittilsynet has adopted a conservative attitude, particularly when it comes to admitting different types of innovative instruments as core capital. New and more restrictive rules regarding credits to a single customer will come into force in 1995.

ADMINISTRATIVE MATTERS

Establishments and cross-border activities

In 1994, eight foreign credit institutions (four banks and four financing companies) sent notifications regarding the establishment of a branch.



UNIVERS clay/stoneware, diam. ca 38 cm. Photo: Knud Larsen.

For the first time in many years, Norwegian financial institutions seem to be establishing operations abroad. Foreign institutions have shown moderate interest in the Norwegian market

New standardised articles of association for municipal funds have been adopted. New articles of association for private pension funds will be given early in 1995

Two of the banks were established in Norway through subsidiaries before they decided to wind them up and establish branches instead.

Ten foreign credit institutions have informed that they wish to provide cross-border financial services, and nineteen companies wish to offer cross-border non-life insurance products. One of the companies has not supplied the necessary information and is thus not allowed to commence business. The extent of the non-life insurance companies' activities is uncertain for the time being. Four companies have informed that they wish to offer life insurance products. Two companies have received confirmations, while Kredittilsynet awaits additional information from a third company.

Den norske Bank has applied to establish branches in Sweden and Germany. Three Norwegian insurance companies have informed that they wish to provide cross-border services (non-life insurance) in other EEA countries.

Implementation of the solvency measures in life and pension insurance

The solvency measures dating from fall 1993 have been followed up by supplementary rules regarding additional reserve requirements and revaluation reserves in life-insurance.

Kredittilsynet finds the reserves for future administrative expenses to be inadequate at several life insurance companies, either because too general allocation rules are used or because prior reserves have been accounted for as income without the consent of Kredittilsynet. Kredittilsynet has therefore asked the life insurance companies to clarify on the need for such reserves.

Guidelines have been issued regarding the distribution of profits in life insurance. Furthermore, supplementary guidelines have been issued regarding interim and final calculations of profits in life insurance.

Standardised articles of association for private and municipal pension funds.

New standardised articles of association for municipal pension funds were adopted in December 1994. For private pension funds, new standardised articles of association are expected to be adopted early in 1995. A new regulation proposal concerning private occupational pension schemes under the tax laws is being considered by the Ministry of Finance. The draft regulation stipulates inter alia rules regarding the use of the private pension funds' capital in the event of mergers, de-mergers, liquidation, etc. The regulation on the application of the Insurance Activities Act to pension funds and pension schemes came into force on 1 July 1993, but became fully effective in 1994. Kredittilsynet has spoken about the purpose and consequences of the regulation at conferences and seminars, and thus been of help to the pension funds in adapting to the new regulations. The need for guidance has been particularly large in the municipal sector.

Improved methods for estimating technical methods in non-life insurance

In co-operation with the insurance industry, a technical calculations committee on methods for estimating technical provisions in non-life

insurance has been set up late 1993. On the basis of proposals from this committee regarding adjustments of the previously established methods, the supplementary regulations on technical provisions were amended in November 1994. These amendments include considerations around the estimation of minimum requirements for technical provisions in "Workmen's compensation insurance".

Quality of equity and subordinated capital

Any increase in equity and subordinated capital except for ordinary retained earnings has to be approved by Kredittilsynet. Usually, the equity and subordinated capital is increased by issuing shares and taking up limited or perpetual subordinated debt. However, Kredittilsynet is being presented many suggestions regarding the use of new financial instruments, particularly from foreign financial management companies. Often classical additional capital instruments are transformed into subordinated loan capital and the companies apply for permission to include them in the core capital. It is a concern for Kredittilsynet to ensure the quality of the equity and subordinated capital, so that it may function as a real buffer in case of increased losses at the institutions. At the same time, it shall satisfy the general requirements of internationally accepted capital standards. Whenever handling applications for raising subordinated capital, Kredittilsynet has emphasised issues related to yield structure, default clauses, the instrument's ability to cover losses and the payback options. An amendment in the supplementary regulation prohibits the inclusion of default clauses in the subordinated capital agreements. Through the process of approving such instruments, Kredittilsynet will keep working on improving the quality of the financial institutions' subordinated capital.

Capital expansion

Due to the improved situation in the banking sector, it has now become easier for the banks to raise capital in the market than during the years of crisis. Five commercial banks were granted authorisation to increase the share capital by a total of NOK 4,254 mill. in 1994. In 1993 five authorisations were granted totalling NOK 488 mill. Four savings banks were authorised to increase their capital by NOK 554 mill. in 1994, while three savings banks were allowed to increase their capital by NOK 126 mill. in 1993. Seven banks, including two commercial banks, have been allowed to raise subordinated loans totalling NOK 3,526 mill. The figure for 1993 was NOK 1,984 mill.

DOCUMENTARY SUPERVISION AND ANALYSIS

The supervision based on documents ("off-site" supervision) comprises the collection of accounting data and capital adequacy data from financial institutions and insurance companies, control of the data, analyses of the capital adequacy, control of various statutory requirements and a review of the annual accounts. The financial status and trends are being analysed on the company level and group level. Reports are being generated regarding the development in the companies' results, the capital adequacy, and the trend in the aggregate balance sheet figures for each group of institutions. A process has been started to develop methods of analysis, improve the early warning systems and the reporting and collection of

The banks could more easily raise capital in 1994. Kredittilsynet is however careful in allowing new instruments as subordinated capital or equity capital, and particularly as core capital

In 1994, the priority was on solvency and result improvements. New reporting routines applicable to the largest institutions were introduced

information. The collection of data is to a large extent done in cooperation with Statistics Norway and Norges Bank.

