



KLP Group SFCR 2020

KLP Group Solvency and Financial Condition Report 2020
(Rapport om Solvens og Finansiell stilling)



KLP Group

KLP Group Solvency and Financial Condition Report 2020
Kommunal Landspensjonskasse gjensidig forsikringselskap
Org. no. 938 708 606

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Summary

The Solvency II regulations were introduced from 01.01.2016. The rules are the same in all countries in the EU and in the EEA area. Among other things, the rules are intended to provide increased protection for policy-holders. Solvency II lays down requirements for information disclosure, including through this report. The report should provide information on the company's business and results, the system of risk management, and how internal control within the company operates. The report is also intended to provide information on the risks to the company, the methods used for valuation of both assets and liabilities, and an overview of the company's solvency capital composition. The solvency capital is meant to cover the risk that the company has assumed by means of statutory solvency capital requirements.

Kommunal Landspensjonskasse gjensidig forsikringselskap (KLP) is a mutual insurance company, and is the parent company of the KLP Group. The Company's principal product is public-sector occupational pension provision. The Company is owned by its customers, which are Norwegian municipalities, county administrations, health enterprises and companies associated with the public sector. The Group includes subsidiaries active within banking, non-life insurance, asset management and property management. The figures in this report are based on KLP and KLP Skadeforsikring AS, the companies in the KLP Group which required to report under Solvency II. The term 'Group' is also used for these companies.

Total financial income for the Group amounted to NOK 35.5 billion in 2020 (NOK 63.2 billion in 2019), of which NOK 25.7 billion was income from the parent company's customer portfolio where all of the income falls to customers.

For 2019, the risk result (arising from the fact that mortality and invalidity in the period differ from what is assumed in the premium tariff), was NOK 1.2 billion within public sector occupational pensions. The corresponding figure for 2019 was NOK 1.0 billion.

The system of governance, as it is organised and implemented, is considered appropriate to KLP's business. The Company's articles of association and applicable legislation provide the framework for proper corporate governance and a clear division of roles between the governing bodies and executive management. The Company's highest authority is the General Meeting. The Company also has a corporate assembly which elects the Company's Board of Directors.

The risk management system within KLP is tailored to Solvency II and organised on the principle of the three lines of defence. In addition to the statutory remuneration committee and audit committee, the Board has also established a separate risk committee.

The Board has adopted a policy for risk management and internal control and a series of other guidelines to provide for good risk management and compliance with laws and regulations. The policies cover subsidiaries where this makes sense. Requirements have also been laid down for the overall competence of the Board, in addition to the 'fit and proper' requirements which also apply to managers and key functions within the Company.

The development of the Company's risk and solvency situation is monitored through detailed reporting to the Board and senior management. This includes reporting from all three lines of defence.

The Group's principal risks are underwriting risk, market risk and credit risk.

Underwriting risk is dominated by longevity risk in the parent company, i.e. the risk that people entitled to pension payments from KLP will live longer than expected and so require larger payments. The risk that more people could suffer early disability is another material underwriting risk. The risk of customers moving away from KLP is not a risk to the Company's financial strength. Solvency capital and capital requirements related to this are nevertheless included in the calculations of the Group's capital adequacy under Solvency II.

A little over 60% of customers' deposits are invested in interest-bearing securities. The rest are invested in equities and property. Market risk is dominated by equity and property risk, along with interest rate and credit risk. The Company has substantial buffers to enable this allocation. The risk profile changes dynamically in that a policy rule adjusts the proportion of risky investments to the buffer level that the Company has. The subsidiaries do not contribute much to the overall risk profile, apart from KLP Eiendom AS which manages the parent company's property investments.

Under Solvency II, all assets and liabilities are valued at market value. There are two key differences in the valuation of assets and liabilities under Solvency II and in the financial accounts. One is the valuation of insurance obligations. The Solvency II accounts take account of real interest rates, whereas the financial statements use guaranteed interest in the valuation. The other main difference is that bonds and loans reported at amortised cost in the financial statements are shown at fair value in the Solvency II accounts. Other differences are due to differing treatment of intangible assets and deferred tax.

The Solvency II regulations lay down requirements for the amount of solvency capital through the solvency capital requirement. KLP applies a transitional rule to the Solvency II regulations for technical provisions. Using this transitional rule, the Group has a capital adequacy ratio of 335 per cent at 31.12.2020. Even without the use of this transitional rule, the Group has capital adequacy of 264 per cent, well above its own target of at least 150 per cent.

The report has been prepared for the Group. A similar report has been prepared for KLP as the life company and KLP Skadeforsikring AS.

KLP Bedriftspensjon AS was sold in 2020 and is no longer part of the Group.

A. Business and performance

A.1 Business

- a) The name of the Company is Kommunal Landspensjonskasse gjensidig forsikringselskap. The Company's address is: Dronning Eufemias gate 10, postboks 400 Sentrum, N-0103 Oslo
- b) The Financial Supervisory Authority of Norway exercises financial supervision of the Company. The address of the Financial Supervisory Authority of Norway is: Revierstredet 3, postboks 1187 Sentrum, N-0151 Oslo
- c) The Company's external auditor is PwC, Dronning Eufemias gate 71. The contact person is Erik Andersen, erik.andersen@pwc.com.
- d) Customers with public-sector occupational pensions from KLP own the Company. These comprise Norwegian municipal and county authorities, the regional healthcare enterprises (RHF) with their subsidiary healthcare companies (HF), and other public-sector businesses.
- e) Kommunal Landspensjonskasse (KLP) is the parent company for the KLP Group. KLP's wholly-owned subsidiaries are organised as limited companies. The following wholly-owned subsidiaries included in the Group:

- KLP Banken AS and its subsidiaries:
 - KLP Boligkreditt AS
 - KLP Kommunekreditt AS
- KLP Eiendom AS
- KLP Forsikringsservice AS
- KLP Kapitalforvaltning AS
- KLP Skadeforsikring AS

Figure 1: Corporate structure



Mutual funds investments where the KLP Group has control over the investments such that there is a consolidation requirement under the rules in IFRS, are consolidated in.

The minority interest is classified as a liability.

Consolidation

In the solvency balance-sheet, the Group's life and non-life business is fully consolidated through the parent company KLP and its subsidiary KLP Skadeforsikring AS.

The other business areas are included as equity investments in the consolidated balance-sheet, as these are

valued by the equity method. This means that earnings from these activities is included in the group's profit and the value of equity investments. Any distributions from these activities reduce share value. These shares are treated as strategic shares in the calculation of solvency capital requirements. Tier 1 and 2 capital from the banking and asset management companies are part of the Group's Tier 1 and 2 capital. The capital requirements from these activities are also included in the Group's capital requirement.

In the Group balance-sheet for accounting purposes, all of the companies are fully consolidated.

- f) The Group's principal product is public-sector occupational pension provision. The Group is also a major provider of non-life insurance, banking services and investment products. The property company KLP Eiendom is the third-largest property management company in the Nordic region. With the exception of the property business, which has a lot of property abroad, KLP's operations are exclusively in Norway.
- g) Apart from the sale of KLP Bedriftspensjon AS and the merger between KLP Bankholding AS and KLP Banken AS, there is nothing to report regarding activities or events occurring in the reporting period which had a significant impact on the Company.

A.2 Underwriting performance

For 2020, following an application to the Financial Supervisory Authority of Norway, the risk result, together with the extraordinary risk surplus, has been used to strengthen the premium reserve for the changed mortality tariff for men and to adjust the calculation rate downwards. After strengthening the premium reserve, the recognised risk result in KLP is minus NOK 395 million. This result is financed by the risk equalisation fund.

The result of technical accounting from non-life insurance for 2020 was NOK -11 million. The result was NOK 131 million for 2019.

The risk result is an expression of how mortality and disability have developed in the insured population in relation to the assumptions used in the annual setting of premiums. The risk result for 2020 was NOK 1,201 million within public-sector occupational pension provision. The corresponding figure for 2019 was NOK 1,031 million. No extra disability provisions have been raised as a result of the coronavirus pandemic. The risk result does not generally fluctuate much from year to year. However, some fluctuations have to be factored in. This is especially true of the risk result for disability. The mortality tables are still felt to allow good margins, and the trend in 2020 shows that margins overall are still somewhat greater than expected.

The extraordinary risk surplus amounts to NOK 2,671 million and relates to changes in longevity adjustment – changes in NAV’s ratios and divisors based on Statistics Norway’s mortality forecasts – and changes in disability tariffs from 1 January 2020.

The total surplus of NOK 3,872 million (a risk result of NOK 1,201 million and an extraordinary risk surplus of NOK 2,671 million) is used to cover the need to strengthen the premium reserve in response to changed mortality assumptions for men (NOK 2,579 million) and to the reduction in the calculation rate (NOK 1,688 million). In the Joint Scheme for Closed Agreements, the amount needed to strengthen the premium reserve is NOK 395 million more than the risk result and the extraordinary risk surplus.

As the whole of the surplus, with the exception of the Joint Scheme for Closed Agreements, has been used to strengthen the premium reserve, the total recognised risk result is equal to minus NOK 395 million.

In order to manage the pension schemes, the Company collects a cost element in the premiums. This element is included in the Company’s administration result, as discussed in section A.5.

A.3 Investment performance

The Group’s financial assets are managed in various portfolios. Financial assets matching the technical provisions for life insurance are managed in portfolios where most of the returns fall to customers. The customer portfolio now consists of portfolios where the Company has guaranteed customers a return. The management of other financial assets is divided into various portfolios where the whole of the return falls to the Company.

Table 2: Income from investments in public and private-sector occupational pensions in the Group. Figures in NOK millions.

Portfolios	2020	2019
Public-sector occupational pensions	25,700	46,037
Total	25,700	46,037

The costs of managing the customer portfolio were NOK 213 million at 31.12.2020. For all products, a premium element is charged to cover the Company’s costs of managing the capital. These elements are part of the Company’s administration result. For public-sector occupational pensions, the Company also collects an interest guarantee premium in payment for the interest guarantee. These elements are discussed in section A.5 under Table 3, Profit and loss elements in the corporate portfolio.

Further details of investment performance are given in the SFCR reports for KLP and KLP Skadeforsikring AS.

A.3.1 Profit from investments falling to the Group

The Group’s other assets, which are primarily investments in the corporate portfolio, totalled NOK 41.1 billion as of 31.12.2020. Financial income from investments in these portfolios totalled NOK 2.0 billion in 2020 compared to NOK 2.1 billion in 2019. The costs of managing the corporate portfolio were NOK 16 million in 2020. Returns on the portfolios and costs of managing them are included in total comprehensive income for the Group.

Further details are given in the SFCR reports for KLP and KLP Skadeforsikring AS.

A.4 Profit/loss from other activities

All significant income and expenses are included in the above.

A.5 Other information

The sections above describe the underwriting performance (risk result) and the investment result for KLP, as well as the underwriting result for own account for KLP Skadeforsikring AS. For KLP, a positive risk result and a positive investment result in the customer portfolio will fall to the customers. The corresponding negative result is charged to the Company's equity. The interest guarantee premium and the administration result are included in the Company's annual results along with the return in the corporate portfolio. KLP is a mutually owned company. These amounts are one reason why the growth in equity follows the growth in the pension obligations. The table below shows the amount of the interest guarantee premium and the administration result for 2020 and 2019 in KLP. The necessary growth in equity over and above this level is provided by calling in an annual capital contribution from the owners.

Table 3: Profit and loss elements in the corporate portfolio for KLP. Figures in NOK millions.

Profit and loss elements	31.12.2020	31.12.2019
Interest guarantee premium	494	476
Administration result	171	248
Total	676	723

B. System of governance

The description in this section covers KLP both as a company and as a group. The section is identical to the corresponding section in the KLP SFCR.

The system of governance, as it is organised and implemented, is considered appropriate to KLP's business, in relation to the nature, scope and complexity of the risks.

B.1 General information on the system of governance

B.1.1 Structure of KLP's administration, management and controlling bodies

The Company's articles of association and applicable legislation provide the framework for proper corporate governance and a clear division of roles between the governing bodies and executive management.

The General Meeting

KLP has a broad ownership structure. Members of the General Meeting are appointed through election meetings in the relevant constituencies, to which all owners are invited. Voting rights are calculated on the basis of the individual member's share of the previous year's ordinary premium. At the General Meeting each individual delegate has one vote.

The General Meeting is the Company's highest authority and comprises elected representatives of the Company's owners.

The General Meeting elected 15 delegates from 179 constituencies for 2020-2022. The county administrations and the municipalities in each county make up 10 of the constituencies. The four regional health enterprises and their subsidiaries each form one constituency. The companies together form one constituency. In each constituency an election meeting is held to elect delegates to the General Meeting. The General Meeting approves the annual report and accounts for the Company and the Group, including the allocation of profits or provision for losses. The tasks of the General Meeting also include electing 24 of the 45 members of the Corporate Assembly and approving the remuneration of the Corporate Assembly.

