Consolidated Financial Statements

2012

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Endorsement and Statement by the Board of Directors and the CEO

The Consolidated Financial Statements of Landsbankinn hf. (the "Bank") for the financial year 2012 include the Bank and its subsidiaries (collectively referred to as the "Group").

Landsbankinn was founded on 7 October 2008. The Group offers a complete range of financial products and services for personal, corporate and institutional customers.

Landsbankinn is currently owned by the Icelandic State Treasury, which wields 81.3% of voting rights, and Landskil ehf., which is owned by LBI hf. (formerly Landsbanki Íslands hf.) and wields 18.7% of voting rights.

Operations in 2012

Consolidated profit amounted to ISK 25,494 million for the financial year 2012. The Board of Directors proposes that up to 40% of the consolidated profit will, subject to an approval at a shareholder´s meeting, be paid in dividends to shareholders. Otherwise the profit will be added to the Bank's equity. Consolidated total equity amounted to ISK 225,166 million at the end of the year, including share capital amounting to ISK 24,000 million. The capital adequacy ratio of the Group, calculated according to the Act on Financial Undertakings, was 25.1% at year-end 2012. The number of full-time equivalent positions was 1.233 at year-end 2012.

In the first and second quarters of 2012, the Bank made an early redemption payment and a partial pre-payment of the Secured Bonds in the amount of ISK 72,115 million. These Bonds were issued in 2010 as a part of the acquisition price for the acquired assets and liabilities assumed from LBI hf. The Bank's strong liquidity position in foreign currencies enabled the Bank to reduce its long-term liabilities faster than contractual provisions require.

Shares in the facilities management company Reginn hf. were listed on the NASDAQ OMX Iceland, following a public offering in June 2012. 75% of the Group's shares in Reginn were sold in the public offering and the acquirers became shareholders of Reginn on 29 June 2012. The Group has committed itself to hold the remaining 25% of the shares in Reginn hf. for a minimum of 10 months from 29 June 2012.

The arbitration panel set up to resolve the dispute between the Bank and the National Treasury regarding the fair value of the financial assets of SpKef, presented its conclusions on 7 June 2012. It was concluded that the fair value, payable by the National Treasury to the Bank, was ISK 19,198 million. Following the Bank's review of the fair value of these financial assets a net loss of ISK 2.889 million was accounted for in the Group's financial statements in the second quarter of 2012.

On 15 February 2012 and 18 October 2012, the Supreme Court of Iceland ruled in two separate cases that a lender could not apply the Central Bank interest rates under circumstances specified in the rulings, inter alia, as the lender had issued final receipt of payment of interests. The Group has accounted for the potential impact of the these rulings and recognised expenses in the amount of ISK 38,042 million and ISK 2,120 million in its consolidated income statement at year end 2011 and 2012, respectively. Further court rulings are awaited to obtain final clarification of the precedence of these rulings. The total amount of the estimated impact may change accordingly. The Bank expects that a part of these expenses will be reversed once the application of the Court's precedent has been fully clarified.

In two separate litigations commenced against the Bank during the year 2012, currency indexation of loans is being disputed. It is the position of the Bank that circumstances in these cases differ from that of the circumstances in previous litigations involving currency indexation of loans, which the Supreme Court has ruled illegal, and that the loans now under litigation shall be regarded as loans in foreign currencies. Further description of the circumstances and the status of these legal proceedings is provided in Notes 4 and 37.

On 11 September 2012, Landsbréf hf., a subsidiary of the Bank, obtained a licence from the Financial Supervisory Authority to undertake asset management. The licence provides Landsbréf with the opportunity to manage projects in the field of asset management for third parties and thus expands greatly the company's opportunities to service its customers.

As at 31 December 2012, the Bank's fair value estimate of the Contingent Bond liability was ISK 87,474 million. This corresponds to a nominal amount of ISK 88,142 million, which is lower than the Bond's nominal amount ceiling of ISK 92,000 million. The estimate is that of the management of the Bank, but the final and binding amount of the Bond is still being determined by a third-party valuation agent, whose conclusions are expected to be presented no later than 31 March 2013. The Bank will issue the Bond to LBI hf. no later than 31 March 2013, based on the valuation agent's final amount, converted into EUR at the exchange rate as of 31 December 2012.

Outlook

Landsbankinn estimates that economic growth in Iceland will continue in 2013 and be 2.4%. Growth will be mostly driven by growth of capital formation and private consumption.

Due to restrictions on the movement of capital between Iceland and other countries, the Group's ability to mitigate the risk from ISK related currency fluctuations is limited. However, the Group has taken various measures to decrease its overall currency risk and expects future currency risk levels to be within acceptable limits.

Horn fjárfestingarfélag hf. is a subsidiary of the Bank with holdings in listed and unlisted equities in a wide variety of industrial sectors. These assets will be offered for sale in 2013.

The Bank's core operations are sound and have been improving continuously. Foundations have been laid with new and revised processes to improve efficiency and customer relationship management. The Group has a strong equity and liquidity base and is, therefore, in a strong position to deal with challenges ahead, and become a force for change in the Icelandic economy.

Risk Management

It is the view of the Board of Directors of Landsbankinn that efficient risk management is a strategic tool to enhance value generation. Internal controls should ensure effective operations and prudent management of risks that could otherwise prevent the Group from attaining its business targets.

The Group has continued to improve its risk management framework and policies in 2012, in line with international best practices, and has defined its risk appetite. The Group aims to strengthen further its risk management processes and enhance the risk culture in the coming year. Further description of the Group's risk management is provided in Notes 43-85.

Other issues

At the end of third quarter of 2012, Landsbankinn concluded its strategic review and set out commitments for 2015. The strategy entails a stronger focus on operational efficiency by reducing cost, strengthening management and team unity, while also pursuing responsible and profitable market initiatives. At the same time, the Bank made significant changes to its organisational structure which became effective as of 1 October 2012.

As explained in the Endorsement by the Board of Directors of the Bank's condensed consolidated interim financial statements for the first nine months of 2012 and in the Bank's Annual Report of 2011, it is of great concern to the Board of Directors that the Bank, a public limited liability company operating in a competitive environment, is unable to determine the salary of the CEO of the Bank. The CEO salary and employment conditions are determined by the Civil Servants Salary Board (Kjararáð). The Salary Board has considered itself not to be authorised to set the CEO salary for "daytime work" higher than the nominal salary of the Prime Minister. When introduced, it was the understanding of the Board of Directors that this would be a temporary arrangement to be abolished at the end of 2010. The arrangement, however, continues to be in place. It is concluded in opinions prepared by legal advisors of the Board of Directors that the current arrangement is contrary to the Constitution of Iceland and the Agreement on the European Economic Area.

The Board of Directors has submitted a letter to the Civil Servants Salary Board formally requesting that the Salary Board determine, by way of a new decision, acceptable salary and employment conditions for the CEO. The Salary Board is still considering the matter. The Board of Directors has, moreover, collected data and documentation on salaries for comparable professions during 2011 and 2012 that will presumably serve as a basis for an eventual final decision on the CEO salary and employment conditions for the same period.

Having regard to the above, the Board of Directors considers that it is prudent to make a provision in the amount of ISK 47 million due to possible corrections or retroactive adjustments of the CEO salary and employment conditions for the years 2011 and 2012 that may be considered necessary, inter alia, due to an eventual revision of the Salary Board's decision or on the premise that the relevant provisions of the Act No 47/2006 on the Civil Servants Salary Board, cf. Act No 87/2009, do not comply with the Constitution of Iceland or with the Agreement on the European Economic Area.

Statement by the Board of Directors and the CEO

The Consolidated Financial Statements of Landsbankinn hf. for the year ended 31 December 2012 have been prepared on a going concern basis in accordance with International Financial Reporting Standards as adopted by the EU.

In our opinion the Consolidated Financial Statements of Landsbankinn hf. give a true and fair view of the consolidated financial performance of the Group for the year 2012, its consolidated financial position as at 31 December 2012 and its consolidated cash flows for the year 2012.

Furthermore, in our opinion, the Consolidated Financial Statements of Landsbankinn hf. and Endorsement of its Board of Directors and CEO give a fair view of the development and performance of the Group's operations and its position and describe the principal risks and uncertainties faced by the Group.

The Board of Directors and the CEO have today discussed the Consolidated Financial Statements of Landsbankinn hf. for the year 2012 and confirmed them by their signatures. The Board of Directors and the CEO recommend that the Consolidated Financial Statements of Landsbankinn hf. be approved at the Annual General Meeting of Landsbankinn hf.

Reykjavík, 7 March 2013.

Board of Directors

Gunnar Helgi Hálfdanarson

Chairman

Þórdís Ingadóttir

Sigríður Hrólfsdóttir

Jón Sigurðsson

Ólafur Helgi Ólafsson

CEO

Steinþór Pálsson

Independent Auditor's Report

To the board of Directors and Shareholders of Landsbankinn hf.

We have audited the accompanying consolidated financial statements of Landsbankinn hf. and its subsidiaries, which comprise the consolidated statement of financial position as at 31 December, 2012, the consolidated income statement, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted by the EU, and for such internal control as management determines is necessary to enable the preparation of consolidated 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 consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated 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 consolidated 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 principles 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 consolidated financial statements give a true and fair view of the consolidated financial position of Landsbankinn hf. as at 31 December, 2012, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU.

Report on the Board of Directors report

Pursuant to the legal requirement under Article 106, Paragraph 1, Item 5 of the Icelandic Financial Statement Act No. 3/2006, we confirm that, to the best of our knowledge, the report of the Board of Directors accompanying the financial statements includes the information required by the Financial Statement Act if not disclosed elsewhere in the Financial Statements.

Reykjavík, 7 March 2013.

KPMG ehf.

Helgi F. Arnarson

Sigríður Helga Sveinsdóttir

Consolidated Statement of Financial Position as at 31 December 2012

Notes		2012	2011
	Assets		
8	Cash and balances with Central Bank	25,898	8,823
7,9,38	Bonds and debt instruments	228,208	221,848
7,9	Equities and equity instruments	36,881	46,037
7,10	Derivative instruments	1,043	159
11	Loans and advances to financial institutions	64,349	100,133
12,38	Loans and advances to customers	666,087	639,130
13	Investments in equity-accounted associates	15,528	11,678
14	Property and equipment	6,776	6,437
15	Intangible assets	541	681
22	Deferred tax assets	48	3,003
16	Other assets	14,108	44,001
		1,059,467	**1,081,930**
17	Assets classified as held for sale	25,320	53,552
	Total assets	**1,084,787**	**1,135,482**
	Liabilities		
18	Due to financial institutions and Central Bank	98,718	112,876
19	Deposits from customers	421,058	443,590
10	Derivative instruments and short positions	9,438	7,916
22	Tax liabilities	0	70
20,38	Secured bonds	221,791	277,076
7,21,38	Contingent bond	87,474	60,826
23	Other liabilities	20,249	23,499
		858,728	**925,853**
	Liabilities associated with assets classified as held for sale	893	9,385
	Total liabilities	**859,621**	**935,238**
24	**Equity**		
	Share capital	24,000	24,000
	Share premium	123,898	123,898
	Statutory reserve	5,053	3,781
	Retained earnings	72,120	47,952
	Total equity attributable to owners of the Bank	**225,071**	**199,631**
	Non-controlling interests	95	613
	Total equity	**225,166**	**200,244**
	Total liabilities and equity	**1,084,787**	**1,135,482**

The accompanying notes are an integral part of these consolidated financial statements.

Landsbankinn hf. Consolidated Financial Statements 2012 5 All amounts are in ISK million

Consolidated Income Statement for the Year ended 31 December 2012

Notes		2012	2011
	Interest income	64,661	60,831
	Interest expense	(29,077)	(28,182)
25	**Net interest income**	**35,584**	**32,649**
26	Net adjustments to loans and advances acquired at deep discount	37,320	58,489
4, 26	Loss from foreign currency linkage of loans and advances to customers	(2,120)	(40,726)
26, 65	Net impairment loss	(12,260)	(7,034)
7,21	Fair value change of contingent bond	(27,331)	(34,316)
	Net adjustments in valuation	**(4,391)**	**(23,587)**
	Net interest income after net adjustments in valuation	**31,193**	**9,062**
	Fee and commission income	7,696	7,437
	Fee and commission expense	(3,248)	(3,014)
27	**Net fee and commission income**	**4,448**	**4,423**
28,30	Net gain on financial assets designated as at fair value through profit or loss	5,703	17,459
29,30	Net gain on financial assets and liabilities held for trading	2,169	1,009
31	Net foreign exchange gain (loss)	4,566	(759)
32	Other income and (expenses)	1,062	(450)
	Other net operating income	**13,500**	**17,259**
	Total operating income	**49,141**	**30,744**
33	Salaries and related expenses	13,176	11,990
34	Other operating expenses	8,878	8,467
14	Depreciation and amortisation	719	771
23	Contribution to the Depositors' and Investors' Guarantee Fund	1,042	583
35	Acquisition-related costs	290	245
	Total operating expenses	**24,105**	**22,056**
13	Share of profit of equity-accounted associates, net of income tax	2,449	1,417
	Profit before tax	**27,485**	**10,105**
36	Income tax	(2,925)	1,411
36	Tax on liabilities of financial institutions	(1,200)	(814)
	Profit for the year from continuing operations	**23,360**	**10,702**
	Profit for the year from discontinued operations, net of income tax	2,134	6,255
	Profit for the year	**25,494**	**16,957**
	Profit for the year attributable to:		
	Owners of the Bank		
	Profit for the year from continuing operations	23,360	10,702
	Profit for the year from discontinued operations	2,079	6,271
	Profit for the year attributable to owners of the Bank	**25,439**	**16,973**
	Non-controlling interests		
	Profit (loss) for the year from discontinued operations	55	(16)
	Profit (loss) for the year attributable to non-controlling interests	**55**	**(16)**
	Profit for the year	**25,494**	**16,957**

The accompanying notes are an integral part of these consolidated financial statements.

Landsbankinn hf. Consolidated Financial Statements 2012 6 All amounts are in ISK million

Consolidated Statement of Changes in Equity for the Year ended 31 December 2012

Notes		Attributable to owners of the Bank						
	Change in equity for the year 2012	Share capital	Share premium	Statutory reserve	Retained earnings	Total	Non-controlling interests	Total
	Balance at 1 January 2012	24,000	123,898	3,781	47,952	199,631	613	200,244
	Profit for the year				25,439	25,439	55	25,494
	Transfer to statutory reserve			1,272	(1,272)	0		0
	Decrease in non-controlling interest due to acquisition of subsidiary						(573)	(573)
24	**Balance at 31 December 2012**	**24,000**	**123,898**	**5,053**	**72,120**	**225,071**	**95**	**225,166**
	Change in equity for the year 2011							
	Balance at 1 January 2011	24,000	123,898	2,932	31,828	182,658	2,208	184,866
	Profit for the year				16,973	16,973	(16)	16,957
	Transfer to statutory reserve			849	(849)	0		0
	Increase in non-controlling interest due to acquisition of subsidiary						130	130
	Decrease in non-controlling interests due to sale of subsidiaries						(1,709)	(1,709)
24	**Balance at 31 December 2011**	**24,000**	**123,898**	**3,781**	**47,952**	**199,631**	**613**	**200,244**

The accompanying notes are an integral part of these consolidated financial statements.

All amounts are in ISK million

Consolidated Statement of Cash Flows for the Year ended 31 December 2012

Notes		2012	2011
	Operating activities		
	Profit for the year	25,494	16,957
	Adjustments for non-cash items included in profit for the year	(43,778)	(32,349)
	Changes in operating assets and liabilities	77,065	(50,887)
	Interest received	48,726	58,630
	Interest paid	(25,386)	(24,650)
30	Dividends received	551	598
	Income tax paid	(895)	(1,254)
	Net cash from (used in) operating activities	**81,777**	**(32,955)**
	Investing activities		
	Cash and cash equivalents included in net assets acquired	(3)	1,969
	Acquisition of additional shares in equity-accounted associates	(1,334)	(6,773)
	Sale of shares in associates	2,598	-
14	Purchase of property and equipment	(849)	(377)
14	Proceeds from sale of property and equipment	71	12
15	Purchase of intangible assets	(126)	(76)
	Sale of financial investments	9,458	-
	Net cash from (used in) investing activities	**9,815**	**(5,245)**
	Financing activities		
	Repayment of secured bonds	(72,115)	-
	Aquisition of non-controlling interest	(472)	-
	Net cash used in financing activities	**(72,587)**	**0**
	Net change in cash and cash equivalents	19,005	(38,200)
	Cash and cash equivalents at the beginning of the year	13,625	52,654
	Effect of exchange rate changes on cash and cash equivalents held	(144)	(829)
	Cash and cash equivalents at the end of the year	**32,486**	**13,625**

Notes		2012	2011
	Investing and financing activities not affecting cash flows		
	Assets acquired and liabilities assumed from SpKef Savings Bank	-	(30,480)
	Non-controlling interests	-	(116)
5	Provisional amount of the bond to be issued by the Icelandic State Treasury	(19,198)	30,596
5	Bonds and debt instruments	19,198	-
	Assets acquired and liabilities assumed from Avant hf.	-	9,722
	Fair value of the Bank's outstanding claim on Avant hf.	-	(9,722)

The accompanying notes are an integral part of these consolidated financial statements.

Landsbankinn hf. Consolidated Financial Statements 2012 8 All amounts are in ISK million

Consolidated Statement of Cash Flows for the Year ended 31 December 2012

Notes		2012	2011
	Adjustments for non-cash items included in profit for the year		
25	Net interest income	(35,584)	(32,649)
26	Net adjustments to loans and advances acquired at deep discount	(37,320)	(58,489)
4, 26	Loss from foreign currency linkage of loans and advances to customers	2,120	40,726
26, 65	Net impairment loss	12,260	7,034
7,21	Fair value change of contingent bond	27,331	34,316
28	Net (gain) on financial assets designated as at fair value through profit or loss	(5,703)	(17,459)
29	Net (gain) on financial assets and liabilities held for trading	(2,169)	(1,009)
	Net gain on assets classified as held for sale	(2,134)	(6,255)
31	Net foreign exchange (gain) loss	(4,422)	1,588
32	(Gain) loss on sale of property and equipment	(14)	61
32	(Gain) loss on repossessed collateral	(537)	1,030
14	Depreciation and amortisation	719	771
13	Share of profit of equity-accounted associates, net of income tax	(2,449)	(1,417)
36	Income tax	2,925	(1,411)
36	Tax on liabilities of financial institutions	1,200	814
		(43,778)	**(32,349)**
	Changes in operating assets and liabilities		
	Change in reserve requirement with Central Bank	448	(452)
	Change in bonds and equities	35,545	(44,088)
	Change in loans and advances to financial institutions	39,838	(12,633)
	Change in loans and advances to customers	44,598	18,812
	Change in investments in associates	(349)	21,839
	Change in other assets	5,069	2,739
	Change in assets classified as held for sale	(5,937)	(16,831)
	Change in due to financial institutions and Central Bank	(15,530)	(55,082)
	Change in deposits from customers	(26,401)	18,095
	Change in repossessed collateral	(1,400)	1,144
	Change in other liabilities	(2,027)	2,362
	Change in liabilities associated with assets classified as held for sale	3,212	13,208
		77,065	**(50,887)**
	Cash and cash equivalents is specified as follows:		
8	Cash and unrestricted balances with Central Bank	23,927	6,404
11	Bank accounts with financial institutions	8,559	7,221
	Cash and cash equivalents at the end of the year	**32,486**	**13,625**

The accompanying notes are an integral part of these consolidated financial statements.

Landsbankinn hf. Consolidated Financial Statements 2012 9 All amounts are in ISK million

Notes to the Consolidated Financial Statements

Notes to the Consolidated Financial Statements

1. Reporting entity

Landsbankinn hf. (hereinafter referred to as the "Bank") was founded on 7 October 2008 by the Ministry of Finance on behalf of the Icelandic State Treasury, thereby taking over part of the domestic operations of LBI hf. (formerly Landsbanki Íslands hf.).

The Bank is a limited liability company incorporated and domiciled in Iceland. The Bank operates in accordance with Act No. 161/2002 on Financial Undertakings and is licensed by the Financial Supervisory Authority in Iceland (FME) as a commercial bank. The Bank is subject to supervision of the FME in accordance with Act No. 87/1998 on Official Supervision of Financial Activities. The registered address of the Bank's office is Austurstræti 11, 155 Reykjavík.

The consolidated financial statements of the Bank for the year ended 31 December 2012 include the Bank and its subsidiaries (collectively referred to as the "Group" and individually as "Group entities"). The Group's primary lines of business are corporate and retail banking, investment banking, asset management and other related services. The Group operates solely in Iceland.

The issue of these consolidated financial statements was authorised by the Board of Directors and the CEO of the Bank on 7 March 2013.

2. Basis of preparation

Statement of compliance

The Consolidated Financial Statements for the year ended 31 December 2012 have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union.

Going concern

The Bank's management has assessed the Group's ability to continue as a going concern and it has a reasonable expectation that the Group has adequate resources to continue its operations. Accordingly, these consolidated financial statements have been prepared on a going concern basis.

Basis of measurement

The consolidated financial statements have been prepared on a historical cost basis except for the following:
• Financial assets and liabilities classified as held for trading are measured at fair value;
• Financial assets and liabilities designated as at fair value through profit or loss are measured at fair value;
• Non-current assets and disposal groups classified as held for sale are measured at the lower of cost or fair value less costs to sell.

Functional and presentation currency

Items included in the financial statements of each individual Group entity are measured using the currency of the economic environment in which the respective entity operates (its functional currency). All amounts are presented in Icelandic krona (ISK), which is also the Bank's functional currency, rounded to the nearest million unless otherwise stated.

Use of estimates and judgements

The preparation of financial statements requires the management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Note 4 discusses estimates and assumptions which involve a substantial risk which could result in material adjustments to the carrying amounts of assets and liabilities during the next year.

3. Significant accounting policies

The consolidated financial statements have been prepared using uniform accounting policies for like transactions and other events in similar circumstances. The accounting policies applied by the Group in the consolidated financial statements are the same as those applied by the Group in its consolidated financial statements as at and for the year ended 31 December 2011.

The principal accounting polices used in preparing these consolidated financial statement are set out below.

3.1 Consolidation

(a) Subsidiaries

Subsidiaries are entities over which the Group has the power to govern financial and operating policies so as to obtain benefits from their activities, generally accompanied by a shareholding of over half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls an entity. Subsidiaries are fully consolidated from the date on which control is obtained, and are de-consolidated from the date on which control ceases.

The acquisition method is used to account for business combinations by the Group. The consideration transferred for the acquisition of a subsidiary is the fair value of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition-related costs are expensed as incurred, except for costs related to the issue of debt and equity instruments. Identifiable assets acquired and liabilities assumed in a business combination are initially measured at their fair value on the acquisition date. A contingent liability of an acquiree is only recognised in a business combination if such a liability represents a present obligation and arises from a past event, and its fair value can be measured reliably. More information about how the Group accounts for goodwill acquired in a business combination is disclosed further in this note.

Intercompany transactions, balances, and unrealised gains on transactions between Group entities are eliminated in the consolidated financial statements. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. The accounting policies of subsidiaries have been changed where this was necessary to ensure consistency with the accounting policies adopted by the Group.

(b) Non-controlling interests

Non-controlling interests represent the portion of profit or loss and equity not owned, directly or indirectly, by the Bank. Such interests are presented separately in the consolidated income statement and are included in equity in the consolidated statement of financial position, separately from equity attributable to owners of the Bank. The Group chooses on an acquisition-by-acquisition basis whether to measure non-controlling interests in an acquiree at fair value or according to the proportion of non-controlling interests in the acquiree's net assets. Changes in the Bank's ownership interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions. In such circumstances the carrying amounts of the controlling and non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiary. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to the owners of the Bank.

3.2 Associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds, directly or indirectly, between 20 and 50 percent of the voting power of another entity. The Group accounts for investments in associates either using the equity method or as financial assets designated as at fair value through profit or loss, as described further in this note. Investments in associates which are accounted for by the Group using the equity method are presented in the consolidated statement of financial position in the line “Investments in equity-accounted associates”. Investments in associates which are accounted for by the Group as financial assets designated as at fair value through profit or loss are presented in the consolidated statement of financial position in the line “Equities and equity instruments”.

Equity-accounted associates

Investments in equity-accounted associates are accounted for using the equity method from the date on which significant influence is obtained and are initially recognised at cost. Goodwill relating to an investment in an associate is included in the carrying amount of the investment. Amortisation of goodwill is not permitted. Any excess of the Group's share of net fair value of the associate's identifiable assets and liabilities over the cost of the investment is included as income in the determination of the Group's share of the associate's profit or loss in the period which the investment is acquired.

Because goodwill included in the carrying amount of an investment in an associate is not recognised separately, it is not separately tested for impairment according to the requirements for goodwill impairment testing in IAS 36 Impairment of Assets. Instead, the entire carrying amount of the investment is tested for impairment under IAS 36 by comparing its recoverable amount with its carrying amount, whenever application of the requirements in IAS 39 Financial Instruments: Recognition and Measurement indicates the investment may be impaired.

The Group's share of its equity-accounted associates' post-acquisition profits or losses is recognised in the income statement, and its share of movements in their reserves is recognised in the Group's equity reserves. Cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group’s share of losses in an associate equals or exceeds its interest in the associate, including any other unsecured receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the associate.

3. Significant accounting policies (continued)

3.2 Associates (continued)

Unrealised gains on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. The accounting policies of associates have been changed where this was necessary to ensure consistency with the accounting policies adopted by the Group.

Associates designated as at fair value through profit or loss

The Group designates certain investments in associates upon initial recognition as at fair value through profit or loss and are accounted for in accordance with IAS 39 Financial Instruments: Recognition and Measurement. The Group measures such investments at fair value, with changes in fair value recognised in the consolidated income statement in the line "Net gain on financial assets designated as at fair value through profit or loss" in the period of the change.

3.3 Foreign currency translation

Transactions in foreign currencies are translated into the functional currency of the respective Group entity at the spot exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are measured at amortised cost or fair value, as applicable, in their respective foreign currencies and are retranslated into the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are first measured at fair value in their respective foreign currencies and then retranslated into the functional currency at the spot exchange rate at the date that the fair value was determined. All foreign currency differences arising on retranslation are recognised in the income statement.

3.4 Financial assets and liabilities

(a) Recognition

The Group initially recognises loans and advances, deposits and debt securities issued on the date at which they are originated. All other financial assets and liabilities are initially recognised on the date at which the Group becomes a party to contractual provisions of the instrument. Regular way purchases and sales of financial assets are recognised on the date at which the Group committed itself to purchasing or selling the asset.

A financial asset or financial liability is initially measured at fair value plus, for an item not subsequently measured at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

(b) Classification

The Group classifies all financial assets either as loans and receivables or as at fair value through profit or loss. The Group classifies all financial liabilities either as at fair value through profit or loss or at amortised cost.

A financial asset or liability is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking. Financial assets held for trading consist of debt, equity and derivative instruments. Financial liabilities held for trading consist of derivative liabilities and short positions, i.e. obligations to deliver financial assets borrowed by the Group and sold to third parties.

The Group designates certain financial assets, including certain investments in associates, upon initial recognition as at fair value through profit or loss when the financial assets are part of portfolios of financial instruments which are managed and reported to senior management on a fair value basis in accordance with the Group's documented risk management or investment strategy.

Loans and advances are financial assets with fixed or determinable payments that are not quoted in an active market which the Group originates or acquires with no intention of trading them.

(c) Derecognition

The Group derecognises a financial asset when the contractual rights to cash flows from the asset expire, or when the Group transfers the rights to receive contractual cash flows relating to the financial asset in a transaction which substantially transfers all the risks and rewards of owning that asset. Any interest in transferred financial assets created or retained by the Group is recognised as a separate asset or liability.

The Group enters into transactions whereby it transfers assets recognised in its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets, or a portion of them. In cases where all or substantially all of the risks and rewards are retained, then transferred assets are not derecognised. Asset transfers whereby all or substantially all risks and rewards are retained include, for example, securities lending and repurchase transactions.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or when they expire.

3. Significant accounting policies (continued)

Financial assets and liabilities (continued)

(d) Offsetting

Financial assets and liabilities are set off and the net amount presented in the statement of financial position when, and only when, the Group has a legal right to set off these amounts and intends either to settle on a net basis or to realise the asset and simultaneously settle the liability.

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity.

(e) Amortised cost measurement

The amortised cost of a financial asset or liability is the amount of the financial asset or liability, as measured at initial recognition, minus principal repayments, plus or minus cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

(f) Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction at the measurement date.

The Group measures the fair value of an instrument using quoted prices in an active market for that instrument, if available. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis. Where available, the relevant market's closing price determines the fair value of financial assets held for trading and of assets designated at fair value through profit or loss; this will generally be the last trading price.

If a market for a financial instrument is not active, the Group establishes fair value using a valuation technique. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties, if available, reference to the current fair value of other instruments that are substantially the same, discounted cash flow analyses and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Group, incorporates every factor that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Bank has a valuation committee which estimates fair value by applying models and incorporating observable market information and professional judgement. The Group calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available, observable market data.

Should the transaction price differ from the fair value of other observable, current market transactions in the same instrument or be based on a valuation technique whose variables include only data from observable markets, the Group immediately recognises the difference between the transaction price and fair value (a Day 1 profit or loss). In cases where fair value is determined using data which is not observable, the difference between the transaction price and the model value is recognised in the income statement depending on the individual circumstances of the transaction but not later than when the inputs become observable, or when the instrument is derecognised.

3.4 (g) Impairment of financial assets

Impairment of loans and advances

At each reporting date, the Group assesses whether there is any objective evidence that a loan or loan portfolio is impaired. A loan or loan portfolio is considered impaired and impairment losses are incurred only when there is objective evidence of impairment as a result of one or more events occurring after initial recognition of the asset ("loss events") and these loss events impact future cash flows that can be estimated reliably for the loan or group of loans. Objective evidence of impairment includes observable data on the following loss events:

- significant financial difficulties of the borrower;
- a breach of contract, such as defaulting on instalments or on interest or principal payments;
- the Group granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a refinancing concession that the lender would not otherwise consider;
- it becomes probable that the borrower will enter into bankruptcy or undergo other financial reorganisation; or
- observable data indicate a measurable decrease in estimated future cash flows from a group of loans since the initial recognition of those assets, even if the decrease cannot yet be identified with individual financial assets within the group, including adverse changes in the payment status of borrowers in the group or a general deterioration of economic conditions connected to that group of loans.