Analyses of the institutions' solvency and revenue trend was prioritised in 1994 as well. The fall in interest rates caused a significant fall in the market value of the certificate- and bond portfolios. Therefore a new quarterly reporting on holdings of shares and bonds and on the interest rate sensitivity of the bond portfolio was introduced for the largest institutions. Particularly the life insurance companies, where certificates and bonds make up a significant part of their assets, are closely watched. Kredittilsynet regularly forecasts their revenue and solvency.

We have furthermore worked on improving the quality of the reporting. Because of changes in the loss trend, a more thorough reporting was initiated as of the third quarter 1994. The adaptation to the EEA regulations is leading to increased reporting requirements. The new regulation on supervision and control of financial institutions' large exposures will be supplemented by a relatively extensive quarterly reporting.

The reporting of technical provisions in non-life insurance companies

The non-life insurance companies report their technical provisions on quarterly basis. The complexity of this reporting makes a certain co-ordination necessary. Accordingly, a standard report regarding the appointed actuaries' estimation of technical provisions was introduced in 1994, especially with respect to the reports prepared as at June 30 and December 31.

Most non-life insurance companies satisfy the minimum requirements concerning technical provisions, some with relatively good margin. Certain companies have actual loss provisions which are significantly higher than the corresponding minimum requirement.

ON-SITE INSPECTIONS

Solvency supervision plays an essential role at the on-site inspections, and has been performed in the usual manner. Since the quality of the banks' loan portfolio has improved, less emphasis has been placed on reviewing the individual loans, and more emphasis has been placed on the credit granting routines and the requirements regarding documentation and quality control. Asset management, risk-awareness, competence, management and control systems have also been important issues. The documentary supervision plays an important role when selecting the areas and institutions to be inspected.

On-site inspections were also in 1994 concentrated on the large banks and insurance companies. However, a number of smaller and medium-size savings banks, particularly savings banks with a high interest rate sensitivity due to heavy exposure in bonds, have also been inspected, while financing companies and mortgage companies have been given less priority. There has been a significant increase of inspections at pension funds.

There has been 49 inspections at banks and finance companies in 1994, compared to 52 in 1993. Inspections at foreign subsidiaries or branches of Norwegian banks are included. Such inspections form part of the

Credit process, asset management, risk awareness, competence, management and control systems, have been given priority at on-site inspections. Larger banks and insurance companies have been inspected. The supervision of pension funds has been intensified

consolidated supervision of groups. According to the EEA agreement, Norway is responsible for the supervision of Norwegian banks' branches in London.

Ten inspections have been performed at insurance companies (vs. 16 in 1993). 15 municipal, regional and private pension funds were inspected, vs. 9 in 1993. Larger pension funds have been a priority. Periodical accounting meetings have been held with the largest institutions under supervision. The on-site inspection activity has in addition been followed up by ad hoc meetings with the supervised entities. Kredittilsynet has talked about its experiences from on-site inspections etc. at seminars for pension funds.

The general impression is that several of the supervised institutions could improve their management and control routines within asset management and within the monetary and foreign exchange activities. Some institutions lack standardised routines. Some pension funds had faulty internal management and control routines within asset management and lacked guidelines for the employees private trading of securities. In one pension fund, Kredittilsynet discovered a fundamental weakness in the derivatives trading system, and a couple of pension funds were criticised for their employees' personal trading.

Upon inspecting the property management activity at a bank, Kredittilsynet found reasons to criticise several aspects regarding the management, inter alia for conflict of interest and for breaching the bank's ethical norms. As a consequence, the bank's managing director and the manager of the real estate company renounced their positions.

Rationalisation and quality improvement efforts have been continued, and much effort has been put into further developing the supervisory methods and in preventive projects. There is an on-going effort to improve the systematic follow-up of the internal control and IT issues in the banks.

MAIN CASES

Issues regarding conflict of interest

The Ministry of Finance requested Kredittilsynet to investigate the handling of certain limited partnership projects by Christiania Bank & Kredittkasse. The main issue of the investigation was the question of conflict of interest.

As a result of the investigations, Kredittilsynet asked most banks to conduct internal investigations as to the participation of employees and trusted officials in limited partnerships.

After this investigation, the banks have become stricter in imposing their ethical guidelines and routines.

Insurance companies under public administration

During the year 1994, Kredittilsynet has had regular contact with the administration boards of Star Forsikring AS u.o.a. (under public administration) and Strand Kredittforsikring AS u.o.a. Also the parent company Star Holding AS is under public administration.

Kredittilsynet's impression is that the institutions can improve their management and control routines. Some institutions lack formalised routines

In some cases, Kredittilsynet discover serious faults and flaws at the institutions. Such cases are often sent to Økokrim

**No companies
were placed under
public
administration in
1994**

Strand Kredittforsikring AS u.o.a. will not be able to meet the claims of others than the preferential creditors. Thus only preferred claims have been examined at the creditors' meetings. The examination of claims on Star Forsikring AS u.o.a. has started. The administration board has discovered extremely reproachful conditions in the Star group. Økokrim has indicted individuals on the board of directors and in the management of some of the companies in the group. The administration board has procured an originating summons in order to try whether any of the involved persons are liable for damages.

Credit insurance companies and non-life insurance companies-guarantee funds

Kredittilsynet is the secretariat for both guarantee funds. The objective of the funds is to prevent or reduce losses for policyholders under direct insurance contracts in Norway. In connection with the public administration of Star Forsikring AS and Strand Kredittforsikring AS, questions have been raised regarding the scope of the funds.

It has been decided that the credit insurance companies guarantee fund should cover insurance claims against Strand Kredittforsikring AS u.o.a. The non-life insurance companies guarantee fund will examine the questions of payments to Star Forsikring's policyholders and the timing of such payments as and when the creditors' meetings are held.

Both guarantee funds are considering whether there are any grounds for legal prosecution in order to cover the losses which the guarantee funds and their contributing members may incur.