The Corporate Assembly

The Corporate Assembly comprises 45 members, 24 of them elected by the General Meeting. A further six representatives are nominated by the staff organisations in the local government sector. 15 representatives are elected from and by the staff in the Group. The Corporate Assembly has essentially the same responsibilities as a corporate assembly under the provisions of the Norwegian Public Limited Liability Companies Act. The corporate assembly elects the Board and its Chair. The Corporate Assembly members elected by the General Meeting elect five members with deputies to the Board of Directors, while the full Corporate Assembly elects the Chair and Deputy Chair of the Board of Directors. The Corporate Assembly elects an election committee with four members and a deputy member.

The Board of Directors of KLP (Group Board)

The Board of Directors is a collective body responsible for the interests of the Company and its owners. The Board is required to monitor the Group's compliance with business regulations and licence requirements. The Board provides for appropriate organisation of the business, determines policies, plans and budgets, keeps abreast of the Company's financial position and obligations and ensures that the business, accounts and asset management are subject to satisfactory control. The Board is required to supervise the executive management and the Company's business generally. The Board of Directors comprises eight members

who are elected for a term of two years in such a way that half are up for election each year. Five Board members with up to the same number of deputies are elected by the members of the Corporate Assembly who are elected by the General Meeting. Two members with deputies are elected by and from KLP's employees. One member and a deputy are nominated by the employee organisation or negotiating alliance with most members in the pension schemes. In addition two observers are nominated from those organisations that are second and third in regard to the number of members. The Group Chief Executive Officer is not a member of the Board of Directors.

Group CEO

The CEO is responsible for the day-to-day management of KLP's business and has to follow the guidelines and orders issued by the Board. The CEO reports to the Company's Board of Directors. The CEO's responsibilities and duties are set out in the instructions adopted by the Board.

Group senior management

The KLP Group senior management comprises ten experienced individuals with a broad background from Norwegian business and public sector activities. Group senior management is the top level of management in KLP and is responsible for the functional management of the company.

Group senior management is organised according to business areas, representing the Life Insurance, Banking, Non-Life Insurance, Capital Management and Property departments. Group senior management also includes the divisional heads with responsibility for Economy and Finance, IT, Communications and Markets, and HR and Internal Services.

The Board's sub-committees

The Board of Directors has three sub-committees: a remuneration committee, an audit committee and a risk committee. The committees do not make decisions on behalf of the Board, but present their assessments and recommendations to the Board.

Remuneration committee

The remuneration committee is a preparatory and advisory working committee for the Board's deliberations on remuneration questions. In 2011 the Financial Supervisory Authority of Norway gave permission for a joint remuneration committee in the KLP Group. On this basis the committee also serves those boards of directors in the KLP Group that are required by law to have remuneration committees. The committee's responsibilities include ensuring the requirements laid down in law and in the regulations on remuneration schemes in financial institutions, investment firms and asset management companies are complied with in those companies in the KLP Group that are subject to these regulations.

Audit committee

The audit committee is a preparatory and advisory working committee for the Board. The Committee was set up in accordance with the requirements for an audit committee pursuant to the Norwegian Act on Insurance Activity. The committee helps to quality-assure the Board's work to do with financial reporting, audit and governance.

Risk committee

The Committee acts as a risk committee for the Board of KLP. The principal tasks of the risk committee are to assist the Board in monitoring and managing the Company's overall risk and assessing whether the Company's management and control systems are appropriate to the level of risk and the scope of the overall business of the Group. The committee also ensures that the Company has good systems for internal control and risk management, and that the second-line functions work properly. The committee also ensures that there is a satisfactory organisation with a clear organisation structure, and an appropriate division of

responsibilities and tasks between executing and monitoring functions. The risk committee assists the Board in preparing Board actions in other matters to do with risk management.

Risk management committee

The Group CEO has established a committee to act as his advisory body in matters concerning the Company's overall risk and solvency. The committee addresses the general risk appetite, the overall risk strategy and risk exposure from all the major risk factors, including market risk, underwriting risk and operational risk.

Key functions

The risk management, compliance and actuarial functions and Internal Audit are the key functions in KLP. The Board ensures that these have the necessary authority, resources and independence through guidelines adopted by the Board for each of the functions. These guidelines allow the managers of each function to report directly to the Board on matters affecting their areas of responsibility. The key functions produce quarterly and annual reports which are discussed by the Board.

B.1.2 Significant changes in the system of governance made during the reporting period

No significant changes were made to the system of governance in the reporting period.

B.1.3 Remuneration policy

Principles

The Board previously adopted remuneration principles for KLP and additional guidelines for KLP Kapitalforvaltning AS. The remuneration rules were last discussed and revised at the Board meeting of KLP on 03.12.2020.

In accordance with the Norwegian Financial Institutions Act and the Act on Securities Funds with associated regulations, the Board of KLP has determined and ensured that the Company always has and applies guidelines and frameworks for a remuneration scheme covering the whole of the Company including its subsidiaries.

The KLP Group aims to have competitive pay and employment conditions compared to similar companies, but without leading the way. The remuneration scheme is designed to be cost-effective for the Group.

The Group's remuneration schemes should be open and performance-based, so as to be perceived as fair and predictable wherever possible. There should be a correlation between agreed performance requirements and the remuneration given.

Remuneration based on results

No individual or collective remuneration (bonus) is given to employees on the basis of KLP's results. In KLP Kapitalforvaltning AS the portfolio managers and their managers have bonus agreements.

Pension scheme

All employees of KLP are members of KLP's pension scheme.

Until 01.05.2013, KLP also had a scheme for 'Pensions for salaries over 12 G¹'. This scheme has been modified:

- Persons employed by KLP after 30.04.2013 are not covered by the scheme.

¹ National Insurance basic amount

- Persons employed before 30.04.2013 who have salaries below 12 G today will not be covered by the scheme even if they later receive salaries over 12 G.
- For persons who have a salary above 12 G at 30.04.2013, the following applies: “Persons with salaries over 12 G have additional cover to ensure that fixed pay in excess of 12 G is counted as fully pensionable. This scheme applies only to qualification time accrued directly in KLP. If the pension is calculated on part-time working as an employee of KLP, the pension base over 12 G will be reduced accordingly.”

B.1.4 Transactions with related parties

KLP has transactions with other companies in the KLP Group, as well as members of the administration, management or control bodies. These are transactions that are part of the products and services offered by KLP or its subsidiaries to their customers. The transactions are entered into on market terms and include occupational pensions, non-life insurance, bank deposits, lending, asset management and fund saving.

B.2 ‘Fit and proper’ requirements

B.2.1 The Company’s ‘fit and proper’ requirements

The companies in the KLP Group ensure that managers and others in the business holding key functions and key functions are suitable and fit to safeguard their work activities and responsibilities as stated in the individual’s Job description.

The boards of the companies in the KLP Group have adopted, and revise annually a guideline for suitable and fitness. The guideline contains qualification requirements which are designed to provide for appropriate diversity of qualifications, knowledge and relevant experience, to ensure that the Company is managed and supervised in a professional manner.

As part of the qualification requirement, the Board of the KLP Group should have sufficient insight and understanding to be able to question the assessments of the administration, take a critical view of the answers and initiate the necessary action. The whole Board of KLP should at least have qualifications in these areas:

- The insurance and finance market
- Business model and strategy
- The business system, including an understanding of the risks the Company is exposed to and its ability to handle them
- Financial and actuarial analysis.
- Regulatory frameworks and requirements.
- Understanding of social issues.
- Customer and product knowledge.

B.2.2 The Company’s process for ‘fit and proper’ assessment

The ‘fit and proper’ assessment is made by the individual’s manager. Persons to be assessed have to submit a completed and signed form for use in the assessment approved by the Financial Supervisory Authority of Norway. These persons are assessed when employed/elected, or in specific situations. An annual confirmation has to be given to the effect that no new circumstances have arisen since the last assessment/confirmation. This is especially important in relation to conduct.

All persons in Group management, key functions and the Board must meet certain standards of suitability (conduct). For persons listed above, KLP assesses the following aspects:

- Criminal record
- Sanctions against companies
- Administrative sanctions and charges
- Financial situation
- Tax matters
- Other matters

Persons to be assessed must present a copy of a police certificate no more than three months old. Information may also be obtained from the publicly accessible Register of Bankruptcies and the Register of Company Accounts.

If any of the criteria listed above is not met, an individual assessment will be made. A principle of proportionality will be applied, whereby consideration will be given to the nature and severity of the offence, whether there has been a final judgment, the number of offences, the person's subsequent behaviour and the time aspect.

B.3 Risk Management system

B.3.1 Risk Management system. Strategies, processes, and reporting procedures

The risk management system at KLP is implemented through policies, processes/strategies and reporting procedures. Mandates, instructions and job descriptions for the various roles are also included in the system.

Guidelines

The Company has drawn up a comprehensive set of guidelines, rules and instructions to provide for effective risk management through appropriate and thorough processes and procedures. The guidelines are reviewed annually and approved by the Board. The Group CEO also lays down the necessary rules to implement the guidelines.

The various guidelines have different areas of application. Some guidelines apply to the whole Group but are still adopted by the boards of the subsidiaries. Other guidelines apply wherever appropriate and provide a basis for the subsidiaries' own guidelines. Every subsidiary will also have its own guidelines to govern matters specified for the Company's business in the acts and regulations to which it is subject.

Processes/strategies

The overall risk in the Company is normally divided into three main parts: market risk, underwriting risk and operational risk, including strategic and reputational risk.

The main processes for monitoring, managing and measuring market risk are the overall risk management strategy, the asset management strategy and the capital plan. The asset management strategy and strategy for overall risk management are adopted in the autumn for the next calendar year. It includes targets for the overall risk, a framework for allocation and the design of the Group's dynamic strategy for exposure to risky assets (policy rule). The capital plan is drawn up in parallel with the Own Risk and Solvency Assessment, and sets the long-term course for the Company's capitalisation.

A strategy for underwriting risk is adopted each year. However, this risk is by nature long-term and the strategy is broadly fixed over time. Operational, strategic and reputational risk are assessed as part of the annual process for risk management and internal control; see section B.4.

Reporting

Risk reporting in KLP takes place at many levels. At each Board meeting, the CEO includes current topics in his briefing. A separate briefing on risk management and asset management is also a fixed item on the agenda. The Board also receives a detailed monthly report on developments in the Group.

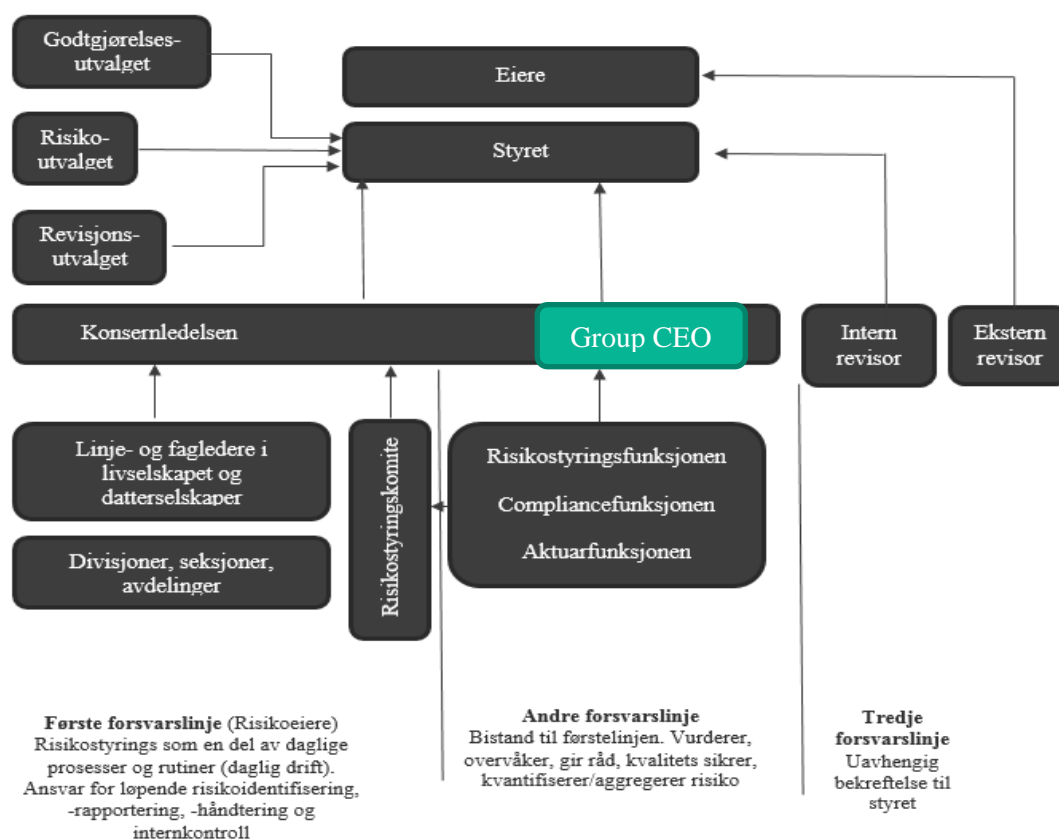
The second-line functions produce quarterly reports from their areas, which are addressed by the Board. The actuarial and compliance functions also produce their own annual reports. The risk management function coordinates the self-assessment of the Company's risk and solvency and compiles the ORSA² report.