The Group defines loans that are individually significant and assesses first whether objective evidence of their impairment exists, and then makes individual or collective assessments for loans and advances that have not been defined as individually significant. If the Group determines that no objective evidence of impairment exists for a significant loan, it includes this loan in a group of loans with similar credit risk characteristics and collectively assesses them for impairment. Individual significant assets for which an impairment loss is recognised are not included in collective impairment assessments.

3. Significant accounting policies (continued)

Financial assets and liabilities (continued)

3.4 (g) Impairment of financial assets (continued)

If there is objective evidence that an impairment loss has been incurred on loans or advances, the amount of the loss is measured as the difference between the asset's carrying amount and its recoverable value. The recoverable value is the present value of estimated future cash flows, excluding future credit losses that have not been incurred, discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced by the amount of impairment, using an allowance account, and the amount of the loss is recognised in the line item "Net impairment loss on loans and advances" in the income statement. In the case of loans with variable interest rates, the discount rate for measuring impairment losses is the current effective interest rate.

The present value calculated for estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure, less the costs involved in obtaining and selling the collateral, whether or not foreclosure is probable.

In order to conduct a collective evaluation of impairment, loans are grouped on the basis of similar credit risk characteristics on the basis of the Group's grading process, which considers asset type, collateral type, industry, past-due status and other relevant factors. These characteristics are appropriate for estimating future cash flows in groups of such loans by indicating the debtors' ability to pay every amount due according to contractual terms.

Groups of loans are collectively evaluated for impairment on the basis of expected cash flows and of peer review regarding assets with similar credit risk characteristics. Such peer review is also adjusted on the basis of current observable data, in order to reflect the effects of current conditions that did not affect the period on which peer review was originally based and to remove the effects of previous loss factors which no longer exist.

Estimates of changes in future cash flows in groups of assets are consistent with changes in observable data from period to period, for example changes in property prices, payment status, or other factors indicative of trends in the probability and magnitude of Group losses. The Group regularly reviews its methodology and assumptions for estimating future cash flows in order to minimise discrepancies between estimated losses and actual loss experience.

When a loan is uncollectible, it is written off against the provision for loan impairment in the statement of financial position. Loans are written off after all the necessary procedures have been completed, as set out in Group lending policies, and the amount of loss has been determined. Any subsequent recovery of an amount previously written off is recognised in the income statement in the line item "Net impairment loss on loans and advances".

If the amount of the impairment loss decreases in the subsequent period and the decrease can be related objectively to an event occurring after the original impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of reversal is recognised in the income statement in the line item "Net impairment loss on loans and advances".

Renegotiated loans

Where possible, the Group seeks to restructure loans rather than to take possession of collaterals. This may involve extending the payment arrangements and an agreement of new loan terms. Loans which are impaired and whose terms are renegotiated are not considered to be new loans. Once the terms have been renegotiated these loans are no longer considered past due and any subsequent impairment is measured using the original effective interest rate as calculated before the modification of terms. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. These loans continue to be subject to individual or collective impairment assessment. Loans which are not individually impaired and whose terms are renegotiated are accounted for as new loans. Accordingly, the original loans are derecognised and the renegotiated loans are recognised as new loans.

3.5 Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents are defined as cash, unrestricted balances with the Central Bank and unrestricted balances with financial institutions.

3.6 Bonds and equities

Bonds and equities which are classified as at fair value through profit or loss are recognised at fair value in the statement of financial position both initially and subsequently to initial recognition. Transaction costs are recognised directly in the income statement. Gains and losses arising from changes in fair value are recognised directly in the consolidated income statement in the line items "Net gain on financial assets and liabilities held for trading" and "Net gain on financial assets designated as at fair value through profit or loss", respectively. The gains and losses include interest income on bonds but exclude foreign exchange gains and losses, which are included in the line item "Net foreign exchange (loss) gain".

Bonds which are classified as loans and receivables are initially measured at fair value plus directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest method. Accrued interest is included in the carrying amount of the bonds and it is recognised in the line item "Interest income" in the income statement.

3. Significant accounting policies (continued)

3.7 Derivative instruments

Derivatives are initially recognised in the statement of financial position at fair value, with transaction costs being recognised in the income statement. Subsequently, derivatives are carried at fair value, with all fair value changes recognised in the line item "Net gain on financial assets and liabilities held for trading" in the income statement, except for fair value changes of derivative currency forwards and net foreign exchange differences arising from OTC currency options, which are included in the line item "Net foreign exchange (loss) gain" in the income statement. In the statement of financial position, derivatives with positive fair values are recognised as assets and derivatives with negative fair values are recognised as liabilities. The Group does not apply hedge accounting.

3.8 Loans and advances

Loans and advances are initially measured at fair value plus directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest method. Accrued interest is included in the carrying amount of loans and advances. Interest income on loans and advances is recognised in the line item "Interest income" in the income statement and foreign exchange differences in the line item "Net foreign exchange (loss) gain".

Loans and advances acquired at deep discount

The Bank acquired loans and advances from LBI hf. at deep discount that reflected credit losses which were already incurred at acquisition date. The deep discount was included in the fair value of these loans and advances estimated at initial recognition. The deep discount is also included in the estimated future cash flows used by the Group to calculate the amortised cost and effective interest rate of these loans and advances.

At each reporting date, the Group assesses the current status of these loans and advances and whether there is any objective evidence of changes in expected cash flows, for example due to differences in estimated and actual payments, changes in the value of collaterals and improvement in the financial situation of debtors. If there is any change in expected cash flows, the Group recalculates the carrying amount of these loans and advances as the present value of the revised estimated future cash flows, using their effective interest rate. The difference between the revised carrying amount of the loans and their current carrying amount, which includes accrued interest, indexation, foreign exchange differences and actual payments received by the Group, is recognised on a portfolio basis in the income statement in the line “Net adjustments to loans and advances acquired at deep discount”.

The Group recognises interest and indexation on these loans and advances based on their carrying amount and only to the extent that the interest and indexation are deemed to be collectible. The interest and indexation are recognised in the income statement in the line ”Interest income”.

3.9 Property and equipment

All property and equipment is recognised at cost, less accumulated depreciation and accumulated impairment losses. The cost includes expenditures directly attributable to acquiring these assets

Subsequent costs are included in an asset’s carrying amount only if it is probable that future economic benefits associated with the item will flow to the Group and if these costs can be reliably measured. All other repairs and maintenance are charged to the income statement of the financial period in which their costs are incurred.

Depreciation of any property and equipment is calculated using the straight-line method. This method is applied to the depreciable amount of the assets, which is their cost less their residual value over their estimated useful lives, as follows:

Buildings	25-50 years
Computer hardware	3 years
Other equipment and motor vehicles	3-10 years

The assets' residual values and useful lives are reviewed annually and adjusted where appropriate.

Gains and losses on disposals are determined by comparing the sale price of an asset with its carrying amount on the date of sale. Gains and losses are included in the item "Other income and expenses" in the income statement.

3.10 Intangible assets

(a) Computer software licenses

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring them into service. Computer software licenses recognised as intangible assets are amortised over their useful life, which is estimated to be 3 - 5 years.

The costs associated with maintaining computer software are recorded as expenses at the time they are incurred.

3. Significant accounting policies (continued)

Intangible assets (continued)

(b) Goodwill

Goodwill is recognised as an asset only if acquired in a business combination. It is recognised as of the acquisition date and measured as the aggregate of (a) the fair value of the consideration transferred, (b) the recognised amount of any non-controlling interest in the acquiree, and (c) the fair value of any previously held equity interest in the acquiree, less the net recognised amount (generally fair value) of the identifiable assets acquired and liabilities assumed, all measured as at the acquisition date. The consideration transferred includes the fair value of assets transferred, liabilities incurred and equity interests issued by the Group. In addition, consideration transferred includes the fair value of any contingent consideration.

Following initial recognition, goodwill is measured at cost, less any accumulated impairment losses. Goodwill is generally reviewed for impairment annually, but more frequently if events or changes in circumstances indicate a potential impairment of the carrying amount. For the purpose of impairment testing, goodwill is allocated as of the acquisition date to each of the Group's cash-generating units (CGUs) or group of CGUs which are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units. Each unit to which this goodwill is allocated represents the lowest level within the Group at which the goodwill is monitored for internal management purposes. Where goodwill is attached to a particular unit of a CGU (or of a group of CGUs) and part of the operations within that unit is disposed of, the goodwill that is associated with the operations disposed of is included in the carrying amount of these operations when determining the gain or loss incurred upon disposing of the operations.

3.11 Impairment of non-financial assets

Assets with an indefinite useful life are not subject to amortisation but are tested annually for impairment. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is either an asset's fair value less selling costs or its value in use, whichever is higher. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). With the exception of goodwill, non-financial assets are reviewed at each reporting date for any possible reversal of impairment.

3.12 Deferred income tax

Deferred tax assets are recognised when it is probable that future taxable profit will be available against which deductible temporary differences can be utilised.

Deferred income tax is recognised in full as a liability, based on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, deferred income tax is not recognised if it arises from the initial recognition of an asset or liability in a transaction other than a business combination, which at the time of the transaction affects neither the Group's accounting nor its taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

The principal temporary differences arise from fair value changes in various financial assets and liabilities and the difference between the fair values of acquired assets and their tax base.

3.13 Assets and liabilities classified as held for sale

The Group classifies non-current assets (or groups of assets together with related liabilities) as held for sale when their carrying amount will be recovered principally through a sale transaction. This is usually the case with collateral foreclosed by the Group which it holds as security for loans and advances, including assets and liabilities of subsidiaries over which the Group obtains control through foreclosure of collateral and/or financial restructuring.

A non-current asset (or group of assets together with related liabilities) is considered to be recovered principally through a sale transaction when the asset's sale is highly probable and it is available for immediate sale in its present condition, subject to ordinary and customary terms on the sale of such assets. Management must be committed to the sale and must actively market the asset for sale at a price that is reasonable in relation to its current fair value. A further condition is that the sale is expected to qualify for recognition as completed within one year from the date of classification.

Assets and disposal groups classified as held for sale are measured at the lower of their carrying amount and their fair value less costs to sell. Additional net assets that become part of a disposal group, for example due to profits generated by the disposal group, increase the carrying amount of the disposal group but not in excess of the fair value less costs to sell of the disposal group as determined at each reporting date.

In the case of single assets classified by the Group as held for sale the Group determines their fair value less costs to sell by reference to the current market price at each reporting date. In the case of subsidiaries classified as held for sale, the Group determines the fair value of disposal groups based on discounted cash flows methodologies. Costs to sell are deemed to be only the costs which are incremental and directly attributable to the disposal of the disposal groups, excluding finance costs and income tax expense.

3. Significant accounting policies (continued)

3.14 Deposits and secured bonds

The Group's sources of debt funding consist of deposits, loans from financial institutions and debt securities.

When the Group sells a financial asset and simultaneously enters into an agreement to repurchase the asset or a similar asset at a fixed price on a future date ("repo"), this arrangement is accounted for as an amount due to financial institutions or the Central Bank, and the underlying asset continues to be recognised in the Group's financial statements.

The Group classifies financial instruments as financial liabilities or equity instruments in accordance with the substance of the contractual arrangement and the definitions of a financial liability, a financial asset or an equity instrument.

Deposits and borrowings are initially measured at fair value plus any directly attributable transaction costs. Subsequently, they are measured at their amortised cost using the effective interest method. The fair value of a financial liability with a demand feature such as a demand deposit, is not less than the amount payable on demand, discounted from the first date that the amount could be required to be paid.

3.15 Contingent bond

The contingent bond is a contingent obligation of the Bank to issue a bond to LBI hf. no later than 31 March 2013 as an additional consideration for the assets and liabilities transferred from LBI hf. on 9 October 2008. The issue of the bond and its nominal amount are contingent on the excess of the value of certain pools of assets, to be determined as at 31 December 2012, over the future value of the acquisition price of those assets as at 9 October 2008, subject to specified adjustments.

The contingent obligation of the Bank is classified as a financial liability and measured initially at fair value. Subsequently, it is measured at fair value, with any resulting gain or loss recognised in the line item "Fair value change of contingent bond" in the income statement.

3.16 Short positions

Short positions are obligations of the Group to deliver financial assets borrowed by the Group and sold to third parties. These obligations are initially recognised in the statement of financial position at fair value, with transaction costs being recognised in the income statement. Subsequently, they are carried at fair value, with all fair value changes recognised in the income statement in the line item "Net gain on financial assets and liabilities held for trading".

3.17 Financial guarantee contracts

Financial guarantee contracts are contracts requiring the issuer to make specified payments to reimburse the holder for a loss it will incur if a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are issued by the Group to banks, financial institutions or other parties on behalf of Group customers so that they can secure loans, overdrafts and other banking facilities.

Financial guarantees issued by the Group are primarily bank guarantees and documentary letters of credit. Fees of long term guarantees are claimed up-front periodically over the life of each guarantee, initially at the inception of a guarantee. Fees of short term guarantees are in essence claimed up-front at inception. Fee income arising from the guarantees is recognised over time as the fees become payable. Provisions for losses on guarantees are subject to the uncertainty of assessing the extent to which guarantees may be called upon. For this purpose outstanding bank guarantees and documentary letters of credit are assessed quarterly in respect of credit losses and recognition of provisions. The provision assessment is based on experience with similar transactions and the history of past losses, supplemented by management judgement.

3. Significant accounting policies (continued)

3.18 Contingent liabilities and provisions

The Group does not recognise contingent liabilities as liabilities in the statement of financial position, other than contingent liabilities which are assumed in a business combination and which have a fair value that can be measured reliably. A contingent consideration transferred by the Group in a business combination is recognised at its acquisition-date fair value. The Group classifies the obligation to pay contingent consideration as liability or equity and accounts for changes in fair value in accordance with applicable IFRS's.

Provisions for expenditures such as those related to legal claims or restructuring are recognised as incurred when (i) the Group has as a result of past events a present legal or constructive obligation to pay, (ii) it is more likely than not that an outflow of resources will be required to settle the obligation, and (iii) the amount has been reliably estimated.

Provisions are measured at the present value of the expenditures expected for settling the obligation. A pre-tax rate is used which reflects current market assessments of the time value of money and the risks specific to the obligation. Any increase in the provision due to the passage of time is recognised as interest expense.

3.19 Employee benefits

All Group entities have defined contribution plans, with the entities paying a fixed contribution to publicly or privately administered pension plans on a mandatory and contractual basis. The Group has no further payment obligations once these contributions have been paid. The contributions are recognised as an expense when they become due. The Group has no defined benefit pension plan.

3.20 Share capital

(a) Share issue costs

Costs directly attributable to the issue of new shares are presented separately in equity as a deduction from share premium, net of any related income tax benefits.

(b) Dividends on ordinary shares

Dividends on ordinary shares are recognised in equity during the period in which they are approved by the Bank's shareholders' meeting.

3.21 Fiduciary activities

The Group acts as a custodian, holding or placing assets on behalf of individuals, institutions and pension funds, including various mutual funds managed by the Group. These assets, together with the income arising from them, are excluded from these financial statements, since they are not assets of the Group.

3.22 Interest income and expense

The interest income and expense presented in the consolidated income statement consist of interest income and expense from financial assets and liabilities measured at amortised cost.

The interest income and expense is recognised in the consolidated income statement using the effective interest method. The effective interest rate is the rate that discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Group estimates future cash flows considering all contractual terms of the financial instrument but it does not consider any future credit losses. The calculation of the effective interest rate includes all fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

3.23 Net impairment loss on loans and advances

Impairment charges relating to loans and advances to financial institutions and customers are presented in the consolidated income statement under the item "Net impairment loss on loans and advances". Once impairment has been recognised, subsequent interest income is recognised at the rate of interest used for discounting future cash flows when measuring impairment losses.

3.24 Fee and commission income and expense

Fees and commissions are generally recognised on an accrual basis as the related services are performed. Arrangement fees are generally deferred together with related direct costs and recognised as an adjustment to the effective interest rate of a loan. Commissions and fees for participation in negotiating a transaction for a third party, such as arrangement of transactions with equities or other securities or the purchase or sale of businesses, are recognised upon completion of the underlying transaction. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportioned basis. Asset management fees related to investment funds are recognised rateably over the period when the service is provided. The same principle for reporting income is applied to other custody services that are continuously provided over an extended period of time.

3. Significant accounting policies (continued)

3.25 Net gain on financial assets designated as at fair value through profit or loss

The net gain on financial assets designated as at fair value through profit or loss relates to financial assets designated by the Group as at fair value through profit or loss and includes:
• All realised and unrealised changes in fair value;
• Interest income on an accrual basis; and
• Dividend income, which is recognised when the Group's right to receive payment is established.

3.26 Net gain on financial assets and liabilities held for trading

The net gain on financial assets and liabilities held for trading relates to financial assets and liabilities classified by the Group as held for trading and includes:
• All realised and unrealised changes in fair value;
• Interest income on an accrual basis;
• Dividend income, which is recognised when the Group's right to receive payment is established; and
• Foreign exchange gains and losses arising from derivative financial assets and liabilities, except for changes in fair value of derivative currency forwards and net foreign exchange differences arising from OTC currency options, which are included in the line item "Net foreign exchange (loss) gain" in the income statement.

3.27 Net foreign exchange gain (loss)

Net foreign exchange gain (loss) includes all gains and losses arising from settlement of transactions in foreign currencies and translation at year end exchange rates of monetary assets and liabilities denominated in foreign currencies, including non-derivative financial assets and liabilities classified as held for trading and financial assets designated as at fair value through profit or loss. Foreign exchange gains and losses arising from derivative financial assets and liabilities are included in the line item "Net gain on financial assets and liabilities held for trading", except for fair value changes of derivative currency forwards and net foreign exchange differences arising from OTC currency options, which are included in the line item "Net foreign exchange (loss) gain" in the income statement.

3.28 Other income and expenses

Other income and expenses include revenue arising from recharging agreements and gains and losses on repossessed collateral and property and equipment.

3.29 Leases

(a) When a Group entity is the lessee

The leases into which the Group enters as a lessee are primarily operating leases. Over the period of the lease, payments for operating leases are charged to the income statement on a straight-line basis, in the line item "Other operating expenses".

If an operating lease is terminated before the lease period has expired, any payment to the lessor required by way of penalty is recognised as an expense in the period in which termination occurs.

(b) When a Group entity is the lessor

When assets are held subject to a finance lease, the present value of lease payments is recognised as a receivable, under loans and advances to customers. Finance income from such a lease is recognised over the term of the lease, using a method that reflects a constant periodic rate of return on the Group's net investment in the lease.

3.30 Discontinued operations

The Group presents discontinued operations in a separate line of the consolidated income statement if an entity or a component of an entity has been disposed of or is classified as held for sale and:
• Represents a major separate line of business;
• Is a part of a single co-ordinated plan to dispose of a major separate line of business; or
• Is a subsidiary acquired exclusively with a view to resale.

The profit from discontinued operations disclosed in the consolidated income statement consists of (a) post-tax profit or loss from discontinued operations and (b) post-tax gain or loss recognised on the measurement to fair value less costs to sell or on the disposal of the assets or the disposal groups constituting the discontinued operation. A component of an entity comprises operations and cash flows that can be clearly distinguished, operationally and for financial reporting, from the rest of the Group's operations and cash flows.

3.31 Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components, whose operating results are reviewed regularly by the Group Management Committee (being the chief operating decision maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

3. Significant accounting policies (continued)

3.32 New standards, amendments to standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are not yet effective for the year ended 31 December 2012, and have not been applied in preparing these consolidated financial statements. The new standards and amendments to standards which might have a material effect on the consolidated financial statements of the Group are the following:

The amendments to IAS 32 and IFRS 7 *Offsetting Financial Assets and Financial Liabilities* , which clarify when an entity currently has a legally enforceable right to set-off financial assets and financial liabilities and require an entity to disclose certain information about the effect or potential effect on an entity's financial position resulting from netting arrangements. The amendments to IAS 32 will become mandatory for the Group starting with its consolidated financial statements for the year 2014. The amendments to IFRS 7 will become mandatory for the Group starting with its consolidated financial statements for the year 2013. Restrospective application is required for both amendments to IAS 32 and IFRS 7. The Group does not plan to early adopt IAS 32 and it is currently in the process of evaluating their impact on its consolidated financial statements. However, the Group already expects that it will be required to provide more extensive disclosures about the effect or potential effect of netting arrangements on the Group's financial position.

IFRS 10 *Consolidated Financial Statements* , which establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. IFRS 10 establishes control as the basis for determining which entities are consolidated. The principle of control sets out three elements of control: (a) power over an investee, (b) exposure, or rights, to variable returns from involvement with the investee, and (c) the ability to use power over the investee to affect the amount of the investor's returns. IFRS 10 contains guidance on how to apply the control principle in various circumstances, including situations where the investor holds less than a majority of voting rights. IFRS 10 carries forward the consolidation procedures from IAS 27 Consolidated and Separate Financial Statements (as amended in 2008). IFRS 10 supersedes IAS 27 (2008) and SIC-12 Consolidation – Special Purpose Entities. IFRS 10 will become mandatory for the Group starting with its consolidated financial statements for the year 2014, with retrospective application but subject to specific transition rules. The Group does not plan to early adopt IFRS 10 and it is currently in the process of evaluationg the possible impact of IFRS on its consolidated financial statements.

IFRS 12 *Disclosure of Interests in Other Entities* , which includes all the disclosure requirements for interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. In general, the disclosures required by IFRS 12 are more extensive than the disclosures required by currently effective standards. IFRS 12 will become mandatory for the Group starting with its consolidated financial statements for the year 2014, with retrospective application required but subject to specific transition rules. The Group does not plan to early adopt IFRS 12 and it is currently in the process of evaluating the impact of IFRS 12 on its consolidated financial statements. However, the Group already expects that it will be required to provide more extensive disclosures about the nature of, and risks associated with, the Bank's interests in other entities and the effects of those interests on the Group's financial position, financial performance and cash flows.

IFRS 13 *Fair value measurement,* which establishes a single framework for measuring fair value of both financial and non-financial items and sets out related disclosure requirements. IFRS 13 does not give rise to any new requirements as to when fair value measurements are required. Instead, IFRS 13 provides guidance on how fair value should be measured and disclosed when required or permitted under other IFRS's. In general, the disclosures required by IFRS 13 are more extensive than the disclosures required by currently effective standards. IFRS 13 will become mandatory for the Group starting with its consolidated financial statements for the year 2013. The Group will have to apply the measurement requirements of IFRS 13 prospectively as of the beginning of the annual period in which it will apply IFRS 13 initially but it will have a choice as to whether it provides the disclosures required by IFRS 13 for comparative periods. The application of IFRS 13 will result in the Group having to provide more extensive disclosures about fair value measurements.

3.32 New standards, amendments to standards and interpretations not yet adopted (continued)

IFRS 9 *Financial instruments* , which replaces those parts of IAS 39 *Financial Instruments: Recognition and Measurement relating* to the classification and measurement of financial assets and financial liabilities. The key features of IFRS 9 are the following:

• Financial assets are required to be classified into two measurement categories: those to be measured subsequently at fair value, and those to be measured subsequently at amortised cost. The decision is to be made at initial recognition. The classification depends on the entity's business model for managing its financial instruments and the contractual cash flow characteristics of the instrument.

• An instrument is subsequently measured at amortised cost only if it is a debt instrument and both the objective of the entity's business model is to hold the asset to collect the contractual cash flows, and the asset's contractual cash flows represent only payments of principal and interest. All other debt instruments are to be measured at fair value through profit or loss.

• All equity instruments are to be measured subsequently at fair value. Equity instruments that are held for trading will be measured at fair value through profit or loss. For all other equity investments, an irrevocable election can be made at initial recognition, to recognise unrealised and realised fair value gains and losses through other comprehensive income rather than profit or loss. There will be no recycling of fair value gains and losses to profit or loss. This election may be made on an instrument-by-instrument basis. Dividends are to be presented in profit or loss, as long as they represent a return on investment.

• Derivatives embedded in contracts with a host that is a financial asset within the scope of the standard are not to be separated; instead the hybrid financial instrument is to be assessed in its entirety as to whether it should be measured at amortised cost or fair value.

• IFRS 9 (2010) generally requires that the amount of change in fair value attributable to changes in the credit risk of liabilities designated by an entity as at fair value through profit or loss be presented in other comprehensive income, with only the remaining amount of the total gain or loss included in profit or loss. The amounts presented in other comprehensive income may not be subsequently reclassified to profit or loss but may be transferred within equity. However, if the recognition of gains and losses in other comprehensive income creates or enlarges an accounting mismatch in profit or loss, then the whole fair value change must be presented in profit or loss. Additionally, all fair value gains and losses continue to be included in profit or loss for loan commitments and financial guarantee contracts designated as fair value through profit or loss.

Currently, IASB has issued two versions of IFRS 9. The first version was issued in 2009 and the second version was issued in 2010. The 2010 version includes all the requirements of the 2009 version without amendment, but in addition, it also includes the requirements with respect to the classification and measurement of financial liabilities and the derecognition of financial assets and financial liabilities. The 2010 version supersedes the 2009 version. However, for annual periods beginning before 1 January 2015, an entity may elect to apply the 2009 version rather than the 2010 version.

If endorsed by the EU, IFRS 9 will become mandatory for the Group starting with its consolidated financial statements for the year 2015. Upon initial application of IFRS 9 the Group will have a choice as to whether it will restate prior periods or not and it will need to provide certain disclosures about the transition from IAS 39 to IFRS 9. The Group does not plan to early adopt IFRS 9 and it is currently in the process of evaluating the potential effect of this standard. Given the nature of the Group's operations, the standard is expected to have a pervasive impact on the consolidated financial statements of the Group.

4. Critical accounting estimates and judgements in applying accounting policies

(a) Effective interest rate on loans and advances

The Bank acquired loans and advances from LBI hf. at a deep discount, reflecting incurred credit losses. The effective interest rate is computed for these loans by estimating their future cash flows and comparing it with their acquisition prices. Estimating the cash flows involves management judgements about the debtors' financial situation and ability to pay their debts, the net realisable value of any underlying collateral and the timing of any potential cash flows. These estimates have a significant risk of resulting in material adjustments to the carrying amounts of loans within the next financial year.

(b) Impairment losses on loans and advances

To assess impairment, the Group reviews its loan portfolios on at least a quarterly basis. To determine whether an impairment loss should be recognised, the Group judges whether there is any observable data indicating a measurable decrease in estimated future cash flows from a portfolio of loans, before any decrease in individual loans becomes identifiable within that portfolio. The evidence may include either observable data indicating that an adverse change has occurred in the payment status of the borrowers in a group, or national or local economic conditions correlating with defaults on assets in the group. In order to schedule its future cash flows, management uses estimates based on historical loss experience, together with objective evidence of impairment in homogenous portfolios. The methodology and assumptions for estimating both the amount and timing of future cash flows are reviewed regularly in order to reduce potential discrepancies between loss estimates and actual loss experience.

(c) Valuation of financial instruments

The fair value of financial instruments where no active market exists or where quoted prices are not otherwise available are determined by using valuation techniques. In these cases, the fair values are estimated from observable data in respect of similar financial instruments or using models. Where market observable inputs are not available, they are estimated based on appropriate assumptions. Where valuation techniques (for example, models) are used to determine fair value, they are validated and periodically reviewed by qualified and independent personnel. All models are certified before use, and calibrated to ensure that the outputs reflect actual data and comparative market prices. Wherever practical, models are confined to observable data; however, areas such as volatility, correlation and credit risk, whether own or counterparty, require management to make estimates. Changing assumptions on these factors could affect the reported fair value of financial instruments.

4. Critical accounting estimates and judgements in applying accounting policies (continued)

(d) Financial asset and liability classification

The Group's accounting policies provide scope for assets and liabilities to be classified at initial recognition into different categories in certain circumstances:
• Where financial assets or liabilities have been classified as "held for trading", the Group has determined that they meet the description of such assets and liabilities set out in its accounting policies.
• Where financial assets have been designated as at fair value through profit or loss, the Group has determined that they meet the criteria set out in the accounting policies.
• Where financial assets have been classified as loans and receivables, the Group has determined that they meet the criteria set out in the accounting policies.

(e) Assets classified as held for sale

The Group classifies assets and groups of assets together with related liabilities as held for sale if such assets or disposal groups are immediately available for sale in their present condition, subject to terms that are usual and customary for selling such assets or disposal groups, if management is committed to selling such assets and is actively looking for a buyer, if the assets are being actively marketed at a reasonable sales price in relation to their fair value, if completion of the sale is expected within one year and if sale is considered highly probable. However, events and circumstances may extend the period to complete the sale beyond one year. An extension of the period required to complete the sale does not preclude an asset (or disposal group) from being classified as held for sale if the delay is caused by events or circumstances beyond the Group's control and the Group remains committed to its plan to sell the asset (or disposal group).

When classifying assets as held for sale the Group has determined that the classification criteria have been met.

(f) Deferred tax assets

Deferred tax assets are recognised in the consolidated statement of financial position. In respect of tax losses carried forward, they are recognised to the extent that it is probable that taxable profits will be available against which to utilise the losses. Judgement is required to determine the amount of deferred tax assets that may be recognised, based upon the likely timing and level of future taxable profits, as well as tax-planning strategies.

(g) Liquidity

The key measure used by the Group for monitoring liquidity risk is the ratio of core liquid assets to deposits. The calculation of this ratio requires judgement as to which assets to consider liquid. Furthermore, the maturity of some assets included in the maturity analysis of the financial assets and liabilities disclosed in the notes, such as loans acquired from LBI hf., is based on expected future cash flows rather than contractual maturities. The estimation of the amount and timing of the cash flows from these financial assets involves management judgements about the debtors' financial situations and their abilities to repay their debts, the net realisable value of any underlying collateral and the timing of any possible cash flows.