UNI Storebrand International Insurance AS

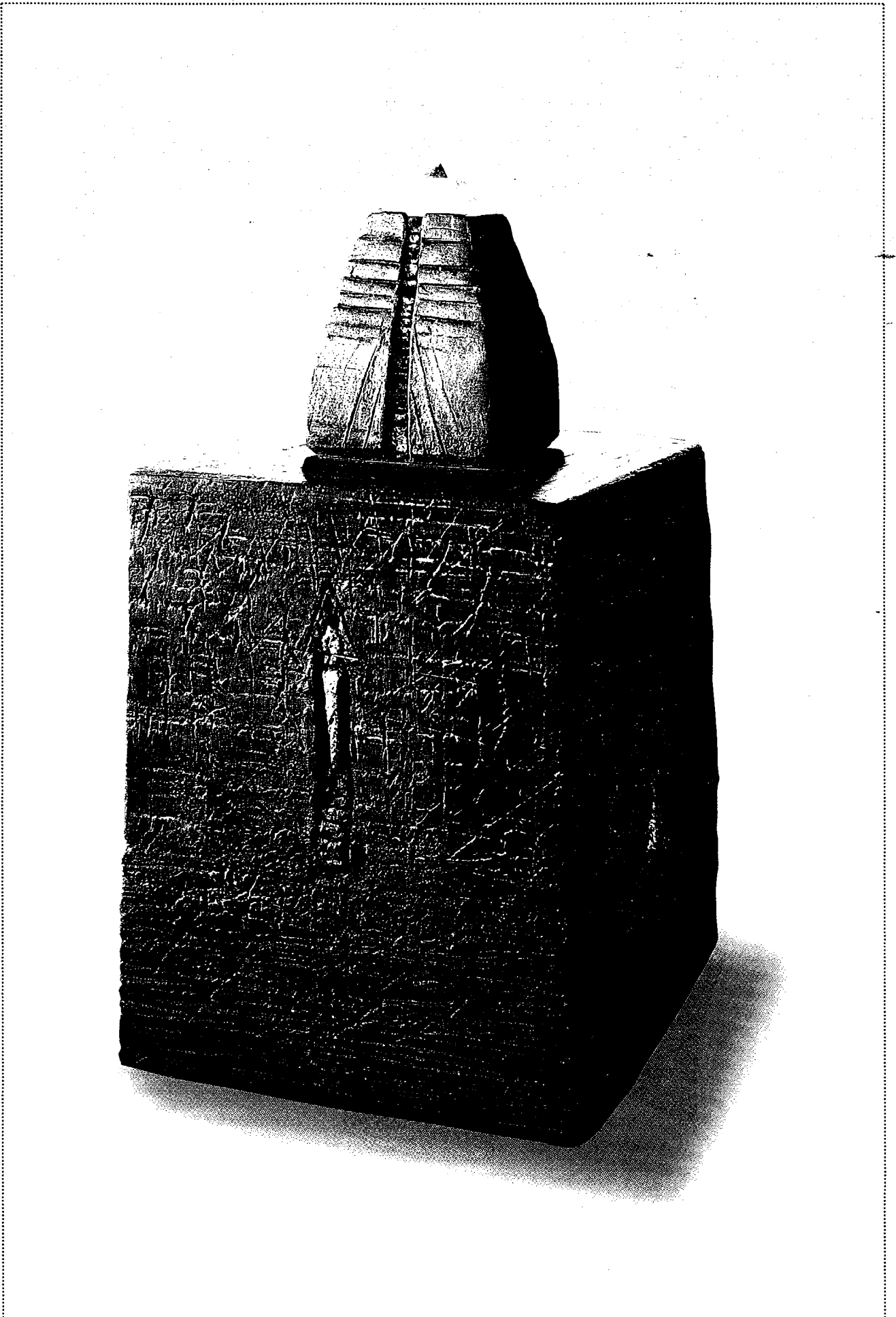
In the beginning of 1994, the UNI Storebrand group decided to withdraw from the international reinsurance market by winding up its subsidiary UNI Storebrand International Insurance AS. One reason was weak results during the period 1990-93, and the ensuing difficulties in fulfilling the requirements regarding own funds and technical provisions.

EVOLUTION AND REVISION OF LAWS AND REGULATIONS

Banking and finance

Kredittilsynet has drawn up proposals for new regulations and amendments to existing regulations in view of adapting the Norwegian regulations to the EEA agreement. Harmonised regulations ensuing from the EU directives have been introduced, and any rules discriminating citizens from other EEA countries have been repealed, including the rules on ownership restrictions in the financial legislation. The regulations are laid down by the Ministry of Finance.

* *The money laundering regulation* is partly a result of the EEA agreement and partly a consequence of international conventions. The regulation which entered into force on 15 February 1994, stipulates measures to prevent that financial institutions be used for money laundering purposes and includes inter alia procedures for identification, registration of suspicious transactions and notification requirements.



KAILAS clay/stoneware, polished gold and cristal, 21 x 21 x 41 cm. Photo: Knud Larsen.

As part of the EEA agreement, the EU's provisions in most areas have been implemented without major problems. This is to a large extent due to the fact that Norwegian legislation, for some time, has been adapted to international standards. Future adaptations to EU regulations, ensuing from the EEA agreement, will probably not cause major difficulties in the financial sector

* *A regulation regarding the credit institutions' own funds* came into force 13 April 1994 and shall ensure that Norwegian credit institutions build up own funds up to the minimum requirement of 5 mill ECU. The own funds of established institutions may not fall below the level of the own funds as at 2 May 1992.

* *The regulation regarding branches of credit institutions* regulates the establishment in Norway of branches of credit institutions from other EEA countries and certain types of subsidiaries. The regulation came into force on 2 May 1994. The provisions are as similar as possible to the provisions applicable to Norwegian banks.

* *Rules regarding the division of supervisory responsibility between the home country supervisor and host country supervisor* have been given. The regulation came into force on 1 June 1994.