The risk management committee monitors changes in the policy rule at each meeting.

B.3.2 Organisation of the risk management system

The risk management system at KLP is organised on the principle of the three lines of defence. This is in line with the latest principles of risk management and adapted to the requirements in the Solvency II rules. The organisation is illustrated in the figure below:

Figure 2: The risk management system at KLP



First line – Risk management and operation

The Group CEO and all managers and employees in the operational units and subsidiaries make up the first line of defence. They bear the primary responsibility for good risk management through their responsibility for doing their jobs in line with authorisations, instructions and guidelines. Managers are also required to establish proper procedures and control measures within their areas.

Second line – Monitoring and quality assurance

² Own Risk and Solvency Assessment

The control functions that make up the second line are the risk management function, the compliance function and the actuarial function. For a more detailed description of the compliance function and the actuarial function, see sections B.4 and B.6.

The risk management function is headed by the Chief Risk Officer (CRO), who reports to the Group CEO. The head of the actuarial function reports to the CRO, as this function is organised as an integral part of the risk management function. The main responsibility of the risk management function is to monitor the Group's overall risk, including the risk management system. The unit, which is headed by the CRO, also calculates the Company's capital adequacy. Capital adequacy is a key part of the quarterly reporting from the risk management function, which is discussed by the Board of Directors. The Own Risk and Solvency Assessment is an important task for the risk management function; see section B.3.3.

To safeguard the independence of the actuarial function from the CRO, the Group CEO approves the remuneration of the head of the function. Independence is also ensured by the fact that the second-line functions have the right to report directly to the Board of Directors on matters concerning their areas of responsibility.

Third line – Independent verification

Independent verification is provided by the Group's own Internal Audit unit and its external auditors. The Internal Audit function is described in detail in section B.5.

Risk management committee

The Group CEO has established a committee to act as his advisory body in matters concerning the Company's overall risk and solvency. The committee includes the CFO and the directors responsible for the company's risk management, as well as the actuarial and compliance functions. The committee addresses the general risk appetite, the overall risk strategy and risk exposure from all the major risk factors, including market risk, underwriting risk and operational risk. Each year, the committee discusses the principal assumptions used to calculate the Company's capital adequacy. The committee is administered by the CRO and assists the CRO in carrying out the 'Own Risk and Solvency Assessment'.

B.3.3 Own Risk and Solvency Assessment

B.3.3.1 Process

The process for the 'Own Risk and Solvency Assessment' (ORSA) is laid down by the Board in a separate guideline. The guideline sets out the main principles for the process, with requirements for implementation, division of responsibilities, performance requirements and documentation. The process is carried out each year and is normally discussed at the Board meeting in June.

The ORSA process is largely based on the Company's other processes for managing risk and solvency. Apart from market and underwriting risk, risks in the process of governance are identified in the autumn. This process also quantifies the most important remaining risks. Quantification is used to calculate the capital requirements for operational risk.

B.3.3.2 Implementation and approval

The risk management function is responsible for coordinating the implementation of the ORSA process and compiling the report. The process follows an established set of tasks, starting with introductory discussions in the risk management committee. These identify factors to be focussed on in the year's process, often based on evaluations and feedback on the process from the previous year.

The ORSA plan and suggested changes in related guidelines are discussed by the Board in March. Work on sensitivity tests, scenario analyses and specially selected factors will continue until the report is completed. An integrated process is followed for KLP as a company and as a group, but separate reports are produced for each of these.

The Board reviews and approves the ORSA by looking first at guidelines for the ORSA and then at the actual reports. This cements the Board's ownership of the process. The Board's risk committee also conducts an extended review of the ORSA plan and the ORSA reports for KLP (both Company and Group) and makes its recommendations to the Board.

An extraordinary ORSA has to be produced if there are changes that could affect the risk and/or capital substantially. Changes may be driven by internal decisions or external factors.

B.3.3.3 Determination of own solvency needs

The Board determines its solvency requirements based on the assessments made in the ORSA process. KLP's solvency capital requirements are defined by the regulatory solvency capital requirement as this is larger than that obtained by using the Company's own assumptions and methods.

The solvency target is that capital adequacy for the KLP Group should be more than 150 per cent without including transitional rules for KLP and KLP Bedriftspensjon AS. The Board of Directors wants there to be a low likelihood of fluctuation, especially on the financial market, so there is a low probability of having to call in extraordinary equity to strengthen the solvency position. The goal is therefore set considerably higher than the regulatory requirement of 100 per cent.

B.4 Internal control system

B.4.1 KLP's internal control system

Internal control is concerned with systematic follow-up of the business. The purpose of good internal control is to maintain effective processes and procedures to meet business objectives. An important aspect of the internal control system in KLP is to deal with any risks that could prevent the Company from achieving its goals in a cost-effective manner and in line with the current framework for the business.

Both risk management and internal control ensure that KLP can achieve its objectives by identifying and analysing relevant risks that could prevent it from attaining its goals, and by implementing effective measures to handle, control and report on the risks. The Board of KLP has adopted a policy for risk management and internal control in KLP. The policy defines fundamental principles, processes, roles and responsibilities connected with governance. Relevant risks and internal control measures should be assessed in decisions on significant changes to the business.

The risk management system helps ensure that KLP can achieve its objectives in all significant areas of business through:

- Identifying, measuring, monitoring, documenting and reporting on all material risks that could prevent target attainment.
- Establishing appropriate risk strategies to manage risk-taking
- Establishing measures to handle and control material risks
- Establishing contingency plans to handle the impact of any remaining risks.
- Establishing appropriate reporting procedures for unwanted events

The company's leaders, at all levels, should at all times have adequate records of set goals, risks, key controls and any adverse events within their area so that they can manage risks associated with their business on a satisfactory manner. The second-line functions also assist all managers in providing for good governance, and make independent assessments of the managers' handling and control of risk. KLP has also established an Internal Audit unit to provide the Board with an independent assessment of whether the internal control system is working. The Board of KLP assesses the internal control within the company at least once a year.

B.4.2 Compliance function

The compliance function helps the Board and senior management to ensure that KLP has implemented effective procedures for compliance with the applicable rules, including the framework for effective management and control.

The compliance function identifies, monitors and reports risks of non-compliance within KLP. In particular, the compliance function monitors the material risks linked to non-compliance in the Group, and is an active 'sparring partner' to the Board, management and staff within KLP in relation to the operational handling of non-compliance risk.

The compliance function works preventively by providing advice, guidance and ongoing quality control when operational changes are made to regulations, and carries out control activities to ensure that internal control in the Company is effective. Advice, dialogue, presence and training take a high priority. The aim of these activities is to develop an organisation structure in which compliance with the framework is an intrinsic value.

The head of the compliance function reports to the Group CEO and briefs the management on his/her own initiative on matters that are or could be of significance to the business. Serious breaches of laws and regulations, or a significantly increased risk of non-compliance, must be reported without undue delay to the Group CEO.

To preserve the independence of the compliance function, the function has no operational or decision-making roles in activities that the function is required to monitor. This does not prevent the compliance function from assisting management in developing appropriate processes, procedures and methods to provide for effective follow-up of managers' control responsibilities. The Board has adopted a special policy for the compliance function.

The Board has also established a special policy for compliance risk. The policy defines roles and responsibilities to ensure compliance within KLP, and sets out the Board's risk appetite and requirements for how to handle risks of non-compliance.

The compliance function in of KLP Skadeforsikring AS is described in the SFCR reports for KLP Skadeforsikring,AS. KLP Bedriftspensjon AS had outsourced its compliance function to the compliance function of the KLP Group. From 1 October 2020, the compliance function was taken over by the new owner.

B.5 Internal Audit function

B.5.1 Exercise

Based on risk assessments etc., an audit plan is drawn up for areas to be audited. The areas to be audited are operational and support processes, risk management systems, IT systems and IT security, products and regulatory requirements. The audit plan is approved by the Board.

The findings from the audit are reviewed with the operational and line managers for the area that has been audited, who take a view on the recommendations and set deadlines for implementing them. The audit reports are reviewed in the audit and risk committee before the conclusions and recommendations are presented to the Board. Progress in implementing the recommendations is presented to the Board in the annual report from Internal Audit. The annual report from Internal Audit provides an assessment of business and risk management and of the internal control in key areas.

In order to perform its function effectively, Internal Audit looks at internal operational reports, Board actions and reports, and communicates with senior management, the risk, compliance and actuarial functions and external auditors.

On its own initiative or at the request of the administration, Internal Audit conducts ad-hoc reviews or tasks within control-related problem areas.

B.5.2 Independence and objectivity

Internal Audit reports to the Board and has to be professionally independent in its work in relation to the areas and persons being audited. The Board engages and dismisses the head of Internal Audit and defines that person's conditions.

Internal Audit has no operational or financial responsibility or decision-making authority within the different areas of activity. Internal Audit cannot therefore perform ongoing operational tasks, take decisions or carry out other activities that might compromise its independence or objectivity.

The head of Internal Audit has to demonstrate to the Board on an annual basis that the function is independent. In the guideline from the Board, the internal auditors are required to comply with the applicable laws, regulations and orders from the Financial Supervisory Authority of Norway and ethical rules and standards issued by the Institute of Internal Auditors.

Every five years, there is an external evaluation of KLP's Internal Audit function; the last of these was in 2018. The audit committee in KLP reviews this evaluation and communicates its findings to the Board.

B.6 Actuarial function

The actuarial function at KLP has responsibilities and duties as described in the Solvency II rules. The actuarial function is organised as an integral part of the risk management function. In order to safeguard its independence, the head of the actuarial function is allowed to report to the Group CEO and the Board on all matters within its area of responsibility. The actuarial function also reports directly to the Group CEO every quarter. The report deals with the activities and assessments made by the actuarial function in the quarter and helps to demonstrate its independence. KLP Skadeforsikring AS has its own actuarial function. The report also contains a summary of its work. The responsibility for the Group-level actuarial function is held by the same person as the actuarial function in KLP. The Group actuarial function in KLP has a coordinating role vis-a-vis all established actuarial functions in the Group, i.e. for KLP and KLP Skadeforsikring AS. Among other things, this helps to ensure consistent assessments of technical provisions across the Group. The actuarial functions in the subsidiary are described in the SFCR reports for Skadeforsikring AS.

The role and responsibilities of the actuarial function are described in the policy for the actuarial function, adopted by the Board of KLP. The actuarial function should ensure that technical provisions are calculated by a combination of:

- Ensuring that methods, models and assumptions used in the calculation of technical provisions are appropriate
- Assessing whether the data used in the calculation of technical provisions is sufficient to ensure the necessary quality
- Comparing best estimates with the Company's experience
- Informing the Board and senior management as to whether the calculation of insurance technical provisions is reliable and sufficient
- Testing any simplified calculations of best estimates based on approximate values and individual assessments of notified claims cases
- Expressing a view on the Company's policy for underwriting risk
- Expressing a view as to whether the Company's reinsurance programme is sufficient
- Contributing to the effective implementation of the risk management system, particularly with regard to the risk modelling which forms the basis for calculating the Solvency Capital Requirement and self-assessment of the Company's capital needs

The actuarial function may use professional resources in other entities for specified tasks. In this case the manager of the actuarial function must ensure that there are no conflicts of interest for the function or the people doing work for the function. The head of the actuarial function in KLP and the Group is a member of the risk management committee at KLP and also has access to Board actions and the right to attend Board meetings where actuarial matters are discussed. The Group-level actuarial function attends board meetings in KLP Skadeforsikring AS when the report from the actuarial function is presented, and may also attend when any other actuarial topics are discussed. The Group-level actuarial function may also participate in the risk management committee for KLP Skadeforsikring AS.

At least once per year, the actuarial function draws up a written report which is submitted to the Board of KLP. This report documents all the tasks carried out by the actuarial function, and the results of these, and clearly identifies any deficiencies and makes recommendations for rectifying these.

B.7 Outsourcing

Outsourcing is used where KLP chooses to use contractors to perform work assignments which could also have been carried out by the Company itself. The Board of KLP has adopted an outsourcing policy. The Code of Conduct applies to both outsourcing contracts within the KLP Group and when the business is contracted out to external companies.