(h) Denomination currencies and interest rates of loan agreements

In 2010, 2011 and 2012 the Supreme Court of Iceland delivered rulings on the illegality of provisions of currency-indexation in loan agreements denominated in Icelandic krona. Under law, such loans are to bear the lowest interest rates of un-indexed loans denominated in Icelandic krona as published by the Central Bank of Iceland.

The Group has accounted for the impact of the these rulings and recognised expenses in the amount of ISK 18,157 million in its consolidated income statement at year end 2010 and an additional ISK 2,684 million in its consolidated income statement at year end 2011. These expenses were recorded in the income statements under line item "Loss from foreign currency linkage of loans and advances to customers".

On 15 February 2012 and 18 October 2012 the Supreme Court ruled in two separate cases that a lender could not apply the Central Bank interest rates under circumstances specified in the rulings, inter alia, as the lender had issued final receipt of payment of interests. The Group has accounted for the potential impact of the these two rulings and recognised, respectively, expenses in the amount of ISK 38,042 million and ISK 2,120 million in its consolidated income statement at year end 2011 and at the end of the third quarter of 2012. These expenses are recorded in the income statements under line item "Loss from foreign currency linkage of loans and advances to customers". Further Court rulings are awaited to obtain final clarification of the precedence of these rulings. The total amount of the estimated impact may change accordingly. The Bank expects that part of these expenses will be reversed once the application of the Court's precedent has been fully clarified.

The litigation section in Note 37 includes two cases commenced against the Bank during the year 2012 where currency indexation of loans is being disputed. It is the position of the Bank that circumstances in these cases are different compared to previous litigations involving currency indexation of loans which the Supreme Court has ruled illegal and that the loans now under litigation shall be regarded as loans in foreign currencies. However, if Court rulings prove unfavourable for the Bank these cases may set precedence for identical loans and have a potential significant impact. The Bank may thus have to recognise expenses in the amount of ISK 28,146 million in the forthcoming periods.

4. Critical accounting estimates and judgements in applying accounting policies (continued)

(i) Contingent bond

As at 31 December 2012 the Bank's estimate of the nominal amount of the contingent bond was ISK 88,142 million, which is lower than the bond´s nominal ceiling amount of ISK 92,000 million. The estimate is that of the management of the Bank but the final and binding amount of the bond is still being determined by an independent third-party valuation agent, whose conclusions are expected to be presented no later than 31 March 2013. Any possible difference between the estimate of the management of the Bank and the valuation agent will be recognised in the Bank's 2013 first quarter financial statements. The difference will be recorded in the Group's income statement under line items "Fair value change of contingent bond". Given the nominal ceiling amount of ISK 92,000 million, the increase in the Group's total liabilities due to this is capped at ISK 3,858 million (using the EUR/ISK exchange rate at 31 December 2012). Whatever the final valuation difference will be, it is likely to be counter-balanced by improved recoverability of the Group's loans, such that the impact on the Group's 2013 performance will not be significant. However, any such changes in the underlying assets and the contingent bond may not necessarily be accounted for in the same quarterly financial statements.

5. Business combination

Acquisition of SpKef Savings Bank

On 7 March 2011, the Bank took over all assets, liabilities and operations of SpKef Savings Bank (SpKef) in accordance with the decision of the Financial Supervisory Authority in Iceland (FME). SpKef was owned entirely and directly by the National Treasury previous to the transfer. The National Treasury made a commitment to issue a bond payable to the Bank in order to compensate for the negative difference between the fair value of the assets taken over and liabilities assumed by the Bank. The Bank and the National Treasury did not reach an agreement on the fair value of financial assets of SpKef and as a result the disagreement was referred to an arbitration panel.

In the arbitration panel's conclusion of 7 June 2012 the fair value of the consideration transferred was determined ISK 19,198 million. This is considerably lower than the Bank's original valuation of ISK 30,596 million, which was based on the Bank's view of the fair value of financial assets of SpKef at the acquisition date. This conclusion is final and binding for both parties and resolves the disagreement on the fair value of the consideration transferred. The National Treasury expanded the Treasury bond series RIKH 18, maturing 9 October 2018, by ISK 19,198 million for the purpose of settling the claim of the Bank on the Treasury. As at 30 June 2012 accrued interest on the Treasury bonds since the acquisition date amounted to ISK 890 million. The Bank's review of the fair value of the financial assets of SpKef, following the conclusion of the arbitration panel, confirmed enhanced recovery rates and improved quality of some of the financial assets. As a result, a net loss of ISK 2,889 million (comprising of a loss of ISK 3,779 million from the financial assets less accrued interest of ISK 890 million on the bonds received) was accounted for in the financial statements in the second quarter of 2012.

6. Operating segments

The business segments are disclosed in accordance with the internal reporting to the CEO and the Board of Directors, who are responsible for allocating resources to the reportable segments and assessing their financial performance.

The Group has four main business segments at the end of the reporting period:

• **Personal Banking** provides financial services through the Bank's branch network to individuals and to small and medium-size businesses,

• **Corporate Banking** provides financial services to large and medium-size corporate clients. Provides restructuring solutions to corporate clients who have defaulted on their loans and can be returned to viability.

• **Markets** provide brokerage services in securities, foreign currencies and derivatives, sale of securities issues, money market lending and advisory services. Markets provides a range of wealth and asset management products and services for individuals, corporations and institutional investors. Horn fjárfestingarfélag and Landsbréf, a subsidiary of the Bank, are included in markets.

• **Treasury** incorporates unallocated capital, funding, liquidity and interbank functions for the Bank as well as management of the Group's market risk.

Other segments comprise of the support functions of Finance, Risk Management, Corporate Development & HR and Operations & IT.

Reconciliation consists of eliminations and transactions that cannot be allocated to any one segment.

Administrative expenses of Group support functions are allocated to appropriate business segments based on the underlying cost drivers.
Expenses are allocated to the business units at market price level. Other segments supplies services to business units, and transactions are settled at unit prices or on an arm's-length basis; if possible, on the basis of consumption and activity.

The following table summarises each segment's financial performance as disclosed in the internal management reports on segments profit before tax. In these reports all income statement items are reported on a net basis, including the total interest income and expense. Inter-segment pricing is determined on an arm’s length basis.

No revenue from transactions with a single external customer or counterparty amounted to 10% or more of the Group's total revenue during the periods from 1 January to 31 December 2012 and 2011.

On 28 September 2012 the CEO of the Bank presented a new organisational chart for the Group which became formally effective as of 1 October 2012. As a result the Group changed the composition of reportable segments accordingly. The new segment composition and comparative information are reported for the first time in the year end 2012 financial statements of the Group.

In the year 2011 the Group reported seven main business segments: Retail Banking, Vehicle and Equipment Financing, Corporate Banking, Asset Restructuring, Markets & Treasury, Asset Management and the subsidiary Horn fjárfestingarfélag hf.

6. Operating segments (continued)

1 January - 31 December 2012	Personal Banking	Corporate Banking	Markets	Treasury	All Other Segments	Total Segments	Recon-ciliation	Total
Net interest income (expense)	17,396	17,739	194	1,728	(835)	36,222	(637)	35,584
Net adjustments in valuation	(10,082)	1,743	-	269	3,679	(4,391)	-	(4,391)
Net fee and commission income	2,382	403	2,035	247	(237)	4,830	(381)	4,448
Net gain on financial assets designated as at fair value through profit or loss	-	(2)	3,450	2,255	-	5,703	-	5,703
Net gain on financial assets and liabilities held for trading	-	-	330	1,839	-	2,169	-	2,169
Net foreign exchange gain (loss)	-	-	881	3,685	-	4,566	-	4,566
Other income and (expenses)	(149)	(22)	62	472	408	771	291	1,062
Total operating income (expense)	**9,547**	**19,861**	**6,952**	**10,495**	**3,015**	**49,870**	**(727)**	**49,141**
Total operating expenses	(13,437)	(3,704)	(2,394)	(2,677)	(2,228)	(24,440)	335	(24,105)
Share of profit of equity-accounted associates, net of income tax	618	-	-	1,793	38	2,449	-	2,449
Profit (loss) before tax	**(3,272)**	**16,157**	**4,558**	**9,611**	**825**	**27,879**	**(392)**	**27,485**
Net revenue (expenses) from external customers	2,973	36,367	6,647	579	3,304	49,870		
Net revenue (expenses) from other segments	6,574	(16,506)	305	9,916	(289)	0		
Total operating income (expense)	**9,547**	**19,861**	**6,952**	**10,495**	**3,015**	**49,870**		
Total assets at 31 December 2012	**486,318**	**403,379**	**33,051**	**539,568**	**37,385**	**1,499,701**	**(414,916)**	**1,084,787**
Total liabilities at 31 December 2012	**449,839**	**330,373**	**28,833**	**428,179**	**37,313**	**1,274,537**	**(414,916)**	**859,621**
Allocated capital at 31 December 2012	**36,480**	**73,006**	**4,218**	**111,389**	**72**	**225,165**	**0**	**225,166**

1 January - 31 December 2011	Personal Banking	Corporate Banking	Markets	Treasury	All Other Segments	Total Segments	Recon-ciliation	Total
Net interest income (expense)	13,833	14,832	(47)	6,215	(634)	34,199	(1,550)	32,649
Net adjustments in valuation	(25,166)	2,024	-	(422)	(23)	(23,587)	-	(23,587)
Net fee and commission income	2,281	295	1,997	259	(219)	4,613	(190)	4,423
Net gain on financial assets designated as at fair value through profit or loss	37	5,304	10,759	1,452	(93)	17,459	-	17,459
Net gain on financial assets and liabilities held for trading	-	-	(345)	1,354	-	1,009	-	1,009
Net foreign exchange gain (loss)	(439)	-	243	(854)	-	(1,050)	291	(759)
Other income and (expenses)	(976)	(171)	29	171	500	(447)	(3)	(450)
Total operating income (expense)	**(10,430)**	**22,284**	**12,636**	**8,175**	**(469)**	**32,196**	**(1,452)**	**30,744**
Total operating expenses	(12,954)	(3,704)	(1,973)	(1,942)	(1,693)	(22,266)	210	(22,056)
Share of profit of equity-accounted associates, net of income tax	566	(159)	-	826	184	1,417	-	1,417
Profit (loss) before tax	**(22,818)**	**18,421**	**10,663**	**7,059**	**(1,978)**	**11,347**	**(1,242)**	**10,105**
Net revenue (expenses) from external customers	(15,594)	39,018	12,713	(3,829)	(113)	32,195		
Net revenue (expenses) from other segments	5,163	(16,733)	(78)	12,004	(356)	0		
Total operating income (expense)	**(10,431)**	**22,285**	**12,635**	**8,175**	**(469)**	**32,195**		
Total assets at 31 December 2011	**493,729**	**458,375**	**26,828**	**549,201**	**33,846**	**1,561,979**	**(426,497)**	**1,135,482**
Total liabilities at 31 December 2011	**458,538**	**376,625**	**19,030**	**473,696**	**33,846**	**1,361,735**	**(426,497)**	**935,238**
Allocated capital at 31 December 2011	**35,191**	**81,751**	**7,798**	**75,504**	**0**	**200,244**	**0**	**200,244**

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Notes to the Consolidated Statement of Financial Position

7. Classification and fair value of financial assets and liabilities

According to IAS 39, financial assets and liabilities must be classified into specific categories which affect how they are measured after initial recognition. Each category's basis of subsequent measurement is specified below:
- Loans and receivables, measured at amortised cost;
- Financial assets and liabilities held for trading, measured at fair value;
- Financial assets designated as at fair value through profit or loss, measured at fair value;
- Other financial liabilities, measured at amortised cost.

The following table shows the classification of the Group's financial assets and liabilities according to IAS 39 and their fair values as at 31 December 2012:

Financial assets	Loans and receivables	Held for trading	Designated as at fair value	Liabilities at amortised cost	Other liabilities at fair value	Total carrying amount	Fair value
Cash and balances with Central Bank	25,898	-	-	-	-	25,898	25,898
Bonds and debt instruments	113,203	100,950	14,055	-	-	228,208	228,208
Equities and equity instruments	-	1,107	35,774	-	-	36,881	36,881
Derivative instruments	-	1,043	-	-	-	1,043	1,043
Loans and advances to financial institutions	64,349	-	-	-	-	64,349	64,349
Loans and advances to customers	666,087	-	-	-	-	666,087	674,417
Other financial assets	10,481	-	-	-	-	10,481	10,481
Total	**880,018**	**103,100**	**49,829**	**0**	**0**	**1,032,947**	**1,041,277**
Financial liabilities							
Due to financial institutions and Central Bank	-	-	-	98,718	-	98,718	98,718
Deposits from customers	-	-	-	421,058	-	421,058	420,856
Derivative instruments and short positions	-	9,438	-	-	-	9,438	9,438
Secured bonds	-	-	-	221,791	-	221,791	221,791
Contingent bond	-	-	-	-	87,474	87,474	87,474
Other financial liabilities	-	-	-	14,369	-	14,369	14,369
Total	**0**	**9,438**	**0**	**755,936**	**87,474**	**852,848**	**852,646**

The following table shows the classification of the Group's financial assets and liabilities according to IAS 39 and their fair values as at 31 December 2011

Financial assets	Loans and receivables	Held for trading	Designated as at fair value	Liabilities at amortised cost	Other liabilities at fair value	Total carrying amount	Fair value
Cash and balances with Central Bank	8,823	-	-	-	-	8,823	8,823
Bonds and debt instruments	112,547	93,063	16,238	-	-	221,848	221,848
Equities and equity instruments	-	1,224	44,813	-	-	46,037	46,037
Derivative instruments	-	159	-	-	-	159	159
Loans and advances to financial institutions	100,133	-	-	-	-	100,133	100,133
Loans and advances to customers	639,130	-	-	-	-	639,130	669,227
Other financial assets	4,321	-	-	-	-	4,321	4,321
Total	**864,954**	**94,446**	**61,051**	**0**	**0**	**1,020,451**	**1,050,548**
Financial liabilities							
Due to financial institutions and Central Bank	-	-	-	112,876	-	112,876	112,876
Deposits from customers	-	-	-	443,590	-	443,590	443,582
Derivative instruments and short positions	-	7,916	-	-	-	7,916	7,916
Secured bonds	-	-	-	277,076	-	277,076	277,076
Contingent bond	-	-	-	-	60,826	60,826	60,826
Other financial liabilities	-	-	-	6,623	-	6,623	6,623
Total	**0**	**7,916**	**0**	**840,165**	**60,826**	**908,907**	**908,899**

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7. Classification and fair value of financial assets and liabilities (continued)

The fair value of financial assets and liabilities was determined based on the following methods and assumptions. For all financial assets and liabilities the foreign currency exchange rates used are from observable markets both for spot and forward contracts and futures in the world's major currencies.

Balances with Central Bank

The carrying amount of balances with Central Bank is a reasonable approximation of their fair value.

Bonds and debt instruments

Quoted prices are generally available for government bonds and certain corporate securities. Where this information is not available, fair value is estimated by adding credit spreads to quoted market rates for similar bonds or relevant interest rate curves.

For bonds issued by defaulting or greatly distressed parties recovery values are used for estimating the fair value. These are published by the defaulting issuers resolution committee or equivalent, estimated based on statement of financial position information or expert opinion.

Interest rates are principally benchmark interest rates such as the London Inter-Bank Offered Rate (LIBOR) and quoted interest rates in the swap, bond and futures markets.

Where available, credit spreads are derived from prices of credit default swaps (CDS) or other credit based instruments, such as debt securities. For others, credit spreads are obtained from pricing services. Counterparty credit spreads are estimated based on the creditworthiness of the counterparty when differing from the assumed counterparty in the market.

Equities and equity instruments

Quoted prices are generally readily available for equity shares listed on the world's major stock exchanges and for major indices on such shares. When this information is not available the fair value is estimated based on market prices and earning multiples from similar securities, recent transactions or by using discounted cash flow methods.

Derivative instruments

The fair value of derivative instruments is determined using valuation methods whose most significant inputs is volatility, which are obtained from broker quotations, pricing services or derived from option prices.

Loans and advances to financial institutions

Loans and advances to banks include inter-bank placements and items in the course of collection. The carrying amount of floating rate placements and overnight deposits is a reasonable approximation of their fair value.

Loans and advances to customers

The estimated fair value of loans and advances represents the discounted amount of estimated future cash flows expected to be received based on future recovery of the loans. The recovery rates and loss given default are used as input into valuation models as an indicator of severity of losses on default. The loans are grouped by type and for each loan the estimated cash flows to be received during each month until end of 2013 are estimated and payments after 2013 are estimated to be received at the end of June each year. Expected cash flows are discounted at current market rates to determine fair value. Interest rates are principally benchmark interest rates such as London Inter-Bank Offered Rate (LIBOR), quoted interest rates in the swap, bond and future markets or the Group's current rates for new loans.

Due to financial institutions and Central Bank

Amounts due to financial institutions and Central Bank are repriced at least monthly and therefore their estimated fair value is the same as their carrying amount.

Deposits from customers

Deposits are recognised at amortised cost. The difference from fair value is the interest-rate dependent value adjustment calculated by comparing current market rates with original market rates of the deposits.

Short positions

The short positions are bonds issud by the Icelandic government or public entities, with readily available quoted market price

Secured bonds

The fair value of the secured bonds equals their carrying amount as the bonds have been discounted upon initial recognition at market rate and no significant changes have occurred in the market rate for these secured bonds since initial recognition.

7. Classification and fair value of financial assets and liabilities (continued)

Contingent bond

The fair value of the Contingent bond equals it's carrying amount as the bonds have been discounted upon initial recognition at market rate and no significant changes have occurred in the market rate for Contingent bond since initial recognition.

Fair value hierarchy

The Group has used a valuation hierarchy for disclosure of inputs to valuation used to measure fair value. This hierarchy prioritises the inputs into three broad levels as follows:
• Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities;
• Level 2: Valuation technique using observable inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
• Level 3: Valuation technique with significant unobservable inputs for the asset or liability that are not based on observable market data (unobservable inputs). Level 3 includes all instruments that are valued according to quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect the differences between instruments.

The following table shows the level in the hierarchy into which the fair value of financial assets and liabilities, carried at fair value in the consolidated statement of financial position, are categorised as at 31 December 2012:

Financial assets	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	63,751	40,643	10,611	115,005
Equities and equity instruments	4,212	2,792	29,877	36,881
Derivative instruments	-	1,043	-	1,043
Total	**67,963**	**44,478**	**40,488**	**152,929**

Financial liabilities				
Derivative instruments	-	519	-	519
Short positions	8,919	-	-	8,919
Contingent bond	-	-	87,474	87,474
Total	**8,919**	**519**	**87,474**	**96,912**

The following table shows the level in the hierarchy into which the fair value of financial assets and liabilities, carried at fair value in the consolidated statement of financial position, are categorised as at 31 December 2011:

Financial assets	Level 1	Level 2	Level 3	Total
Bonds and debt instruments	69,543	28,155	11,603	109,301
Equities and equity instruments	14,290	3,488	28,259	46,037
Derivative instruments	-	159	-	159
Total	**83,833**	**31,802**	**39,862**	**155,497**

Financial liabilities				
Derivative instruments	-	1,729	-	1,729
Short positions	6,187	-	-	6,187
Contingent bond	-	-	60,826	60,826
Total	**6,187**	**1,729**	**60,826**	**68,742**

During the year 2012 there were no transfers between individual levels.

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7. Classification and fair value of financial assets and liabilities (continued)

The following tables show the reconciliation for fair value measurement in Level 3 for the year 2012 and 2011:

1 January - 31 December 2012	Bonds and debt instruments	Equities and equity instruments	Total financial assets	Contingent bond
Carrying amount at 1 January 2012	11,603	28,259	39,862	(60,826)
Total gains (losses) recognised in income statement	462	5,061	5,523	(26,648)
Purchases	-	2,629	2,629	-
Sales	(40)	(6,281)	(6,321)	-
Settlements	(1,414)	209	(1,205)	-
Carrying amount at 31 December 2012	**10,611**	**29,877**	**40,488**	**(87,474)**
1 January - 31 December 2011				
Carrying amount at 1 January 2011	14,042	10,477	24,519	(26,510)
Total (losses) gains recognised in income statement	(64)	13,097	13,033	(34,316)
Purchases	3,391	4,585	7,976	-
Sales	(2,754)	(7,418)	(10,172)	-
Acquisitions through business combination	48	192	240	-
Settlements	(2,999)	2,936	(63)	-
Reclassification from assets held for sale	-	4,390	4,390	-
Transfers out of Level 3	(61)	-	(61)	-
Carrying amount at 31 December 2011	**11,603**	**28,259**	**39,862**	**(60,826)**

The following tables show the line items in the consolidated income statement where the total gains (losses) were recognised during the year 2012 and 2011, for fair value measurements in Level 3:

1 January - 31 December 2012	Bonds and debt instruments	Equities and equity instruments	Contingent bond	Total
Fair value change of contingent bond	-	-	(27,331)	(27,331)
Net gain on financial assets designated as at fair value through profit or loss	643	4,534	-	5,177
Net foreign exchange gain (loss	(181)	527	683	1,029
Total	**462**	**5,061**	**(26,648)**	**(21,125)**
1 January - 31 December 2011				
Fair value change of contingent bond	-	-	(34,316)	(34,316)
Net gain on financial assets designated as at fair value through profit or loss	(333)	13,084	-	12,751
Net foreign exchange gain (loss)	269	13	-	282
Total	**(64)**	**13,097**	**(34,316)**	**(21,283)**

The following table shows the line items in the consolidated income statement where gains (losses), relating only to financial assets and liabilities held by the Group at 31 December 2012 and categorised in Level 3, were recognised:

	Bonds and debt instruments	Equities and equity instruments	Contingent bond	Total
Fair value change of contingent bond	-	-	(27,331)	(27,331)
Net gain on financial assets designated as at fair value through profit or loss	156	3,455	-	3,611
Net foreign exchange gain (loss)	9	508	683	1,200
Total	**165**	**3,963**	**(26,648)**	**(22,520)**

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7. Classification and fair value of financial assets and liabilities (continued)

Although the Group believes that its estimates of fair value are appropriate, the use of different valuation methodologies and assumptions could lead to different measurements of fair value. The following table shows how profit before tax would have been affected if one or more of the inputs for fair value measurements in Level 3 were changed to reasonably possible alternatives:

	Effect on profit before tax	
Financial assets	**Favourable**	**Unfavourable**
Bonds and debt instruments	3,571	(1,909)
Equities and equity instruments	2,988	(2,988)
Total	**6,559**	**(4,897)**

The effect on profit was calculated using methods suitable for the models used. For equities valued using comparables or recent transactions the price was changed by +/-10%. For bonds issued by defaulting or greatly distressed parties the recovery value was changed by +/-500 basis points. For the contingent bond the volatility of the value of the underlying assets was changed by +/-250 basis points.

8. Cash and balances with Central Bank

	2012	**2011**
Cash on hand	2,749	2,355
Reverse repurchase agreements with Central Bank	21,178	4,010
Unrestricted balances with Central Bank	-	39
Total cash and unrestricted balances with Central Bank	**23,927**	**6,404**
Restricted balances with Central Bank	1,971	2,419
Total cash and balances with Central Bank	**25,898**	**8,823**

The Group has entered into short-term reverse repurchase agreements with the Central Bank of Iceland according to which the Group acquired certificates of deposit issued by the Central Bank and committed to resell the certificates to the Central Bank at a fixed price at the end of the contractual period. The Group does not recognise the certificates of deposit as its assets because the Group does not bear substantially all the risks and rewards of ownership of the certificates. However, the Group derecognised the cash transferred to the Central Bank and recognised a receivable from the Central Bank, including accrued interest.

The Bank holds a mandatory reserve deposit account with the Central Bank of Iceland. The average balance of this account for each month must be equivalent to at least mandatory reserve deposits, which amounted to ISK 7,262 million for December 2012 (December 2011: ISK 7,510 million). Any excess balance is available for use by the Group. Other cash and balances with the Central Bank are available for the Group's immediate use.

9. Bonds and equities

	2012				2011			
Bonds and debt instruments	**Loans and receivables**	**Held for trading**	**Designated as at fair value**	**Total**	**Loans and receivables**	**Held for trading**	**Designated as at fair value**	**Total**
Domestic								
Listed	113,203	45,251	1,820	160,274	112,547	30,902	628	144,077
Unlisted	-	-	11,837	11,837	-	371	13,012	13,383
	113,203	**45,251**	**13,657**	**172,111**	**112,547**	**31,273**	**13,640**	**157,460**
Foreign								
Listed	-	55,699	-	55,699	-	61,790	1,917	63,707
Unlisted	-	-	398	398	-	-	681	681
	0	**55,699**	**398**	**56,097**	**0**	**61,790**	**2,598**	**64,388**
Total bonds and debt instruments	**113,203**	**100,950**	**14,055**	**228,208**	**112,547**	**93,063**	**16,238**	**221,848**
Equities and equity instruments								
Domestic								
Listed	-	1,105	996	2,101	-	256	9,277	9,533
Unlisted	-	-	31,362	31,362	-	-	27,836	27,836
	0	**1,105**	**32,358**	**33,463**	**0**	**256**	**37,113**	**37,369**
Foreign								
Listed	-	2	561	563	-	968	3,777	4,745
Unlisted	-	-	2,855	2,855	-	-	3,923	3,923
	0	**2**	**3,416**	**3,418**	**0**	**968**	**7,700**	**8,668**
Total equities and equity instruments	**0**	**1,107**	**35,774**	**36,881**	**0**	**1,224**	**44,813**	**46,037**
Total	**113,203**	**102,057**	**49,829**	**265,089**	**112,547**	**94,287**	**61,051**	**267,885**

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9. Bonds and equities (continued)

Bonds and equities are classified as "domestic" or "foreign" according to the country of incorporation of the issuer.

Bonds and debt instruments classified as loans and receivables as at 31 December 2012 and 2011 consist partly of the government bonds which the Bank received in settlement of the capital contribution in 2009. The bonds were listed on the OMX Stock Exchange in Iceland during 2010.

10. Derivative instruments and short positions

	2012			2011		
	Notional	Fair value		Notional	Fair value	
Foreign exchange derivatives	amount	Assets	Liabilities	amount	Assets	Liabilities
Currency forwards	57,302	1,040	113	70,297	143	1,262
Cross-currency interest rate swaps	1,506	-	377	1,715	-	450
	58,808	**1,040**	**490**	**72,012**	**143**	**1,712**
Interest rate derivatives						
Total return swaps	4,668	3	8	5,834	16	17
	4,668	**3**	**8**	**5,834**	**16**	**17**
Equity derivatives						
Total return swaps	562	-	21	-	-	-
	562	**0**	**21**	**0**	**0**	**0**
Short positions - listed bonds	**-**	**-**	**8,918**	**-**	**-**	**6,187**
Total	**64,038**	**1,043**	**9,438**	**77,846**	**159**	**7,916**

The Group uses derivatives both for hedging and trading purposes.

11. Loans and advances to financial institutions

	2012	2011
Bank accounts with financial institutions	8,559	7,221
Money market loans	37,769	79,407
Overdrafts	7,726	3,857
Other loans	10,295	9,648
Total	**64,349**	**100,133**

12. Loans and advances to customers

	2012	2011
Public entities	11,682	12,143
Individuals	207,608	186,033
Corporations	490,827	469,374
Less: Allowance for impairment	(44,030)	(28,420)
Total	**666,087**	**639,130**

During the reporting period the Group was not permitted to sell or repledge any collateral in absence of default by the owner of the collateral.

Further disclosures on loans and advances are provided in the risk management section of the notes.

13. Investments in associates

a) Investments in equity-accounted associates	2012	2011
Carrying amount at the beginning of the year	11,678	3,340
Acquisitions through business combination	-	234
Acquisitions	1,334	6,778
Reclassification from assets held for sale	2,665	-
Share of profit of equity-accounted associates, net of income tax	2,449	1,417
Disposals	(2,598)	(91)
Total	**15,528**	**11,678**

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13. Investments in associates (continued)

At 31 December 2012*	Total assets	Total liabilities	Profit (loss)	Ownership interest	Share of profit of associates	Carrying amount
Valitor Holding hf.	43,391	35,098	918	38%	352	3,155
Framtakssjóður Íslands slhf.	29,526	118	6,014	28%	1,660	8,113
Reginn hf.	28,004	16,811	533	25%	133	2,798
Borgun hf.	20,599	18,548	654	31%	204	660
Reiknistofa bankanna hf.	2,187	478	91	37%	34	629
Motus ehf.	569	355	129	40%	62	125
Auðkenni hf.	224	32	21	20%	4	38
Other	-	-	-	-	-	10
Total	**124,500**	**71,440**	**8,360**		**2,449**	**15,528**

At 31 December 2011*	Total assets	Total liabilities	Profit (loss)	Ownership interest	Share of profit of associates	Carrying amount
Valitor Holding hf.	39,608	32,231	1,218	38%	463	2,803
Framtakssjóður Íslands slhf.	28,153	605	2,344	28%	839	7,600
Borgun hf.	16,075	14,677	210	31%	66	455
Reiknistofa bankanna hf.	1,979	361	166	37%	32	596
Motus ehf.	646	276	82	40%	32	181
Auðkenni hf.	222	51	4	20%	-	34
Other	-	-	-	-	(15)	9
Total	**86,683**	**48,201**	**4,024**		**1,417**	**11,678**

*The amounts for the years 2011 and 2012 in the table above are estimated not actual amounts at the end of the respective years.

The subsidiary Reginn hf. was listed on the OMX Nordic Exchange in Iceland following a public offering in June 2012. 75% of the Group´s shares were sold in the public offering and the acquirers became shareholders of Reginn hf. on 29 June 2012. The Group has committed itself to hold the remaining 25% of the shares in Reginn hf. for minimum of 10 months from 29 June 2012. The shareholding in Reginn hf. is presented under „Investments in equity-accounted associates“ in the statement of financial position and the gain from the sale amounting to ISK 1,650 million is presented under the line item „Profit for the period from discontinued operations, net of income tax“ in the income statement.

All associates are unlisted companies except for Reginn hf., which is listed on the OMX Stock Exchange in Iceland. Based on its closing price of 11,0 at the reporting date, the fair value of the investment is ISK 3,575 million.