* On 7 July 1994, *the regulation regarding cross-border provision of services* came into force. This regulation stipulates the right for credit institutions from other EEA countries and certain subsidiaries to provide services in Norway.

* *A regulation regarding large exposures* has been drafted, and will apply to all financial institutions, including insurance companies. The principal rule is that financial institutions may not have a large single claim exceeding 25% of their own funds. The sum of large claims, i.e. claims corresponding to over 10% of the institution's own funds, may not exceed 800% of the institution's own funds.

* Furthermore, *a regulation regarding consumer credit* has been drafted. The regulation stipulates mainly minimum requirements regarding the credit agreement for consumer loans between 200 and 20.000 ECU.

* Kredittilsynet has also worked on implementing the directive on capital adequacy ratio for investment companies and credit institutions.

Insurance

Through the additional package to the EEA agreement, Norway adopted the third generation insurance directives, which as of 1 July 1994 ensure a single market for insurance services in Europe. Concurrently, the Act on Insurance Activities was amended. The regulation concerning cross-border provision of services which entered into force on 7 July 1994, allows for life and non-life insurance activities across borders for insurance companies from other EEA-countries in Norway. Kredittilsynet has drafted a number of new regulations and amendments to current regulations aiming at implementing the directives. Not all the regulations were in force by April 1 1995. Most regulations are to be laid down by the Ministry of Finance.

* *A new regulation regarding notification requirements* for calculating scales of premiums and technical provisions entered into force 10 November 1994. The regulation impose the life insurance companies to report to Kredittilsynet specific information related to calculating scales and technical provisions etc. for life insurance products.

* The requirement that the methods applied to calculation of the insurance fund and the basis for calculation of capital value shall be approved by Kredittilsynet, have been removed from the Insurance Activities Act and shall be replaced by a *regulation regarding premiums and technical provisions in life insurance*. The draft regulation contains among other things rules regarding the maximum basic interest rate which may be used in the calculation basis when computing premiums,

and gives Kredittilsynet the authority to impose upon the companies to make additional reserves for solvency purposes.

* *The draft regulation on insurance companies' investments* stipulates a number of rules regarding the management of assets, inter alia diversification rules.

* *The draft regulation regarding the transfer of insurance portfolio* concerns the transfer of its portfolio of contracts, concluded under either the right of establishment or under the freedom to provide services.

* *A draft regulation regarding the solvency margin for insurance companies* stipulates inter alia requirements that an insurance company shall have capital in addition to the technical reserves, the so-called solvency margin. The solvency margin is calculated on basis of the extent of insurance activities, and shall serve as a buffer against insurance risk and financial risk. The solvency requirements will apply in addition to the Norwegian capital adequacy rules.

* *Another draft regulation specifies rules for insurance companies from other EEA countries regarding the establishment of branches or provision for freedom to provide services in Norway.* Companies which are authorised to conduct insurance activities in their home country, may conduct insurance activities in Norway based on their home countries authorisation.

* A regulation has been drafted *regarding the provision of services and establishment of branches of Norwegian insurance companies within the EEA.*

* A regulation has been drafted *regarding the insurance companies duty to disclose information according to the Insurance Contract Law.*

* A proposed new regulation regarding *insurance intermediaries which among other things sets up requirements for the establishment of insurance agencies and insurance brokerages.*

* The regulation regarding *record keeping and statement of accounts in life and pension insurance* on policyholder level is currently being revised. The regulation specifies for example the type of information to be disclosed annually to the policyholders.

Securities trading

Uncertainty regarding the interest rate trend characterised the securities market in 1994. Until October interest rates had been rising, since then, the interest rate level has been falling and the stock index rising

Secondary trading in government bonds dominated the market also in 1994

GENERAL FEATURES

During most of 1994, the securities market was characterised by unrest and nervousness. This may first of all be ascribed to the uncertainty and shifting expectations regarding the development in the interest rate level in Norway, as well as in the international arena. After a period of rise until October 1994, the interest rate level has been falling and the stock indices rising. In 1994 as well, the Norwegian interest rate market implied significantly higher yields on long term investments.

The sharp fall in interest rates led to a significant rise in the equity market in 1993. The volume of trade and new issues of shares stagnated somewhat in 1994. NOK 122.6 billion worth of quoted shares were traded, compared to NOK 124.2 billion in 1993. There has been less new issues in the equity market compared to 1993. A diffident attitude among investors and lower share prices most of the year have probably affected the market. Official statistics, however, show a significant volume of share issues, totalling NOK 12.5 billion, a large part being the Norwegian government's and foreign investors' subscription of NOK 4.7 billion in Norsk Hydro. The issue level of shares in 1993, including issues in companies acceding the equities market after the new year, was estimated at about NOK 12. billion. The figures for 1993 were however affected by special circumstances, e.g. the re-financing of UNI Storebrand.

There was a high activity level in the bond market during the first quarter, both in sales volume and new issues. As a consequence of the interest rate trend and partly down-graded estimates on government lending needs, the volume of new issues has fallen compared to 1993. Secondary trading in government bonds took up a dominant and increasing part, in certain periods up to 80-90%, of the market.

Total assets in securities funds (UCITS)² have grown moderately in 1994 compared to 1993. This may be due to periodical weak results following a price fall in the markets for bonds and equities. The aggregate value of the securities funds investing in shares as at 31.12.94 was NOK 15 billion compared to NOK 14.2 billion in 1993. The aggregate value of the securities funds investing in bonds as at 31.12.94 was NOK 21,2 billion compared to NOK 22.6 billion in 1993.

THE SUPERVISORY FUNCTION

On-site inspections have been carried out at all brokerage firms in 1994, partly as a complete inspection of the firm and partly as an inspections of certain activities. Increased emphasis has been placed on thematic inspections, i.e. control of the compliance with specific regulatory provisions. This requires less resources and enables the control of all brokerage firms. In addition, the follow-up of prior warnings and orders has been a priority.