The guideline is meant to ensure that outsourcing from KLP is handled in a proper manner and in accordance with the applicable rules. It gives guidance as to what should be regarded as outsourcing for KLP (the life insurance company), and the Company's responsibilities with regard to such outsourcing. The guideline also lays down requirements for assessing reliability, notification, outsourcing contracts and checks on the contractor's business.

Even if work activities are outsourced, KLP will still be responsible for the business that has been contracted out. KLP must therefore be able to fulfil its obligations, and check the contractor's risk management and internal control systems, including compliance with laws and regulations for the outsourced business.

B.8 Other information

The foregoing is considered to cover all the key details of the risk management system.

C. Risk profile

The risks to which the Group is exposed fall into three main groups:

- Market and counterparty risk
- Underwriting risk
- Operational, strategic and reputation risk

The dominant position of the parent company within the Group means that the Group's exposure to these risks is totally dominated by the parent company's activities.

C.1 Underwriting risk

The two biggest underwriting risks for KLP are longevity risk and disability risk, both characterised by slight variations in measurable risk from year to year. Longevity risk means that the customer lives longer than presumed, and disability risk means that more people than expected are becoming disabled, or that fewer than expected are returning to work.

Longevity and disability risk are monitored every quarter via reports of underlying risk items from KLP's membership system, while a full analysis including a calculation of risk results forms part of an annual process. The risk result is followed up carefully and provides the basis for assessing whether prices and provisions are sufficient. The analysis entails statistical processing of relevant data on the membership base with a view to measuring the trend in mortality and disability, in order to arrive at a best estimate of how this trend may be expected to evolve in the coming years. The expected development is quantified by deriving a new basis for calculation. This will be the basis for best estimate assumptions in Solvency II calculations and perhaps also for new premium and reserve calculations (before actuarial safety margin).

- Longevity risk
Because old-age pensions after the age of 67 in public-sector occupational pension schemes are age-adjusted in the same way as the national insurance-based old-age pension, the potential economic consequences of the trend towards greater longevity in the future will be limited. If longevity increases more than the projections used by Statistics Norway (SSB), this will cause a downward adjustment of accrued old-age pensions compared to what has been insured and financed for all year-groups that have not yet turned 61.

In the Joint Scheme for Municipalities and Enterprises, the Joint Scheme for County Administrations, the Joint Scheme for State Health Enterprises, the Joint Scheme for Closed Agreements and the Pension Scheme for Publicly Elected Representatives, the premium reserve at 31 December 2020 has been determined from a strengthened calculation basis based on the K2013 tables with a higher mortality rate for men. The change in the assumption of a decline in mortality for men is based on Statistics Norway's updated forecasts in 2020.

The K2013 tariff is defined by the formulae and parameters explicitly provided by the Financial Supervisory Authority of Norway in 2013. This data has a basic margin in the initial mortality rate of 12 per cent. For the Pension Scheme for Nurses and for the Pension Scheme for Hospital Doctors, a bigger margin is used in the initial mortality rate. Experience shows a significantly greater longevity among the persons insured in these schemes and the assumptions provide for tariffs with roughly the same safety margin in all risk groups. For the Pension Scheme for the Nurses, a higher mortality rate for men is also used.

The overall calculation base used by KLP (K2021_KLP) is described in a separate product report to the Financial Supervisory Authority of Norway. The marital status elements of the premium tariff are as specified in K2013.

The current mortality base has been found to have good margins and a robust level of premiums and provisions. There are substantial resources in the risk equalisation fund. This reduces the risk that deficits might have to be covered by equity outside the risk equalisation fund.

An abrupt fall in mortality, as assumed by stress tests for solvency purposes, is much less of a real risk than longer lives in the future, but companies still need to maintain solvency to withstand this because such stress tests are essential to the capital requirements placed on companies under Solvency II.

- **Disability**
KLP's disability tariff was changed from 1 January 2020 based on observations of its own population for the period 2015-2018. From 31 December 2020, the disability tariff is changed in all risk groups based on observed trends up to and including 2019. The new disability tariffs use specific parameters for disability and re-entry into work in each risk group. In the past, all risk groups had a common disability tariff except for the Pension Scheme for Nurses and the Pension Scheme for Hospital Doctors. The changes involve some easing or marginal changes in all risk groups.
- **Departure risk**
Customers with public-sector occupational pensions from KLP can opt to move to another provider at each year-end. Customers then take with them all the assets assigned to them, but they also take all the technical provisions associated with the customer relationship. Customers also take away their share of the equity contributed. On the other hand, retained earnings stay with KLP. The result of a customer moving is thus an improvement in the Company's solvency.

Customers moving are only regarded as a strategic risk to the Company if large numbers are involved. Disposals are not considered to be a risk to the Company's solvency.

In calculating capital requirements under the Solvency II rules, departures are categorised as an underwriting risk. The capital requirement associated with departure risk is significant as the standard method requires KLP's schemes to assume that 70 per cent of customers will move. The capital requirement arises from the fact that future margins factored into the Company's capital disappear. This means that the capital requirement for underwriting risk is much higher than that calculated for longevity risk and disability alone.

Underwriting risk is mainly managed by maintaining a robust level of premiums and provisions. This gives an expected low probability of a negative insurance result. Great use is made of the risk equalisation fund, which can cover any negative risk result, to minimise the risk of losses related to underwriting risk affecting other equity. The Company is allowed to allocate a maximum of half of any positive risk result to the risk equalisation fund, while the rest has to go to the customers' premium fund.

KLP has no reinsurance contracts related to underwriting risk. The extent of reinsurance is regularly assessed in light of the Company's risk-bearing capacity and the nature of the products.

As KLP exists mainly to provide occupational pension solutions to municipal and county authorities and health enterprises, it is not considered appropriate to exclude any of these customer categories from offers from KLP on grounds of risk. KLP can anyway decline to offer public-sector occupational pension schemes to businesses that represent an unreasonably large risk. This applies mainly where historical data indicate a particularly high disability risk, but very few of our potential customers have such a prevalence of disability and it is very rare for anyone to be refused. Customer selection is therefore very little used to manage underwriting risk.

In practice, as it is specified what the insurance cover in public-sector occupational pension schemes must include, the underwriting risk is contained within these limits. There is also a general requirement to equalise premiums so customers cannot be charged individually, except for the interest guarantee premium and capital management costs.

Underwriting risk and the development of the market for relevant pension products are reported each year in a separate report from the Actuarial/Product department. The Board of Directors sets an annual strategy for underwriting risk and reinsurance.

C.2 Market risk

Market and counterparty risks for the Group are dominated by KLP's portfolios. The dominant risk is from shares in the parent company's common portfolio. The proportion of equity is managed dynamically through a policy rule, and it will be the dominant risk as long as the customer buffers are sufficient to maintain an equity element in line with long-term targets. This section will therefore describe the Group's market risk in terms of the market risk for KLP. For the market risk in KLP Skadeforsikring AS, refer to the notes in the Company's SFCR report (section C.2 Market Risk).

Market risk is the risk that the value of investments will change. Typical factors are changes in share prices, property prices, interest rates and exchange rates.. Market risk in KLP arises in the management of the pension assets and equity in the Company. In its long-term asset management strategy, KLP seeks to put together a portfolio which, in relation to KLP's obligations, can give the highest possible (competitive) return subject to limits on risk-taking. The limitations on risk mean that the risk is adjusted to ensure that the Company is solvent at all times and that it maintains sufficient risk capacity over time. This means that the Company should have a capacity for risk that allows us to maintain a certain level of risky assets in the short and long term, even after a year of heavy losses in asset management. The risk capacity is also assessed in a long-term perspective, taking into consideration the impact of interest rates on risk capacity over time.

The risk capacity is regularly monitored and reported on at each Board meeting. The risk is measured both at the end of the year and on a rolling one-year horizon. Measurements are taken at intervals through the year.

To support these goals, the following principles form the basis of the capital management approach:

- Long-term investment perspective
- Diversified portfolios
- Focus on efficient markets and cost-effective management

- Risk management adapted to the company's long-term financial risk within regulatory limits
- Active corporate social responsibility

KLP's market risk is made up of equity risk, property risk, interest rate risk, credit risk, concentration risk and currency risk. The gross capital requirement for market risk under Solvency II as at 31.12.2020 was estimated at NOK 94.5 billion, allowing for the diversification effect between the various asset classes. Net capital requirements for KLP (after using buffer capital etc.) related to market risk were NOK 4.6 billion at 31.12.2020.

It should be possible to record, measure and report all investments in relation to external and internal guidelines for risk monitoring and reporting in place at any given time. This means that the Company should not trade in instruments without having developed the expertise and systems to provide for proper follow-up.

KLP follows up the market risk by way of stress tests and sensitivity analyses etc. Market risk is also a key part of the self-assessment of risk and solvency in the annual ORSA process. KLP calculates its solvency capital coverage at least quarterly.

KLP have its financial assets invested in customer portfolios and a corporate portfolio. The customer portfolios are made up of customers with public-sector occupational pensions, and the portfolios are divided according to risk-bearing capability. The market risk affects income and profits differently for the different portfolios.

The risks in the customer portfolios are compared taking account of objectives such as remaining solvent and maintaining risk capacity over time. Annual investment limits are set for the different asset classes. The portfolio breakdown for each asset class is generally well diversified so non-systematic risk is very limited. The risk in the portfolio is also handled dynamically through operational rules. This means that the risk in the customer portfolios is constantly adjusted to the risk-bearing capacity. During the year, the trend in profit or loss will send signals to the policy rule to adjust the level of risk exposure by buying and selling. The adjustments will normally be made in the equity market, as long as equities account for the bulk of the total risk in the common portfolio.

The market risk in the corporate portfolio affects equity directly. For the corporate portfolio, KLP aims to take low market risk. The majority of the funds are invested in interest-bearing securities with an average duration of 4.2 years as of 2020. The corporate portfolio has a low correlation with the customer portfolios.

Equities

The listed equity component of the common portfolio includes Norwegian exposure and global exposure in developed and emerging markets. Investments in unlisted shares consist of investments in special funds, private equity and other equity investments. Management is mainly through mandates issued to KLP Kapitalforvaltning AS.

The corporate portfolio has investment limits relative to the total assets under management in the corporate portfolio. The equity portfolio is made up of shares in subsidiaries and, to a lesser extent, associates, based on Board resolutions.

Property

KLP's portfolio of property is mainly managed by the subsidiary KLP Eiendom AS, along with some investments in global real estate funds. Investments by KLP Eiendom AS are mainly in Norway, but portfolios have also been established in Sweden, Denmark and the UK. We aim

at long leases with solid counterparties. KLP's fundamental management philosophy is to hold high-quality properties in central shopping streets.

The property exposure in the corporate portfolio is made up of KLP's offices in Oslo and Bergen and low-risk leasehold sites.

Interest

The technical provisions are long-term, but it is not appropriate to have investments with the same duration. This is because investments with durations equal to the obligations are difficult to obtain, and because the duration in KLP is perceived to be short in regulatory terms as KLP can collect an annual interest guarantee premium.

Interest rate risk is not a significant contributor to KLP's capital requirements, but persistent low interest rates are naturally a challenge to the Company's ability to generate good returns for its customers.

The risk of the Company being unable to achieve a return greater than the guaranteed return is reduced in any given year by posting a substantial part of the interest-bearing investments to the accounts at amortised cost. The expected return for the hold-to-maturity portfolio in 2021 is around 3.5 per cent, and the average duration is around 5 years.

Other

The basic principles for asset management are set out above. This, combined with management mandates and limits that restrict exposure to individual issuers, means that KLP has only minimal exposure to concentration risk.

With few exceptions, KLP hedges its portfolios against currency fluctuations. The hedging rate for global equities in developed markets is around 60 per cent. No significant changes are expected in 2021. The Company will therefore continue to have little exchange rate risk across all portfolios.

There were no significant changes in market risk in 2020.

C.3 Credit risk

The Group's credit and counterparty risk are also dominated by the parent company's risk in these areas. The discussion of the Group's exposure to these risks is therefore based on the description of these areas for KLP. For KLP Skadeforsikring AS, refer to that company's SFCR report (section C.3 Credit Risk). KLP Banken AS contributes some interest and credit risk from its activities, but the capital requirement for the Bank is included in the Group's solvency capital calculation.

Credit risk is a risk of losses where counterparties cannot meet their debt obligations. The risk includes losses on loans and losses related to bank deposits, or non-fulfilment of contracts by counterparties in reinsurance contracts or financial derivatives. Losses in the securities portfolio that can be linked to these types of losses are categorised as market risk.

Credit and counterparty risk are part of market risk, so they are included as 'other market risk' in the various risk assessments and analyses carried out. Credit risk is classified at least once a year by country, rating and sector. Assessments of bad debt provision/valuation and default are made in line with the relevant accounting principles.