According to Framtakssjóður Íslands slhf. (FSI) the estimated fair value of the bank investment in FSI is higher than their carrying amount at year end 2012 by ISK 4,881 million.

As part of the agreement with FSÍ, the Bank committed itself to invest up to ISK 15.0 billion in FSÍ. This amount will be callable during the years 2011-2016 as needed to fund investments by FSÍ, in proportion to the Bank's holding in FSÍ. At 31 December 2012 the Bank had invested in FSÍ ISK 8,842 (2011: 7,508) million representing 27.6% of total called in commitments ISK 32,048 milljon (2011: ISK 29,407 million). FSÍ is required to redeem its shareholders with the proceeds from sales of assets.

b) Investments in associates designated as at fair value through profit or loss

Four investments in associates are accounted for in their entirety by the Group as financial assets designated as at fair value through profit or loss and presented in the consolidated statement of financial position in the line “Equities and equity instruments”. Those investments are 49.5% shareholding in Promens hf., 29.6% shareholding in Reitir hf., 21.2% in Eyrir Invest hf. and 24.5% of the voting right in Stoðir hf.

14. Property and equipment

	2012			2011		
	Buildings	Fixtures, equipment and vehicles	Total	Buildings	Fixtures, equipment and vehicles	Total
Carrying amount at the beginning of the year	4,531	1,906	6,437	3,299	1,717	5,016
Acquisitions through business combination	-	-	-	1,329	284	1,613
Additions during the year	61	788	849	2	375	377
Sold during the year	(28)	(29)	(57)	-	(3)	(3)
Disposals	-	-	-	-	(68)	68)
Depreciation	(98)	(355)	(453)	(99)	(399)	(498)
Carrying amount at 31 December	**4,466**	**2,310**	**6,776**	**4,531**	**1,906**	**6,437**
Gross carrying amount	4,820	5,158	9,978	4,789	4,375	9,164
Accumulated depreciation	(354)	(2,848)	(3,202)	(258)	(2,469)	(2,727)
Carrying amount at 31 December	**4,466**	**2,310**	**6,776**	**4,531**	**1,906**	**6,437**
Depreciation rates	2-4%	10-33%		2-4%	10-33%	

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14. Property and equipment (continued)

Official assessment value of buildings at 31 December	2012	2011
Official assessment value used for tax purposes	4,998	3,823
Replacement value used for insurance purposes	12,556	8,774

Depreciation and amortisation presented in the income statement consists of	2012	2011
Depreciation of property and equipment	453	498
Amortisation of intangible assets	266	273
Total	**719**	**771**

15. Intangible assets

Computer software licenses	2012	2011
Carrying amount at the beginning of the year	681	877
Additions	126	77
Amortisation	(266)	(273)
Carrying amount at 31 December	**541**	**681**
Amortisation rates	20-33%	20-33%
Gross carrying amount	1,571	1,508
Accumulated amortisation	(1,030)	(827)
Carrying amount at 31 December	**541**	**681**

16. Other assets

	2012	2011
Provisional amount of the bond to be issued by the National Treasury*	-	30,596
Legally disputed collections	28	3,666
Unsettled securities trading	1,877	1,848
Receivables from Framtakssjóður Íslands slhf.	-	600
Receivables from LBI hf.	465	470
Other accounts receivable	2,814	1,403
Claim on LBI hf. due to court ruling	5,325	-
Sundry assets	3,599	5,418
Total	**14,108**	**44,001**

*The provisional amount of the bond to be issued by the Icelandic State Treasury is due to the acquisition of SpKef Savings Bank as disclosed in Note 5.

17. Assets and liabilities classified as held for sale

	2012	2011
Repossessed collateral	25,221	51,711
Assets of disposal groups classified as held for sale	99	1,841
Total	**25,320**	**53,552**

Repossessed collateral

Repossessed collateral consists mainly of property and equipment resulting from collateral foreclosed by the Group as security for loans and advances. The Group's policy is to pursue timely realisation of the repossessed collateral in an orderly manner. The Group generally does not use the non-cash repossessed collateral for its own operations. The repossessed collateral is recognised as assets of either the Bank or its subsidiary Hömlur hf. During the second quarter of 2012 the Bank ceased its control of the subsidiary Reginn hf. due to sale of the Group's 75% shareholding in the company, see Note 13.

	31.12.2012	31.12.2011
Carrying amount at the beginning of the year	51,711	43,831
Acquisitions through business combination	-	2,304
Repossessed during the period	12,171	22,668
Disposed during the period	(37,979)	(11,730)
Reclassification to equities and equity instruments	-	(4,390)
Impairment	(682)	(972)
Carrying amount at the end of the year	**25,221**	**51,711**

Assets of disposal groups classified as held for sale

Assets of disposal groups classified as held for sale consist of all the assets and liabilities of subsidiaries acquired by the Bank exclusively with a view to resale. During the first quarter of 2012 the Bank ceased its control of the subsidiary Vörður líftryggingar hf. due to a sale of the Bank's 11% shareholding in the company. The remaining shareholding was sold during the second quarter of 2012.

The profit (loss) for the period from discontinued operations which is presented in the consolidated income statement consists only of the results of those subsidiaries acquired by the Bank exclusively with a view to resale as they meet the definition of discontinued operations in IFRS 5.

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18. Due to financial institutions and Central Bank

	2012	2011
Loans and repurchase agreements with Central Bank	180	40
Loans and deposits from financial institutions	98,538	112,836
Total	**98,718**	**112,876**

19. Deposits from customers

	2012	2011
Demand deposits	310,088	344,952
Time deposits	110,970	98,638
Total	**421,058**	**443,590**

20. Secured bonds

	Nominal amount					Carrying amount	
	Foreign currency		ISK		Contractual	ISK	
Secured bonds	2012	2011	2012	2011	interest rate (%)	2012	2011
EUR	649 million	871 million	109,730	138,281	EURIBOR + 1.75/2.90	109,380	136,818
GBP	205 million	275 million	42,503	52,330	LIBOR + 1.75/2.90	42,397	51,702
USD	548 million	734 million	70,186	89,741	LIBOR + 1.75/2.90	70,014	88,556
Total			**222,419**	**280,352**		**221,791**	**277,076**

On 12 October 2010 the Bank issued secured bonds to LBI hf. as part of the acquisition price for its Icelandic operations. These bonds are denominated in EUR, GBP and USD and carry interest from October 2008. The carrying amount of the bonds as at 31 December 2012 and 2011 assumes the effective interest of EURIBOR/LIBOR+2.90% to maturity. The bonds are secured by pools of loans to customers, see Note 38.

The bonds mature in October 2018 with original scheduled quarterly instalments starting in 2014. As a result of prepayment of principals of the bonds in June 2012 the next instalments are scheduled for April 2015. The interest rates are 3 months EURIBOR for the EUR-denominated bond and 3 months LIBOR for the GBP and USD-denominated bonds, plus a margin of 1.75% for the first 5 years and a margin of 2.90% for the remaining 5 years. The first interest payment date was on 12 October 2010. From 30 June 2010, bondholders have had the right to require the Bank to convert the bonds into Eurobonds. Upon such conversion, the Bank will make reasonable endeavours to list such Eurobonds on a qualified stock exchange, as soon as feasible following conversion. The bondholders have not yet exercised their right to require the Bank to convert the bonds into Eurobonds.

On 29 February 2012 the Bank made a mandatory early redemption amount of ISK 1,615 million, due to a clause on Asset Disposition. The Bank shall redeem such part of the principal amount of the bonds as is equal to 50% of excess disposal amounts in regards to asset dispositions, subject to a maximum redemption amount.

On 15 June 2012 the Bank made an optional and partial pre-payment of 25% of the principal of each of the above bonds in the amount of EUR 216 million, GBP 68 million and USD 183 million, plus accrued interest from the last interest payment date to the partial early repayment date. The pre-payment of principal shall be considered as payment of the first five out of twenty scheduled principal payments of each bond. The next repayment of the principal will thus be in April 2015 instead of January 2014. This results in decreased pools of loans which the Bank has to pledge for the bonds, see Note 38.

21. Contingent bond

Pursuant to the provisions of the settlement agreement between the Bank, LBI hf. and the Icelandic State of 15 December 2009, the Bank shall issue a bond to LBI hf. no later than 31 March 2013, as an additional consideration for the assets and liabilities transferred from LBI hf. to the Bank on 9 October 2008. The value of the bond is contingent on the excess fair value of certain pools of assets as at 31 December 2012 over the future value of their acquisition price as at 9 October 2008, subject to specified adjustments. As at 31 December 2012 the Bank's estimate of the nominal amount of the contingent bond was ISK 88,142 million, which is lower than the bond's nominal ceiling amount of ISK 92,000 million. The estimate is that of the management of the Bank but the final and binding amount of the bond is still being determined by an independent third-party valuation agent, whose conclusions are expected to be presented no later than 31 March 2013. The Bank will issue the bond to LBI hf. no later than 31 March 2013, based on the valuation agent's final amount, converted into Euros at the exchange rate as published by the Central Bank of Iceland on 31 December 2012. The bond bears floating interest and matures in October 2018 with quarterly instalments starting in 2014.

Any possible difference between the Bank's estimate in these financial statements and the third-party valuation agent's final and binding amount will be accounted for in the Bank's 2013 first quarter financial statements. Given the nominal ceiling amount of ISK 92,000 million, the increase in the Group's total liabilities due to this is capped at ISK 3,858 million (using the EUR/ISK exchange rate at 31 December 2012). Whatever the final valuation difference will be, it is likely to be counter-balanced by improved recoverability of the Group's loans, such that the impact on the Group's 2013 performance will not be significant. However, any such changes in the underlying assets and the contingent bond may not necessarily be accounted for in the same quarterly financial statements.

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21. Contingent bond (continued)

The contingent obligation of the Bank is classified as a financial liability and measured initially at fair value. Subsequently, it is measured at fair value, with any resulting gain or loss recognised in the line item "Fair value change of contingent bond" in the income statement. As of 1 January 2013 the contingent bond is reclassified as a secured bond issued by the Bank and measured at amortised cost at the effective interest rate of LIBOR+2.9% to maturity.

22. Tax assets and liabilities

Tax assets and liabilities are specified as follows:

Tax assets	2012	2011
Deferred tax assets	48	3,003

Tax liabilities		
Current tax liabilities	0	70

Recognised deferred tax assets and liabilities are attributable to the following:

	2012			2011		
	Assets	Liabilities	Net	Assets	Liabilities	Net
Property and equipment	-	(1,061)	(1,061)	-	(1,332)	(1,332)
Intangibles	-	(105)	(105)	-	(17)	(17)
Loans and advances to customers	450	-	450	3,640	-	3,640
Deferred foreign exchange differences	-	(342)	(342)	-	(1,259)	(1,259)
Other items	-	(68)	(68)	-	(348)	(348)
Tax losses carried forward	1,174	-	1,174	2,319	-	2,319
	1,624	**(1,576)**	**48**	**5,959**	**(2,956)**	**3,003**
Set-off of deferred tax assets together with liabilities of the same taxable entities	(1,575)	1,575	-	(2,956)	2,956	-
Total	**49**	**(1)**	**48**	**3,003**	**0**	**3,003**

The deferred tax assets and liabilities are measured based on the tax rates and tax laws enacted by the end of 2012, according to which the domestic corporate income tax rate was 20% as at 31 December 2012 (2011: 20%).

The movements in temporary differences during the period were as follows:

		Recognised in income statement		
2012	**Balance 1.1**	**Tax (expense) income**	**Changes from prior year**	**Balance 31.12**
Property and equipment	(1,332)	271	-	(1,061)
Intangibles	(17)	(88)	-	(105)
Loans and advances to customers	3,641	(3,191)	-	450
Deferred foreign exchange differences	(1,259)	917	-	(342)
Other items	(348)	273	8	(67)
Tax losses carried forward	2,318	(2,107)	960	1,172
Total	**3,003**	**(3,925)**	**968**	**48**
2011				
Property and equipment	(1,943)	589	22	(1,332)
Intangibles	(101)	96	(12)	(17)
Loans and advances to customers	4,302	(661)	-	3,641
Other assets	(43)	43	-	0
Deferred foreign exchange differences	(1,714)	452	3	(1,259)
Other items	(168)	(167)	(13)	(348)
Tax losses carried forward	1,189	2,478	(1,349)	2,318
Total	**1,522**	**2,830**	**(1,349)**	**3,003**

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23. Other liabilities

	2012	2011
Excess payments on lease and loan agreements	8,857	11,156
Unsettled securities trading	3,873	4,852
Withholding tax	2,121	2,165
Accounts payable	1,293	1,348
Contribution to the Depositors' and Investors' Guarantee Fund	270	348
Tax on liabilities of financial institutions	300	35
Sundry liabilities	3,535	3,595
Total	**20,249**	**23,499**

Unsettled securities trading were settled in less than three days from the reporting date.

Contribution to the Depositors' and Investors' Guarantee Fund

According to Act No. 98/1999 on Deposit Guarantees and Investor Compensation Schemes ("the Act") and the amendment of the Act from 31 May 2011, the Bank was required during the year 2011 to make a non-refundable general and variable quarterly contributions to the Depositors' and Investors' Guarantee Fund ("the Fund"). The amount of the general contributions was determined on a quarterly basis as the amount equivalent to 0.05625% of all guaranteed deposits in the Bank, as defined in the amendment of the Act from 19 June 2012. The amount of the variable contributions was determined on a quarterly basis based on the risk rating of the Bank by the Icelandic Financial Supervisory Authority in Iceland (FME). The general and variable contributions become payable in the event of the Fund's total assets do not reach a minimum of 1% of the amount of guaranteed deposits in commercial banks and savings banks in the preceding year. In addition to the general and variable contributions, the Fund must demand that the Bank make additional contributions to the Fund if so commonly proposed by the FME and the Central Bank of Iceland. Furthermore, the Fund is allowed to demand additional contributions from the Bank in order for the Fund to repay its borrowings and related costs. The maximum amount of additional contributions that the Bank may be required to make to the Fund is the amount equivalent to 0.6% of guaranteed deposits in the Bank.

The Bank's management has concluded that the amount to be recognised as a liability in respect of the general and variable contribution shall only equal the amount that the Bank has no realistic alternative but to settle at each reporting date in accordance with the Act. This is the amount to be paid by the Bank during the following quarter, in respect of the preceding quarter. Other regular contributions to be made by the Bank to the Fund in future quarters do not exist independent of the Bank's future actions and therefore do not represent a present obligation of the Bank at the reporting date. Accordingly, they are not recognised as part of the liability towards the Fund. Therefore, the amount recognised as liability as at 31 December 2012 amounts to ISK 270 million to be paid no later than 1 March 2013 (31 December 2011: ISK 348 million).

24. Equity

Share capital

The total number of ordinary shares authorised and issued by the Bank at year end 2012 and 2011 was 24 billion shares, with par value of ISK 1 per share. One vote is attached to each share of one ISK and the holders of ordinary shares are entitled to one vote per share at general meetings of the Bank. All issued shares are fully paid.

Restriction of dividend payments

As part of the aquisition price for the domestic operations of LBI hf., the Bank issued senior secured bonds (see Notes 20 and 38). If the Bank makes a dividend payment then it shall redeem or shall have redeemed (such redemption not having been required by any other provision hereof) the bonds on a pro-rata basis in an amount equal to such dividend payment. In June 2012, the Bank made an optional and partial prepayment of principal of each of the bonds in an amount equivalent to ISK 71,200 million. In consequence of the Bank having redeemed part of the principal of the bonds with an optional prepayment, future dividend payments (and other payments of similar nature) up to ISK 71,200 million will not require further early redemptions of the bonds.

According to the Company Act No. 2/1995, it is only permissible to allocate as dividend profit in accordance with approved annual financial statements for the immediate past financial year, profit brought forward from previous years and free funds after deducting loss which has not been met and the funds which according to laws or Articles of Association must be contributed to a reserve fund or for other use.

Share premium

Share premium represents the difference between the ISK amount received by the Bank when issuing share capital and the nominal amount of the shares issued, less costs directly attributable to issuing the new shares, net of any related tax benefit.

Statutory reserve

The statutory reserve is created in accordance with requirements of the Company Act No. 2/1995, according to which at least 10% of the profit of the Bank, which is not devoted to meeting losses of previous years and is not contributed to other legally stipulated reserves must be contributed to the statutory reserve until it amounts to 10% of the share capital of the Bank. When that limit has been reached the contribution to the statutory reserve must be at a minimum 5% until the reserve amounts to a quarter of the share capital of the Bank.

Retained earnings

Retained earnings consist of undistributed profits and losses accumulated by the Group since the foundation of the Bank, less transfers to the statutory reserve of the Bank.

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Notes to the Consolidated Income Statement

25. Net interest income

Interest income	2012	2011
Cash and balances with Central Bank	1,091	1,186
Bonds and debt instruments classified as loans and receivables	4,921	3,768
Loans and advances to financial institutions	585	938
Loans and advances to customers	57,131	54,672
Other interest income	933	267
Total	**64,661**	**60,831**

Interest expense		
Due to financial institutions and Central Bank	(2,048)	(2,139)
Deposits from customers	(16,485)	(15,225)
Secured bonds	(10,482)	(10,653)
Other interest expense	(62)	(165)
Total	**(29,077)**	**(28,182)**

Net interest income	**35,584**	**32,649**
Interest spread (as the ratio of net interest income to the average carrying amount of total assets during the year).	**3.2%**	**2.9%**
Adjusted interest spread (as the ratio of net interest income after net adjustments in valuation to the average carrying amount of total assets during the year).	**2.8%**	**0.8%**

All the interest income and interest expense disclosed above is from financial assets and financial liabilities that are not carried at fair value through profit or loss.

26. Net valuation change in loans and advances

	2012	2011
Net adjustments to loans and advances acquired at deep discount	37,320	58,489
Loss from foreign currency linkage of loans and advances to customers	(2,120)	(40,726)
Net impairment loss	(12,260)	(7,034)
Total	**22,940**	**10,729**

Individuals	(233)	(14,920)
Corporations	23,173	25,649
Total	**22,940**	**10,729**

27. Net fee and commission income

Fee and commission income	2012	2011
Investment banking and capital markets	1,223	1,287
Asset management	1,009	1,022
Lending	1,060	981
Cards	1,524	1,385
Interbank clearing	1,079	991
Collection and payment services	792	790
Foreign trade	638	524
Other commissions and fees	371	457
Total	**7,696**	**7,437**

Fee and commission expense		
Investment banking and capital markets	(316)	(252)
Interbank clearing	(1,082)	(988)
Other fees	(1,850)	(1,774)
Total	**(3,248)**	**(3,014)**

Net fee and commission income	**4,448**	**4,423**

The net fee and commission income above excludes amounts that are otherwise included in determining the effective interest rate for financial assets and liabilities that are not at fair value through profit or loss. Moreover, it does not include any net fee and commission income relating to such financial assets and liabilities.

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28. Net gain on financial assets designated as at fair value through profit or loss

	2012	2011
Bonds and debt instruments	740	1,319
Equities and equity instruments	4,963	16,140
Total	**5,703**	**17,459**

29. Net gain on financial assets and liabilities held for trading

	2012	2011
Bonds and debt instruments	2,200	1,749
Equities and equity instruments	205	(388)
Derivative instruments	(236)	(352)
Total	**2,169**	**1,009**

30. Dividend income

Dividend income was recognised in the consolidated income statement in the following line items:

	2012	2011
Net gain on financial assets designated as at fair value through profit or loss	531	488
Net gain on financial assets and liabilities held for trading	20	110
Total	**551**	**598**

31. Net foreign exchange gain (loss)

Assets	2012	2011
Cash and balances with Central Bank	56	7
Bonds and debt instruments	4,972	3,315
Equities and equity instruments	1,085	168
Derivative instruments	2,438	(2,772)
Loans and advances to financial institutions	2,643	2,797
Loans and advances to customers	9,465	12,729
Other assets	1,194	192
Total	**21,853**	**16,436**
Liabilities		
Due to financial institutions and Central Bank	(1,347)	167
Deposits from customers	(3,281)	(5,047)
Secured bonds	(12,631)	(12,308)
Other liabilities	(28)	(7)
Total	**(17,287)**	**(17,195)**
Net foreign exchange gain (loss)	**4,566**	**(759)**

The foreign exchange differences which were recognised during the year 2012 in the consolidated income statement and arose on financial instruments not measured at fair value through profit or loss, amounted to a ISK 13,304 million gain for financial assets (2011; gain 15,725 million) and loss of ISK 15,940 million for financial liabilities (2011: loss of ISK 5,778 million).

32. Other income and expenses

	2012	2011
Recharged expenses	235	324
Gain (loss) on sale of property and equipment	14	(61)
(Loss) on assets classified as held for sale	(176)	(1,030)
Other	989	317
Total	**1,062**	**(450)**

33. Salaries and related expenses

	2012	2011
Salaries	10,224	9,618
Contributions to defined contribution pension plans	1,365	1,320
Other personnel expenses	1,587	1,052
Total	**13,176**	**11,990**
Number of full-time equivalent positions at year end	1,233	1,311
Average number of full-time equivalent positions during the year	1,260	1,283

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34. Other operating expenses

	2012	2011
Software licensing and other information technology costs	2,025	2,067
Real estate and fixtures	1,150	967
Advertising and marketing	736	739
Operating lease rentals	660	553
FME supervisory expenses	417	335
Contribution to the Debtor's Ombudsman	203	182
Audit and related services	130	178
Other professional services	879	884
Other operating expenses	2,678	2,562
Total	**8,878**	**8,467**

Audit and related services	2012	2011
Audit of financial statement and audit related service	79	121
Review of interim financial statement	51	54
Other services	-	3
Total	**130**	**178**

35. Acquisition-related costs

	2012	2011
Cost of acquisition of assets and liabilities from SpKef hf.	-	245
Cost of acquisition of assets and liabilities from LBI hf.	290	-
Total	**290**	**245**

36. Income tax and other taxes

Income tax is recognised based on the tax rates and tax laws enacted during the current year, according to which the domestic corporate income tax rate was 20.0% (2011: 20.0%). An additional special income tax on pre-tax profit over ISK 1,000 million at a rate of 6.0% is imposed on financial institutions for the first time in 2012.

Tax on liabilities of financial institutions

On 27 December 2010 the Parliament of Iceland passed a bill (Act No. 155/2010 on special tax on financial institutions) according to which certain types of financial institutions must pay annually a tax calculated as 0.041% of the carrying amount of their liabilities as determined for tax purposes. Additional tax of 0.0875% on the same tax base was imposed in respect of the years 2011 and 2012. The total additional tax in respect of the year 2012 amounts to ISK 1,200 million. The additional tax was recognised in the consolidated financial statements of the Group for the year 2012.

Income tax recognised in the income statement is specified as follows:

	2012	2011
Current tax expense	-	(70)
Difference of prior year's imposed and calculated income tax	1,087	913
Deferred tax expense	(4,012)	568
Total	**(2,925)**	**1,411**

The tax on Group profits differs to the following extent from the amount that would theoretically arise by the domestic corporate income tax rate:

	2012		2011	
Profit before tax		27,485		10,105
Tax on liabilities of financial institutions		(1,200)		(814)
Profit before income tax		26,285		9,291
Income tax calculated using the domestic corporate income tax rate	20.0%	(5,257)	20.0%	(1,858)
Income not subject to tax	(5.2%)	1,357	(33.2%)	3,080
Non-deductable expenses	1.4%	(371)	1.3%	(118)
Other*	(5.1%)	1,346	(3.3%)	307
Effective income tax	**11.1%**	**(2,925)**	**(15.2%)**	**1,411**

*The 2012 amount is due to revaluation of deferred tax assets whereas the 2011 amount is due to other tax sources.

Tax exclusively imposed on financial institutions is specified as follows:

	2012	2011
Special financial activities tax on salaries*	(620)	-
Tax on liabilities of financial institutions**	(1,200)	(814)
Total	**(1,820)**	**(814)**

*The Special financial activities tax on salaries at a rate of 5.45% is expensed in the line item "Salaries and related expenses" in the income statement.

**The Tax on liabilities of financial institutions is paid annually at a rate of 0.041% of the carrying amount of liabilities as determined for tax purposes. Additional tax of 0.0875% on the same tax base is imposed in respect of the years 2011 and 2012.

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Other notes

37. Litigation

The status of legal proceedings relating to the Group at year end 31 December 2012 is the following:

a) Litigation concluded in 2012 and early 2013

1) In September 2009, Handelsbanken AB, a Swedish bank, commenced litigation before the District Court of Reykjavík against the Bank, demanding a payment of ISK 835 million (SEK 42.4 million) plus interest based on a sub-guarantee issued by LBI hf. (previously Landsbanki Íslands hf.) to Handelsbanken. The District Court of Reykjavík ruled in favour of the Bank with reference to a decision of the FME dated 19 October 2008 stating that sub-guarantees such as this was not transferred from LBI to the Bank. Handelsbanken AB appealed the District Court's ruling to the Supreme Court which reversed the ruling in favour of Handelsbanken AB. The Court's decision was based on the fact that the Bank transmitted a SWIFT message to Handelsbanken AB on 23 October 2008 stating that the Bank was the guarantor. The Court found that even though the sub-guarantee had not been transferred to the Bank according to FME decision on 19 October 2008 the Bank had become a guarantor by sending the SWIFT message on 23 October and therefore obligated to pay the claimed amount. After the Bank paid Handelsbanken AB the claimed amount, Handelsbanken AB transferred to the Bank its claim on the estate of LBI in liquidation.

2) In March 2009 the Spanish bank Aresbank commenced litigation against the Bank, submitting claims to the District Court of Reykjavík demanding the Bank to pay ISK 5,069 million (EUR 30 million) and ISK 1,451 million (GBP 7 million), in addition to interests and litigation costs and that, alternatively that the FME and the Icelandic State are to pay damages on the basis of tort. The case involved two money market loans to LBI hf. each amounting to ISK 2,534 million (EUR 15 million) and a third money market loan amounting to ISK 1,451 million (GBP 7 million). In short, Aresbank claimed that money market loans were to be considered deposits according to the Act on Deposit Insurance, No. 98/1999. Aresbank cited the Icelandic government's declaration of 6 October 2008, that states that the government guarantees all deposits in domestic commercial banks and their branches in Iceland. On 22 December 2010 the District Court of Reykjavík ruled in favour of the Bank and confirmed that money market loans are not deposits according to the Act on Deposit Insurance. Aresbank appealed the ruling to the Supreme Court which subsequently requested an advisory opinion from the EFTA Court. The request mainly regarded the interpretation of the notion "deposit" in Article 1(1) of Directive 94/19/EC on deposit-guarantee schemes and whether "money market loans" fall there within. The EFTA Court delivered its opinion at the end of 2012, subsequently proceedings continued before the Icelandic Supreme Court which ruled in favour of the Bank and dismissed all claims made by Aresbank.

3) In May 2011 the City of Reykjavík commenced litigation against Landsvaki hf. (a subsidiary of the Bank), submitting claims to the District Court of Reykjavík. The claim of City of Reykjavík amounted to ISK 1,200 million plus interest. On 6 October 2008, the Icelandic Parliament, Althingi, adopted Act No. 125/2008, authorising the FME to assume the powers of the shareholders' meetings and Board of Directors of financial undertakings and to appoint resolution committees for them. A Resolution Committee was appointed for LBI on 7 October 2008. Landsvaki's money-market-fund "Peningabréf ISK" was closed on 6 October 2008 in accordance with an FME decision. Landsvaki subsequently dissolved all money market funds under management by the company in cooperation with the authorities. The disbursement ratio of "Peningabréf ISK" was 68.8% and the City of Reykjavík received their deposits accordingly. The claim was that Landsvaki should compensate the remaining 31.2% (ISK 1,200 million). On behalf of City of Reykjavík it is claimed that an order to sell was placed with Landsvaki on Friday 3 October 2008 and the instructions should have been executed before the fund was closed on Monday 6 October 2008. After the first hearing before the District Court the City of Reykjavik withdrew the case.

4) On 8 September 2010 the EFTA Surveillance Authority (ESA) opened a formal investigation on alleged state aid granted by the Icelandic State to investment funds and associated fund management companies connected to the three failed Icelandic banks Glitnir, Kaupthing and Landsbanki Íslands. It was alleged that in the autumn of 2008, the Icelandic authorities intervened in the market for investment funds that operated in accordance with Act No. 30/2003 on Undertakings for Collective Investment in Transferable Securities. On 11 July 2012 ESA concluded its investigation and approved the state aid granted for the restructuring of the Bank.

5) On 15 December 2010 ESA opened a formal investigation on state aid granted in October 2008 and September 2009 to rescue domestic operations of the three main Icelandic banks. On 11 July 2012 ESA concluded its investigation and with reference to the serious disturbance in the Icelandic economy at the time ESA found the aid compatible with the EEA Agreement.

37. Litigation (continued)

6) In December 2009 documents were served on the Bank by Basler Kantonalbank (BKB), a bank of the Swiss canton Basel City. Written summons were filed with the Commercial Court of the Swiss canton Zurich which subsequently ruled that it has jurisdiction in the matter. BKB's claim amounts to ISK 2,687 million (CHF 19,2 million) plus 5% interest from 9 October 2008, and is for the non-performance of FX Swap transactions by LBI. BKB argues that according to an FME decision the Bank took over LBI rights and obligations under derivatives contracts. BKB also argues that the FME decision of 12 October 2008, whereby the decision of 9 October was amended to the effect that derivative contracts were not transferred to the Bank, should be interpreted to apply only to derivative contracts after 12 October 2008. The Bank takes the view that the claim is without merit and should be directed at LBI. Court proceedings began in the fall of 2012 with a settlement procedure involving an opinion of an impartial judge. The opinion was favorable to the Bank and in February 2013 BKB relinquished the claim.

b) Ongoing Litigation

7) Fortis Bank was a correspondent bank of LBI hf. for international payments. The account had also been used by customers of LBI for international payments. After the foundation of the Bank, Fortis Bank was repeatedly notified thereof and that a resolution committee had been appointed for LBI on 7 October 2008. Fortis Bank was instructed not to receive payments into the account as the transferred payments were in fact owned by customers of the Bank. Fortis Bank did not act on the instructions and continued to receive payments and crediting the account of LBI. The Bank's customers who did not receive their payments due to the actions of Fortis Bank were reimbursed by the Bank. Of those customers, ten individual account holders were selected to commence litigation against Fortis Bank. On 23 May 2012 the Commercial Court of Brussels ruled in favour of the account holders ordering that Fortis Bank pay the total amount of ISK 372 million (EUR 2,2 million). Fortis bank has now appealed the court's decision to a higher court. It is foreseeable that the proceedings will be ongoing at least until 2014.