The following themes have been of particular interest:

- the management of clients' funds,
- the keeping of order books and sales records,
- routines regarding the trade in derivatives,
- possible assistance in punishable offences or breach of good business practice by institutional investors, resulting from an intermingling of the employees' and the employer's interest.

Ordinary inspections have been conducted in about half of the management companies for securities funds. In addition to looking at the activities and the organisation, emphasis has been placed on examining the internal guidelines and control routines. Compliance with investment constraints and the management companies' computation of unit values have also been stressed.

Supervision of transactions, i.e. supervision of the compliance with rules of conduct in the market, has also been given much attention. The focus has first and foremost been on issues related to insider trading, clearance responsibilities and price manipulation. A preventive effect has been emphasised, inter alia through random checks and controls. Two major cases were uncovered after random checks.

Kredittilsynet has invested in improved information systems and mathematical models, which have proven useful as for example when controlling for price manipulation or whenever there have been suspicions of insider trading.

Increased efforts towards thematic supervision, follow-up supervision and transaction supervision combined with demanding individual cases have inevitably led to fewer full-fledged inspections of individual brokerage firms.

A new Act on Securities Funds imposes new requirements regarding the management companies' duty to draw up articles of association for the securities funds. Kredittilsynet has drawn up standard articles of association. This has simplified the work for the management companies and made the task of approving the articles of association easier for Kredittilsynet.

MAIN CASES

The pricing of non-standardised products

After a pension fund lost significant amounts trading in derivatives and

The securities market has functioned well, even though some reprehensible cases have been uncovered at several stock brokers

interest-bearing instruments, Kredittilsynet investigated inter alia the size of the commissions three of the involved brokerage firms had charged for trading the non-standardised options on interest-bearing instruments. At one of the firms, Kredittilsynet found that the commission was unreasonably high in proportion to the service rendered. The firm was also criticised for their significant secondary trading in non-standardised options, which normally is not allowed. The second company was criticised for a number of issues. The commission was considered to be too high compared to the services rendered, and the firm did not have adequate competence to trade in non-standardised options on interest bearing-securities. The firm was furthermore not able to show the necessary documentation regarding the transactions. The third brokerage firm was not criticised for its part in the transactions.

Brokerage firm suffers significant losses on trading in interest rate futures

In April it became evident that one brokerage firm had lost about NOK 300 million trading in interest rate futures, mostly from trading on own books in foreign interest rate futures. At the time, the brokerage firm had an equity capital amounting to NOK 130 million. Kredittilsynet followed the developments closely and let the company have the opportunity to lower its exposure before the situation became known to the public. There was a constant dialogue with the owners' representatives regarding re-capitalisation of the company. The firm would only be allowed to continue operating if an immediate injection of equity capital or subordinated capital was pledged. After the re-capitalisation had taken place, the company was examined in order to find an explanation for how these losses could occur.

Kredittilsynet's conclusion was that a range of circumstances led to the losses:

- lack of competence in handling the settlement and accounting of the trade in interest rate futures,
- faulty registration of actual sales,
- unsatisfactory internal reporting and control routines.

The chief broker had exceeded his broad powers, but this was not detected by the internal control routines. Lack of accounting systems caused continuous matching problems. The matter has been forwarded to Økokrim.

Illegal and reproachful handling of bond issue

In a random check, Kredittilsynet investigated the issue of a subordinated loan in fall 1993. Several reproachful and partly illegal matters were revealed. A brokerage firm was responsible for the management of the issue, which was very favourable since the coupon rate was significantly higher than the market rate at the time of subscription. Fictitious underwriters were used, hiding the fact that the brokerage firm itself was the real underwriter at the time of subscription. When allotting the loan, the brokerage firm gave itself bonds amounting to a large sum, without subscription. A number of subscribers were allotted smaller amounts than they were entitled to. The brokerage firm did not document its real responsibility as underwriter and did not reveal its own allotment neither to other parties involved nor in the form of internal documentation. The same day as the issue allotment took place, the brokerage firm sold a

large part of its bonds to a subscriber who had seen his subscription reduced by the same amount. The purchase price was significantly higher than the subscription price. The identity of the seller was not revealed, contrary to regulations. The brokerage firm made a significant profit on the transaction, at the expense of the customer. The external underwriter did not receive any underwriting commission. The roles of the firm should have been disclosed in the monthly reporting to Kredittilsynet. Because of incorrect reporting, Kredittilsynet was not immediately made aware of this. The matter has been forwarded to Økokrim.

Lack of funds on clients' bank account

At an inspection of a brokerage firm, Kredittilsynet discovered a significant deficit on the clients' bank account. In addition, the firm lacked satisfactory routines for the safe-keeping, follow-up and balancing of the clients' funds. In two cases, the clients' bank account was lacking funds. In both cases, the firm had custody of over NOK 10 million. The abuse occurred at a time when the firm had overdrawn its bank overdraft facilities. The matter has been reported to Økokrim.

Illegal sale of Norwegian bonds abroad

In spring 1993 the media and the Storting (the Norwegian Parliament) showed a renewed interest in the irregular sale of bonds through Norges Bank (the Central Bank) in 1984 and 1985. The matter had previously been investigated by Kredittilsynet and a report had been sent to the public prosecutor in November 1987. The public prosecutor dismissed the case in December 1989. In 1991 Kredittilsynet sent a summary of the case and of the police investigation to the Ministry of Finance.

On the basis of the renewed interest, the Ministry of Finance requested that Kredittilsynet should examine whether there may be new aspects in the case and whether there would be any grounds for requesting the re-opening of the case. New investigations in Norway and abroad, e.g. in Guernsey, led to a report by Kredittilsynet to the director of public prosecution in November 1994, requesting the re-opening of the case.