Credit limits are set on all credit exposure before an investment is undertaken. These limits are set by a separate credit committee. The credit limits are reviewed annually and monitored quarterly. The limits for Norwegian credit are primarily based on internal credit

assessments. Lending to foreign borrowers is largely based on external ratings from recognised rating agencies.

In addition to the credit limits, special requirements for diversification are laid down up in the mandates to KLP Kapitalforvaltning AS. These ensure that portfolios without diverse indices have limited non-systemic risk.

C.4 Liquidity risk

The liquidity risk in the Group is considered to be very limited. The parent company's portfolios are largely made up of liquid investments. At the same time, the cash flows from these activities are large relative to the liquidity needs for day-to-day operations. The companies in the Group are responsible for their own liquidity management. This section describes the liquidity risk for KLP. For KLP Skadeforsikring AS, refer to its SFCR report (section C.4 Liquidity risk), and for KLP Banken AS and KLP Kapitalforvaltning AS, refer to their ICAAP reports. All companies are subject to specific liquidity requirements.

KLP has a liquidity portfolio which should be able to meet ongoing obligations relating to payment of pensions and to coverage of operating costs. Liquidity needs that may arise as a result of people moving also form part of the overall assessment of the size of the liquidity portfolio. In normal circumstances the portfolio should have sufficient funds to prevent the Company needing to release funds from other portfolios for expected payments. As a large part of KLP's funds are invested in highly liquid assets and KLP's liquidity requirements are normally covered by quarterly premium payments from customers, the liquidity risk is considered to be limited.

For KLP, the insurance commitment is long-term, and the cash flows are largely known long before they fall due. The liquidity risk is handled through the liquidity strategy, covering measurement, management and contingency planning relating to liquidity risk.

From each quarterly premium payment, KLP aims to set aside liquid assets that are greater than or equal to three months' liquidity requirement. In situations where there are insufficient liquid assets to cover the liquidity need, funds have to be released from other portfolios or obtained in some other way. The contingency plan will come into effect when an exceptional liquidity need has arisen and the liquidity has fallen below certain defined levels. Based on this, the liquidity risk is considered to be low.

Liquidity planning is based on financial accounting values. The financial accounts do not include a margin from future premiums. The size of margin from future premiums is therefore not very relevant to liquidity risk and liquidity management.

C.5 Operational risk

Operational risk is defined as the risk of financial loss or loss of reputation as a result of failure of internal processes, human error or system failure, or any other loss due to external events. Operational risk management involves detecting risk factors that can cause losses, and estimating the likelihood and impact of possible adverse events.

KLP's property investments are gathered together in its subsidiary KLP Eiendom AS, which both manages and develops property. This carries some non-traditional operational risk for a company in the insurance sector. The Company has its own ISO-certified processes to measure and manage its operational risk.

The capital requirement for operational risk for the KLP Group is calculated on the basis of the individual operational risks for the companies subject to Solvency II reporting and ICAAP

reporting. The operational risk for the Group is dominated by the parent company. The capital requirement for operational risk is NOK 2.6 billion for the Group and NOK 2.5 billion for KLP. The discussion of the Group's operational risk is therefore based on the description of the operational risk for KLP. For KLP Bedriftspensjon AS and KLP Skadeforsikring AS, refer to their SFCR reports, and for the subsidiaries subject to ICAAP reporting, refer to their ICAAP reports.

KLP carries out an annual governance process (risk management and internal control) in which the heads of all departments identify operational risks within their areas of responsibility. The likelihood and impact of each risk are assessed, and it is decided whether the risks are acceptable or whether risk reducing measures must/should be taken. Where the risk assessment concludes that the risk is higher than is acceptable, measures will be established to reduce the likelihood or the impact of this risk. Measures identified earlier are followed up and are included in the assessments. The identified risks are grouped together for each division. Finally, a list is produced for the Company, which is included in the Group's list. The risk management function facilitates the process and reports performance to senior management and the Board. Strategic risk and risk to reputation are valued separately.

The internal control process is supplemented with a valuation of the principal operational risks. The Company's own assessment includes a calculation of the capital requirements for operational risk based on the valuation. The Risk Management function helps to quantify the economic losses. The capital requirement for the operational risk is calculated by the standard formula based on a volume target for premiums and reserves.

The major identified operational risks in KLP are linked to the increasing scope of new general regulation, stable IT operation, data quality and increasing exposure to new IT security threats.

C.6 Other material risks

It is considered that other significant risks in the Group are dominated by KLP and thus covered in KLP's SFCR report, section C.6.

C.7 Other information

The foregoing is considered to cover all the key details of the Company's risk profile.

D. Valuation for solvency purposes

D.1 Assets

Total assets valued in the solvency balance amounted to NOK 639.5 billion at 31.12.2020. This is an increase of NOK 67 billion since 31.12.2019. Total financial assets (accounting values) amounted to NOK 657 billion at 31.12.2020. This is an increase of NOK 25,6 billion since 31.12.2019.

Assets under Solvency II are recognised at fair value. The valuation principles are largely congruent with the principles for valuation at fair value under International Financial Reporting Standards (IFRS). The financial statements for KLP are drawn up in accordance with the Regulations on annual accounts for insurance companies. These rules broadly match IFRS, but bonds at amortised cost and bonds classified as loans and receivables are recognised at amortised cost. There are also differences in the valuation of intangible assets and deferred taxes.

Table 5: Assets. Figures in NOK billions

Asset classes	Solvency II 2020	Accounts 2020	Solvency II 2019	Accounts 2019
Intangible assets		0.6		0.5
Deferred tax assets/assets after tax*	0.5	0.0	0.5	0.1
Property for own use	2.4	2.4	-2.0	-2.0
Property (other than for own use)	68.8	68.8	57.1	57.1
Investments in associates, including participations	4.0	4.0	4.5	4.5
Equities etc.	36.2	36.2	42.2	42.2
Bonds	268.2	253.3	253.9	246.3
Asset management companies etc.	167.0	167.0	165.3	165.3
Derivatives	6.8	6.8	5.0	5.0
Deposits other than cash equivalents	0.6	0.6	1.5	1.5
Assets linked to contracts with investment options	0.0	0.0	4.9	4.9
Lending	91.9	90.7	85.7	85.2
Reinsurance share of gross technical provisions	0.1	0.1	0.1	0.1
Other assets**	24.5	27.5	16.8	16.8
Total	671.3	657.5	639.7	631.4

* With gross tax assets under Solvency II.

**Other assets are made up of: 'Cash and cash equivalents', 'Receivables from policy-holders', 'Receivables from reinsurers', 'Other receivables' and 'Miscellaneous other assets'.

There may be some differences between S.02.01 and the table due to different classifications.

D.1.1 Intangible assets

Valuation, Solvency II:

Intangible assets are valued at zero. Under Solvency II, intangible assets are valued at zero unless the asset can be sold separately and the company can demonstrate that it has a market value.

Valuation, accounts:

Intangible assets are valued for accounting purposes at cost and depreciated over their expected service life. If there are indications that the book value of an intangible asset is higher than the recoverable amount, an impairment test is carried out. If the recoverable

amount is less than the book value, the asset is depreciated to the recoverable amount. Intangible assets are posted to the balance-sheet in the amount of NOK 0.6 billion.

D.1.2 Assets subject to tax

Valuation, Solvency II:

Deferred tax is split into a deferred tax asset of NOK 0.5 billion and a deferred tax liability of NOK 1.5 billion under Solvency II in 2020 for the Group. The calculations include the transitional scheme for technical provisions.

This valuation is based on the accounting calculation but also factors in the effect of assets and liabilities with a different valuation than in the accounts, where this difference could have a tax effect. This includes assets measured at amortised cost in the corporate portfolio as well as the valuation of financial liabilities (hybrid Tier 1 perpetual capital and subordinated debt). Financial liabilities are valued slightly higher in the Solvency II balance-sheet, which produces a deferred tax asset. Assets in interest-bearing portfolios valued at amortised cost in the accounts are valued higher in the Solvency II balance-sheet, and so give rise to a deferred tax liability. KLP Skadeforsikring AS does not use any temporary deduction in technical provisions.

Valuation, accounts

Capitalised deferred tax assets or liabilities represent the nominal value minus any impairment of the holding which is not assumed to be usable and so has no value. The nominal value is calculated on the basis of differences between the accounting and taxation timing of changes in the value of assets and liabilities. To the extent that these differences will reverse at a later date, there will be deferred tax (accounting income taken before taxable income) or a deferred tax asset (taxable income taken before accounting income). Temporary differences are offset against each other where they are expected to reverse within the same time frame and the differences can be equalised through Group-level allocations. Net temporary differences which mean that the Company has brought forward taxable income or deferred taxable deductions are posted as deferred tax assets.

At 31.12.2020, the Group had net deferred taxes of NOK 0.6 billion. See section D.3.3.

D.1.3 Property for own use

Valuation, Solvency II

Property for own use is measured at fair value.

Property investments are measured at fair value. Fair value is calculated using an internal valuation model because there is not considered to be an active market with observable prices in the property markets that KLP invests in. In order to quality-assure the interval valuation model, a selection of the Group's property stock is regularly valued by external, independent and qualified valuers. In the event of significant deviation from our own assessment of fair value, the differences are analysed and the valuation model's parameters are adjusted if this proves necessary.

Valuation, accounts

In the accounts, property for own use is measured at fair value by the revaluation method. This means that property for own use is depreciated on a regular basis, then revalued to fair value. The calculation of fair value matches the calculation defined for valuation under Solvency II.

D.1.4 Property (other than for own use)

Solvency II valuation equal to reported value

The property investments are measured at fair value by the same method used to determine the fair value of property held for own use; see description in section D.1.3.

D.1.5 Investments in associates, including participations

Valuation, Solvency II

Investments in associates, including participations, are measured at fair value. Fair value is estimated to equal net assets and liabilities in the subsidiary measured at fair value.

Valuation, accounts

Investments in associates, including participations, are measured by the equity method. Where the subsidiary's accounts are prepared according to different principles than KLP's own accounting principles, the subsidiary's accounts are converted to KLP's principles before KLP's share of the profit/loss is entered in the accounts.

D.1.6 Equities etc.

Solvency II valuation equal to reported value

Equities etc. are measured at fair value. Fair value should be a representative price based on what a corresponding asset would have been traded for on normal market terms and conditions.

A share is considered as listed in an active market if quoted prices are easily and regularly available from a stock market, dealer, broker, industry group, price-setting service or regulatory authority, and these prices represent actual and regularly occurring transactions at arm's length. Liquid shares are generally valued on the basis of prices provided by an index provider. At the same time, prices are compared between different sources to pick up possible errors.

If the market for the share is not active, or the share is not listed on a stock market or similar, the Group uses valuation techniques to set fair value. These are based for example on information on recently completed transactions carried out on commercial terms, and reference to trading in similar instruments. As far as possible the estimates are based on externally observable market data and rarely on company-specific information.

D.1.7 Bonds

Valuation, Solvency II

Investments in bonds are measured at fair value. Fair value should be a representative price based on what a corresponding asset would have been traded for on normal market terms and conditions. A financial instrument is considered as listed in an active market if quoted prices are easily and regularly available from a stock market, dealer, broker, industry group, price-setting service or regulatory authority, and these prices represent actual and regularly occurring transactions at arm's length.

If the market for the security is not active, or the security is not listed on a stock market or similar, the Group uses valuation techniques to set fair value. These are based, for example, on information on recently completed transactions carried out on commercial terms, reference to trading in similar instruments and pricing using externally collected yield curves

and yield spread curves. As far as possible the estimates are based on externally observable market data and rarely on company-specific information.

Valuation, accounts

Investments in bonds are reported in the accounts partly at fair value and partly at amortised cost. For the portion measured at fair value, there is no difference from the valuation principles described for Solvency II.

Bonds where the intention is to receive a fixed rate of interest for the whole term to maturity are valued for accounting purposes at amortised cost. This amounts to NOK 183 billion out of a total of NOK 327 billion. The difference in valuation is NOK 15 billion.

Bonds are measured at amortised cost using the effective interest method. The internal rate of return is set through discounting contractual cash flows over the expected duration. The cash flows include setting-up charges and direct transaction costs as well as any residual value at the end of the expected duration. Amortised cost is the present value of these cash flows discounted by the internal rate of return.

D.1.8 Asset management companies etc.

Solvency II valuation equal to reported value

Securities funds etc. are measured at fair value; see description under D.1.6.

Securities funds etc. also include investments in private equity funds. The fair value of these funds is based on reported market values, as quoted in the International Private Equity and Venture Capital Valuation Guidelines (IPEV Guidelines). These guidelines are issued by the European Venture Capital Association (EVCA) and based on the principle of approximate market valuation of the companies in the funds.