8) In May 2012 Stígandi ehf., a limited liability company, commenced litigation against the Bank. In the year 2007 Stígandi's CEO signed three loan agreements on behalf of the company (total amount ISK 2,302 million when the summons were filed). Now the board of directors claims that the CEO acted alone without consent of the board. The person who signed the loan agreements is still the CEO of Stígandi, holds 25% of Stígandi's shares and is on the board of directors together with his parents and brothers. Stígandi demands that the loan agreements be found invalid by the District Court of Reykjavík as well as repayment of ISK 13 million plus interest. Alternatively Stígandi claims damages amounting to ISK 2,302 million from the Bank plus interest. The Bank takes the view that the claims are without merit. It is foreseeable that the case will be heard by the District Court of Reykjavík in the early months of 2013.

9) In November 2011 Norðurturn ehf. (Norðurturn) a limited liability company in liquidation commenced litigation against Eignarhaldsfélag Smáralindar ehf. a limited liability company owned by Reginn hf. (previously a subsidiary of the Bank). The main operation of Norðurturn was the construction of an office building in the municipality of Kópavogur next to the shopping mall Smáralind owned by Eignarhaldsfélag Smáralindar. Norðurturn constructed a parking complex adjacent to Smáralind. Norðurturn now claims that the construction was done in accordance with an agreement between Norðurturn and Eignarhaldsfélag Smáralindar. Norðurturn's claim amounts to ISK 1,300 million plus interest. On behalf of Eignarhaldsfélag Smáralindar it is argued that there was no such agreement. The Bank has issued a guarantee for payment of the disputed amount on behalf of Eignarhaldsfélag Smáralindar if the case were to be lost. On 21 November 2012 the District Court ruled in favour of Eignarhaldsfélag Smáralindar. Norðurturn has expressed its intention to appeal the ruling to the Supreme Court.

10) In the year 2012 Plastiðjan ehf. a limited liability company commenced litigation against the Bank. In light of the Supreme Court rulings on the illegality of loans indexed to foreign currency the Bank recalculated loans to their customers. The dispute regards the method on how to recalculate Plastiðjan's interest payments. The disputed amount is approximately ISK 1 million but the Court's ruling on the method of recalculation is likely to affect other similar loans owned by the Bank which might call for new recalculations. Based on the Supreme Court's rulings in cases No. 600/2011 and 464/2012 regarding interest payments, an additional claim for payment must be considered substantial in order to fall under the precedence. In the case of Plastiðjan the Bank takes the view that the amount is insubstantial and therefore the recalculation to be correct. The District Court ruled in favour of the Bank but Plastiðjan has expressed its intention to appeal the ruling to the Supreme Court.

11) In December 2012 Ísleifur Jónsson, EP fjármál ehf., Upsir ehf. and Magnús Ingi Erlingsson commenced litigation against the Bank claiming damages in the amount of ISK 943 million plus interest. The plaintiffs were shareholders in the limited liability company Nýja Jórvík ehf., a company that was established for the purpose of buying in 2002 a rundown industrial building at Mýrargata 26 in Reykjavík, demolishing it and rebuilding on the same land a luxury apartment building. LBI and Nýja Jórvík entered into a loan agreement in 2005 for a total ISK 1,130 million where LBI agreed to lend money on terms relating to the progress and total building cost of the project. In the summer of 2008 the loans' principal had reached its maximum and Nýja Jórvík asked for another loan to continue the construction. At that time the market for real estate had crashed and building cost had increased significantly. On those grounds LBI declined Nýja Jórvík's request for a new loan and on the grounds that Nýja Jórvík was unable to provide increased equity. In 2010 Nýja Jórvík was declared bankrupt after not being able to pay its main contractor. The Plaintiffs claim that they lost the claimed amount when Nýja Jórvík went bankrupt because the loan agreement was illegally indexed to foreign currency. The Bank takes the view, first, that the plaintiffs cannot claim damages which supposedly Nýja Jórvík incurred. Second, eventually that such a claim should be directed at LBI. Third, that there was no damage incurred by the plaintiffs. Fourth, that the Bank is not liable if there was damage. The Bank has submitted its defence and it is foreseeable that the case will be heard before the District Court of Reykjavík in the spring of 2013.

37. Litigation (continued)

12) In December 2012 Visir hf., a limited liability company, commenced litigation against the Bank. Visir claims that its loan should be recalculated as a loan in ISK, illegally indexed to foreign currency. The Bank takes the view that the loan is a legitimate foreign currency loan and should not be recalculated in accordance with legislation No. 151/2010 and the Supreme Court's precedence. The Bank argues inter alia that all payments of Visir to the Bank, based on the loan agreement, were in foreign currency. It is expected that the case will be heard before the District Court of Reykjavík in the early months of 2013.

13) In June 2012 Reynir Finndal Grétarsson commenced litigation against the Bank. Mr. Grétarsson claims that his loan should be recalculated as a loan in ISK, illegally indexed to foreign currency. The Bank takes the view that the loan is a legitimate foreign currency loan and should not be recalculated in accordance with legislation No. 151/2010 and the Supreme Court´s precedence. The Bank argues inter alia that the loan was paid out in foreign currency, not ISK. It is expected that the case will be heard before the District Court of Reykjavík in the early months of 2013.

14) In March 2012 Flugastraumur ehf., a limited liability company, commenced litigation against the Bank. Flugastraumur maintains that its lease should be regarded as a loan agreement denominated in ISK and indexed to foreign currency and recalculated as such. The Bank's view is that the contract is in fact a lease contract that can be legally indexed to foreign currency in accordance with precedence of the Supreme Court. It is foreseeable that the case will be heard by the District Court in the early months of 2013.

15) In November 2012 Landsbankinn Guernsey Ltd. commenced litigation against the Bank, the FME and the Icelandic government. The plaintiff claims are that the Bank pay approximately ISK 2,694 million (GBP 13 million), ISK 106 million (EUR 628 thousand) and ISK 397 million (USD 3,1 million) plus interest, based on money market loans between the plaintiff and LBI that were transferred to the Bank with FME´s decision on 9 October 2008. After the Supreme Court's judgement of 17 January 2013, in the case of Aresbank, the plaintiff has expressed its view that it will withdraw its summons against FME and the Icelandic government. The case will however continue against the Bank. The plaintiff claims that money market loans are to be considered deposits according to the Act on Deposit Insurance, No. 98/1999. The plaintiff cites the Icelandic government's declaration from 9 October 2008, that states that the government guarantees all deposits in domestic commercial banks and their branches in Iceland. The Bank´s view is that money market loans were not transferred to the Bank on 9 October 2008 with FME's decision. This is based on the Supreme´s Court conclusion after reviewing all facts in the case of Aresbank. The Bank has not yet submitted written arguments but it is foreseeable that the case will be heard by the District Court of Reykjavík in the spring of 2013.

16) In December 2012 fourteen foreign banks commenced litigation against the Bank claiming payment of damages of approximately ISK 338 million (EUR 2 million). The plaintiffs base their claim on a syndicated loan to Samson, a limited liability company, that later underwent bankruptcy proceedings. When the plaintiffs submitted their claim to the liquidator of Samson's estate they failed to provide details on pledged assets. As a result of this failure the previously pledged assets were distributed to claimants of the estate as if they were not pledged assets in accordance with the Act on Bankruptcy, etc. No. 21/1991. The plaintiffs commenced legal action against the liquidator and in August 2011 Supreme Court ruled in favour of the liquidator. The plaintiffs now argue that the Bank should not have given the liquidator access to the previously pledged assets and is therefore liable for damages. The Bank takes the view that it only operated in accordance with Act on Bankruptcy and that the plaintiffs failure to correctly submit their claims to the bankrupt estate of Samson cannot create a liability for the Bank. The case is in its early stages and the Bank has not yet submitted its defence. It is foreseeable that the case will be heard by the District Court of Reykjavík in 2013.

17) In June 2011 Hestafl ehf. (Hestafl), a limited liability company, commenced litigation before the District Court of Reykjavík against the Bank. Hestafl's claim amounts to ISK 230 million plus interests from 12 December 2009 on the basis of a demand guarantee issued by the Bank in August 2008. The Bank issued the guarantee in connection with Hestafl's acquisition of the construction company TSH hf., a limited liability company. TSH had rights issued to build an apartment complex in the municipality of Selfoss, however after the collapse of the economy in Iceland in the following months, the construction never broke ground. The guarantee's terms for payment were based on the construction reaching certain milestones which were never reached. On those grounds it is the Bank's view that Hestafl's claim lacks merit. In June 2012 the District Court found in favour of the Bank and dismissed all claims made by Hestafl. Hestafl has appealed the judgment to the Supreme Court and it is expected that the case will be heard by the Court in the spring of 2013.

18) In May 2012 LBI hf. commenced litigation against the Bank's subsidiary, Landsvaki hf., based on the Act on Bankruptcy etc. No. 21/1991, claiming rescission of the purchase by LBI of bonds in the amount of approximately ISK 25,000 milion. Moreover, with respect to these claims, LBI claimed a set-off in the amount of ISK 5,000 million against a claim of the Bank that has been acknowledged in a Supreme's Court ruling of 22 March 2012. Landsvaki rejects the claims of LBI arguing that Landsvaki acted only in accordance with law and in collaboration with the FME. Furthermore, the Bank rejects the set-off claim as not being admissible in this case. The case will be heard by the District Court of Reykjavík in the early months of 2013.

37. Litigation (continued)

19) In October 2012 Kaupthing hf. commenced litigation before the District Court of Reykjavík against Landsbréf hf., Landsbanki Structured Finance III and Landsvaki hf. Kaupthing's claim amounts to ISK 724 million based on a derivative contract between Kaupthing and Landssjóður hf., dated 28 February 2008. Landssjóður's operating company was at that time the Bank's subsidiary Landsvaki. On 13 November 2008 Kaupthing informed Landsvaki that Landsvaki owed Kaupthing ISK 747 million as a final settlement based on the derivative contract. On 9 October 2008 a Resolution Committee was appointed for the estate of Kaupthing in accordance with Act. No. 125/2008 which has now jointly direct Kaupthing's estate with its Winding-up Board. Landsvaki filed a claim to the Winding-up Board based on a bond issued by Kaupthing amounting to ISK 1,282 million (USD 10 million) and declared set off against Kaupthing's claim based on the derivative contract. The Winding-up Board rejected Landsvaki's claim and declaration of set off. Landsbréf hf., Landsbanki Structured Finance III and Landsvaki have not yet submitted their comments on the case as it is in the initial stage of proceedings.

20) On 16 September 2011 Arion bank hf. lodged a complaint to EFTA Surveillance Authority (ESA) on the grounds of an alleged infringement of EEA state aid rules claiming that Landsbankinn through state resources has an advantage on the market. It was claimed that the Bank distributed funds to its customers through debt relief measures instead of allocating them to shareholders therefore not operating in accordance with the "market investor principle". The Bank has responded to the complaint and rejected the allegations. ESA has not yet concluded its assessment of the complaint.

38. Encumbered assets

On 12 October 2010 the Bank and LBI hf. signed a pledge agreement according to which the Bank pledged certain pools of loans to customers as collateral for the secured bonds issued on 12 October 2010 and the contingent bond the Bank might issue to LBI hf. The Bank must maintain a minimum cover ratio of 127.5% for the secured bonds. Once the contingent bond has been issued, the Bank must pledge assets for the contingent bond, with a minimum cover ratio of 118%. However, no assets must be pledged for the contingent bond before its issue date. Pledged assets added to the pledged pool must comply with certain eligibility criteria.

	Encumbered			
At 31 December 2012	**Pledged as collateral against secured bonds**	**Other***	**Un-encumbered**	**Total**
Cash and balances with Central Bank	-	-	25,898	25,898
Bonds and debt instruments	-	17,821	210,387	228,208
Equities and equity instruments	-	-	36,881	36,881
Derivative instruments	-	-	1,043	1,043
Loans and advances to financial institutions	-	8,091	56,258	64,349
Loans and advances to customers	319,240	-	346,847	666,087
Investments in equity- accounted associates	-	-	15,528	15,528
Property and equipment	-	-	6,776	6,776
Intangible assets	-	-	541	541
Deferred tax assets	-	-	48	48
Other assets	-	-	14,108	14,108
Assets classified as held for sale	-	-	25,320	25,320
Total	**319,240**	**25,912**	**739,635**	**1,084,787**

	Encumbered			
At 31 December 2011	**Pledged as collateral against secured bonds**	**Other***	**Un-encumbered**	**Total**
Cash and balances with Central Bank	-	-	8,823	8,823
Bonds and debt instruments	27,490	18,647	175,711	221,848
Equities and equity instruments	-	-	46,037	46,037
Derivative instruments	-	-	159	159
Loans and advances to financial institutions	-	5,892	94,241	100,133
Loans and advances to customers	337,959	-	301,171	639,130
Investments in equity-accounted associates	-	-	11,678	11,678
Property and equipment	-	-	6,437	6,437
Intangible assets	-	-	681	681
Deferred tax assets	-	-	3,003	3,003
Other assets	-	-	44,001	44,001
Assets classified as held for sale	-	-	53,552	53,552
Total	**365,449**	**24,539**	**745,494**	**1,135,482**

*Other represents assets pledged as collateral to the Central Bank of Iceland to secure settlement in the Icelandic clearing systems, assets pledged as collateral to secure trading lines and credit support for ISDA master agreements and other pledges of similar nature.

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39. Leasing

Operating lease commitments where the Group is lessee

In cases where the Group is a lessee, the future minimum lease payments under none-cancellable operating leases on 31 December were as follows:

	2012	2011
Less than one year	219	47
Between one and five years	292	339
More than five years	158	183
Total	**669**	**569**

Operating lease commitments where the Group is legal lessor

The Group acts as the legal lessor whereby tools and equipment are purchased and leased to third parties under arrangements that in substance are loans and advances accounted for under IAS 39 in the consolidated financial statements of the Group.

The future minimum lease payments expected to be received under none-cancellable operating leases on 31 December were as follows:

	2012	2011*
Less than one year	139	193
Between one and five years	206	286
More than five years	18	25
Total	**363**	**504**

Finance lease commitments where the Group is lessor

The Group acts as lessor whereby items of plant and equipment are leased to third parties under arrangements qualifying as finance leases. Finance lease receivables are included within loans and advances to customers.

The net investment in finance lease receivables was as follows:

At 31 December 2012	Gross investment in finance lease	Future finance income	Present value of minimum lease
Less than one year	1,567	(153)	1,414
Between one and five years	2,710	(210)	2,500
More than five years	354	(27)	327
Total	**4,631**	**(390)**	**4,241**
At 31 December 2011*			
Less than one year	1,713	(167)	1,546
Between one and five years	2,963	(229)	2,734
More than five years	387	(30)	95
Total	**5,063**	**(426)**	**4,375**

*One of the assumptions for the year 2011 amounts, disclosed in this same note in the consolidated financial statements of the Group as at 31 December 2011, proved incorrect. The incorrect asumption had no effect on the amounts reported by the Group in the income statement or statement of financial position as at 31 December 2011. The Group uses the correct assumptions for the comparative amounts of 2011, disclosed in this note as at 31 December 2012.

Unguaranteed residual value at year end 2012 is nil (2011: nil).

40. Fiduciary activities

The Group provides asset custody, asset management, investment management and advisory services. All of them require the Group to make decisions on the handling, acquisition or disposal of financial instruments. Assets in Bank custody are not reported in the consolidated financial statements, since they are not assets of the Bank. One aspect of these services is that the Group is involved in approving objectives and criteria for investing assets in its custody. As of 31 December 2012, financial assets managed by the Group amounted to ISK 95 billion (2011: ISK 112 billion). Custody accounts amounted to ISK 1.368 billion (2011: ISK 1.093 billion).

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41. Related party transactions

Related parties

The Icelandic State Treasury, on behalf of the Icelandic State, holds 81.3% of the shares in the Bank. Government bodies and public institutions qualifying as related parties are the Ministry of Finance, the ISFI (Icelandic State Financial Investments), and entities and institutions related to them.

Transactions between the Bank and its subsidiaries meet the definition of related party transactions. All transactions with subsidiaries are eliminated on consolidation and are thus not disclosed in the Group's consolidated financial statements. The main subsidiaries held directly or indirectly by the Bank at 31 December 2012 were the following:

Company	Ownership interest	Activity
Eignarhaldsfélag Landsbankans ehf. (Iceland)	100%	Holding company
Horn fjárfestingarfélag hf. (Iceland)	100%	Investment company
Landsvaki ehf. (Iceland)	100%	Management company for mutual funds
Landsbréf hf. (Iceland)	100%	Management company for mutual funds
Hömlur ehf. (Iceland)	100%	Holding company
Blámi - fjárfestingafélag ehf. (Iceland)	100%	Holding company
Landsbanki Vatnsafl ehf. (Iceland)	100%	Holding company
Span ehf. (Iceland)	100%	IT-services
Landsbanki Holdings UK plc. (United Kingdom)	100%	Holding company

LBI hf. has significant influence over the Bank, indirectly through its wholly owned subsidiary Landskil ehf., which holds 18.7% of the shares in the Bank. Landskil ehf. appoints one of the five members of the Board of Directors of the Bank and LBI hf. has also influence through its observers role in the Bank's Credit committee. Although these observers do not have rights to take part in the decision process during meetings of the Credit committee of the Bank they can submit their own comments outside such meetings, which can have an impact on the valuation of the contingent bond. Due to the ownership, its member on the Board of Directors of the Bank and influence through the Credit committee of the Bank, LBI hf. meets the definition of related party. As of 1 January 2013 LBI hf. no longer has the right to attend meetings of the Bank's Credit committee.

The key management personnel of the Bank and its close family members meet the definition of related parties and in some cases the key management personnel of the Bank's subsidiaries. The key management personnel of the Bank are the members of the Board of Directors, CEO, Managing Directors and other directors having authority and responsibility for planning, directing, and controlling the activities of the Bank. The Minister of Finance and the members of the Board of Directors of ISFI meet the definition of related party due to their ability to influence the policy of the Bank.

Transactions with related parties

(a) Transactions with the Icelandic government and government-related entities

The Group's products and services are offered to the Icelandic government and government related entities in competition with other vendors and under generally accepted commercial terms. In a similar manner, the Bank and other Group entities purchase products and services from government related entities at market price and otherwise under generally accepted commercial terms. The nature and outstanding amounts receivable from public entities are disclosed in Note 56.

(b) Transactions with other related parties

The deposits from LBI hf. amounted to ISK 43,807 million as at 31 December 2012 (2011: ISK 29,942 million). During the year 2012 the Bank recognised ISK 235 million from administrative services provided to LBI hf. based on a service level agreement (2011: ISK 324 million).

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41. **Related party transactions (continued)**

The following table presents the total amounts of loans to key management personnel and parties related to them and loans to associates of the Group:

	2012		2011	
Loans in ISK million	**Balance at 31 December**	**Maximum exposure**	**Balance at 31 December**	**Maximum exposure**
Key management personnel	108	237	112	133
Parties related to key management personnel	176	333	247	299
Associates	44,544	72,677	48,136	84,971
Total	**44,828**	**73,247**	**48,495**	**85,403**

No specific allowance for impairment was recognised in respect of these loans.

No pledges or commitments have been given or received in respect of these transactions in the period. There are no leasing transactions between related parties in the period.

The following table presents the total amounts of deposits received from key management personnel and parties related to them and associates of the Group:

	2012		2011	
Deposits in ISK million	**Balance at 31 December**	**Maximum exposure**	**Balance at 31 December**	**Maximum exposure**
Key management personnel	112	168	124	194
Parties related to key management personnel	56	166	65	88
Associates	18,432	36,667	17,330	25,187
Total	**18,600**	**37,001**	**17,519**	**25,469**

The following table presents the total amount of guarantees to key management personnel and parties related to them and associates of the Group:

Guarantees in ISK million	**2012**	**2011**
Key management personnel	-	4
Associates	507	501
Total	**507**	**505**

All the above transactions were made in the ordinary course of business and on substantially the same terms, including interest rates and collaterals, as those prevaling at the time for comparable transactions with third party counterparties.

(c) Compensation to directors, CEOs and managing directors

Salary and benefits for the year 2012	**Salary and benefits***	**Defined contri-butions****	**Termi-nation benefits**	**Total**
Gunnar Helgi Hálfdanarson, Chairman of the Board of the Bank	8.1	0.6	-	8.7
Sigríður Hrólfsdóttir, Vice-chairman of the Board of the Bank	6.0	0.5	-	6.5
Þórdís Ingadóttir, member of the Board of the Bank	5.1	0.4	-	5.5
Ólafur Helgi Ólafsson, member of the Board of the Bank	5.1	0.4	-	5.5
Andri Geir Arinbjarnarson, member of the Board of the Bank	5.5	0.4	-	5.9
Alternate directors of the Board of the Bank	5.1	0.4	-	5.5
Steinþór Pálsson, CEO of the Bank	14.2	2.4	-	16.6
7 Managing Directors of the Bank's divisions	134.6	25.5	-	160.1
2 former Managing Directors of the Bank	41.6	8.0	-	49.6
Other managing directors	16.6	2.6	-	19.2
Total	**241.9**	**41.2**	**0.0**	**283.1**

*Benefits are non-monetary benefits in the form of free use of cars owned by the Group.

**Includes both private and statutory contributions to independent pension funds without further obligation.

In 2012 the total monthly salary and benefits of the current CEO of the Bank amounted to ISK 1.2 million and the average monthly salary and benefits of current Managing Directors of the Bank's divisions amounted to ISK 1.8 million.

In addition to the salaries and related expenses of the CEO in the table above the Bank makes a provision at year end 2012 in the amount of ISK 47 million, due to possible corrections or retroactive adjustments of the CEO's salary and employment conditions for the years 2011 and 2012.

41. Related party transactions (continued)

(c) Compensation to directors, CEOs and managing directors (continued)

Salary and benefits for the year 2011	Salary and benefits*	Defined contri-butions**	Termi-nation benefits***	Total
Gunnar Helgi Hálfdanarson, Chairman of the Board of the Bank	6.4	0.5	-	6.9
Sigríður Hrólfsdóttir, Vice-chairman of the Board of the Bank	5.1	0.4	-	5.5
Guðríður Ólafsdóttir, member of the Board of the Bank	1.6	0.1	-	1.7
Þórdís Ingadóttir, member of the Board of the Bank	4.1	0.3	-	4.4
Ólafur Helgi Ólafsson, member of the Board of the Bank	4.1	0.3	-	4.4
Andri Geir Arinbjarnarson, alternate member of the Board of the Bank	4.4	0.3	-	4.7
Other alternate directors of the Board of the Bank	3.5	0.3	-	3.8
Steinþór Pálsson, CEO of the Bank	13.9	2.3	-	16.2
8 Managing Directors of the Bank's divisions	168.0	31.9	-	199.9
Managing Directors of subsidiaries Vestia, Horn, Reginn, Landsvaki and SP fjármögnun	77.3	9.6	24.0	110.9
Total	**288.4**	**46.0**	**24.0**	**358.4**

*Benefits are non-monetary benefits in the form of free use of cars owned by the Group.
**Includes both private and statutory contributions to independent pension funds without further obligation.
***Termination benefits payable in the year 2011 were fully recognised as an expense in the year 2010.

In 2011 the total monthly salary and benefits of the current CEO of the Bank amounted to ISK 1,2 million and the average monthly salary and benefits of current Managing Directors of the Bank's divisions amounted to ISK 1,8 million.

(d) Transactions with the Minister of Finance and members of the Board of Directors of the ISFI

The Minister of Finance and the members of the Board of Directors of the ISFI did not receive any salaries or similar payments from the Group during the year 2012. The Group did not enter into any transactions with these persons or close members of their families, other than lending and deposit taking during the normal course of commercial banking operations.

42. Events after the reporting period

The main event after the reporting period is the following:

In January 2013 a client of the Bank commenced litigation against the Bank claiming acknowledgement by the Court that he is not legally bound by a clause on consumer price index in a bond issued by himself to the Bank, alternatively that the Court confirms that the Bank is not entitled to revalue the principal amount of the bond on a monthly basis according to the consumer price index. Furthermore, the client claims confirmation by the Court that he is not legally bound by a clause in the same bond regarding the issuer's duty to pay a settlement fee. The client claims that the bond´s clauses are illegal according to the Securities Transaction Act No. 108/2007 and EU Directive No. 2004/39/EB. The Bank will submit its defence and it is foreseeable that the case will be heard before the District Court of Reykjavík in the spring of 2013.

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Capital management

43. Capital management

The Group's capital management policies and practices ensure that the Group has sufficient capital to cover the risk associated with its activities. The capital management framework of the Group comprises four interdependent activities: Capital Assessment, Risk Appetite/Capital Target, Capital Planning, and Reporting/Monitoring. The Group regularly monitors and assesses its current risk profile in the most important business areas and for the most important risk types. Risk appetite sets out the level of risk the Group is willing to take in pursuit of its business objectives.

Capital requirements are defined by two external bodies: the European Council (EU) and the Financial Supervisory Authority in Iceland (FME). The basis of the requirements of both bodies is the EU Capital Requirements Directive (CRD). The regulatory minimum capital requirement under Pillar I of the directive is 8% of risk weighted assets for credit risk, market risk and operational risk. The Capital Adequacy Requirement (CAD) is reviewed by the FME in the Supervisory Review and Evaluation Process (SREP).

The Group uses the standardised approach in measuring Pillar I risks. Risk-weighted assets (RWA) for credit risk, the single largest risk type, amounted to 77.3% of total RWA. The Internal Capital Adequacy Assessment Process (ICAAP) under Pillar II is the Group's calculation of its solvency need (as percentage of RWA) and is based on economic capital calculations, stress tests and result of the Supervisory Review and Evaluation Process (SREP). The economic capital is estimated at 15.5% for year end 2012. In the latest SREP process, based on year end 2011, the FME determined the Capital Adequacy Ratio to be at 19.5%, mainly because of uncertainty regarding currency loans. This is 11.5% additional to the requirement of the EU directive.

The FME requires the Group to maintain a minimum core Tier 1 capital ratio of 12% unless revised by FME. The previous Capital Adequacy Ratio (CAD ratio) requirement of the FME for the Group was increased from 16% to 19.5% in the fourth quarter of 2012 (estimation based on year end 2011) and is now determined by the Group's calculation of its solvency need (ICAAP report) and SREP by the FME which is performed each year.

44. Capital base and capital adequacy ratio

The Group's equity at 31 December 2012 amounted to ISK 225,166 million (31.12.2011: ISK 200,244 million), equivalent to 20.8% (31.12.2011: 17.6%) of total assets, according to the condensed consolidated statement of financial position. The Capital Adequacy Ratio, calculated in accordance with Article 84 of Act No. 161/2002 on Financial Undertakings, was 25.1% at 31 December 2012 (31.12.2011: 21.4%). Under the Act the minimum requirement for this ratio is 8%.

Capital base	31.12.2012	31.12.2011
Share capital	24,000	24,000
Share premium	123,898	123,898
Statutory reserve	5,053	3,781
Retained earnings	72,120	47,952
Non-controlling interests	95	613
Total equity	**225,166**	**200,244**
Intangible assets	(541)	(681)
Deferred tax assets	(48)	(3,003)
Tier 1 capital	**224,577**	**196,560**
Deduction from original and additional own funds	(3,815)	(4,531)
Capital base	**220,762**	**192,029**
Risk-weighted assets (RWA)		
Credit risk	679,516	696,402
Market risk	98,486	120,557
Operational risk	101,393	81,500
Total Risk-weighted assets	**879,395**	**898,459**
Tier 1 capital ratio	25.5%	21.9%
Capital adequacy ratio (CAD)	25.1%	21.4%

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Economic Capital

45. Economic Capital framework

Economic Capital (EC) is a risk measure which is applied to all material risks. It captures unexpected losses and reduction in value or income for which the Bank needs to hold capital to avoid insolvency. It arises from the unexpected nature of losses as distinct from expected losses. EC is defined as the difference between unexpected losses and expected losses, where unexpected loss is defined as the 99.9% Value-at-Risk, with a one year time horizon.

The purpose of the EC framework is to enable the Bank to assess the amount of capital it requires to cover the economic effects of risk taking activities as well as to compare different risk types using a common "risk currency".

The objective of the EC framework is to measure unexpected losses as well as to decompose EC on various levels to enable capital allocation, limit setting, pricing of products, risk adjusted performance measurement and value based management.

The framework covers the following risk types: credit risk; market risk; operational risk; concentration risk, interest rate risk in the non-trading book; legal risk and business risk.

The following summarises how the Group calculates its Economic Capital for these risks.

Credit risk:
The credit risk Economic Capital model is the asymptotic single risk factor (ASRF) model from the Basel II internal rating based (IRB) approach's risk weight formula, i.e. the EC equals the capital requirements of the IRB approach in the capital requirements directive. The main input to the model are the risk parameters probability of default (PD), loss given default (LGD) and exposure at default (EAD).

Market risk:
Market risk EC for interest rate and equity risks is calculated using the standardised measurement method of the Basel framework, i.e EC equals the Bank´s capital requirements for interest rate and equity risks.

Currency risk:
For FX positions a VaR-model is used to calculate Economic Capital. 1-day 99% VaR as well as stressed VaR (SVaR) are calculated and scaled to one-year 99% VaR in accordance with the Basel framework. Stressed VaR is calculated from the worst case of the previous 250 trading days. Economic Capital for FX-risk equals the sum of the two one-year 99% VaR measures.

Concentration risk:
EC for single name concentration is calculated by adjusting for the granularity and inhomogenities in the portfolio. This is necessary as the credit risk EC-model assumes that the portfolio is infinitely large and homogenous hence the single name concentration EC is given as an add-on.