NEW REGULATIONS

A number of statutory amendments have been brought about, most of them as a result of the adaptation to the EEA agreement. Significant amendments to the Act on Securities Funds came into force 1 January 1994. At the same time, several amendments to the Act on Securities Trading were implemented, e.g. an amendment allowing foreign and Norwegian financial institutions and foreign investment firms to conduct brokerage activities in Norway.

In February, the Ministry of Finance established a committee with the objective to revise the Act on Securities Trading. The new act will come into force on 1 January 1996. Kredittilsynet has a representative on the committee and shares the secretariat function with the Ministry of Finance. During 1994, the Ministry of Finance implemented a number of regulations. Several were drafted by Kredittilsynet.

* In January the following regulations came into force: a new *stock*

A number of rules and regulations have been amended, inter alia as a consequence of the EEA agreement. Revisions of the Act on Securities Trading have commenced, and a new act is expected to enter into force 1. January 1996

exchange regulation, regulations on prospectuses for the issue of unlisted securities and for the issue of unlisted securities over a certain amount, and a regulation regarding the duty to draw up invitations to subscribe for certain securities and the content of such. An interim regulation regarding the trade in options listed on a foreign stock exchange was repealed by a new regulation in February.

* Based on *the annex to the regulation regarding branches of banks and other credit institutions with their head office in another EEA member state*, branches may conduct securities brokerage activities. At the same time the regulations regarding the banks' brokerage activities and the separation of such activities from the banking activities were repealed. The banks may thus again conduct their brokerage activities within the legal framework of the bank. On the basis of this, and the possibility to open branches in Norway, a need was felt for more detailed regulations regarding the internal organisation of the brokerage activities. Kredittilsynet has thus, in consultation with the Ministry of Finance, issued guidelines which require that the banks establish routines in order to ensure that the brokerage activities are not intermingled with the other activities of the bank.

* *The regulation regarding foreign companies' right to act as account operator in the Norwegian Registry of Securities (Verdipapirsentralen)* was issued in January. The regulation allows branches of credit institutions established in Norway and headquartered in another EEA country, to act as account operators in the Norwegian Registry of Securities.

* *The new regulation regarding the freedom to provide services for banks and credit institutions headquartered in another member state of the EEA*, also covers brokerage activities.

* *A regulation regarding the provision of services of investment firms from another member state of the EEA* has been implemented. The regulation allows firms which conduct securities brokerage activities, but which are not credit institutions, to trade in Norwegian securities in Norway.

* In June, a regulation was adopted *regarding the right of securities funds headquartered in another EEA state and which comply with the Council Directive 85/611/EEC (UCITS) to market and sell their units in Norway*. According to the regulation, the units may be offered and sold through representative offices, sales representatives in Norway or directly from the securities fund's home office.

* *A regulation regarding prospectus for securities funds* has been issued. The regulation requires that management companies issue a prospectus containing the information necessary for the unit subscribers be able to assess the proposed investment. The regulation gives detailed rules about the contents of the prospectus.



FUGL stoneware, 43 x 64 cm, KE. Photo: BLUELINE.

International activities

The EEA agreement bestows upon Norwegian authorities important consultation rights.

Kredittilsynet will emphasise good bilateral contacts with the EU countries, including Sweden, Finland and Denmark. The Nordic co-operation may prove to be very important and must be given particularly priority by Norwegian authorities

1 994 was characterised by increased international activity. The internationalisation of the financial markets and the harmonisation of regulations imply an increased and closer co-operation between supervisory authorities. The number of meetings, seminars and conferences, either on a bilateral or multilateral basis is increasing, whereby supervisors have the opportunity to exchange their experience and knowledge regarding supervisory methods.

The EEA agreement led to a significant increase in international activities. Like other authorities from Norway and from the other EFTA countries which were parties to the EEA agreement, Kredittilsynet was called to advisory meetings before the meetings in the EU Banking Committee and Insurance Committee, and participated at subsequent orientation meetings. In the committees' working groups and expert groups, Kredittilsynet has had an observer status, which in practice was close to the EU countries' own status.

In the independent co-operative bodies for banking supervision (Groupe de Contact) and insurance supervision (The Conference of Insurance Supervisory Authorities of the European Union), there has been a period of shifting participation. It appears that the EEA countries which are not member of the EU will be able to participate in the meetings as observers, i.e. with the right to speak but not to vote.

EU committees and working groups on supervisory issues:

Banking

Banking Advisory Committee

Groupe de Contact

EMI - Banking Supervisory Subcommittee

Insurance

Insurance Committee

The Conference of Insurance Supervisory Authorities of the European Union

Securities trading

Meetings of supervisory authority chairmen

Norway has, together with the other EEA countries, participated in advisory meetings for authorities supervising securities markets.

Since Norway had applied for membership in the European Union, the Norwegian authorities were admitted as observers in all bodies, committees and groups under the Commission (including the Insurance Committee) and the EU council after 1 July. Norwegian authorities were also invited to participate in the Banking Committee. This does not longer apply after the referendum.

The EU commission organises expert meetings, and Kredittilsynet sent experts to the preparatory discussions to the negotiations regarding the additional package to the EEA agreement. The expert meetings were

arranged by EFTA's "Standing Committee". In addition, Kredittilsynet has participated in seminars regarding the interpretation of a number of directives, organised by EFTA and by the EU commission.

The Conference of Insurance Supervisory Authorities of the European Union meets twice a year. This conference is not a formal EU institution, but is reserved for EU members.