D.1.9 Derivatives

Solvency II valuation equal to reported value

Derivatives are measured at fair value.

D.1.10 Deposits other than cash equivalents

Valuation, Solvency II

Deposits other than cash equivalents are measured at fair value.

Valuation, accounts

Deposits other than cash equivalents are measured at nominal intrinsic value.

D.1.11 Assets linked to contracts with investment options

Solvency II valuation equal to reported value

Assets linked to contracts with investment options are made up of units in investment funds. These are measured at fair value; see description under D.1.8.

D.1.12 Lending

Valuation, Solvency II

Lending is measured at fair value; see discussion of Solvency II valuation of bonds in section D.1.7.

Valuation, accounts

Loans are reported in the accounts at amortised cost. This produces a valuation NOK 1.3 billion lower than the fair value reported in the Solvency II balance-sheet.

Lending is measured at amortised cost using the effective interest method. The internal rate of return is set through discounting contractual cash flows over the expected duration. The cash flows include setting-up charges and direct transaction costs as well as any residual value at the end of the expected duration. Amortised cost is the present value of these cash flows discounted by the internal rate of return.

Loans are written down where there is objective proof of impairment. Loss assessment and loss write-down is carried out quarterly on individual loans.

Lending is also assessed by group. If there is objective proof of impairment in a group of loans, a write-down is carried out.

D.1.13 Reinsurance share of gross technical provisions

Valuation, Solvency II

The reinsurance portion of gross technical provisions is measured at fair value. This means that the receivable is discounted, taking account of expected losses on claims against reinsurance companies.

Valuation, accounts

Valuation for accounting purposes uses nominal value with a deduction for losses resulting from default.

D.1.14 Other assets

Solvency II valuation equal to reported value

Other assets are measured at fair value.

D.2 Technical provisions

Insurance liabilities are valued differently under Solvency II and in the financial statements. Under Solvency II, the insurance liabilities are referred to as technical provisions, while the financial statements refer to them as insurance provisions.

D.2.1 Value of technical provisions, basis, methods and assumptions

Under Solvency II, all assets and liabilities are valued at market value (also called fair value). The technical provisions in Solvency II are made up of a best estimate plus a risk margin. The best estimate consists of guaranteed payments and discretionary benefits. The value of the best estimate is calculated as the sum of future cash flows from all receipts and payments expected within the contract limit and the probability-weighted average of future cash flows.

Because of uncertainty in the best estimate, a risk margin is added. This is intended to cover the costs of providing risk capital. The risk margin is calculated as the present value of the

capital cost, by keeping the risk capital equal to the solvency capital requirement which arises from taking over the portfolio.

KLP uses transitional rules to calculate technical provisions in accordance with Article 56 of the Solvency II Regulation. Technical provisions (Solvency II Directive, Article 308d). The effect is calculated as the difference between the technical provisions (sum of best estimate and risk margin) and the insurance provisions in the accounts (the sum of the premium reserve, supplementary provisions, securities adjustment fund, other provisions for insurance funds and other technical provisions). The effect is reduced on a linear basis at the beginning of each year from 100 per cent on 1 January 2016 to 0 per cent on 1 January 2032. There is also a floor defined for valuation which limits the effect of the transitional rule.

Tables 6 and 7 below show the technical provisions under Solvency II and the technical provisions in the financial accounts for the Group broken down by industries for KLP. Technical provisions under Solvency II are shown both with and without the use of transitional rules for the technical provisions which KLP uses. The Solvency II provisions are calculated with a volatility adjustment as set out in Article 3(2) of the Solvency II Regulation. Yield curve (Article 77d of the Solvency II Directive). The volatility adjustment provides a mark-up in the risk-free market interest rate. This means that the obligations will be lower than they would have been without this adjustment. The effect depends on the amount of the markup. The adjustment as at 31.12.2020 represents an interest markup of 0.40 percentage points for the first ten years, after which it decreases slightly.

KLP Skadeforsikring AS is not covered by the transitional rules and does not use any volatility adjustment in its calculations.

Table 6 Technical provisions for KLP with volatility adjustment and with transitional rules for technical provisions under Solvency II. Figures in NOK billions.

Technical provisions 2020 including transitional rules	Best estimate	Risk margin	Technical provisions, Solvency II	Technical provisions, Accounts
Public-sector occupational pensions	584.7	13.9	598.6	594.7
Life insurance	584.7	13.9	598.6	594.7

Table 7 Technical provisions for KLP with volatility adjustment but without transitional rules for technical provisions under Solvency II. Figures in NOK billions.

Technical provisions 2020 without transitional rules	Best estimate	Risk margin	Technical provisions, Solvency II	Technical provisions, Accounts
Public-sector occupational pensions	595.9	14.2	610.1	594.7
Life insurance	595.9	14.2	610.1	594.7

With the use of the transitional rules, the technical provisions under Solvency II are lower than without the use of transitional rules.

In order to calculate the time value of future cash flows, economic scenarios are generated in an economic scenario generator (ESG). KLP uses the scenario generator from Moody's Analytics. The scenario generator is calibrated to the risk-free interest rates published by EIOPA. This yield curve is used both to discount the cash flows and as an initial yield curve for simulating future returns. The scenarios are generated to be risk neutral, so all asset

classes are assigned a yield that assumes risk-free interest rates. This is in line with the Solvency II rules.

For KLP Skadeforsikring AS, claims provision in the Solvency II balance-sheet represents the present value of future claims for losses incurred plus claims handling costs. In practice, this is calculated by discounting the reported claims reserves.

For KLP Skadeforsikring AS, the premium provision in the Solvency II balance-sheet represents the present value of future claims for losses incurred plus administration costs for potential claims. The Solvency II values also take into account expected departures and expected accepted business for quotations that the company has undertaken to abide by.

The risk margin in the Solvency II balance sheet is a provision which is intended to cover costs incurred in engaging another company to take over the Company's insurance portfolio. This is calculated from the present value of the capital cost a successor company will assume when it has to keep the risk capital equal to the solvency capital requirement arising from taking over the portfolio.

More specifically, the solvency capital requirement is calculated as the liability that arises immediately upon taking over the insurance portfolio with all related insurance liabilities and receivables. The solvency capital requirement going forward decreases with the reduction in the best estimate of the technical liabilities. The risk margin is the present value of the capital cost, keeping the risk capital equal to the solvency capital requirement throughout the winding-up period.

The values of the technical provisions under Solvency II and the technical provisions in the financial accounts are shown in table 8 below.

Table 8: Technical provisions for KLP Skadeforsikring AS. Figures in NOK billions.

Technical provisions 2020	Best estimate	Risk margin	Technical provisions, Solvency II	Technical provisions, Accounts
Occupat. injury	0.544	0.030	0.574	0.582
Loss of income	0.373	0.026	0.399	0.422
Third-party insurance for motor vehicles	0.083	0.009	0.092	0.133
Other motor insurance	0.106	0.017	0.123	0.262
Insurance against fire and other material damage	0.870	0.047	0.917	1.014
Third-party liability	0.146	0.011	0.157	0.155
Assistance	0.008	0.002	0.010	0.033
Non-life insurance, excl. health insurance	2.130	0.142	2.272	2.601
Health insurance	0.112	0.004	0.116	0.129
Non-life insurance, total	2.241	0.146	2.387	2.729

D.2.2 Uncertainty related to the value of technical provisions

When using complex cash flow models, there will always be some uncertainty in the results. The results are sensitive to the assumptions, choice of methods and processing of input prior to each calculation. The level of uncertainty in the calculations of the insurance obligation is driven by uncertainty in the underlying assumptions. Such assumptions are reviewed at least

once a year in the companies' risk management committees to ensure that they still accurately reflect the Company and its strategies.

The interest rates given by EIOPA are based on some assumptions that are uncertain, including the extrapolation methodology, time taken to obtain long-term interest, long-term interest rates and volatility adjustment levels. As part of the ORSA process, sensitivity analyses are carried out for the value of solvency capital and the capital requirements for changed assumptions. One intention is to increase understanding of the sensitivity of the calculations.

D.2.3 Value of technical provisions, basis, methods and assumptions

KLP

In the financial accounts, the provisions are made up of the premium reserve, additional provisions, the securities adjustment fund, other provisions to insurance funds and other technical provisions.

The calculation of a premium reserve in the financial accounts is based on the present value of deposits and payments using the same assumptions as in the premium calculation basis. The present value is calculated with a discount rate equal to the guaranteed interest at the time of accrual throughout the term of the individual insurance contract.

The valuation of the technical provisions in the financial accounts is deterministic. The biometric assumptions in the premium calculation basis in use at any given time are also used. Biometric assumptions cover mortality, invalidity and re-entry into work. The assumptions include safety margins in relation to what is considered as a best estimate.

For longevity/mortality, the K2013 price tariff is used, except for hospital doctors and nurses who have reduced mortality rates. Based on the latest forecasts from Statistics Norway on longevity trends, along with analyses of KLP's own membership, KLP strengthened the mortality base for men from 31.12.2020, except for members of the pension scheme for hospital doctors. The new tariff, K2021_KLP, is a modified version of the current tariff K2013, in which the function expressing the decline in mortality has changed. Like the other formulae in K2013, the change applies to both longevity risk and mortality risk. The calculation basis for the best estimate uses the same assumptions as the price tariff, but without a safety margin. For women, no changes have been made.

For disability and re-entry into work, KLP's own calculation basis is used for each risk group. The price tariff is included in a security premium in relation to the calculation basis for the first estimate. The calculation basis for the best estimate is based on historical data, and the latest updated basis will be adopted as of 31.12.2020, with variations for each risk group. The current pandemic situation could affect the drawing of disability pensions in the next few years. In view of this, the margins have been reduced, albeit rather conservatively. Beyond this, no significant changes have been made to the assumptions used to calculate the technical provisions during 2020. The assumptions are assessed each year and updated as needed.

KLP Skadeforsikring AS

In calculating technical provisions, individual claim provisions are made for all claims reported but not settled. The provisions are continuously adjusted as claims are processed. All open claims should have a special assessment at least once a year.

Provision for claims incurred but not yet reported to the company is calculated using statistical models. The models take account of the historic reporting pattern in the different risk groups.

In non-life insurance, measurements and adjustments are also made to the total claims provisions (reported + not reported claims) so the total level of provision is measured against changes in risk elements such as claim frequency, major claim occurrence, population mix and population size. The claims provisions are valued in line with expectations and include provisions for future indirect claims handling costs.

The provision for unearned premiums is the pro rata portion of premiums payable accrued after the accounting close.

D.2.4 Matching adjustment

The Group does not apply the matching adjustment described in Article 3(3) of the Solvency II Regulation. Yield curve (Article 77b of the Solvency II Directive).

D.2.5 Volatility adjustment

KLP applies the volatility adjustment described in Article 3(2) of the Solvency II Regulation. Yield curve (Article 77d of the Solvency II Directive). The volatility adjustment provides a mark-up in the risk-free market interest rate. This means that the obligations will be lower than they would have been without this adjustment. The effect depends on the amount of the markup. The adjustment at 31.12.2020 represents an interest mark-up of 0.30 percentage points for the first ten years, after which it decreases. The effect is shown for KLP, as the Group’s technical provisions are dominated by the parent company.