An internal model is used to measure the additional EC for credit risk related to industry concentrations in the loan portfolio, i.e. a concentration add-on. EC is given by the increase in credit risk EC when a correlation adjusted for the concentration in the portfolio is used.

Interest rate risk in the banking book:
Interest rate risk in the banking book EC is equal to the loss of economic value resulting from a simultaneous parallel shift in the relevant interest rate curves.

Operational risk:
Economic Capital for Operational risk is calculated using the basic indicator approach, hence it equals the Bank´s capital requirement.

Business risk:
Economic Capital for Business risk is calculated using an internal model, which is based on the volatility of the Bank's income, before profit or losses due to any other material risk.

Legal and regulatory risk:
Economic Capital for legal and regulatory risk is calculated by adding the potential loss of ongoing disputes.

46. Economic Capital by risk type

The Economic Capital decreased slightly during 2012 mainly due to improved quality of the loan portfolio and lower assessment of Economic Capital for Creditor concentration risk. Legal and regulatory risk has increased as well as Interest rate risk but the Group has revised its methodology for interest rate sensitivity measurements for non-trading portfolios by applying more severe interest rate shocks to the relevant yield curves taking historical interest rate volatility into account. Credit risk is the largest source of risk confronting the Bank and in the year 2012 the EC for this risk type decreased slightly. The reduction is, as mentioned above, attributed to improved quality of the loan portfolio.

Economic Capital ISK Million	2012	2011
Credit risk - Loans to customers and credit institutions	68,764	69,296
Credit risk - Other assets	5,041	6,834
Market risk	5,865	7,399
Currency risk	3,676	2,443
Operational risk	8,111	6,520
Single name concentration risk	8,099	21,603
Industry concentration risk	2,710	2,466
Interest rate risk	10,688	5,055
Business risk	4,056	3,260
Legal and regulatory risk	18,913	12,800
Total	**135,923**	**137,676**
EC/RWA	15.5%	15.3%

	Weighted average			
Credit risk at 31 December 2012	**Probability of default (PD)**	**Loss given default (LGD)**	**Exposure at default (EAD)**	**Economic Capital (EC)**
Financial institutions	1.5%	45.0%	58,357	2,716
Public entities	1.2%	44.9%	26,277	1,687
Individuals	2.7%	33.2%	214,516	8,078
Corporates	6.0%	44.0%	527,410	56,283
Total	**4.6%**	**41.3%**	**826,560**	**68,764**

	Weighted average			
Credit risk at 31 December 2011	**Probability of default (PD)**	**Loss given default (LGD)**	**Exposure at default (EAD)**	**Economic Capital (EC)**
Financial institutions	3.1%	45.0%	95,656	2,838
Public entities	0.9%	44.8%	19,725	1,052
Individuals	2.8%	32.3%	173,013	7,081
Corporates	8.8%	43.8%	493,207	58,325
Total	**6.6%**	**41.4%**	**781,601**	**69,296**

Risk management

47. Risk management structure

The Group's risk management governance structure as at year end 2012 is as follows:

Supervision by the Board of Directors	**Board of Directors** Internal Audit, Audit and Risk Committee, Governance Committee				
Key risk management bodies and committees	**The CEO** Credit Committee Risk and Finance Committee Executive Management Committee				
Risk types	Compliance risk	Credit risk	Market risk	Operational risk	Liquidity risk

The Board of Directors of the Bank has overall responsibility for the establishment and oversight of the Group's risk management framework and risk appetite setting. The CEO is responsible for the effective implementation of the framework and risk appetite through the corporate governance structure and committees. The CEO has established and is a member of the Credit Committee, the Risk and Finance Committee and the Executive Management Committee.

47. Risk management structure (continued)

The Credit Committee deals with credit risk, both credit limits for individual customers as well as credit risk policy issues, while the Risk and Finance Committee covers primarily market risk, liquidity risk and legal risk. The Risk and Finance Committee monitors all the Group's risks, is responsible for enforcing the Bank's risk appetite and risk limits and reviews and approves changes to risk models before presented to the Board of Directors. The Executive Management Committee serves as a forum for consultation and communication between the CEO and managing directors, addressing the main current issues in each division. This committee makes all major decisions which are not being consulted on elsewhere or being considered in other standing committee.

The Bank's Risk Management Division is responsible for the functioning of the Group's risk management framework. Subsidiaries of the Bank have their own risk management functions, but the Risk Management Division receives information on exposures from the subsidiaries and collates them into Group exposures.

The Risk Management division has six units.

• The Credit Management Unit is responsible for risk assessment and secondary voting on credit applications from customers with exposures exceeding the credit limits of individual business units and customers which have been classified yellow, orange or red (see Note 52). Secondary voting on decisions exceeding the authorisation of the Risk Management Division is referred to the Bank's Credit Committee.

• The Credit Risk Monitoring Unit is responsible for monitoring credit risk within the Bank's credit portfolio. This is done by operating a credit monitoring system. The Credit Risk Monitoring unit is also responsible for the portfolio valuation methodology as for the operation of the Bank's write off process. In addition the unit works with other units on impairment analysis.

• The Market risk Unit is responsible for measuring and monitoring market risk, liquidity risk and interest rate risk in the banking book for the Group. The Market risk unit is also responsible for monitoring all derivatives trading the Group enters into, both for hedging and trading purposes. Market Risk monitoring also includes FX balance monitoring for the Group as well as providing limit monitoring for Pension funds that are managed within the Group. The Market risk unit is also responsible for comprehensive risk reporting to various departments and committees.

• The Operational Risk Unit is responsible for ensuring that Group operational risks are monitored and that the Group implements and maintains an effective operational risk management framework.

• The Models and Analysis Unit is responsible for providing, developing and maintaining the Bank's internal models and related processes to measure risk, including the Economic Capital framework; as well as to support the implementation of such models and processes within the Bank. In addition the unit is responsible for credit risk, economic capital and risk appetite reporting within the Bank as well as reporting to supervisory authorities.

• The Economic Research Unit is responsible for the analysis of the external domestic and international economic environment relevant to the Bank's operations. The analysis provides support to management in planning, risk management and decision making. The main task of the department within the risk management context is to design and analyse macroeconomic scenarios which are applied in the stress testing process.

The Bank's Compliance Department ensures that the Group adheres to its own rules on securities trading and insider trading and that the Group's operations comply with Act No. 108/2007, on Securities Transactions, Act No. 67/2006 on Actions to Combat Money Laundering and Terrorist Financing, and other relevant legislation and regulations. The Compliance department also concentrates on Group adherence to codes of ethics and on limiting market abuse, minimising conflicts of interest and ensuring best practice. Such compliance is one of the Group's support functions and is integral to its corporate culture.

Internal Audit is part of the Group's risk management framework as well as being a part of the surveillance system. The purpose of Internal Audit in the risk management process is to confirm that risk management is functioning and is sufficient for the Group. The effectiveness of the Group's risk management and risk assessment procedures, including the Internal Capital Adequacy Assessment process (ICAAP), is evaluated by Internal Audit and the findings are reported to the Board of Directors. Internal audit activities extend to every operating unit, including the Bank's subsidiaries.

48. Risk appetite

During 2012 the Group's risk appetite has been reviewed, revised and implemented for 2013. The statement of the Group's risk appetite is as follows:

It is the policy of The Group to take only on risks that the Group is able to understand, measure and manage. The Bank's strategy and long term vision is to attain the same credit rating as comparable leading banks in the Nordic countries.

The Bank seeks to maintain solid business relationships and avoids taking part in transactions that might damage the Bank's reputation. It will take advantage of market opportunities to ensure diversified and sound financing.

48. Risk appetite (continued)

Transactions entered into by the Group aim to limit fluctuations in its operations and ensure that the Group is always in a position to withstand shocks. Moreover, transactions shall take into account the current standing of both the Bank and its customers and and their potential interrelationship. The profitability of the Group should be assessed with respect to risk taken by the Bank. The Bank's corporate culture is characterised by professionalism and processes that support its risk strategy.

Executives and employees are responsible for monitoring and managing risks taken on within their units in accordance with the Bank's rules and local law. Decisions are based on a thorough and professional discussion with the Group's long-term interests in mind. Regular and thorough follow-up on decisions and risk monitoring are integral part of the Group's operations.

49. Risk management process

Risk is inherent in the Group's activities and is managed through a process of ongoing identification, measurement, management and monitoring, subject to risk limits and other controls. Risk identification involves finding the origins and structures of possible risk factors in the Group's operations and undertakings. Risk measurement entails measuring the identified risks for management and monitoring purposes. Finally, risk controls and limits ensure compliance with rules and procedures as well as to ensure compliance with the Group's risk appetite.

The objective of the Group's risk policies and procedures is to ensure that the risks in its operations are known, measured, monitored and effectively managed. Exposure to risks is managed to ensure that it will remain within limits as well as the risk appetite adopted by the Group and will comply with regulatory requirements. In order to ensure that the fluctuations which might affect the Group's equity as well as performance are kept limited and manageable the Group has adopted several policies regarding the risk structure of its portfolio which are covered in more detail under each risk type.

Risk policy is implemented through goal setting, business strategy, internal rules and limits that comply with the regulatory framework of the financial markets.

The Group is exposed to the following material risks which arise from financial instruments:
· Credit risk
· Market risk
    -Currency risk
    -Interest rate risk
    -Other market risk
· Liquidity risk
· Operational risk
The Group also manages other relevant risk, such as business, legal and compliance risk.

The above material risks are addressed in the following notes.

Credit risk

50. Credit risk identification

Credit risk is defined as the risk of loss if counterparts fail to fulfil their obligations and collaterals pledged by them do not cover existing claims.

Credit risk is the greatest single risk faced by the Group and arises principally from loans and advances to customers and from investments in debt securities, but also from commitments, guarantees and documentary credits, counterparty credit risk in derivatives contracts, and settlement risk.

51. Credit risk assessment

Credit risk is measured in three main dimensions: the probability of default (PD); the loss given default (LGD) and the exposure. For the purpose of measuring PD the Group has developed an internal rating system, including a number of internally developed rating models. The objectives of the rating system are to provide a meaningful assessment of obligor characteristics; a meaningful differentiation of credit quality; and accurate and consistent quantitative estimates of default risk, i.e. probabilities of default. Internal ratings and associated PD play an essential role in the risk management and decision-making process, and in the credit approval and corporate governance functions.

The rating system has an obligor 'rating scale' which reflects exclusively quantification of the risk of obligor default, i.e. credit quality. The obligor rating scale has 10 rating grades for non-defaulted obligors going from '1' to '10', '10' indicating the highest credit quality, and the grade '0' for defaulted obligors. The rating assignment is supported by rating models, which takes information such as industry classification, financial accounts and payment behaviour into account.

The rating assignment and approval is an integrated part of the credit approval process and assignment shall be updated at least annually or when material information on the obligor or exposure becomes available, whichever is earlier.

51. Credit risk assessment (continued)

LGD is measured using the models defined in the Basel framework for the purpose of Economic Capital calculations. In addition, during 2012 the Group implemented in the business processes an internal LGD model, which takes into account more types of collateral and is more sensitive to the collateralisation level than the forementioned Basel model.

The exposure is calculated using the credit conversion factors of the Basel framework.

52. Credit risk control and monitoring

The Group monitors exposures to identify signs of weakness in customer operations affecting their earnings and liquidity at the earliest possible time.

To monitor customers the Group uses, supplemental to using ratings, a credit monitoring classification of four credit risk groups (green, yellow, orange and red). The colour classification is the following:

• Green customers are those that are considered performing without difficulties.

• Yellow customers are those that are on Watch list 1, which have temporary difficulties and may need some instalments postponed or modification to terms or loan covenants.

• Orange customers are those that are on Watch list 2. They are still under the supervision of the relevant business unit but are likely to go through debt restructuring or postponement of instalments.

• Red customers are those that are under the supervision of the Corporate Solutions division and need restructuring, write-offs or debt-to-equity conversion. The management of the customer's operations will possibly be taken over by the Group. In some cases, collateral or guarantees will be collected and/or the operations sold.

The Credit Risk Monitoring unit within Risk Management is together with the business units responsible for the verification of colour for the customer and transfer of customers from the business units to Corporate Solutions if necessary.

External ratings were used where applicable to assist in managing the credit risk exposure of bonds. Otherwise the Group used fair value estimates base on available information and the Group's own estimates.

The Group measures the credit risk of derivatives by calculating a credit equivalent value for each derivative. The credit equivalent value is the market value of a contract plus a percentage of the nominal amount of the derivative which depends on the type of derivative. The percentage is twice that of the 99% Value at Risk (VaR), calculated for each underlying security or currency based on historical volatility, for a holding period of five days.

53. Credit risk management

The Group's credit risk management is based on active monitoring by the Board of Directors, the CEO, the Risk and Finance Committee, the Credit Committee, the credit units within the Risk Management and the business units. The Group manages credit risk according to its risk appetite statement and credit policy approved by the Board of Directors as well as detailed lending rules approved by the CEO. The risk appetite statement and credit policy include exposure limits on large exposures to individual borrowers or groups of borrowers, concentration of risk and exposures to certain industries. The CEO ensures that the risk policy is reflected in the Group's internal framework of regulation and guidelines. The CEO monitors together with the Bank's managers that the Bank's business units execute the risk policy appropriately.

Incremental credit authorisation levels are defined based on size of units, types of customers and lending experience of credit officers. Credit decisions exceeding authorisation levels of business units are subject to confirmation by Credit Management within the Risk Management. Credit decisions exceeding the limits of Credit Management are subject to approval by the Bank's Credit Committee. Credit decisions exceeding the limits of the Credit Committee are subject to approval by the Board of Directors which has the highest credit authorisation within the Bank.

54. Credit risk mitigation

Mitigating risks in the credit portfolio is a key element of the Group's credit policy as well as being an inherent part of the credit decision process. Securing loans with collateral is the main method of mitigating credit risk whereas for many loan products, collateral is required by legislation, as in the mortgage finance market, or is standard market practice.

The most important types of collaterals are real property and financial assets (shares or bonds).

54. Credit risk mitigation (continued)

The amount and type of collateral required depends on an assessment of the credit risk associated with the counterparty. Valuation parameters and the acceptability of different types of collateral are defined in the Groups's lending rules. Credit extended by the Group may be secured on residential or commercial properties, land, securities, transport vessels, fishing vessels together with their non-transferable fishing quotas, aircraft, etc. The Group also secures its loans by means of receivables and operating assets, such as machinery and equipment. Residential mortgages involve the underlying residential property. Less stringent requirements are set for securing short term personal loans, such as overdrafts and credit card borrowings.

The Group regularly assesses the market value of collateral received. The Group has developed models to estimate the value of the most frequent types of collateral. For collateral for which no valuation model exists, the Group estimates the value manually. It calculates the value as the market value less a haircut. The haircut represents a conservative estimate of the costs to sell in a forced sale. Costs to sell include maintenance costs in the period over which the asset is up for sale, fees for external advisory services and any loss in value. For listed securities, haircuts are calculated with an internal model based on variables, such as price volatility and marketability.

The Group monitors the market value of mark to market collaterals and may require additional collateral in accordance with underlying loan agreements.

The Group is finalising the implementation of a new collateral system, which is developed internally and allows the Group to analyse the quality and value of the collateral held to secure the loan portfolio.

In order to limit further the credit risk arising from financial instruments, the Group enters into netting agreements, under which in cases of default the Group is able to set off all contracts covered by the netting agreement against the debt. The arrangements generally include all market transactions between the Group and the client.

Generally, collateral is not held over loans and advances to financial institutions, nor is it usually held against bonds and debt instruments.

Derivative financial instruments

In order to mitigate credit risk arising from derivatives the Group chooses the counterparties for derivatives trading based on stringent rules, according to which clients must qualify as professional clients but only if certain conditions are met. The Group also enters into standard International Swaps and Derivatives Association (ISDA) master agreeements with financial institutions and similar general agreements with other derivatives counterparties of the Bank. Such agreements include, among other things, netting and set-off arrangements.

The Bank makes appropriate collateral and margin requirments for all derivative contracts the Group enters into. Collateral management and monitoring is performed daily and derivative contracts with clients are usually fully hedged.

The Group's supervision system monitors derivatives exposures and collateral value intraday, it issues margin calls and manages netting and set-off agreements.

55. Loan impairment

Group policy requires that individual financial assets above materiality thresholds be reviewed at least quarterly, and more frequently when circumstances require. Impairment allowances on individually assessed accounts are determined case-by-case by evaluating incurred losses at the reporting date. Collectively assessed impairment allowances are permitted in the following cases: (i) portfolios of homogenous loans that are individually below materiality thresholds, and (ii) losses that have been incurred but not yet identified, using the available historical experience together with experienced judgement and statistical techniques.

Should the expected cash flows be re-examined and the present value of the cash flows (calculated using the effective interest rate) be revised, the difference is then recognised in profit or loss (as either impairment or net adjustments to loans and advances). Impairment is calculated using the effective interest rate, before any revision of the expected cash flows. Any adjustments to the carrying amount which result from revising the expected cash flows are recognised in profit or loss. The impact of financial restructuring of the Group's customers is reflected in loan impairment, or net adjustments to loans and advances, as the expected cash flow of customers has changed.

The Group has significantly reduced granting loans in foreign currency unless the customer's income is in the same currency or a comparable currency.

56. Maximum exposure to credit risk and concentration by industry sectors

The following tables shows the Group's maximum credit risk exposure at 31 December 2012 and 2011. For on-balance sheet assets, the exposures set out below are based on net carrying amounts as reported in the statement of financial position. Off-balance sheet amounts in the tables below are the maximum amounts the Group might have to pay for guarantees, loan commitments in their full amount, and undrawn overdraft and credit card facilities.

The Group uses the ISAT 08 industry classification for corporate customers.

				Corporations									
At 31 December 2012	**Financial institutions**	**Public entities***	**Individuals**	**Fisheries**	**Construction and real estate companies**	**Services**	**Retail**	**Holding companies**	**Manufacturing**	**Agriculture**	**ITC****	**Other**	**Carrying amount**
Cash and balances with Central Bank	-	25,898	-	-	-	-	-	-	-	-	-	-	**25,898**
Bonds and debt instruments	9,528	216,935	-	-	3	-	-	397	352	-	-	993	**228,208**
Derivative instruments	1,039	-	-	-	-	-	-	-	-	-	-	4	**1,043**
Loans and advances to financial institutions	64,349	-	-	-	-	-	-	-	-	-	-	-	**64,349**
Loans and advances to customers	-	11,576	195,047	142,952	104,928	52,700	42,019	60,009	25,665	10,199	19,413	1,579	**666,087**
Other financial assets	8,106	276	600	11	300	587	-	-	253	-	2	346	**10,481**
Total on-balance sheet exposure	**83,022**	**254,685**	**195,647**	**142,963**	**105,231**	**53,287**	**42,019**	**60,406**	**26,270**	**10,199**	**19,415**	**2,922**	**996,066**
Off-balance sheet exposure	**4,054**	**14,215**	**28,146**	**14,374**	**30,797**	**11,465**	**8,612**	**1,147**	**2,361**	**1,049**	**2,496**	**46**	**118,762**
Financial guarantees and underwriting commitments	-	95	463	1,731	23,149	2,123	1,685	208	584	39	552	35	30,664
Undrawn loan commitments	1,500	9,022	22	10,592	5,628	2,122	1,948	278	194	701	901	-	32,908
Undrawn overdraft/credit card facilities	2,554	5,098	27,661	2,051	2,020	7,220	4,979	661	1,583	309	1,043	11	55,190
Maximum exposure to credit risk	**87,076**	**268,900**	**223,793**	**157,337**	**136,028**	**64,752**	**50,631**	**61,553**	**28,631**	**11,248**	**21,911**	**2,968**	**1,114,828**
Percentage of carrying amount	7.8%	24.1%	20.1%	14.1%	12.2%	5.8%	4.5%	5.5%	2.6%	1.0%	2.0%	0.3%	100%

* Public entities consist of central government, state-owned enterprises, Central Bank and municipalities.

** ITC consists of corporations in the information, technology and communication industry sectors.

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56. Maximum exposure to credit risk and concentration by industry sectors (continued)

At 31 December 2011	Financial institutions	Public entities*	Individuals	Corporations: Fisheries	Corporations: Construction and real estate companies	Corporations: Services	Corporations: Retail	Corporations: Holding companies	Corporations: Manufacturing	Corporations: Agriculture	Corporations: ITC**	Other	Carrying amount
Cash and balances with Central Bank	-	8,823	-	-	-	-	-	-	-	-	-	-	**8,823**
Bonds and debt instruments	10,118	208,802	-	-	2	-	-	2,249	306	-	-	371	**221,848**
Derivative instruments	100	-	-	43	-	-	-	-	-	-	-	16	**159**
Loans and advances to financial institutions	100,133	-	-	-	-	-	-	-	-	-	-	-	**100,133**
Loans and advances to customers	-	12,139	173,222	135,397	101,958	66,120	42,401	48,622	28,008	8,506	20,168	2,589	**639,130**
Other financial assets	3,089	42	-	11	-	562	-	600	2	-	4	11	**4,321**
Total on-balance sheet exposure	**113,440**	**229,806**	**173,222**	**135,451**	**101,960**	**66,682**	**42,401**	**51,471**	**28,316**	**8,506**	**20,172**	**2,987**	**974,414**
Off-balance sheet exposure	**0**	**7,583**	**31,658**	**11,272**	**8,192**	**8,586**	**11,348**	**6,466**	**2,876**	**2,150**	**2,626**	**1,156**	**93,913**
Financial guarantees	-	28	512	1,232	3,949	2,529	1,723	275	690	170	1,195	32	12,335
Undrawn loan commitments	-	4,130	22	7,875	2,380	254	4,851	5,507	369	1,655	371	327	27,741
Undrawn overdraft/credit card facilities	-	3,425	31,124	2,165	1,863	5,803	4,774	684	1,817	325	1,060	797	53,837
Maximum exposure to credit risk	**113,440**	**237,389**	**204,880**	**146,723**	**110,152**	**75,268**	**53,749**	**57,937**	**31,192**	**10,656**	**22,798**	**4,143**	**1,068,327**
Percentage of carrying amount	10.6%	22.2%	19.2%	13.7%	10.3%	7.1%	5.0%	5.5%	2.9%	1.0%	2.1%	0.4%	100.0%

* Public entities consist of central government, state-owned enterprises, Central Bank and municipalities.

** ITC consists of corporations in the information, technology and communication industry sectors.

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57. Collaterals and Loan-to-value by Industry sectors

The loan-to-value (LTV) ratio expresses the maximum exposure of credit risk (carrying amount of loans and off-balance sheet items) as a percentage of the total appraised value of collateral. Loan to value is one of the key risk factors that is assessed when qualifying borrowers for a loan. The risk of default is always at the forefront of lending decisions, and the likelihood of a lender absorbing a loss in the foreclosure process increases as the collateral value decreases. A high LTV indicates that there is less cushion to protect against pricefalls or increases in the loan if repayments are not made and interest is added to the outstanding balance.

	LTV Ratio - Fully collateralised					LTV Ratio - Partially collateralised				
At 31 December 2012	**0% - 25%**	**25% - 50%**	**50% - 75%**	**75% - 100%**	**Total**	**>100%**	**Collateral value**	**Without Collaterals***	**Allowance for impairment**	**Maximum exposure to credit**
Financial institutions	-	-	-	-	-	-	-	68,404	-	68,404
Public entities	25	43	172	104	344	6,002	1,142	19,552	107	25,791
Individuals	6,621	11,206	14,577	18,473	50,877	100,197	64,967	84,679	12,560	223,193
Corporations										
Fisheries	1,091	4,765	24,202	20,277	50,335	90,952	58,291	22,564	6,525	157,326
Construction and real estate companies	320	1,833	3,167	9,321	14,641	121,949	49,980	6,765	7,630	135,725
Holding companies	402	163	1,043	1,950	3,558	49,780	32,115	14,044	6,226	61,156
Retail	159	641	1,281	1,065	3,146	42,039	17,042	10,977	5,530	50,632
Services	803	811	10,719	1,581	13,914	34,793	14,160	18,673	3,217	64,163
Information, technology and communication	25	35	65	29	154	20,727	6,396	1,383	357	21,907
Manufacturing	72	278	729	1,010	2,089	19,283	10,786	7,792	1,138	28,026
Agriculture	176	119	262	64	621	10,205	3,910	970	547	11,249
Other	3	-	77	-	80	41	26	1,696	193	1,624
Total	**9,697**	**19,895**	**56,294**	**53,874**	**139,759**	**495,968**	**258,815**	**257,499**	**44,030**	**849,196**
At 31 December 2011										
Financial institutions	-	-	-	-	-	-	-	100,133	-	100,133
Public entities	29	43	105	214	391	2,135	1,041	17,270	74	19,722
Individuals	9,466	13,732	25,297	21,487	69,982	46,169	26,231	96,463	7,732	204,882
Corporations										
Fisheries	919	10,067	34,247	16,160	61,393	73,407	26,500	16,843	4,975	146,668
Construction and real estate companies	920	1,008	3,421	9,302	14,651	93,926	49,199	7,526	5,955	110,148
Holding companies	38	167	278	129	612	51,469	13,682	6,550	3,544	55,087
Retail	1,270	889	1,760	1,908	5,827	46,687	13,270	3,512	2,277	53,749
Services	571	1,476	1,856	1,174	5,077	32,967	12,202	38,809	2,146	74,707
Information, technology and communication	120	70	16	29	235	19,646	3,961	3,071	158	22,794
Manufacturing	60	751	592	2,209	3,612	12,572	4,554	15,092	426	30,850
Agriculture	100	302	205	227	834	8,942	2,322	1,835	957	10,654
Other	1	-	-	70	71	27	18	3,823	177	3,744
Total	**13,494**	**28,505**	**67,777**	**52,909**	**162,685**	**387,947**	**152,980**	**310,927**	**28,421**	**833,138**

*Credit card loans and overdraft on debit cards are assumed to be without collateral. If LTV is less than 100% the loan is considered fully secured. If LTV is greater than 100% the loan is partially collateralised and the respective collateral value is shown in the table.

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58. Loans and advances by geographical area

At 31 December 2012	Domestic	Foreign	Carrying amount
Loans and advances to financial institutions	8,358	55,991	64,349
Loans and advances to customers	622,800	43,288	666,087
Total loans and advances to customers	**631,158**	**99,279**	**730,436**

At 31 December 2011	Domestic	Foreign	Carrying amount
Loans and advances to financial institutions	6,242	93,891	100,133
Loans and advances to customers	589,666	49,465	639,130
Total loans and advances to customers	**595,908**	**143,356**	**739,263**

59. Collateral types

The following tables shows the collaterals used to mitigate credit risk.

At 31 December 2012	Real Estate	Vessels	Deposits	Securities	Other*	Total
Public entities	1,575	-	32	-	38	1,645
Individuals	152,374	23	2,339	2,438	88	157,262
Corporates						-
Fisheries	5,395	112,632	136	2,564	5,455	126,182
Construction and real estate companies	77,958	-	1,162	340	1,559	81,019
Holding companies	4,751	-	210	27,304	3,627	35,892
Retail	11,515	-	219	627	10,514	22,875
Services	30,372	430	866	2,678	1,982	36,328
ITC	756	8	125	1,843	4,357	7,089
Manufacturing	7,179	-	385	5,408	1,370	14,342
Agriculture	3,203	-	4	-	2,671	5,878
Other	261	-	1	-	-	262
Total	**295,339**	**113,093**	**5,479**	**43,202**	**31,661**	**488,774**

At 31 December 2011	Real Estate	Vessels	Deposits	Securities	Other*	Total
Public entities	1,627	-	271	-	38	1,936
Individuals	141,471	-	2,503	1,001	60	145,035
Corporates						-
Fisheries	5,877	98,933	1,386	3,514	5,179	114,889
Construction and real estate companies	92,070	91	1,780	231	1,432	95,604
Holding companies	7,028	-	3,469	15,263	2,312	28,072
Retail	12,440	-	1,536	56	7,689	21,721
Services	22,995	63	1,134	810	1,311	26,313
ITC	715	-	144	1	2,368	3,228
Manufacturing	7,263	-	282	608	944	9,097
Agriculture	4,015	-	23	-	27	4,065
Other	731	-	31	239	1,232	2,233
Total	**296,232**	**99,087**	**12,559**	**21,723**	**22,592**	**452,194**

*Other includes collaterals like financial claims, invoices, liquid assets, vehicles, machines, aircrafts and inventories.

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60. Loans and advances credit monitoring

The following tables shows the credit risk monitoring split on colour classification. Futher details on the credit risk monitoring and color classification can be seen in note 52, Credit risk control and monitoring.

Industry sectors as at 31 December 2012	Green	Yellow	Orange	Red	Carrying amount 31.12.2012
Financial institutions	64,349	-	-	-	64,349
Public entities	10,849	571	152	4	11,576
Individuals	149,615	9,641	19,010	16,781	195,047
Corporations					
Fisheries	102,319	29,130	3,006	8,497	142,952
Construction and real estate companies	55,038	16,190	18,318	15,382	104,928
Holding companies	32,668	10,867	8,028	8,446	60,009
Retail	18,643	16,075	2,470	4,831	42,019
Services	34,944	5,389	6,096	6,271	52,700
Information, technology and communication	18,853	192	202	166	19,413
Manufacturing	18,037	3,044	1,505	3,079	25,665
Agriculture	8,624	952	187	436	10,199
Other	346	657	471	105	1,579
Total	**514,285**	**92,708**	**59,445**	**63,998**	**730,436**

Industry sectors as at 31 December 2011	Green	Yellow	Orange	Red	Carrying amount 31.12.2011
Financial institutions	99,972	-	17	144	100,133
Public entities	8,342	539	1,057	2,201	12,139
Individuals	91,241	22,747	28,612	30,622	173,222
Corporations					
Fisheries	78,560	20,644	10,405	25,788	135,397
Construction and real estate companies	40,096	10,504	8,609	42,749	101,958
Holding companies	12,416	10,525	1,933	23,748	48,622
Retail	17,013	6,692	475	18,221	42,401
Services	40,196	1,833	10,238	13,853	66,120
Information, technology and communication	19,996	68	45	59	20,168
Manufacturing	18,606	2,328	478	6,596	28,008
Agriculture	7,752	271	34	449	8,506
Other	1,118	1,243	31	197	2,589
Total	**435,308**	**77,394**	**61,934**	**164,627**	**739,263**

61. Credit quality of financial assets

	Gross carrying amount					
At 31 December 2012	Neither past due nor individually impaired	Past due but not individually impaired	Individually impaired	Total	Allowance for impairment	Carrying amount
Cash and balances with Central Bank	25,898	-	-	25,898	-	25,898
Bonds and debt instruments	219,009	9,199	-	228,208	-	228,208
Derivative instruments	1,043	-	-	1,043	-	1,043
Loans and advances to financial institutions	64,349	-	-	64,349	-	64,349
Loans and advances to customers	450,885	60,078	199,154	710,117	(44,030)	666,087
Other financial assets	10,481	-	-	10,481	-	10,481
Total	**771,665**	**69,277**	**199,154**	**1,040,096**	**(44,030)**	**996,066**
At 31 December 2011						
Cash and balances with Central Bank	8,823	-	-	8,823	-	8,823
Bonds and debt instruments	212,930	8,918	-	221,848	-	221,848
Derivative instruments	159	-	-	159	-	159
Loans and advances to financial institutions	99,972	161	-	100,133	-	100,133
Loans and advances to customers	439,699	117,264	110,587	667,550	(28,420)	639,130
Other financial assets	4,321	-	-	4,321	-	4,321
Total	**765,904**	**126,343**	**110,587**	**1,002,834**	**(28,420)**	**974,414**

The allowance for impairment includes both the allowance for individual impairment and the allowance for collective impairment.

