

CAPITAL ADEQUACY AND
RISK MANAGEMENT REPORT 2010
PILLAR 3

NIBC HOLDING

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Introduction

Goal and overview

NIBC's Capital Adequacy and Risk Management (Pillar 3) Report contains information that enables an assessment of the risk profile and capital adequacy of NIBC Holding N.V. This publication fulfils the requirements of the Basel II framework, as stipulated in the *Capital Requirements Directive (CRD)*. The CRD is legally enforced by Dutch law by the Financial Supervision Act (Wet Financieel Toezicht).

The CRD is based on the Basel II framework, which contains three pillars:

- Pillar 1 defines the regulatory minimum capital requirements by providing rules and regulations for the measurement of credit risk, market risk and operational risk. These capital requirements need to be covered by regulatory own funds. NIBC received approval from the *Dutch Central Bank (DNB)* to use, as of 1 January 2008, the *Advanced Internal Ratings Based (AIRB)* approach for calculating solvency requirements regarding credit risk for its most important exposure classes, namely corporate and retail, and the *Internal Model Approach (IMA)* regarding market risk in the Trading book. Furthermore, NIBC uses the internal ratings-based method for the securitisation exposure class and the simplified risk-weight approach for the equity exposure class. Solvency requirements for the remaining portfolios and for operational risk are calculated using the Standardised approach.
- Pillar 2 covers the Supervisory Review Process. This consists of the *Internal Capital Adequacy Assessment Process (ICAAP)*, the bank's own assessment of its capital adequacy in relation to all its risks, and the *Supervisory Review and Evaluation Process (SREP)*, the response of the Supervisor to the institution's ICAAP.
- Pillar 3 focuses on disclosure requirements, covering all relevant pieces of information for a market participant to assess the risk profile and capital adequacy of the credit institution. The risk disclosures are connected to the first pillar of the Basel II framework, as information is provided regarding the underlying exposures, risk weighted assets and regulatory capital.

NIBC's Capital Adequacy and Risk Management Report is prepared to meet the requirements of Pillar 3, as well as the increased need for transparency in the financial market. The Capital Adequacy and Risk Management Report follows the structure below:

- Risk management strategy & process
- Credit risk
- Market risk
- Operational risk
- Liquidity risk
- Securitisation exposures
- Internal capital adequacy assessment process
- Capital base components
- Capital adequacy

The scope of application in this report refers to NIBC Holding, henceforth referred to as NIBC. The main entity of NIBC Holding is NIBC Bank. Where necessary, a distinction between NIBC Holding and NIBC Bank is made explicitly. The starting point of the Basel II prudential scope of application is the consolidation scope of

NIBC, according to the *International Financial Reporting Standards (IFRS)*. In line with the requirements of the CRD, a prudential filter is applied for non-financial subsidiaries. These entities are excluded from the consolidation scope and are, instead, treated as investments in associates. Appendix 1 provides further details regarding the consolidation scope.

The credit exposures in this report are not directly comparable to the numbers in the Annual Report. The numbers in the Annual Report refer to book values and classifications in line with IFRS requirements. The numbers in this report refer to *exposure at default (EAD)*, which is a risk measure of the potential amount outstanding in the event of default. EAD is, therefore, a different measure than on- and off-balance sheet amounts, and the method employed for its calculation differs per exposure class. A more detailed explanation on EAD can be found in the Credit Risk chapter.

NIBC's Risk Management and Capital Adequacy (Pillar 3) Report is produced at least on an annual basis and is published on NIBC's website (www.nibc.com). The report may also be published more frequently if special market circumstances require so. Information regarding risk management and key data on capital adequacy are presented in NIBC's Annual Report as well.

Risk Management Strategy & Process

Highlights of 2010

The financial crisis drastically changed risk priorities. Where the pre-crisis emphasis was on credit, market and operational risk, our Risk Management department's top priority also became liquidity risk in 2009 and remained so in 2010.

We have significantly reduced our exposure to market risk since 2007. We reduced our already conservative appetite for credit risk in anticipation of a severe economic recession. Timely steps such as these have ensured our risk profile to remain healthy.

Next to liquidity risk, Risk Management's other main area of focus in 2010 was credit risk – the selective acceptance and intensive supervision of distressed exposure. We rigorously assess risks before accepting new exposures.

Nevertheless, impairments have been an inevitable by-product of the economic downturn, for NIBC as well as for our peers. Additions to impairments were significantly lower in 2010 than in 2009.