Figure 3: EIOPA’s interest rates with and without volatility adjustment at 31.12.2020

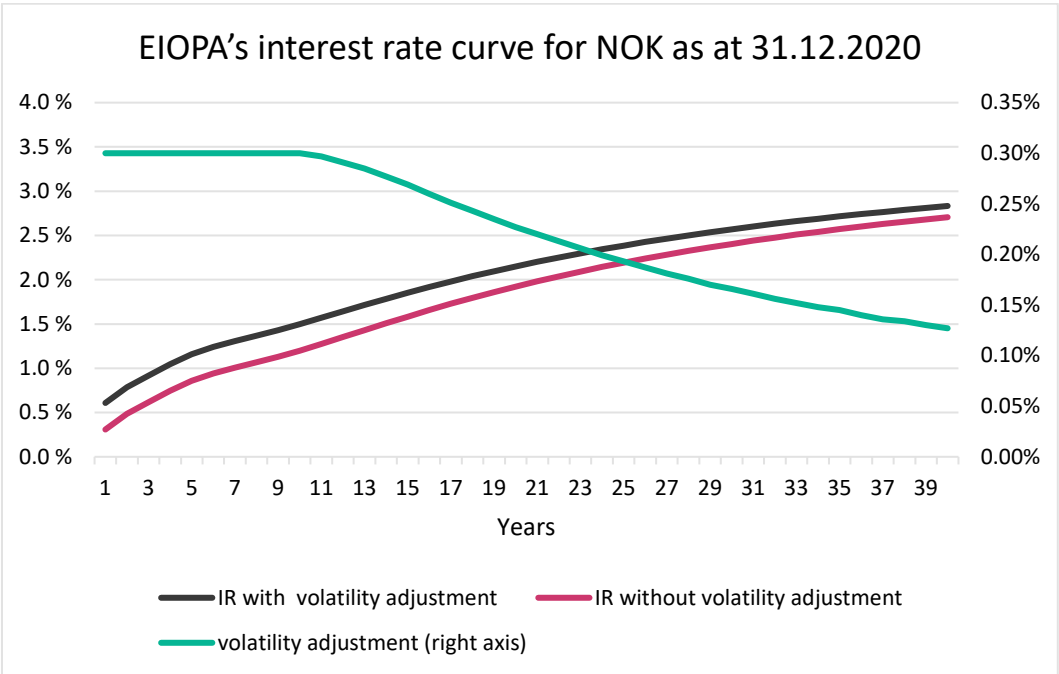


Figure 4: EIOPA's interest rates with and without volatility adjustment at 31.12.2019

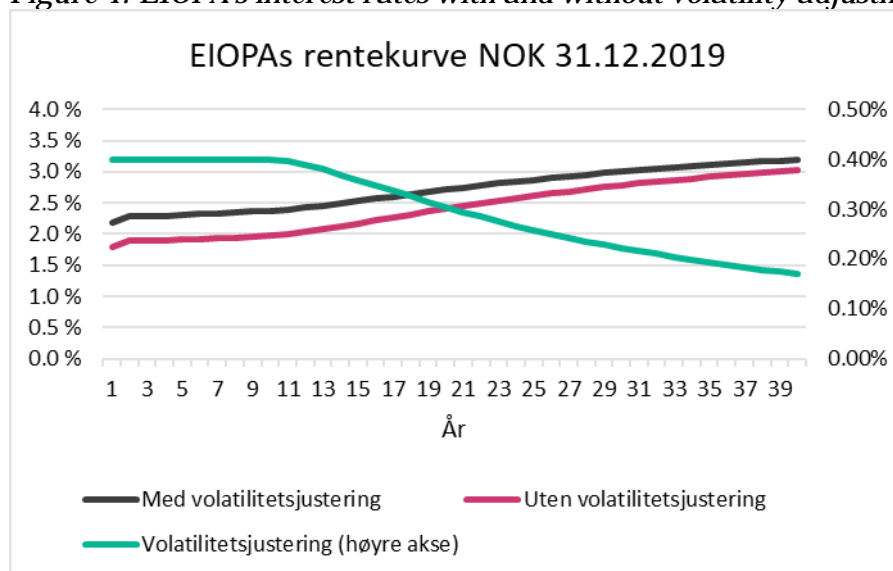


Table 9: Effect of utilising volatility adjustment and transitional rules for technical provisions for KLP Group. Figures in NOK billions.

2020	With the use of volatility adjustment	Without the use of volatility adjustment	Difference
Technical provisions	600.9	600.9	-0.1
Solvency Capital Requirement	16.5	16.8	0.3
Eligible Tier 1 and 2 capital to cover the SCR	54.3	55.1	0.8
Capital adequacy	329%	327%	-2%
Minimum consolidated group solvency capital requirement	7.0	7.2	0.2

Difference in per cent, is percentage points.

As table 9 above shows, KLP has a solvency capital coverage of 327 per cent without the use of volatility adjustment and a solvency capital coverage of 329 per cent with the use of volatility adjustment at 31.12.2020. Use of the volatility adjustment gives a 2 percentage point increase in capital adequacy. Both calculations include the use of transitional rules for the technical provisions.

D.2.6 Transitional provisions on risk-free interest rates

The Group does not apply the transitional provisions on risk-free interest rates described in Article 308c of the Solvency II Directive. To measure their insurance obligations, insurance companies must use the latest risk-free yield curves published by the Financial Supervisory Authority of Norway (Article 3(1) of the Solvency II Regulation).

D.2.7 Transitional rule for technical provisions

In reporting to the Financial Supervisory Authority of Norway, KLP applies the temporary deduction provided for by the transitional rule for technical provisions described in Article 308d of the Solvency II Directive. Note 26 Capital requirements in the KLP Group's financial statements show the calculations without the use of this temporary deduction. The calculations are shown in table 10 below.

The technical provisions with transitional rules are valued at NOK 600.9 billion in the solvency balance-sheet for the whole of the KLP Group at 31.12.2020. This is NOK 3.7 billion more than the liabilities of NOK 597.1 billion shown in the financial statements. Without transitional rules, the technical provisions in the solvency balance are valued at NOK 612.5 billion, NOK 15.4 billion higher than the liabilities in the financial statements.

The transitional provisions say that in 2020 one can deduct 12/16 of this difference in the Solvency II valuation. That means that the valuation of the best estimate under Solvency II including the transitional scheme is NOK 612,5 billion. The difference between the technical provisions with and without transitional arrangements is NOK 11.5 billion.

The deduction will be reduced on a linear basis until 2032. The difference for 2020 will be multiplied by 12/16, which means that there are 12 years left of the transition period. The transition period is 16 years from 2016 to 2032.

Table 10: Effect of applying the transition rule to the technical provisions for the Group. Figures in NOK billions.

2020	With the use of transitional rules	Without the use of transitional rules	Difference
Technical provisions	600.9	612.5	11.5
Solvency Capital Requirement	16.3	16.3	0.0
Eligible Tier 1 and 2 capital to cover the SCR	54.3	42.7	-11.5
Capital adequacy	329%	259%	-70%
Minimum consolidated group solvency capital requirement	7.0	7.0	0.0

Difference in per cent (percentage points).

With the use of the transitional provision, the technical provisions are lower than without the use of it. The eligible Tier 1 and 2 capital is increased at the same time if we use the transitional provision. Both of these changes tend towards higher solvency capital coverage with the use of the transitional provision than without the use of the transitional provision. Even without the use of the transitional rules for the technical provisions, the KLP Group meets the solvency capital requirement by a good margin.

D.2.8 Miscellaneous

D.2.8.1 Reinsurance

KLP currently only has collective products without any option to choose the amount of cover for the individual parties insured. Based on this limitation, and given the size of the company and hence its large risk-bearing capacity, the need for reinsurance in KLP is considered small. KLP does not currently use reinsurance.

KLP Skadeforsikring AS has its own reinsurance programme. The Company optimises the reinsurance programme in relation to reinsurance costs and the Company's risk capacity. The reinsurance programme for KLP Skadeforsikring AS is reassessed and renewed annually. There are minimum rating requirements for reinsurers. The proportion of the programme placed with one reinsurer is limited.

D.2.8.2 Significant changes in assumptions

KLP

Changes have been made to the calculation basis for mortality for men in the best estimate and in the price tariff from 31.12.2020 onwards. The initial mortality rate is unchanged, but life expectancy has changed. The changes are based on forecasts from Statistics Norway

and analyses of KLP's own membership. The change has been implemented for all men, except for male hospital doctors who already have an enhanced calculation basis.

Changes have also been made to the calculation basis for disability based on updated historical data through 2019. These will be applied to all risk groups from 31.12.2020.

A new calculation method for national insurance has been used under a new collective agreement from 01.01.2020.

KLP Skadeforsikring AS

During 2020, no significant changes have been made to the assumptions used to calculate the technical provisions for KLP Skadeforsikring AS.

D.3 Other liabilities

The table below shows the breakdown of other liabilities.

Table 11: Other liabilities Figures in NOK billions.

Other liabilities	Solvency II 2020	Accounts 2020	Solvency II 2019	Accounts 2019
Provisions other than technical provisions	1.6	1.6	1.4	1.4
Pension obligations	0.7	0.7	0.6	0.6
Deferred tax liability*	1.5	0.6	1.5	0.7
Derivatives	0.6	0.6	0.7	0.6
Financial liabilities other than liabilities to credit institutions	5.9	5.9	4.0	4.0
Liabilities related to direct insurance, including insurance brokers	0.8	0.8	1.0	1.1
Payment obligations (to suppliers, excl. insurance)	2.4	2.4	-2.0	-2.0
Hybrid Tier 1 and subordinated loan capital	5.3	4.9	8.1	7.8
Other liabilities**	6.7	5.2	5.8	0.2
Total	25.5	22.5	25.2	18.3

* With gross tax liabilities under Solvency II

** Reinsurance and other obligations not shown elsewhere From 2019 onwards, this also includes risk equalisation fund belonging to KLP.

D.3.1 Provisions other than technical provisions

Solvency II valuation equal to reported value

Provisions other than technical provisions are measured at fair value.

D.3.2 Pension obligations - own employees

Solvency II valuation equal to reported value

KLP's employees have a defined-benefit pension entitlement. Most are covered through KLP's public sector occupational pensions by virtue of membership of the joint pension scheme for municipalities and enterprises ('Fellesordningen'). Other entitlements are also defined-benefit, but covered via operations.

The liability is posted to the Solvency II balance-sheet at the present value of the obligation on the reporting date, minus the fair value of the pension assets. The gross obligation is calculated using the straight-line method. The present value of the gross liability is

discounted at 1.7 per cent, which is meant to reflect interest rates on Norwegian high-quality bonds.

The table below shows the pension obligations in NOK billions:

Table 12: Net pension obligations - own employees, 2020. Figures in NOK billions.

Net pension obligations for employees	Joint scheme	Via operation	Total
Present value of the obligations	2.5	0.3	2.8
Fair value of the pension assets	1.9	-	1.9
Net pension obligation, own employees	0.6	0.3	0.9

Table 13: Net pension obligations - own employees, 2019. Figures in NOK billions.

Net pension obligations for employees	Joint scheme	Via operation	Total
Present value of the obligations	2.1	0.3	2.4
Fair value of the pension assets	1.6	0.0	1.6
Net pension obligation, own employees	0.5	0.3	0.8

Table 14: Allocation of pension funds for own employees

Composition of the pension assets	2020	2019
Property	13.3%	12.4%
Shares and units	24.2%	25.9%
Lending	12.9%	12.5%
Fixed-income securities	49.6%	49.3%
Total	100.0%	100.0%

D.3.3 Deferred tax

Valuation, Solvency II

See discussion in section D.1.2.

Valuation, accounts:

At 31.12.2020, the Group recognised net deferred tax of NOK 1.0 billion; see notes in section D.1.2.

D.3.4 Derivatives

Solvency II valuation equal to reported value

Derivatives are measured at fair value.

D.3.5 Financial liabilities other than liabilities to credit institutions

Solvency II valuation equal to reported value

These liabilities are measured at fair value.

D.3.6 Liabilities related to direct insurance, including insurance brokers

Solvency II valuation equal to reported value

These liabilities are measured at fair value.

D.3.7 Payment obligations (to suppliers, excl. insurance)

Solvency II valuation equal to reported value

These liabilities are measured at fair value.

D.3.8 Hybrid Tier 1 perpetual capital

Valuation, Solvency II

Under Solvency II, financial liabilities are measured at fair value when the loan is taken. Later valuations will not take account of changes in the Company's own creditworthiness after this point. In the Solvency II balance-sheet, the hybrid Tier 1 perpetual capital is valued using an interest curve which does not include any credit mark-up to the Company, which produces a conservative valuation of the loan.

Valuation, accounts

The hybrid Tier 1 perpetual capital is valued for accounting purposes at amortised cost, adjusted for changes in value resulting from currency and interest rate movements according to the rules on fair value hedging.

D.3.9 Subordinated loan capital

Valuation, Solvency II

Under Solvency II, financial liabilities are measured at fair value when the loan is taken. Later valuations will not take account of changes in the Company's own creditworthiness after this point. Subordinated debt is valued in the Solvency II balance-sheet using an interest curve where the Company's credit mark-up is kept unchanged from when the loan was taken out.

Valuation, accounts

Subordinated debt is measured at amortised cost. Subordinated debt in foreign currency has been translated to NOK using the exchange rate at the end of the reporting period. This means that the reported book value is NOK 396 million less than the Solvency II valuation.

KLP had one subordinated loan as of 31.12.2020.

D.4 Alternative methods for valuation

KLP's valuation principles for assets that cannot be valued based on quoted prices are described in Note 7 Fair value hierarchy in the 2020 annual report for the KLP Group.

D.5 Other information

The foregoing is considered to cover all the key information on valuation.

E. Capital management

The main purpose of the KLP Group is to manage the capital invested by its members in the Company either as owners (equity) or as retail customers (pension funds) as well as possible within the Company's risk capacity.