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62. Loans and advances neither past due nor individually impaired

The following tables shows the credit quality, measured by rating grade, of Loans and advances neither past due nor individually impaired. Further details on rating grades can be seen in note 51, Credit risk assessment.

	Rating grades					
At 31 December 2012	10-7	6-4	3-1	0*	Unrated	Total
Financial institutions	64,349	-	-	-	-	64,349
Public entities	2,357	73	4,866	10	88	7,394
Individuals	11,266	21,276	97,272	3,968	5,987	139,769
Corporations						
Fisheries	391	31,227	47,886	3,442	19	82,965
Construction and real estate companies	-	41,960	20,039	7,129	248	69,376
Retail	-	23,468	13,203	1,174	477	38,322
Holding companies	-	26,667	2,775	223	248	29,913
Services	10,884	18,201	11,454	1,131	488	42,158
ITC	-	239	13,724	30	26	14,019
Agriculture	54	4,872	16,337	230	154	21,647
Manufacturing	2	914	3,138	72	30	4,156
Other	-	534	3	-	630	1,167
Total	**89,303**	**169,431**	**230,697**	**17,409**	**8,395**	**515,235**

	Rating grades					
At 31 December 2011	10-7	6-4	3-1	0*	Unrated	Total
Financial institutions	100,133	-	-	-	-	100,133
Public entities	2,761	86	5,699	12	103	8,661
Individuals	7,347	13,874	63,433	2,587	3,904	91,145
Corporations						
Fisheries	486	38,787	59,480	4,276	23	103,052
Construction and real estate companies	-	40,895	19,530	6,948	241	67,614
Retail	-	25,187	14,171	1,260	512	41,130
Holding companies	-	20,566	2,140	172	191	23,069
Services	13,370	22,360	14,070	1,389	599	51,788
ITC	-	304	17,408	38	33	17,783
Agriculture	64	5,716	19,169	270	181	25,400
Manufacturing	3	1,420	4,874	109	46	6,452
Other	-	489	3	-	576	1,068
Total	**124,164**	**169,684**	**219,977**	**17,061**	**6,409**	**537,295**

*Due to the accounting policies, loans and advances acquired at deep discount are not impaired even though the Group considers the obligor likely not to meet its obligations. Hence such loans can be defaulted but neither past due nor individually impaired.

63. Loans and advances past due but not individually impaired

The following table shows the gross carrying amount of loans and advances to financial institutions and customers that have failed to make payments which had become contractually due by one or more days.

At 31 December 2012	Past due 0 - 5 days	Past due 6-30 days	Past due 31 - 60 days	Past due 61 - 90 days	Past due over 90 days	Gross carrying amount
Public entities	-	2	1	-	19	22
Individuals	115	7,545	3,156	1,487	11,450	23,753
Corporates	1,052	4,570	2,134	1,262	27,285	36,303
Total	**1,167**	**12,117**	**5,291**	**2,749**	**38,754**	**60,078**

At 31 December 2011						
Financial institutions	-	1	7	8	144	161
Public entities	-	18	2	102	65	188
Individuals	3,205	7,810	4,523	2,725	24,655	42,918
Corporates	3,009	8,971	7,301	4,813	50,064	74,158
Total	**6,214**	**16,800**	**11,833**	**7,648**	**74,928**	**117,425**

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64. Loans and advances by industry sectors

At 31 December 2012	Gross carrying amount	Not individually impaired	Individually impaired: Of which performing	Individually impaired: Individual allowance	Individually impaired: Of which non-performing*	Individually impaired: Individual allowance	Collective allowance	Carrying amont
Financial institutions	64,349	64,349	-	-	-	-	-	64,349
Public entities	11,682	7,750	3,717	51	108	11	44	11,576
Individuals	207,608	165,035	22,436	3,549	7,577	6,379	2,632	195,047
Corporates								
Fisheries	149,477	86,823	54,380	2,448	1,749	1,496	2,582	142,952
Construction and real estate companies	112,558	78,437	22,988	1,926	3,503	1,869	3,835	104,928
Holding companies	66,235	37,378	22,050	564	582	2,575	3,087	60,009
Retail	47,549	32,217	8,763	2,376	1,039	1,634	1,520	42,019
Services	55,917	44,958	6,713	1,323	1,028	908	986	52,700
ITC	19,770	14,076	5,287	186	50	46	126	19,413
Manufacturing	26,802	22,461	2,889	458	315	334	346	25,665
Agriculture	10,747	4,850	5,093	127	256	173	248	10,199
Other	1,772	1,471	-	-	110	90	101	1,579
Total	**774,466**	**559,805**	**154,316**	**13,008**	**16,317**	**15,515**	**15,507**	**730,436**

At 31 December 2011	Gross carrying amount	Not individually impaired	Individually impaired: Of which performing	Individually impaired: Individual allowance	Individually impaired: Of which non-performing*	Individually impaired: Individual allowance	Collective allowance	Carrying amont
Financial institutions	100,133	100,133	-	-	-	-	-	100,133
Public entities	12,143	8,607	3,457	24	-	0	50	12,139
Individuals	186,033	135,840	21,612	3,354	8,039	4,025	353	173,222
Corporates								
Fisheries	137,878	115,326	12,729	1,876	2,367	821	2,278	135,397
Construction and real estate companies	107,013	74,563	19,358	1,090	2,082	1,888	2,977	101,958
Holding companies	51,112	40,406	4,317	1,160	355	1,598	786	48,622
Retail	44,443	34,270	3,882	295	1,972	1,032	950	42,401
Services	68,301	58,225	4,450	305	1,300	1,097	744	66,120
ITC	20,261	18,161	1,770	3	79	61	94	20,168
Manufacturing	28,709	26,172	1,201	137	210	253	36	28,008
Agriculture	8,834	6,031	1,470	477	48	41	439	8,506
Other	2,823	2,216	-	-	195	159	17	2,589
Total	**767,683**	**619,950**	**74,246**	**8,721**	**16,647**	**10,975**	**8,724**	**739,263**

*Non-performing past due more than 90 days

All amounts are in ISK million

65. Allowance for impairment on loans and advances to financial institutions and customers and other financial assets

	1.1-31.12.2012			1.1-31.12.2011		
	Customers	Other financial assets	Total	Customers	Financial institutions	Total
Balance at the beginning of the year	28,420	-	28,420	21,122	2,178	23,300
Impairment loss for the period	15,960	-	15,960	9,212	(2,178)	7,034
Collected previously written-off loans	811	-	811	98	-	98
Loans written-off	(1,161)	-	(1,161)	(2,012)	-	(2,012)
Balance at the end of the period	**44,030**	**0**	**44,030**	**28,420**	**0**	**28,420**
Individual allowance	28,523	-	28,523	19,696	-	19,696
Collective allowance	15,507	-	15,507	8,724	-	8,724
Total	**44,030**	**0**	**44,030**	**28,420**	**0**	**28,420**
Net impairment loss						
Impairment loss for the period	15,960	-	15,960	9,310	(2,178)	7,132
Impairment of claims reversed	-	(3,700)	(3,700)	(98)	-	(98)
Net impairment loss for the period	**15,960**	**(3,700)**	**12,260**	**9,212**	**(2,178)**	**7,034**

66. Renegotiated loans

Financial restructuring and renegotiation of loans to the Group's customers acquired from LBI hf. started in 2009. In regard to financial restructuring of customers, the Group has put remedies in place for those experiencing financial difficulties and also presented procedures for financial restructuring. These restructuring approaches include extended and modified repayment arrangements and approved external management plans. During the year 2012 the Bank continued its focus and effort in restructuring loans to individuals and companies.

67. Large exposures

At 31 December 2012, two Group clients were rated as large exposures (31 December 2011: two clients), including subsidiaries of the Group classified as held for sale. Clients are rated as large exposures if their total obligations, or those of financially or administratively connected parties, exceed 10% of the Group's capital base. The large exposures amount is calculated after taking account of collateral held, in accordance with the Financial Supervisory Authority's Rules on Large Exposures Incurred by Financial Undertakings No. 216/2007. According to these rules, no exposure may attain the equivalent of 25% of the capital base. All of the Group's large exposures were within these limits as at 31 December 2012 and 2011.

At 31 December 2012, no exposure exceeded 20% (31 December 2011: one exposure). According to the Group's risk appetite, the total utilisation percentage of a large exposure ought to remain below 50% of the Group's capital base.

At 31 December 2012	Number of large exposures	Large exposures
Large exposures above 20% of the Group's capital base	-	-
Large exposures between 10% and 20% of the Group's capital base	2	71,610
Total	**2**	**71,610**
Utilisation ratio (400% max limit)		32%
At 31 December 2011		
Large exposures above 20% of the Group's capital base	1	47,989
Large exposures between 10% and 20% of the Group's capital base	1	33,131
Total	**2**	**81,120**
Utilisation ratio (400% max limit)		42%

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68. Bonds and debt instruments

A breakdown of the Group's bond portfolio, by Moody's rating, is as follows:

Carrying amount	2012	2011
Aaa	55,699	61,752
Aa3	-	38
Baa1 to Baa3	160,087	144,791
Lower than Baa3	-	959
Unrated	12,422	14,308
Total	**228,208**	**221,848**

Unrated bonds and bonds with ratings lower than Baa3 are primarily bonds issued by domestic corporations, some of which developed into liquidating estates.

The following table shows the carrying amounts of bonds for which the issuers have failed, by one or more days, to make a payment when it was contractually due:

At 31 December 2012	Past due 0 - 90 days	Past due over 90 days	Carrying amount
Financial institutions	-	8,995	8,995
Holding companies	-	147	147
Public entities	-	54	54
Real estate companies	-	3	3
Total	**0**	**9,199**	**9,199**
At 31 December 2011			
Financial institutions	-	8,434	8,434
Holding companies	-	484	484
Total	**0**	**8,918**	**8,918**

69. Derivative instruments

The following table summarises the Group's exposure in derivative instruments, classified by the Bank into equivalent Moody's ratings by counterparty:

	2012			2011		
	Notional	Fair value		Notional	Fair value	
	amount	Assets	Liabilities	amount	Assets	Liabilities
Aa3	774	3	-	635	-	2
A1 to A3	32,202	504	54	64,832	100	1,254
Baa1 to Baa3	19,076	533	406	1,715	-	450
Unrated	11,986	3	59	10,664	59	24
Total	**64,038**	**1,043**	**519**	**77,846**	**159**	**1,729**

Liquidity risk

70. Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting its obligations associated with financial liabilities that are settled by delivering cash or another financial asset, or of having to do so at excessive cost. This risk arises from earlier maturities of financial liabilities and financial assets.

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71. Liquidity risk management

A liquidity management policy for the Bank and its subsidiaries is in place and is formulated by The Risk and Finance Committee. The objective of the liquidity management policy is to ensure, even in times of stress, that sufficient liquid assets and funding capacity are available to meet financial obligations in a timely manner and at reasonable cost. Enforcing this policy has the further objective of minimising fluctuations in liquidity. The policy is built on a framework published in Basel III standards on liquidity risk measurement. The Group has performed monthly reports on new liquidity measurements set forward in the framework in 2012 and will continue implementation on those measurements in the year 2013.

The Group follows liquidity rules set by the Central Bank of Iceland to govern the ratio of weighted liquid assets and liabilities as well as following guidelines No. 1/2008 from the Icelandic Financial Supervisory Authority in Iceland (FME) on best practice for managing liquidity in banking organisation. The rules set by the Central Bank require the ratio of weighted assets to weighted liabilities to stay above 1 for the next three months, and involve a stress test, weighting assets and liabilities with specific coefficients and reflecting how accessible each asset would be in a liquidity crisis and how great the need would be to repay the liability in question when due. The guidelines set by the Icelandic Financial Supervisory Authority require the ratio of core liquid assets to deposits to stay above 20% and the ratio of cash and cash equivalents to on-demand deposits to stay above 5%. The Bank submits monthly reports on its liquidity position to the Central Bank of Iceland and the Icelandic Financial Supervisory Authority. The Group has implemented a risk appetite where these rules and guidelines as well as inner requirements within the Bank set benchmark for liquidity management.

The Group's liquidity risk is managed centrally by Treasury and is monitored by Market Risk. This allows management to monitor and manage liquidity risk throughout the Group. The Risk and Finance Committee monitors the Group's liquidity risk, while the Group's internal audit assesses whether the liquidity management process is designed properly and operating effectively.

The Group monitors intraday liquidity risk, short-term liquidity risk, and risk arising from mismatches of longer term assets and liabilities. Short-term liquidity risk is defined as under 12 months. The Group has neither defaulted on any principal or interest nor breached any covenants in respect of liabilities.

The Group's liquidity management process includes; projecting expected cash flows in a maturity profile rather than relying merely on contractual maturities, monitoring balance sheet liquidity, monitoring and managing the maturity profile of liabilities and off-balance sheet commitments, monitoring the concentration of liquidity risk in order to avoid undue reliance on large financing counterparties projecting cash flows arising from future business, and maintaining liquidity and contingency plans which outline measures to take in the event of difficulties arising from liquidity crisis.

Market Risk Unit conducts weekly stress tests by applying various hypothetical scenarios on the Group's liquidity position to ensure that it has adequate liquidity to withstand stressed conditions. Different assumptions are drawn for each stress test to estimate the impact of a variety of market conditions, in particular the lifting of capital controls in Iceland and how that would impact the Group's deposit base.

The key measure used by the Group for monitoring liquidity risk is the ratio of core liquid assets to deposits, which shows the ratio of deposits that the Group could deliver on demand without incurring any significant losses due to forced asset sales or other costly actions. Core liquid assets are comprised of cash at hand, balances with Central Bank, loans to financial institutions (maturity within seven days) and assets eligible for repo transactions with Central Bank (such as government bonds). Another method the Group uses is the cash ratio which shows the ratio of on-demand deposits that the Group could deliver with cash and cash equivalents such as cash at hand, balances with Central Bank and loans to financial institutions (maturity within seven days). The core liquidity ratio as at 31 December 2012 was 48% (31 December 2011: 43%) and the ratio of cash and cash equivalents to on-demand deposits was 12% (31 December 2011: 20%). The following table shows various values of the core liquidity ratio and cash ratio in the year 2012 and 2011. Aggregated values for the core liquidity ratio are based on daily values and aggregated values for the cash ratio are based on monthly values:

	Core Liquidity ratio		Cash ratio	
	2012	2011	2012	2011
Year end	48%	43%	12%	20%
Maximum	51%	57%	32%	27%
Minimum	36%	42%	12%	17%
Average	45%	48%	20%	21%

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72. Deposit stickiness

Stickiness is a method that the bank uses to estimate the stability of the deposit base. The Bank for International Settlements (BIS) defines stickiness as tendency of funding not to run off quickly under stress. The Bank has categorised its deposit base into seven different groups representing different levels of stickiness. The groups are based on Basel III's LCR methodology and are reflected in the Bank's internal liquidity stress tests where a concentration charge is applied to account for possible outflows.

The defining criteria for the groups are as follows:

		31/12/2012		31/12/2011	
Groups	**Criteria**	**% of total**	**Amount**	**% of total**	**Amount**
Individuals	Individuals	42.6%	221,617	40.6%	226,132
Small and medium size corporates	Businesses that have less than 1 million EUR in deposits	9.7%	50,593	9.5%	52,999
Large corporates	Businesses that have greater than or equal to 1 million EUR in deposits	11.7%	60,934	24.5%	136,327
Financial institutions, in resolution process	Financial institutions in resolution process	9.6%	50,083	5.4%	29,995
Government, municipalities and Central Bank	Government, municipalities and Central Bank	6.0%	31,353	4.4%	24,604
Financial institutions, securities firms and incurance companies	Financial institutions, securities firms and incurance companies	19.6%	101,857	14.9%	82,881
Other foreign counterparties	Businesses with residency outside of Iceland	0.6%	3,339	0.6%	3,528
Total		**100%**	**519,776**	**100%**	**556,466**

The table above shows the deposit base split between different groups at year end 2012 and 2011 from the estimated most sticky group to the least sticky.

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73. Maturity analysis of financial assets and liabilities

The following table shows a maturity analysis of the Group's financial instruments as at 31 December 2012:

Non-derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	Total	Carrying amount
Cash and balances with Central Bank	25,898	-	-	-	-	25,898	25,898
Bonds and debt instruments	-	52,191	12,202	48,362	158,688	271,443	228,208
Loans and advances to financial institutions	-	55,035	7,726	1,591	-	64,352	64,349
Loans and advances to customers	15,169	68,164	97,531	396,142	374,154	951,160	666,087
Other financial assets	-	10,016	-	465	-	10,481	10,481
Total	**41,067**	**185,406**	**117,459**	**446,560**	**532,842**	**1,323,334**	**995,023**
Derivative financial assets							
Gross settled derivatives							1,040
Inflow	-	31,169	-	-	-	31,169	
Outflow	-	(33,694)	-	-	-	(33,694)	
Total	**0**	**(2,525)**	**0**	**0**	**0**	**(2,525)**	**1,040**
Net settled derivatives	-	3	-	-	-	3	3
Total	**0**	**(2,522)**	**0**	**0**	**0**	**(2,522)**	**1,043**
Non-derivative financial liabilities							
Due to financial institutions and Central Bank	(97,646)	(1,054)	(18)	-	-	(98,718)	(98,718)
Deposits from customers	(310,088)	(52,739)	(33,049)	(26,362)	(4,137)	(426,375)	(421,058)
Short positions	-	(8,918)	-	-	-	(8,918)	(8,918)
Secured bonds	-	(1,164)	(3,401)	(184,607)	(60,329)	(249,501)	(221,791)
Contingent bond	-	-	-	(90,261)	(23,351)	(113,612)	(87,474)
Other financial liabilities	-	(14,369)	-	-	-	(14,369)	(14,369)
Total	**(407,734)**	**(78,244)**	**(36,468)**	**(301,230)**	**(87,817)**	**(911,493)**	**(852,328)**
Off-balance sheet items							
Financial guarantees and underwriting commitments	(297)	(19,855)	(3,434)	(2,102)	(4,976)	(30,664)	
Undrawn loan commitments	(32,908)	-	-	-	-	(32,908)	
Undrawn overdraft/credit card	(55,190)	-	-	-	-	(55,190)	
Total	**(88,395)**	**(19,855)**	**(3,434)**	**(2,102)**	**(4,976)**	**(118,762)**	**0**
Total non-derivative financial liabilities and off-balance sheet items	**(496,129)**	**(98,099)**	**(39,902)**	**(303,332)**	**(92,793)**	**(1,030,255)**	**(852,228)**
Derivative financial liabilities							
Gross settled derivatives							(490)
Inflow	-	26,093	276	839	284	27,492	
Outflow	-	(22,650)	(347)	(1,074)	(371)	(24,441)	
Total	**0**	**3,443**	**(71)**	**(235)**	**(87)**	**3,051**	**(490)**
Net settled derivatives	-	(29)	-	-	-	(29)	(29)
Total	**0**	**3,414**	**(71)**	**(235)**	**(87)**	**3,022**	**(519)**
Net liquidity position	**(455,062)**	**88,199**	**77,486**	**142,993**	**439,962**	**293,579**	**143,219**

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73. Maturity analysis of financial assets and liabilities (continued)

The following table shows a maturity analysis of the Group's financial instruments as at 31 December 2011:

Non-derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	Total	Carrying amount
Cash and balances with Central Bank	8,823	-	-	-	-	8,823	8,823
Bonds and debt instruments	-	59,081	9,893	37,571	146,843	253,388	221,848
Loans and advances to financial institutions	-	93,179	5,654	1,397	7	100,237	100,133
Loans and advances to customers	62,090	75,903	124,517	302,650	403,888	969,048	639,130
Other financial assets	-	3,852	-	470	-	4,322	4,321
Total	**70,913**	**232,015**	**140,064**	**342,088**	**550,738**	**1,335,818**	**974,255**
Derivative financial assets							
Gross settled derivatives							
Inflow	-	12,624	-	-	-	12,624	
Outflow	-	(12,490)	-	-	-	(12,490)	
Total	**0**	**134**	**0**	**0**	**0**	**134**	**143**
Net settled derivatives	-	16	-	-	-	16	16
Total	**0**	**150**	**0**	**0**	**0**	**150**	**159**
Non-derivative financial liabilities							
Due to financial institutions and Central Bank	(112,788)	(87)	(8)	(16)	-	(112,899)	(112,876)
Deposits from customers	(344,952)	(43,578)	(31,714)	(24,426)	(4,641)	(449,311)	(443,590)
Short positions	-	(8,538)	-	-	-	(8,538)	(6,187)
Secured bonds	-	(1,934)	(5,838)	(197,905)	(115,753)	(321,430)	(277,076)
Contingent bond	-	-	-	(38,901)	(37,309)	(76,210)	(60,826)
Other financial liabilities	-	(6,623)	-	-	-	(6,623)	(6,623)
Total	**(457,740)**	**(60,760)**	**(37,560)**	**(261,248)**	**(157,703)**	**(975,011)**	**(907,178)**
Off-balance sheet items							
Financial guarantees	(6,500)	(19,879)	(2,984)	(1,472)	-	(12,335)	
Undrawn loan commitments	(27,741)	-	-	-	-	(27,741)	
Undrawn overdraft/credit card commitments	(53,837)	-	-	-	-	(53,837)	
Total	**(88,078)**	**(19,879)**	**(2,984)**	**(1,472)**	**0**	**(93,913)**	**0**
Total non-derivative financial liabilities and off-balance sheet items	**(545,818)**	**(80,639)**	**(40,544)**	**(262,720)**	**(157,703)**	**(1,068,924)**	**(907,178)**
Derivative financial liabilities							
Gross settled derivatives							
Inflow	-	57,725	291	1,160	282	59,458	
Outflow	-	(58,988)	(398)	(1,557)	(375)	(61,318)	
Total	**0**	**(1,263)**	**(107)**	**(397)**	**(93)**	**(1,860)**	**(1,712)**
Net settled derivatives	-	(17)	-	-	-	(17)	(17)
Total	**0**	**(1,280)**	**(107)**	**(397)**	**(93)**	**(1,877)**	**(1,729)**
Net liquidity position	**(474,905)**	**150,246**	**99,413**	**78,971**	**392,942**	**265,167**	**65,507**

The tables above only take into account the contractual maturity of the Groups assets and liabilities but does not account for measures that the Group could decide upon to convert assets into cash at hand by liquidation either through sale or participation in Central Bank operations. Furthermore all instant access deposits are categorised as outflows in the first time bucket. The Groups liquidity position can withstand 50% outflow of deposits (see note 71). Further information on the Group's liquidity management can also be found in the forementioned note.

The amounts in the maturity analyses as at year end 2012 and 2011 are allocated to maturity buckets in respect of remaining contractual maturity (i.e. based on the timing of future cash flows according to contractual terms). For loans and advances in moratorium or in the process of liquidation the Group estimates the amounts from the historical recovery rate. For bonds issued by companies in moratorium or in the process of liquidation the amounts presented are future cash flows estimated as their fair value at the reporting date. These bonds and loans all fall in time band of 1-5 years.

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73. Maturity analysis of financial assets and liabilities (continued)

Amounts presented in the maturity analyses are the undiscounted future cash flows receivable and payable by the Group, including both principal and interest cash flows. These amounts differ from the carrying amounts presented in the statement of financial position, which are based on discounted rather than undiscounted future cash flows. If an amount receivable or payable is not fixed, the amount presented in the maturity analyses has been determined by reference to the conditions existing at the reporting date. For example, for inflation-linked assets and liabilities, the Group estimates the inflation related future cash flows using an internally estimated inflation curve based on the Central Bank of Iceland's inflation target for the annualised inflation rate. When there is a choice of when an amount shall be paid, future cash flows are calculated on the basis of the earliest date at which the Group can be required to pay, which is the worst case scenario from Group perspective. An example of this is that demand deposits are included in the earliest time band. Where the Group is committed to have amounts available in instalments, each instalment is allocated to the earliest period in which the Group might be required to pay. Thus undrawn loan commitments are included in the time band together with the earliest date at which such loans may be drawn. For financial guarantee contracts issued by the Group, the amount included in the maturity analysis is the guarantee's maximum amount, allocated to the earliest period in which the guarantee might be called.

Nonetheless, the Group's expected cash flows on demand deposits vary significantly from the amounts presented in the maturity analyses. Demand deposits from customers have short contractual maturities but are considered a relatively stable financing source with expected maturity exceeding one year, and it is not expected that every committed loan will be drawn down immediately. See Note 72 on deposit stickiness. The Group conducts a weekly stress test to estimate the impact of fluctuating market conditions and deposit withdrawals.

Amounts presented in non-derivative financial assets and non-derivative financial liabilities include all spot deals at year end 2012 and 2011. When managing liquidity risk the Group regards spot deals as a non-derivative assets or liabilities.

74. Maturity analysis of financial assets and liabilities by currency

The following table shows a maturity analysis of the Group's financial instruments by currency of denomination as at 31 December 2012:

Non-derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	Total	Carrying amount
Total in foreign currencies	2,109	122,299	45,852	172,123	24,002	366,385	335,019
ISK	38,958	63,107	71,607	274,436	508,840	956,948	660,004
Total	**41,067**	**185,406**	**117,459**	**446,559**	**532,842**	**1,323,333**	**995,023**
Derivative financial assets							
Total in foreign currencies	-	(1,964)	-	-	-	(1,964)	1,040
ISK	-	(558)	-	-	-	(558)	3
Total	**0**	**(2,522)**	**0**	**0**	**0**	**(2,522)**	**1,043**
Non-derivative financial liabilities							
Total in foreign currencies	(62,542)	(5,127)	(6,495)	(274,868)	(83,680)	(432,712)	(378,847)
ISK	(345,192)	(73,117)	(29,973)	(26,362)	(4,137)	(478,781)	(473,480)
Total	**(407,734)**	**(78,244)**	**(36,468)**	**(301,230)**	**(87,817)**	**(911,493)**	**(852,328)**
Off-balance sheet items							
Total in foreign currencies	(13,398)	(19,144)	(2,509)	(571)	(286)	(35,909)	-
ISK	(74,997)	(711)	(924)	(1,530)	(4,689)	(82,852)	-
Total	**(88,395)**	**(19,855)**	**(3,434)**	**(2,102)**	**(4,976)**	**(118,762)**	**0**
Derivative financial liabilities							
Total in foreign currencies	-	9,228	101	302	101	9,731	(490)
ISK	-	(5,814)	(172)	(537)	(188)	(6,709)	(29)
Total	**0**	**3,414**	**(71)**	**(235)**	**(87)**	**3,022**	**(519)**
Net liquidity position in foreign currencies	**(73,831)**	**105,292**	**36,949**	**(103,014)**	**(59,863)**	**(94,469)**	**(43,278)**
Net liquidity position in ISK	**(381,231)**	**(17,093)**	**40,538**	**246,007**	**499,826**	**388,048**	**186,498**
Net liquidity position	**(455,062)**	**88,199**	**77,486**	**142,992**	**439,963**	**293,578**	**143,219**

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74. Maturity analysis of financial assets and liabilities by currency (continued)

The following table shows a maturity analysis of the Group's financial instruments by currency of denomination as at 31 December 2011:

Non-derivative financial assets	On demand	Up to 3 months	3-12 months	1-5 years	Over 5 years	Total	Carrying amount
Total in foreign currencies	16,034	173,674	49,304	119,155	24,912	383,079	359,014
ISK	54,879	58,341	90,760	222,933	525,826	952,739	615,241
Total	**70,913**	**232,015**	**140,064**	**342,088**	**550,738**	**1,335,818**	**974,255**
Derivative financial assets							
Total in foreign currencies	-	2,727	-	-	-	2,727	143
ISK	-	(2,577)	-	-	-	(2,577)	16
Total	**0**	**150**	**0**	**0**	**0**	**150**	**159**
Non-derivative financial liabilities							
Total in foreign currencies	(73,007)	(5,408)	(10,173)	(197,905)	(115,753)	(402,246)	(357,868)
ISK	(384,733)	(55,352)	(27,387)	(63,343)	(41,950)	(572,765)	(549,310)
Total	**(457,740)**	**(60,760)**	**(37,560)**	**(261,248)**	**(157,703)**	**(975,011)**	**(907,178)**
Off-balance sheet items							
Total in foreign currencies	(11,760)	(761)	(2,311)	(109)	-	(14,941)	-
ISK	(76,318)	(618)	(673)	(1,363)	-	(78,972)	-
Total	**(88,078)**	**(1,379)**	**(2,984)**	**(1,472)**	**0**	**(93,913)**	**0**
Derivative financial liabilities							
Total in foreign currencies	-	(307)	97	397	99	286	(1,712)
ISK	-	(973)	(204)	(794)	(192)	(2,163)	(17)
Total	**0**	**(1,280)**	**(107)**	**(397)**	**(93)**	**(1,877)**	**(1,729)**
Net liquidity position in foreign currencies	**(68,733)**	**169,925**	**36,917**	**(78,462)**	**(90,742)**	**(31,095)**	**(423)**
Net liquidity position in ISK	**(406,172)**	**(1,179)**	**62,496**	**157,433**	**483,684**	**296,262**	**65,930**
Net liquidity position	**(474,905)**	**168,746**	**99,413**	**78,971**	**392,942**	**265,167**	**65,507**

The amounts in the maturity analysis as at 31 December 2012 and 31 December 2011 are allocated to maturity buckets in respect of remaining contractual maturity (i.e. based on the timing of future cash flows according to contractual terms). Exceptions to this are loans and advances to customers and bonds issued by companies in moratorium or in the process of liquidation as disclosed in Note 73.