We have access to liquidity through our retail savings programme NIBC Direct in the Netherlands and Germany. This now represents some 19% of our total funding. We further diversified our funding position in 2010 with the successful public issue of Dutch MBS XV, a EUR 750 million residential mortgage-backed securitisation, and the private placement of EUR 1 billion of triple-A rated residential mortgage-backed notes.

With the financial world remaining in constant flux, there are continuous new insights into risk management. In response, we adapted our Risk Management organisation in 2010. We revamped our operational risk unit to create synergies, combining internal control, business continuity, information security and operational risk.

Following on from our creation in 2009 of a dedicated Financial Markets Credit Risk department, we adapted our market risk models last year to reflect changes in the market risk environment. We further developed our modelling of economic capital and improved our assessments of the creditworthiness of financial counterparties. We allocated more dedicated focus on country risk, despite our moderate country risk exposure.

In line with the risk management practice of previous years, NIBC's sovereign exposure consists in its vast majority of cash placed with the Dutch Central Bank and the Dutch State Treasury Agency. NIBC has zero sovereign exposure to Greece, Italy, Ireland, Spain and Portugal.

Risk appetite and risk management strategy

NIBC has a clearly defined business model around two strategic pillars – Merchant Banking and Specialised Finance – focusing on mid-sized corporate clients in the Benelux and Germany, as well as being a meaningful player in a select number of asset classes. Indispensable to those pillars and the entire business of NIBC are the Treasury, Risk Management and Corporate Center departments. Because of its focus and the in-depth understanding of the business and its clients, NIBC has good understanding of the risks in this select number of markets. The risk strategy of NIBC is aligned with this business model, resulting in the following markets and portfolios, where the risks are concentrated:

- Credit risk in the Corporate Loan portfolio in six different asset classes (Commercial Real Estate, Infrastructure & Renewables, Shipping, Corporate Lending, Leveraged Finance and Oil & Gas Services) and in the Residential Mortgage portfolio (consisting of Dutch and German residential mortgages). Further, credit risk exists also in the Investment Management loan portfolio. Investment Management loans are originated and monitored by the Investment Management BU (part of Merchant Banking) and may contain equity characteristics such as attached warrants or conversion features. Examples of this exposure include mezzanine loans, convertible loans and shareholder loans. Finally, credit risk exists in derivatives and cash management activities of NIBC;
- Investment risk in equity investments;
- Market risk in the Treasury portfolios, mainly consisting of interest rate risk in the Trading¹ and Mismatch portfolio, and credit spread risk in the Debt Investments portfolio. The latter consists of the Securitisations portfolio and the portfolio of debt investments in financial institutions, corporate and sovereign entities. Note that in 2010, NIBC held zero debt investments in sovereign entities.

The business model described above is also reflected in the Economical Capital framework, which is further described in the section *Internal Capital Adequacy Assessment Process*. NIBC uses Economical Capital as a universal risk measure throughout the company. For each business activity, Economical Capital is allocated and reported to the Asset & Liability Committee (**ALCO**) once every two weeks.

Risk management processes and governance

Under the supervision of the Managing Board and the Risk Policy Committee of the Supervisory Board, formal authority and ultimate decision-making in respect of risk management matters is the responsibility of four committees: the *Risk Management Committee (RMC)*, the *Asset & Liability Committee (ALCO)*, the *Transaction Committee (TC)* and the *Investment Committee (IC)*. These committees are chaired by the Chief Risk Officer (**CRO**) and ensure that assessment and acceptance of credit, market, investment and liquidity risk exposure is made independently of the business originators within the operating segments.

The RMC determines the overall risk appetite and risk profile at a strategic level, evaluates new activities and products on client suitability and the bank's operational and risk management capabilities, as well as reviews risks at portfolio level, sets country risk and sector limits, approves acceptance policies and guidelines, new products, risk policies and manuals. Three members of the Managing Board are members of the RMC, which also includes representatives from the TC and the ALCO. As necessitated by the topics to be discussed, specialists in certain areas are also invited to the meetings of the RMC. The RMC meets once a month.

¹ This report uses the terms *Trading book* and *Trading portfolio* interchangeably.

The ALCO monitors the development of NIBC's balance sheet and market risk profile. The ALCO monitors traded market risks, exposure to interest rates and currency risks, the capital structure and liquidity position. The ALCO also approves large funding transactions such as securitisations and sets overall limits on market risk exposures. The ALCO receives reports on all breaches of risk limits. Three members of the Managing Board are members of the ALCO. The ALCO meets once every two weeks.