E.1 Tier 1 and 2 capital

The Group's Tier 1 and 2 capital is dominated by own funds in the parent company. Smaller amounts come from KLP Skadeforsikring AS and Tier 1 and 2 capital calculated according to relevant sector-level rules for KLP Banken AS and KLP Kapitalforvaltning AS. The purpose of the Company's Tier 1 and 2 capital is to satisfy regulatory requirements under Solvency II by a good margin. The Company reports its capital adequacy ratio for the Solvency Capital Requirement and the Minimum Capital Requirement every quarter. KLP Bedriftspensjon AS was sold to DNB in 2020, and completely removed from the consolidated balance-sheet from Q4 2020.

The boards of KLP, KLP Bedriftspensjon AS and KLP Skadeforsikring AS have adopted a policy for capital management. The purpose of the guideline is to ensure that the respective companies are sufficiently capitalized and meet the regulatory minimum requirements for capital set by the financial authority. The Company has also set its own targets for solvency capital coverage which are well above the requirements of the FSA.

The policy defines bands for solvency capital coverage. An annual capital plan is drawn up, in which the banding and targets for solvency capital coverage are defined for the plan period, which is normally three years. It also defines the measures that can or should be taken at different levels of capital adequacy.

In the current plan period, KLP and KLP Skadeforsikring AS both have a goal of having capital adequacy of over 150 per cent. The companies meet the requirement with a good margin.

KLP applies the transitional rule for technical provisions, but the Group sets targets for capital adequacy without using this. For the same reason, capital adequacy is reported without using the transitional rule in notes to the companies' and the KLP Group's accounts. The Group's capital adequacy without using the transitional rules for technical provisions is 261 per cent at 31.12.2020, well above its own target of 150 per cent, which is in turn well above the official requirements. Capital adequacy using the transitional rule for technical accruals was 332 per cent for the Group.

KLP's articles of association allow it to call in capital from its owners. The Company also collects an annual capital contribution from its owners. For 2020 the equity contribution was 0.30 per cent of the premium reserve.

The Tier 1 and 2 capital is classified in three capital groups based on the characteristics of each capital entry. Quality and availability are crucial for the classification. The main breakdown is based on whether

- The capital can be used for or paid in on demand to cover any loss at any time
- The capital can be used to cover losses and will not be refunded until all other claims have been covered, including claims arising out of insurance and reinsurance contracts.

Tier 1

The Company's unrestricted Tier 1 regulatory capital is made up of equity contributed in KLP, share capital in KLP Skadeforsikring, the share premium reserve in KLP Bedriftspensjon AS, and a reconciliation reserve for the Group. The reconciliation reserve ensures that the difference between assets and liabilities in the Solvency II balance-sheet is reflected in Tier 1 and 2 capital. The hybrid Tier 1 perpetual capital is also included in Tier 1 (restricted). To cover the Solvency Capital Requirement at Group level, participations in KLP Banken AS and KLP Kapitalforvaltning AS are deducted and replaced with these companies' Tier 1 and 2 capital calculated according to relevant sector-level rules. All Tier 1 capital is classed as own funds.

Tier 2

Tier 2 capital includes subordinated debt and provisions to the natural perils pool fund as own funds. KLP has also been granted the right under its Articles of Association to call in capital as supplementary capital, as long as the conditions are met. This supplementary capital is calculated as 2.5 per cent of KLP's total premium reserve at any given time, with approval for this method granted until 31.12.2023. Approval from the Financial Supervisory Authority of Norway was granted on 14.06.2019.

Tier 3

Tier 3 includes any net deferred tax asset, with some restrictions. At year-end 2020 and year-end 2019, this was zero for the Group.

The hybrid Tier 1 perpetual capital (JPY 15 billion) with a Solvency II value of NOK 1.764 billion at 31.12.2020, has a fixed USD interest rate of 5.07 per cent per year. The loan is perpetual, but KLP has the right to repay it by 28.04.2034. If KLP does not exercise its right to repay in 2034, the loan will move onto floating interest. The credit margin will then increase by 1 percentage point to 6-month JPY LIBOR interest + a margin of 3.30 per cent per year. The loan was issued on 22.04.2014.

The subordinated loan (EUR 600 million), with a Solvency II value of NOK 3.340 billion at 31.12.2020, has a fixed interest rate of 4.25 per cent per year. The loan was issued on 10.06.2015 and is time-limited to mature in 2045. In 2020, the Company effected a buy-back of the loan to the tune of EUR 306 million of the nominal value. The loan can be repaid by KLP after 10 years, and on each interest payment date from then until the maturity date. The debt is listed on the London Stock Exchange.

The Solvency II rules lay down requirements for the composition of Tier 1 and 2 capital to cover the solvency capital requirement and the minimum capital requirement. This is known as eligible Tier 1 and 2 capital.

E.1.1 Classification of Tier 1 and 2 capital able to cover the Solvency Capital Requirement

The Tier 1 and 2 capital to cover the solvency capital requirement at year-end 2020 and year-end 2019 was composed as shown in table 15. The calculations of the technical provisions are with transitional rules.

Table 15: Classification of own funds for the Group. Figures in NOK billions.

Eligible Tier 1 and 2 capital to cover the SCR	31.12.2020	31.12.2019
Unrestricted capital	44.9	37.7
Hybrid Tier 1 perpetual capital	1.7	1.7
Deduction for participations in financial institutions	-2.7	-2.5
Tier 1 and 2 capital in financial institutions	2.7	2.5
Total Tier 1 capital	46.6	39.3
Total eligible Tier 1 capital	46.6	39.3
Subordinated debt	3.3	6.4
Risk equalisation fund	0.0	0.0
Natural perils pool fund	0.2	0.2
Supplementary capital	11.4	11.5
Total Tier 2 capital	14.9	18.2
Total eligible Tier 2 capital	7.7	7.5
Deferred tax assets	0.0	0.0
Total Tier 3 capital	0.0	0.0
Total eligible Tier 3 capital	0.0	0.0
Eligible Tier 1 and 2 capital able to cover the Solvency Capital Requirement	54.3	46.8

Unrestricted capital is the difference between assets and liabilities in the Solvency II balance-sheet (NOK 45.1 billion) minus the natural perils fund (NOK 0.2 billion) and adjusted for ownership in financial institutions. This totalled NOK 46.6 billion at 31.12.2020.

Restricted capital cannot exceed 20 per cent of the total of the items in Tier 1. The hybrid Tier 1 perpetual capital is well below this limit.

The sum of eligible capital in Tiers 2 and 3 may not exceed 50 per cent of the Solvency Capital Requirement either. For the Group, this had a limiting effect at year-end 2020 and at year-end 2019. In the event of an increase in the Solvency Capital Requirement, the unused Tier 2 capital will significantly reduce the negative effect on capital adequacy.

E.1.2 Classification of own funds able to cover the minimum required to meet the Solvency Capital Requirement for the Group

The own funds to cover the minimum capital requirement at year-end 2020 and year-end 2019 was composed as shown in table 16 below. The calculations of the technical provisions are with transitional rules.

Table 16: Classification of Tier 1 and 2 capital for the Group. Figures in NOK billions.

Eligible Tier 1 and 2 capital to cover the MCR	31.12.2020	31.12.2019
Unrestricted capital	44.9	37.7
Hybrid Tier 1 perpetual capital	1.7	1.7
Deduction for participations in financial institutions	-2.7	-2.5
Total Tier 1 capital	46.6	36.9
Total eligible Tier 1 capital	46.6	36.9
Subordinated debt	3.3	6.4
Risk equalisation fund	0.0	0.0
Natural perils pool fund	0.2	0.2
Supplementary capital	11.4	11.5
Total Tier 2 capital	14.9	18.2
Total eligible Tier 2 capital	1.5	1.3
Deferred tax assets	0.0	0.0
Total Tier 3 capital	0.0	0.0
Total eligible Tier 3 capital	0.0	0.0
Eligible Tier 1 and 2 capital able to cover the minimum SCR	48.1	38.2

Restrictions on capital in group 1 are as described in section E.1.1.

The sum of eligible capital in Tiers 2 and 3 may not exceed 20 per cent of the minimum Solvency Capital Requirement either. For the Group, this had a limiting effect at year-end 2020 and at year-end 2019. In the event of an increase in the minimum Solvency Capital Requirement, the unused Tier 2 capital will reduce the negative effect on capital adequacy significantly.

E.1.3 Differences between equity reported in the Company's accounts and the balance of assets and liabilities under Solvency II

The difference between equity in the accounts and the balance of assets and liabilities in the Solvency II balance-sheet for the KLP Group at year-end 2020 and 2019 was as shown in Table 17 below:

Table 17: Total equity in the accounts and difference between the assets and liabilities under Solvency II. Figures in NOK billions.

KLP Group	31.12.2020	31.12.2019
Paid-up equity	18.2	16.5
Accrued equity	21.2	20.8
Total owners' equity	39.4	37.3
Balance of assets and liabilities under Solvency II	45.0	37.9
Difference	5.6	0.6

The temporary deduction in technical provisions under Solvency II means that technical provisions were valued differently from the technical provisions in the accounts for the life insurance business. The difference between equity in the accounts and the balance of assets and liabilities under Solvency II in 2020 comes from added value in interest-bearing portfolios reported at amortised cost, and deferred tax. There are also smaller contributions from differing valuations of financial liabilities and technical provisions for non-life insurance and the fact that intangible assets are valued at zero in the Solvency II balance-sheet.

E.2 Solvency Capital Requirement and minimum required to meet the Solvency Capital Requirement for the Group:

E.2.1 Solvency Capital Requirement

At year-end 2020, the capital requirements were as follows:

Minimum required to meet the Solvency Capital Requirement for the Group: NOK 7.0 billion
Solvency Capital Requirement: NOK 16.3 billion

The capital requirements above include transitional rules for technical provisions.

The Group uses the standard formula without any company-specific parameters. The Solvency Capital Requirement at year-end 2019 and 2018 was broken down as shown in table 18 below.

Table 18: Composition of the solvency capital requirement with transitional rules for technical provisions. Figures in NOK billions.

KLP Group	31.12.2020	31.12.2019
Market risk	4.4	4.1
Counterparty risk	0.1	0.2
Underwriting risk	11.4	11.2
Health-related underwriting risk	0.0	0.3
Non-life underwriting risk	0.4	0.4
Diversification	-3.2	-2.9
Operational risk	2.7	2.6
Loss-absorption capacity for deferred tax	-0.8	-1.0
Capital requirements for KLP Banken and KLP Kapitalforvaltning	1.1	1.0
Solvency Capital Requirement	16.3	15.9

The reduction in the solvency capital requirement is mainly due to increased loss absorption capacity for deferred tax.

E.2.2 Simplified processes

The Group uses the simplifications to the counterparty risk module described in Articles 111 and 112 of the Norwegian Regulation laying down supplementary rules to the Solvency II Regulation.

The simplification in Article 111 means that diversification effects within a module are not taken into account in calculating the risk-reducing effects of derivatives. The simplification in Article 112 means that the risk-adjusted value of a security is set to 75 per cent across the board. Both simplifications are used to make the calculation work easier and produce insignificant increases in the capital requirement for counterparty risk.

E.2.3 Company-specific parameters

The Group does not use any company-specific parameters.

E.2.4 Minimum required to meet the Solvency Capital Requirement for the Group

The amount for the Group's minimum solvency capital requirement is made up of the minimum solvency capital requirements for KLP and KLP Skadeforsikring AS. At the end of 2020 and of 2019 this was made up as shown in table 19 below.

Table 19: Composition of minimum solvency capital requirements with transitional rules for technical provisions. Figures in NOK billions.

Minimum consolidated group solvency capital requirement	31.12.2020	31.12.2019
Minimum capital requirement for KLP	6.8	6.1
Minimum capital requirement for KLP Bedriftspensjon		0.1
Minimum capital requirement for KLP Skadeforsikring	0.4	0.4
Minimum solvency capital requirement - MSCR	7.0	6.5

E.3 Use of the duration-based equity risk sub-module in the calculation of the Solvency Capital Requirement

The Group does not use the duration-based sub-module for equity risk.

E.4 Differences between the standard formula and any internal models used

The Group does not use internal models.

E.5 Non-compliance with the Solvency Capital Requirement

The Group satisfies both the Solvency Capital Requirement and the minimum amount required to meet the Solvency Capital Requirement for the Group.

E.6 Other information

Developments in the capital situation since the end of the year are described in the individual companies' Solvency and Financial Condition Reports.

Approval

The report was approved by the Board of Directors of KLP on 18 March 2021.

Sverre Thornes, CEO

Templates

The following QRTs (quantitative reporting templates) are included below.

QRT code	QRT name
S.01.02.04	General information about the Group
S.02.01.01	Financial position statement
S.05.01.01	Premiums, claims and costs by insurance sector
S.05.02.01	Premiums, claims and costs by country
S.22.01.04	Effect of transitional rules and other measures related to long-term guarantees
S.23.01.04	Tier 1 and 2 capital
S.25.01.04	Solvency capital requirements - for groups using the standard method
S.32.01.04	Companies included in the group

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