In 1994, Kredittilsynet participated at two common meetings between the EEA insurance supervisory authorities. The status of implementation of the third generation insurance directives was discussed and compared. The co-operation between the supervisory authorities was the specific topic at a seminar in fall 1994. A meeting of the EFTA countries' insurance supervisors was held in Oslo in spring 1994. The purpose of the meeting was to prepare the co-operation with the EU countries ensuing from the EEA agreement. Within the insurance sector, the supervisory authorities of the EU countries have informally adopted a common protocol of collaboration. The new EU members' supervisory authorities will adhere to the protocol, while a separate supervisory protocol of collaboration is being suggested for the remaining EEA countries.

Within the banking sector, there is no such common document of collaboration. However, the collaboration is formally drawn up in bilateral documents between supervisory authorities, called "Memorandum of Understanding" (MoU). During the course of 1994, Kredittilsynet signed several MoU's. These are agreements which formally lay out the responsibilities and co-operation regarding the supervision of banks and credit institutions which have established branches or provide services in the respective countries. In 1994 Kredittilsynet signed MoU's with Bank of England, Finanstilsynet in Denmark, Banktilsynet in Finland, Finansinspektionen in Sweden, Sedlabanki Islandi in Iceland, Commission Bancaire in France and Institut Monetaire in Luxembourg. Towards the end of the year, discussions were initiated with the central bank of the Netherlands. The signature of a MoU is expected in 1995. Contacts have also been established with German supervisory authorities.

International co-operation outside the European Union and the European Economic Area

The liberalisation and internationalisation of the financial markets is not only happening within the EEA, but is a world-wide phenomenon. In the securities field, there is an increased need for co-operation and communication. Kredittilsynet is participating at annual meetings in IOSCO (the International Organisation of Securities Commissions) and ISMA (the International Securities Market Association) in addition to bilateral meetings. Within the OECD there is also on-going work aiming at liberalising the financial markets. At the same time, there is an increased need for contact and communication between countries regarding supervision and regulation of the national markets. Kredittilsynet participates regularly at the meetings in the OECD's

Participation of Kredittilsynet in EU and EEA meetings abroad:

	Number of meetings
Expert meetings:	8
EEA-seminars:	3
Working groups:	17
Misc. Committees:	9
Other common meetings/conferences:	3
Bilateral contact meeting with EEA supervisors (including 4 MoU meetings abroad):	8
Total number of EU/EEA meetings:	48

In the opinion of Kredittilsynet, emphasis should be placed on building competence and capacity in international issues

Insurance Committee and the Capital Markets Committee. Kredittilsynet also co-operates with other authorities and receives useful information when participating at meetings organised by the Basel Committee on Banking Supervision.

The IAIS (International Association of Insurance Supervisors) was founded in 1993, thereby formalising the co-operation between supervisory authorities on a world-wide basis. Kredittilsynet participated at the first meeting of the IAIS in 1994.

Denmark, Sweden and Norway are the only countries with a common supervisory authority for the whole financial sector (i.e. banks, financial institutions, insurance companies and securities trading). A routine practice of common Nordic meetings has been established, where Finland and Iceland also participate. There is a close co-operation between the Nordic supervisory authorities regarding professional challenges, administrative matters and in international organisations.

Kredittilsynet participates together with Økokrim and the Ministry of Finance in the international efforts to combat money laundering, by attending the meetings of the FATF (Financial Action Task Force on Money Laundering). Kredittilsynet has also participated in a conference organised by the European Council which aimed at attracting Central and Eastern European countries into this co-operation. At a FATF meeting in April 1994, a report regarding the money laundering situation in Norway and the Norwegian authorities' measures to combat money laundering was presented. The conclusion of the report regarding the Norwegian regulations was mainly positive.



BLÅ FISK clay/stoneware, diam. ca. 40 cm. Photo: Knud Larsen.

The organisation

The organisation of Kredittilsynet is in a positive phase, with many new and highly qualified employees and a more efficient utilization of resources

THE BOARD

Kredittilsynet is headed by a board of five members. The members and alternates are appointed by the King in Council for a period of four years. On 3 December 1993 the following board was appointed for the period 1994-1997:

Mr. Erling Selvig, Professor, Dr. Juris, Chairman
Ms. Else Bugge Fougner, Supreme Court Justice, Deputy Chair
Mr. Asbjørn Rødseth, Professor
Ms. Mary Kvidal, Deputy Director of Education
Mr. Ingebrigt Børsheim, Managing Director

Alternates:

Mr. Jan Halvorsen, Director
Ms. Hilde Louise Krogh, Government Authorised Auditor

Mr. Harald Bøhn, Deputy Director, Norges Bank, was appointed observer to the board.

As of 25 November 1994 Ms. Turid Hundstad, Director and Mr. Steinar Undrum, Director, are replacing Ms. Hilde Louise Krogh and Mr. Jan Halvorsen.

Two members elected by and from among the employees supplement the board when administrative matters are dealt with. Employee representatives in 1994 were Ms. Runa Christiane Sæther, Deputy Director General, Ms. Kjersti Elvestad, Adviser