The TC, NIBC's credit committee, makes decisions on individual debt transactions, including terms and conditions for lending and the acceptance of derivative counterparty exposures and underwriting strategies. It also evaluates opportunities for potential subsequent distribution of the asset. The TC sets counterparty exposure limits, monitors exposure and decides on impairments. Three members of the Managing Board are members of the TC. Meetings of the TC take place twice a week.

The IC is responsible for investment risk. The IC approves transactions with respect to equity, Investment Management loans and subordinated debt exposures, as well as impairments and revaluations for these assets. Two members of the Managing Board are members of the IC. The IC meets, in principle, once every two weeks. Investment decisions of the Funds managed by Investment Management are made by the Investment Committees of the various Funds.

In addition to the above risk management committees, there is also the *Engagement and Compliance Committee (ECC)*, which is responsible for the prevention of potential commercial conflicts of interest and compliance issues in evaluating potential assignment for clients. All five members of the Managing Board are member of the ECC.

Overlap of committee membership among Managing Board members contributes to consistency in communication and decision-making.

The CRO is supported by centralised risk management functions, which consist of four risk management departments, the Credit Risk Management department, the Asset & Liability Management and Market Risk department, the Financial Markets Credit Risk and Risk Policy & Reporting department and the Operational Risk Management department. These departments support the various risk management committees dedicated to monitoring the different risk categories NIBC faces.

The *Credit Risk Management department (CRM)* is responsible for the credit risk management of the Corporate Loan portfolio. CRM develops and implements policies and procedures regarding credit risk, advises on credit proposals, reviews, waivers and amendments, and reviews impairments. Furthermore, CRM validates NIBC's internal counterparty credit ratings and loss given default ratings. The *Distressed Assets department (DA)* is a sub-department of CRM. DA manages assets which are defaulted and/or impaired, or at significant risk of becoming defaulted and/or impaired. Credit risk management of the Investment Management loans, as well as investment risk management of the private equity positions are the responsibility of the IC or the Investment Committee of one of the NIBC Funds (depending on whether the specific Investment Management loan or equity position is part of NIBC's direct portfolio or part of one of the NIBC Funds).

The *Asset & Liability Management department (ALM)* manages balance sheet and liquidity risk and supports NIBC's asset and liability management policies, as established by the ALCO. Additionally, ALM is responsible for the market risk management of the Residential Mortgage portfolio, contacts with rating agencies, model validation and parts of quantitative risk modelling.

The *Market Risk department (MR)* is responsible for monitoring the market risk of the Treasury activities, both inside and outside the trading book. MR also manages the bank-wide currency position and co-ordinates the ongoing compliance with the Basel II regulation, including new legislation.

The *Financial Markets Credit Risk department (FMCR)* is responsible for managing issuer and counterparty credit risk resulting from NIBC's Treasury activities and financial market product execution, such as over-the-counter derivatives with financial institutions and corporate entities. FMCR develops and implements policies and procedures regarding credit risk related to financial markets products, and advises on counterparty credit limits and issuer limits for financial institutions and corporate entities. Furthermore, FMCR is responsible for implementing and managing country risk limits across NIBC.

The *Risk Policy & Reporting department (RP&R)* is a sub-department of FMCR and monitors risk on portfolio level. RP&R develops policies and methods for measuring risk, notably the credit rating system used to evaluate probability of default and loss given default in NIBC's credit portfolio. RP&R is also responsible for the reporting of credit portfolio information to various users within and outside NIBC. RP&R is pivotal in NIBC's Basel II process and also performs parts of quantitative risk modelling.

The *Operational Risk Management department (ORM)* is responsible for monitoring and managing operational risk stemming from NIBC's business and operational practices. ORM co-ordinates the New Product Approval Process and the bank-wide process of new activities with respect to the assessment of operational, risk management, compliance and reporting capabilities and into the RMC for final product approval.

Credit Risk

NIBC defines credit risk as the current or potential threat to the company's earnings and capital as a result of a counterparty's failure to make required debt or financial payments on a timely basis or to comply with other conditions of an obligation or agreement, including the possibility of restrictions on or impediments to the transfer of payments from abroad.

Credit risk at NIBC exists in different shapes and forms. Almost every activity at NIBC is related to credit risk: credit risk is present in the Corporate Loan portfolio, the Residential Mortgage portfolio, the Debt Investments portfolio, cash management and derivatives. Credit risk is also present in NIBC's portfolio of Investment Management loans. It is the largest source of risk to which NIBC is exposed, representing approximately 95% of total *Risk Weighted Assets (RWA)* and of the company's capital requirements. Specifically for the Debt Investments portfolio, NIBC defines the credit risk as issuer risk, which is the credit risk of losing the principal amount on products like bonds and CDS positions (where it concerns sold protection).