Market risk

75. Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate because of changes in market prices. Market risk arises from open positions in currency, equity and interest rate products, all of which are exposed to general and specific market movements and changing volatility levels in market rates and prices, for instance in interest rates, credit spreads, foreign exchange rates and equity prices. Other market risk such as equity price risk and inflation risk, each of which is disclosed in the following notes.

76. Market risk management

The Group separates its exposure to market risk into trading and non-trading portfolios, managing each of them separately. Trading portfolios include positions arising from market-making and proprietary position-taking (i.e. bonds classified as held for trading, equities, unsettled securities trading, derivatives and short positions) managed by Treasury. Non-trading portfolios include positions arising from the Group's retail and commercial banking operations and proprietary position-taking as part of the Asset and Liability Management (ALM) within Treasury (i.e. loans and advances, deposits and bonds designated as at fair value through profit or loss or classified as loans and receivables). ALM is also responsible for daily liquidity management and therefore hold positions in interest rate related instruments, creating exposure to market risk.

The Board of Directors is responsible for determining the Group's overall risk appetite, including for market risk. The CEO of the Bank appoints the Risk and Finance Committee, which is responsible for developing detailed market risk management policies and setting market risk limits. Treasury and the Market Making department within Markets are responsible for managing market-related positions under the supervision of Market Risk. The objective of market risk management is to identify, locate and monitor market risk exposures and analysing and reporting to appropriate parties.

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76. Market risk management (continued)

Market risks arising from trading and non-trading activities are monitored and reported on a daily, weekly and monthly basis to the head of each business unit along with detailed input to a comprehensive quarterly risk report. The Group's market risk is thereby measured and monitored on a daily basis, and Market Risk monitors the limits set in the Bank's risk appetite and submits these and other market risk measurements to the Risk and Finance Committee every other week. Several indicators are used, including daily profits and losses as well as net positions across different attributes such as the currency and issuer.

Risk-weighted assets are determined by applying specific risk weights to Group assets, following methodology developed by the Basel Committee on Banking Supervision. The following table summarises the Group's exposure to market risk at year end 2012 and 2011:

The following table summarises the Group's exposure to market risk as at 31 December 2012 and 2011:

	31.12.2012	31.12.2011
Market risk factor	% of RWA	% of RWA
Equity price risk	6.3%	7.7%
Interest rate risk	2.0%	2.6%
Foreign exchange risk	2.9%	3.1%
Total	**11.2%**	**13.4%**

The currency risk in the Group's trading portfolios is disclosed together with that in its non-trading portfolios in Notes 81-82, together with the related sensitivity analysis.

77. Interest rate risk

The interest rate risk is the risk that the fair value or future cash flow of financial instruments will fluctuate due to changes in market interest rates.

Changes in interest rates for the Group's assets and liabilities, other than those in its trading portfolios, have an impact on its interest rate margin. This risk results primarily from duration mismatch between assets and liabilities.

Interest rate risk is managed principally by monitoring interest rate gaps. Interest rate risk is managed centrally within the Group by the Treasury of the Bank, and is monitored by Market Risk. In the current economic environment, the Group has limited access to derivative instruments and other tools for managing interest rate risk.

The following tables summarise the Group's exposure to interest rate risk. The tables include interest bearing financial assets and liabilities at their carrying amounts, while off-balance sheet amounts are the notional amounts of the derivative instruments (see Note 7). The amounts presented are categorised by the earlier of either the contractual repricing or the maturity date.

At 31 December 2012	Up to 3 months	3-12 months	1-5 years	Over 5 years	Carrying amount
Financial assets					
Cash and balances with Central Bank	25,898	-	-	-	25,898
Bonds and debt instruments	214,996	6,395	1,331	5,486	228,208
Derivative instruments	1,043	-	-	-	1,043
Loans and advances to financial institutions	55,032	7,726	1,591	-	64,349
Loans and advances to customers	483,493	62,515	58,198	61,881	666,087
Other financial assets	10,017	-	464	-	10,481
Total	**790,479**	**76,636**	**61,584**	**67,367**	**996,066**
Financial liabilities					
Due to financial institutions and Central Bank	(98,718)	-	-	-	(98,718)
Deposits from customers	(418,750)	(1,861)	(447)	-	(421,058)
Derivative instruments and short positions	(521)	(5,257)	(2,717)	(943)	(9,438)
Borrowings	(221,791)	-	-	-	(221,791)
Contingent bond	(87,474)	-	-	-	(87,474)
Other financial liabilities	(14,369)	-	-	-	(14,369)
Total	**(841,623)**	**(7,118)**	**(3,164)**	**(943)**	**(852,848)**
Net on-balance sheet position	(51,144)	69,518	58,420	66,424	143,218
Net off-balance sheet position	698	(133)	(418)	(146)	
Total interest repricing gap	**(50,446)**	**69,385**	**58,002**	**66,278**	

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77. Interest rate risk (continued)

At 31 December 2011	Up to 3 months	3-12 months	1-5 years	Over 5 years	Carrying amount
Financial assets					
Cash and balances with Central Bank	8,823	-	-	-	8,823
Bonds and debt instruments	209,646	4,905	1,112	6,185	221,848
Derivative instruments	159	-	-	-	159
Loans and advances to financial institutions	93,176	5,621	1,329	7	100,133
Loans and advances to customers	507,251	63,844	24,773	43,262	639,130
Other financial assets	3,851	-	470	-	4,321
Total	**822,906**	**74,370**	**27,684**	**49,454**	**974,414**
Financial liabilities					
Due to financial institutions and Central Bank	(112,876)	-	-	-	(112,876)
Deposits from customers	(441,345)	(2,142)	(103)	-	(443,590)
Derivative instruments and short positions	(1,876)	(2,114)	(2,447)	(1,479)	(7,916)
Secured bonds	(277,076)	-	-	-	(277,076)
Contingent bond	(60,826)	-	-	-	(60,826)
Other financial liabilities	(6,623)	-	-	-	(6,623)
Total	**(900,622)**	**(4,256)**	**(2,550)**	**(1,479)**	**(908,907)**
Net on-balance sheet position	(77,716)	70,114	25,134	47,975	65,507
Net off-balance sheet position	808	(539)	(126)	(143)	
Total interest repricing gap	**(76,908)**	**69,575**	**25,008**	**47,832**	

78. Sensitivity analysis for trading portfolios

The management of market risk in the trading book is supplemented by monitoring sensitivity of the trading portfolios to various scenarios in equity prices and interest rates.

The following table shows how the Group's profit before tax would have been affected by parallel shifts in interest yield curves through changes in the fair value of its bond trading portfolios at year end 2012 and 2011 and cash flows for the next 12 months, assuming a constant position.

	2012			2011		
Currency (ISK million)	**Parallel shift in yield curve in basis points**	**Effect of downward shift on profit**	**Effect of upward shift on profit**	**Parallel shift in yield curve in basis points**	**Effect of downward shift on profit**	**Effect of upward shift on profit**
ISK, non-CPI indexed	100	99	(132)	100	196	(195)
ISK, CPI indexed	50	129	(122)	50	77	(73)
USD	20	8	(8)	20	-	-
Total		**236**	**(262)**		**273**	**(268)**

The Group's equity would have been affected to the same extent as the income statement, but net of income tax. This is because the increase (decrease) in profit before tax would have affected retained earnings.

The following table shows how the Group's profit before tax would have been affected by a change of +/-10% in the price of equity and equity instruments held by the Group at year end which are classified into Level 1 and 2 (as defined in Note 7):

	2012		2011	
Currency (ISK million)	**Increase**	**Decrease**	**Increase**	**Decrease**
ISK	186	(186)	956	(956)
EUR	-	-	6	(6)
DKK	-	-	97	(97)
SEK	-	-	302	(302)
NOK	278	(278)	378	(378)
Other	-	-	39	(39)
Total	**464**	**(464)**	**1,778**	**(1,778)**

78. Sensitivity analysis for trading portfolios (continued)

The Group's equity would have been affected to the same extent as the income statement, but net of income tax. This is because the increase (decrease) in profit before tax would have affected retained earnings.

The following table shows how the Group's profit before tax would have been affected by a change of +/-10% in the price of equity and equity instruments held by the Group at year end which are classified into Level 3 (as defined in Note 7):

	2012		2011	
Currency (ISK million)	**Increase**	**Decrease**	**Increase**	**Decrease**
ISK	1,849	(1,849)	1,983	(1,983)
EUR	1,138	(1,138)	811	(811)
GBP	-	-	1	(1)
Total	**2,987**	**(2,987)**	**2,795**	**(2,795)**

The Group's equity would have been affected to the same extent as the income statement, but net of income tax. This is because the increase (decrease) in profit before tax would have affected retained earnings.

79. Sensitivity analysis for non-trading portfolios

The management of interest rate risk against interest rate gap limits is supplemented by monitoring the sensitivity of financial assets and liabilities to various interest rate scenarios. The Group employs a quarterly stress test of the interest rate risk in the Group's overall non-trading net on-balance sheet position. In this test, the interest rate curve is shifted for every currency.

The following table shows how the Group's profit before tax would have been affected by a parallel shift in all yield curves, with all other variables held constant, as related to risk exposure at year end 2012 and 2011 and cash flows for the next 12 months, assuming a constant position.

	2012			2011		
Currency (ISK million)	**Parallel shift in yield curve in basis points**	**Effect of downward shift on profit**	**Effect of upward shift on profit**	**Parallel shift in yield curve in basis points**	**Effect of downward shift on profit**	**Effect of upward shift on profit**
ISK, unindexed	100	107	(107)	100	21	(21)
ISK, CPI indexed	50	47	(47)	50	93	(93)
EUR	20	35	(35)	20	18	(18)
Other	20	18	(18)	20	22	(22)
Total		**207**	**(207)**		**154**	**(154)**

The Group's equity would have been affected to the same extent as the income statement, but net of income tax. This is because the increase (decrease) in profit before tax would have affected retained earnings.

80. CPI indexation risk (all portfolios)

The consumer price index (CPI) indexation risk is the risk that the fair value or future cash flows of CPI-indexed financial instruments may fluctuate due to changes in the Icelandic CPI index. The Group has a considerable imbalance in its CPI-indexed assets and liabilities. To mitigate this imbalance, which the bank is in a limitied position to do, the bank offers non-CPI indexed loans and CPI-indexed deposits.

CPI indexation risk is managed centrally within the Group by the Treasury of the Bank, and is monitored by Market Risk. At 31 December 2012 the CPI imbalance, calculated as the difference between CPI-indexed financial assets and liabilities, was ISK 145,784 million (31 December 2011: 128,958 million). This increase in CPI imbalance is mainly caused by loan impairment re-evaluation.

Carrying amount	31.12.2012	31.12.2011
Assets		
Bonds and debt instruments	7,586	10,812
Loans and advances to customers	239,432	217,131
Total	**247,018**	**227,943**
Liabilities		
Due to financial institutions and Central Bank	(23)	(123)
Deposits from customers	(100,768)	(97,127)
Short positions	-	(924)
Total	**(100,791)**	**(98,174)**
Total on-balance sheet position	146,227	129,769
Total off-balance sheet position	(443)	(811)
Total CPI indexation balance	**145,784**	**128,958**

Management of the Group's CPI indexation risk is supplemented by monitoring the sensitivity of the Group's overall position in CPI-indexed financial assets and liabilities net on-balance sheet to various inflation/deflation scenarios. As an example, a 1% change in CPI index applied to the inflation risk exposures in existence at 31 December 2012, with no change in other variables, would have changed net interest income by ISK 1,462 million (31 December 2011: 1,298 million). Group equity would have been affected by the same amount as the income statement, but net of income tax. This is because the increase/decrease in net interest income would have affected retained earnings. However, in a scenario of ongoing high (low) inflation, floating unindexed interest rate are likely to remain higher (lower) than would be the case in the reverse scenario, thus counterbalancing the positive (negative) income effects for the Group in the longer term.

81. Currency risk (all portfolios)

The Group follows the Rules No. 950/2010 on Foreign Exchange Balances, as set by the Central Bank of Iceland. The rules stipulate that an institution's foreign exchange balance (whether long or short) must always be within 15% of the Bank's Capital base, in each currency and for all currencies combined. The Bank submits daily and monthly reports to the Central Bank with information on its foreign exchange balance.

The Group's combined net foreign exchange balance as at 31 December 2012 was -9,1% of the Group's Capital base (2011: +10,4%). Uncertainty regarding the denomination currencies of the Groups loan portfolio has not been fully resolved in the year 2012. As explained in note 4 and 37 there are few rulings concerning these denomination currencies that the Icelandic courts have not passed judgement on yet.

82. Concentration of currency risk

The following tables summarise the Group's exposure to currency risk at year end 2012 and 2011. The off-balance sheet amounts shown are the notional amounts of the Group's derivative instruments.

Amounts presented under assets and liabilities include all spot deals at year end 2012 and 2011. When managing liquidity risk the Group regards spot deals as a non-derivative assets or liabilities.

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82. Concentration of currency risk (continued)

As explained in Note 21 in these consolidated financial statements, a contingent bond shall be issued no later than 31 March 2013 and be denominated in EUR. Using the exchange rate as published by the Central Bank of Iceland on 31 December 2012, the Bank shall convert the final value of the ISK balance, which amounts to 87,474 million into Euros which shall be the new balance of the contingent bond.

At 31 December 2012	EUR	GBP	USD	JPY	CHF	Other	Total
Assets							
Cash and balances with Central Bank	400	173	229	13	40	377	1,232
Bonds and debt instruments	8,995	35,200	34,483	-	-	-	78,678
Equities and equity instruments	11,381	-	1	-	-	3,339	14,721
Derivative instruments	1,037	-	3	-	-	-	1,040
Loans and advances to financial institutions	32,399	1,630	9,360	3,095	2,961	4,600	54,045
Loans and advances to customers	90,044	19,250	58,169	12,406	12,777	6,642	199,288
Other assets	502	-	1,761	1	-	30	2,294
Assets classified as held for sale	288	-	-	-	-	-	288
Total	**145,046**	**56,253**	**104,006**	**15,515**	**15,778**	**14,988**	**351,586**
Liabilities							
Due to financial institutions and Central Bank	(5,438)	(4,068)	(4,870)	-	(148)	(823)	(15,348)
Deposits from customers	(15,814)	(6,007)	(21,671)	(520)	(428)	(6,456)	(50,895)
Derivative instruments and short positions	(176)	-	(314)	-	-	-	(491)
Secured bonds	(109,380)	(42,397)	(70,013)	-	-	-	(221,791)
Contingent bond	(87,474)						(87,474)
Other liabilities	(580)	(70)	(2,197)	(6)	(2)	(536)	(3,391)
Total	**(218,862)**	**(52,542)**	**(99,065)**	**(526)**	**(578)**	**(7,815)**	**(379,390)**
Net on-balance sheet position	(73,816)	3,711	4,941	14,990	15,201	7,171	**(27,802)**
Net off-balance sheet position	49,234	(2,948)	(5,532)	(13,882)	(13,768)	(5,337)	**7,767**
Net currency position	**(24,582)**	**763**	**(591)**	**1,108**	**1,433**	**1,834**	**(20,035)**

At 31 December 2011	EUR	GBP	USD	JPY	CHF	Other	Total
Assets							
Cash and balances with Central Bank	366	137	243	14	36	250	1,046
Bonds and debt instruments	25,163	168	51,947	-	-	-	77,278
Equities and equity instruments	8,167	13	390	-	-	8,085	16,655
Derivative instruments	97	-	46	-	-	-	143
Loans and advances to financial institutions	32,338	17,875	30,768	3,370	865	6,609	91,825
Loans and advances to customers	72,586	12,022	57,930	21,653	17,496	7,103	188,790
Other assets	680	77	125	1	-	18	901
Total	**139,397**	**30,292**	**141,449**	**25,038**	**18,397**	**22,065**	**376,638**
Liabilities							
Due to financial institutions and Central Bank	(1,296)	(1,780)	(1,120)	(357)	(1,414)	(5,140)	(11,107)
Deposits from customers	(18,700)	(4,005)	(37,789)	(428)	(418)	(5,415)	(66,755)
Derivative instruments and short positions	(842)	(513)	(356)	-	(1)	-	(1,712)
Secured bonds	(136,818)	(51,702)	(88,556)	-	-	-	(277,076)
Other liabilities	(1,484)	(184)	(931)	-	(14)	(353)	(2,966)
Total	**(159,140)**	**(58,184)**	**(128,752)**	**(785)**	**(1,847)**	**(10,908)**	**(359,616)**
Net on-balance sheet position	(19,743)	(27,892)	12,697	24,253	16,550	11,157	**17,022**
Net off-balance sheet position	33,880	20,144	(10,812)	(20,437)	(11,269)	(8,494)	**3,012**
Net currency position	**14,137**	**(7,748)**	**1,885**	**3,816**	**5,281**	**2,663**	**20,034**

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83. Sensitivity to currency risk

The following table shows how other net operating income would have been affected by a 10% depreciation/appreciation of ISK against each foreign currency, with all other variables held constant. The sensitivity analysis is applied to the Group's overall position in foreign currency on-balance sheet as disclosed in Note 82.

	2012		2011	
Currency (ISK million)	**-10%**	**+10%**	**-10%**	**+10%**
EUR	(2,458)	2,458	1,414	(1,414)
GBP	76	(76)	(775)	775
USD	(59)	59	189	(189)
JPY	111	(111)	382	(382)
CHF	143	(143)	528	(528)
Other	183	(183)	266	(266)
Total	**(2,004)**	**2,004**	**2,004**	**(2,004)**

The Group's equity would have been affected to the same extent as the income statement, but net of income tax. This is because the increase/decrease in other net operating income would have affected retained earnings.

84. Foreign exchange rates used

The following foreign exchange rates were used by the Group:

	At 31 December 2012	At 31 December 2011	% Change	Average for 1.1-31.12 2012	Average for 1.1-31.12 2011
EUR/ISK	168.95	158.80	6.4%	161.60	161.18
GBP/ISK	207.22	190.29	8.9%	198.77	185.68
USD/ISK	128.16	122.22	4.9%	125.07	115.55
JPY/ISK	1.49	1.59	(6.3%)	1.57	1.45
CHF/ISK	139.94	130.79	7.0%	134.15	131.04
CAD/ISK	128.73	120.24	7.1%	125.00	117.18
DKK/ISK	22.64	21.36	6.0%	21.71	21.64
NOK/ISK	22.96	20.51	11.9%	21.59	20.72
SEK/ISK	19.68	17.81	10.5%	18.58	17.93

Operational risk

85. Operational risk

Operational risk is the risk of financial losses resulting from the failure or inadequacy of internal processes or systems, from employee error or from external events. Operational risk includes legal risks, but excludes reputational risks. It is therefore inherent in all areas of business activities.

Whereas the executive managing director of each division is responsible for that division's operational risk, the daily management of operational risk is in the hands of general managers of each department. The Bank establishes, maintains and coordinates its operational risk management framework on a group level. This framework complies with the Basel Committee's 2011 publication "Principles for the Sound Management of Operational Risk". The Bank ensures that operational risk management stays consistent throughout the Bank by upholding a system of prevention and control that entails detailed procedures, permanent supervision and insurance policies, together with active monitoring by the Internal Audit Department. By managing operational risk in this manner, the Bank intends to ensure that all of the Bank's business units are kept aware of any operational risks, that a robust monitoring system remains in place and that controls are implemented efficiently and effectively.

Consolidated Key Figures

86. Operations by years

Operations	2012	2011	2010	2009	7.10. - 31.12.2008
Interest income	64,661	60,831	61,060	81,476	28,021
Interest expense	(29,077)	(28,182)	(36,374)	(66,902)	(23,730)
Net interest income	**35,584**	**32,649**	**24,685**	**14,574**	**4,291**
Net adjustments in valuation of loans and advances	(4,391)	(23,587)	641	6,954	(1,256)
Net interest income after adjustments in valuation	**31,193**	**9,062**	**25,326**	**21,528**	**3,035**
Fee and commission income	7,696	7,437	6,292	6,835	1,710
Fee and commission expense	(3,248)	(3,014)	(2,710)	(2,622)	(723)
Net fee and commission income	**4,448**	**4,424**	**3,582**	**4,213**	**987**
Other operating income	**13,500**	**17,258**	**21,941**	**4,983**	**(6,864)**
Net operating income	**49,141**	**30,743**	**50,849**	**30,725**	**(2,842)**
Salaries and related expenses	(13,176)	(11,990)	(9,331)	(8,468)	(1,506)
Administrative expenses	(9,887)	(9,482)	(8,485)	(7,706)	(5,100)
Contribution to the Depositors' and Investors' Guarantee Fund	(1,042)	(583)	(680)	(680)	(665)
Operating expenses	**(24,105)**	**(22,055)**	**(18,496)**	**(16,854)**	**(7,271)**
Share of profit of associates, net of income tax	**2,449**	**1,418**	**291**	**383**	**193**
Pre-tax profit	**27,485**	**10,105**	**32,644**	**14,253**	**(9,920)**
Income and bank tax	(4,125)	597	(8,182)	(615)	2,941
Profit from continuing operations	**23,360**	**10,703**	**24,462**	**13,638**	**(6,979)**
Profit for the period from discontinued operations, net of income tax	**2,134**	**6,255**	**2,769**	**693**	**43**
Net profit	**25,494**	**16,957**	**27,231**	**14,332**	**(6,936)**
Attributable to:					
Shareholders of Landsbankinn	25,439	16,973	27,228	14,477	(6,945)
Minority interests	55	(16)	3	(145)	9

Balance Sheet	2012	2011	2010	2009	2008
Cash and cash balances with Central Bank	25,898	8,823	47,777	26,174	30,071
Bonds and debt instruments	228,208	221,848	161,559	165,721	189,121
Equities and equity instruments	36,881	46,037	29,429	23,411	39,681
Loans and advances to financial institutions	64,349	100,133	91,882	83,129	8,845
Loans and advances to customers	666,087	639,130	592,954	667,122	705,182
Other assets	38,044	65,959	28,743	31,666	56,907
Assets classified as held for sale	25,320	53,552	128,789	63,878	7,584
Total assets	**1,084,787**	**1,135,482**	**1,081,133**	**1,061,101**	**1,037,391**
Due to financial institutions and Central Bank	98,718	112,876	147,478	98,228	132,219
Deposits from customers	421,058	443,590	371,558	452,655	431,006
Secured bonds	221,791	277,076	261,313	306,493	305,056
Contingent bond	87,474	60,826	26,510	10,241	-
Other liabilities	29,687	31,485	27,800	14,203	21,385
Liabilities associated with assets classified as held for sale	893	9,385	61,609	21,689	4,440
Equity	225,166	200,244	184,866	157,593	143,285
Total liabilities and equity	**1,084,787**	**1,135,482**	**1,081,133**	**1,061,101**	**1,037,391**

Key ratios	2012	2011	2010	2009
Return on equity before taxes (Average equity)	14.0%	8.1%	20.8%	9.9%
Return on equity after taxes (Average equity)	12.0%	8.4%	16.0%	9.5%
Equity ratio (CAD)	25.1%	21.4%	19.5%	15.0%
Cost-income ratio	45.0%	40.6%	36.8%	70.9%
Operating expenses as a ratio of average total assets	2.2%	2.0%	1.7%	1.6%
Interest spread as a ratio of average total assets	3.2%	2.9%	2.3%	1.4%
Loans / deposits	158.2%	144.1%	159.6%	147.4%
Deposits / total assets	38.8%	39.1%	34.4%	42.6%
Number of positions at year-end	1,233	1,311	1,146	1,161

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87. **Operations by quarters (Unaudited)**

Operations	2012 Q4*	2012 Q3	2012 Q2	2012 Q1	2011 Q4*	2011 Q3	2011 Q2	2011 Q1
Interest income	16,624	12,962	18,306	16,769	15,091	14,242	18,315	13,183
Interest expense	(7,395)	(5,180)	(8,286)	(8,216)	(7,033)	(6,500)	(8,611)	(6,038)
Net interest income	**9,229**	**7,782**	**10,020**	**8,553**	**8,058**	**7,742**	**9,704**	**7,145**
Net adjustments to loans and advances acquired at deep discount	17,935	8,213	3,610	7,562	38,291	7,212	8,994	3,992
Loss from foreign currency linkage of loans and advances to customers	-	(2,120)	-	-	(40,726)	-	-	-
Net impairment loss	(1,307)	(4,514)	(5,151)	(1,288)	(4,323)	(318)	16	(2,409)
Fair value change of contingent bond	(13,932)	(5,201)	(2,251)	(5,947)	(17,623)	(8,775)	(4,564)	(3,354)
Net adjustments in valuation	**2,696**	**(3,622)**	**(3,792)**	**327**	**(24,381)**	**(1,881)**	**4,446**	**(1,771)**
Net interest income after net adjustments in valuation	**11,925**	**4,160**	**6,228**	**8,880**	**(16,323)**	**5,861**	**14,150**	**5,374**
Fee and commission income	2,103	1,917	1,836	1,840	1,996	1,843	1,955	1,643
Fee and commission expense	(777)	(887)	(746)	(838)	(917)	(716)	(768)	(613)
Net fee and commission income	**1,326**	**1,030**	**1,090**	**1,002**	**1,079**	**1,127**	**1,187**	**1,030**
Net gain on financial assets designated as at fair value through profit or loss	2,446	(549)	1,429	2,377	5,427	1,634	1,260	9,138
Net gain on financial assets and liabilities held for trading	356	586	112	1,115	1,485	(241)	(706)	471
Net foreign exchange gain (loss)	2,831	899	(1,280)	2,116	290	(910)	2,440	(2,579)
Other income and (expenses)	316	255	269	222	(906)	603	(9)	(138)
Other net operating income	**5,949**	**1,191**	**530**	**5,830**	**6,296**	**1,086**	**2,985**	**6,892**
Total operating income	**19,200**	**6,381**	**7,848**	**15,712**	**(8,948)**	**8,074**	**18,322**	**13,296**
Salaries and related expenses	3,477	3,103	3,364	3,232	4,044	2,703	2,933	2,310
Other operating expenses	2,112	2,250	2,331	2,185	2,304	1,590	2,622	1,951
Depreciation and amortisation	181	177	181	180	240	182	172	177
Contribution to the Depositors' and Investors' Guarantee Fund	275	213	204	350	77	106	150	250
Acquisition-related costs	290	-	-	-	(3)	7	241	-
Total operating expenses	**6,335**	**5,743**	**6,080**	**5,947**	**6,662**	**4,588**	**6,118**	**4,688**
Share of profit of equity-accounted associates, net of income tax	1,762	14	673	-	257	(12)	1,182	(10)
Profit before tax	**14,627**	**652**	**2,441**	**9,765**	**(15,353)**	**3,474**	**13,386**	**8,598**
Income tax	(1,925)	1,277	(400)	(1,877)	4,285	(795)	(1,947)	(132)
Tax on liabilities of financial institutions	(399)	(265)	(205)	(331)	(474)	(120)	(120)	(100)
Profit for the year from continuing operations	**12,303**	**1,664**	**1,836**	**7,557**	**(11,542)**	**2,559**	**11,319**	**8,366**
Profit for the year from discontinued operations, net of income tax	(350)	-	2,312	172	1,546	(40)	424	4,325
Profit for the period	**11,953**	**1,664**	**4,148**	**7,729**	**(9,996)**	**2,519**	**11,743**	**12,691**

Balance sheet	31/12/2012	30/09/2012	30/06/2012	31/03/2012	31/12/2011	30/09/2011	30/06/2011	31/03/2011
Cash and cash balances with Central Bank	25,898	25,235	16,364	25,494	8,823	22,229	30,374	34,256
Bonds and debt instruments	228,208	217,485	203,863	202,195	221,848	215,008	185,417	166,008
Equities and equity instruments	36,881	33,198	38,161	42,803	46,037	28,801	38,461	38,043
Loans and advances to financial institutions	64,349	60,787	59,529	130,946	100,133	81,616	97,597	104,422
Loans and advances to customers	666,087	657,050	666,890	653,949	639,130	643,880	653,189	621,896
Other assets	38,044	37,688	37,082	66,771	65,959	78,735	66,582	93,543
Assets classified as held for sale	25,320	25,382	26,684	52,104	53,552	53,981	54,661	47,422
Total assets	**1,084,787**	**1,056,825**	**1,048,573**	**1,174,262**	**1,135,482**	**1,124,250**	**1,126,281**	**1,105,590**
Due to financial institutions and Central Bank	98,718	90,206	91,018	115,300	112,876	112,642	134,542	131,648
Deposits from customers	421,058	439,853	440,392	455,402	443,590	450,163	425,158	436,688
Secured bonds	221,791	211,699	209,028	289,908	277,076	271,566	273,922	269,781
Contingent bond	87,474	74,225	69,024	66,773	60,826	43,203	34,428	29,864
Other liabilities	29,687	26,561	26,130	29,166	31,485	28,465	35,618	28,142
Liabilities associated with assets classified as held for sale	893	603	959	9,839	9,385	7,985	14,906	13,617
Equity	225,166	213,678	212,022	207,874	200,244	210,226	207,707	195,849
Total liabilities and equity	**1,084,787**	**1,056,825**	**1,048,573**	**1,174,262**	**1,135,482**	**1,124,250**	**1,126,281**	**1,105,590**

*The first three quarter results for the years 2012 and 2011 were reviewed by the Bank's independent auditors.

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