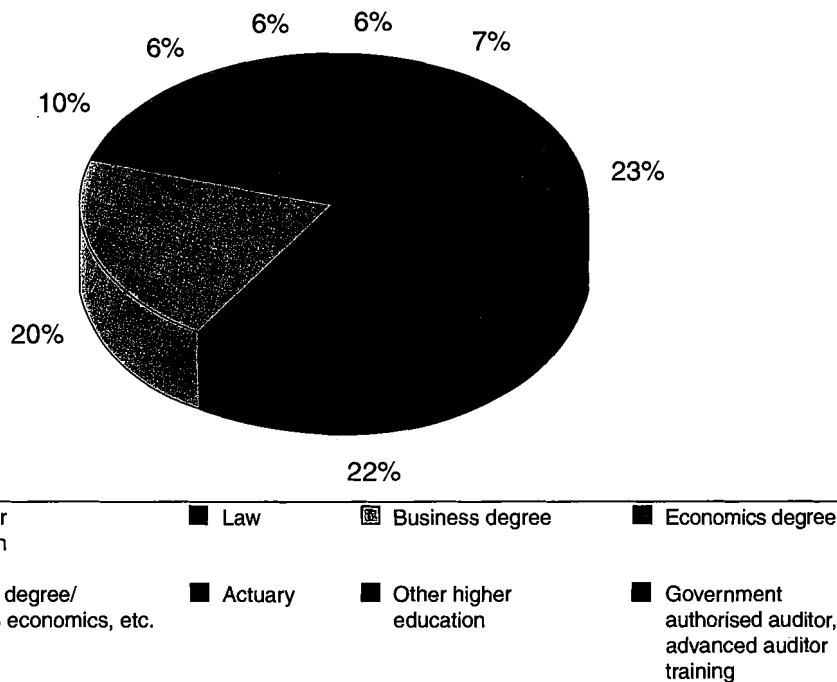
The board held 15 meetings in 1994. In addition, a number of resolutions were adopted based on circulation to board members. The board dealt with altogether 143 supervisory and administrative matters. In addition, a large number of matters were submitted to the board for their information only.

ADMINISTRATION AND HUMAN RESOURCES

Fourteen new positions were added to Kredittilsynet in 1994, bringing the total number of positions to 131. At year-end there was a permanent staff of 124, compared to 109 at year-end 1993.

In 1994, 33 vacancies were advertised including 5 internally. There were 650 applicants to these positions. There was in general a satisfactory flow of high-quality applicants recently graduating from a university or with an equivalent degree. Kredittilsynet also considers it important to recruit staff with substantial experience from its areas of supervision. At year-end 1994, 25 staff members had such experience, of which 5 were on short term contracts, compared with 21 the previous year. 77% of the staff has a higher education, compared to 74% in 1993.

Staff education background, 31. December 1994



FINANCES

Kredittilsynet's total expenditure for 1994 came to NOK 67.7 million. Remuneration, national insurance and superannuation amounted to NOK 40.7 million, an increase of 15% on 1993.

The expenses incurred by Kredittilsynet are, according to the Act on the Supervision of Financial institutions, Insurance companies and Securities trading etc., to be covered by the institutions under supervision at the beginning of the financial year. The expenses are distributed on the different institutions based on the extent of supervision, and are being levied the year after the expenses have incurred. Total amount to be levied in 1993 was NOK 50.9 million and was approved by the Ministry of Finance 19 September 1994. There were 3.701 supervised entities in 1993, which is 1.484 entities less than in 1992. This decrease is due to the fact that auditors who did not have their own independent business in 1993 have been left out. Nevertheless, the auditors still represent 63% of the institutions under supervision. In the other areas of supervision there is a slight increase in the number of supervised entities.

Kredittilsynet's total expenditures in 1994 came to NOK 67.7 million. The number of positions within the organisation has increased by 27 percent since 1992, and expenses for remuneration, national insurance and superannuation increased the most. Kredittilsynet has to expect a relatively high increase in these costs in 1995 as well

NUMBER OF SUPERVISED ENTITIES AS AT 31.12.94

BANKS AND FINANCIAL INSTITUTIONS

- 132 savings banks
- 17 commercial banks (including 3 foreign banks)
 - Norges Postbank (the postal bank)
 - 9 branches of Norwegian banks abroad
 - 3 branches of foreign banks in Norway
- 44 financing companies
 - 1 branch in Norway of foreign financial institution
- 14 mortgage institutions

INSURANCE

- 10 life insurance companies
- 54 non-life insurance companies
- 20 regional marine insurance associations
- 20 insurance brokers
- 39 regional fire insurance associations
- 15 general agents of foreign companies
 - (3 are being wound up)
- 131 private pension funds
- 138 private pension schemes
- 33 municipal pension funds and pension schemes
- 22 private relief funds

SECURITIES TRADING

- 31 brokerage firms (including 26 which also trade in options and 11 active management companies)

- 25 management companies
- 15 limited partnership brokers

REAL ESTATE AGENTS

- 288 real estate agents
- 843 independent lawyers providing real estate brokerage services

DEBT COLLECTING AGENCIES

- 133 debt collection agencies

AUDITORS

- 3699 auditors
- 426 auditing firms

DATA PROCESSING CENTRES

- Norsk Opsjonssentral (The Norwegian Option Clearing house)
- Verdipapirsentralen (The Norwegian Registry of Securities)
- Bankenes Betalingssentral (The Interbank Payment System)
- Fellesdata

OTHER

- The Brønnøysund Registry (Register of Accounts)
- The Accountants Authorisation Board

Kredittilsynet Organisational plan

The Board
Erling Selvig
Chairman

Director General
Bjørn Skogstad Aamo

Chief legal advisor
Marius Nygaard Haug

Adm. Dept.
Deputy Dir. Gen.
Elisabeth
Morthen

**International
Departement**
Deputy Dir. Gen.
Olav Strømme

**Finance and
Insurance Dept.**
Deputy Dir. Gen.
Sven-Henning
Kjelsrud

**Capital Markets
Supervision Dept.**
Deputy Dir. Gen.
Eirik Bunæs

**Accounting and
Auditing Dept.**
Deputy Dir. Gen.
Knut Løken

**Licencing, Laws
and Regulations**
Ass. Dir. Gen.
Kjell Arne
Aasgaarden

**Securities
Markets**
Ass. Dir. Gen.
Anders Kvam

Accounting
Ass. Dir. Gen.
Gøril Onarheim

**Documentary
Supervision and
analysis**
Ass. Dir. Gen.
Runa Sæther

**Estate Agents and
Brokers, Debt-
collection firms**
Ass. Dir Gen.
Magnar Skofteby

Auditing

**On-site
Inspections**
Ass. Dir. Gen.
Harald Hammer

**Supervision of
Ins. Regulations**
Ass. Dir. Gen.
Per Simonsen

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