The Pillar 3 disclosure requirements prescribe that a credit institution classifies its assets into a number of standard exposure classes. For a credit institution using the AIRB approach, these exposure classes are defined in article 86 of the CRD. Table 1 presents the relationship between the classification in this report and the portfolios in NIBC's Annual Report:

Table 1 Comparison between Pillar 3 exposure classes and portfolios in NIBC's annual report

Pillar 3 exposure classes	Portfolios in Annual Report
Sovereign Institutions	Debt investments in sovereign entities and cash at central banks.
Corporate	Debt investments in financial institutions, and cash and derivative transactions with financial institutions.
Retail Equities	Corporate Loan portfolio, including guarantees, derivatives and debt investments in corporate entities, and Investment Management Loan portfolio.
Securitisations	Dutch and German Residential Mortgage portfolio, excluding securitised portfolios.
Other	Equity investments and uncalled capital commitments.
	Securitisation portfolio and retained notes of own securitisations.
	Non-credit related exposures.

Apart from the above differences in classification, differences can also be found between the numbers presented in this report and the numbers in the risk paragraph and risk notes in NIBC's Annual Report. The main reasons that these numbers are not directly comparable are the following:

- For exposures treated under the AIRB approach, Pillar 3 numbers refer to EAD, a risk measure of the potential outstanding amount in the event of default. Counterparties typically tend to utilise their credit lines more intensively when approaching default, which implies that the amount outstanding at default is expected to be higher than the current outstanding amount.
- For undrawn parts of credit facilities, a credit conversion factor is applied on the Pillar 3 numbers, which cannot be recognised on the balance sheet. This credit conversion factor is incorporated in the calculation of EAD.
- For derivative transactions, Pillar 3 numbers refer to the market value and add-on, including the effect of netting and collateral.

Credit risk exposures

This section presents NIBC's credit risk exposures based on the definitions and approaches that are used in the calculation of capital requirements. In 2007, NIBC received approval by the DNB to use, as of 1 January 2008, the AIRB approach for the calculation of its capital requirements for the corporate and retail exposure classes. Furthermore, NIBC uses the internal ratings-based method for the securitisation exposure class and the simplified risk-weight approach for the equity exposure class. The AIRB approach is the most sophisticated approach within the Basel II framework for the calculation of capital requirements and it is based on internal estimation of various risk parameters. The section *Calculation of Risk Weighted Assets* in this chapter provides more information on the ways that NIBC uses for the estimation of these parameters.

The Standardised approach applies to all other NIBC exposure classes containing credit risk.

Table 2 shows a breakdown of exposure, EAD, RWA and capital requirement per exposure class and calculation approach, as at 31 December 2010 and 2009.

Table 2 Breakdown of exposure, EAD, RWA and capital requirement for credit risk

IN EUR MILLIONS	2010				2009			
	Exposure	EAD	RWA	Capital requirement	Exposure	EAD	RWA	Capital requirement
AIRB APPROACH								
- of which corporate	9,625	9,434	6,340	507	8,425	8,356	5,206	417
- of which retail	5,066	5,066	789	63	4,573	4,573	624	50
- of which securitisations	1,461	1,461	1,055	84	1,076	1,106	892	71
- of which equities	540	540		160	501	501	1,847	148
SUBTOTAL	16,692	16,502	10,184	815	14,575	14,536	8,569	686
STANDARDISED APPROACH								
- of which institutions	2,453	2,309	703	56	4,146	3,993	775	62
- of which sovereign	1,644	1,644	2	0	1,864	1,864	0	0
- of which corporate	626	625	625	50	760	737	737	59
- of which retail	507	507	222	18	576	576	248	20
- of which equities	4	4	3	0	49	49	24	2
- of which other	62	62	62	5	92	92	92	7
SUBTOTAL	5,296	5,151	1,617	129	7,487	7,311	1,876	150
TOTAL CREDIT RISK	21,988	21,653	11,801	944	22,062	21,847	10,445	836

Small differences are possible in the table due to rounding

The RWA of NIBC increased by 13% between 2009 and 2010 and this is due to a variety of factors.

The RWA for the corporate exposure class increased by 17%, mainly due to the increase in the size of this portfolio. Furthermore, NIBC introduced a change in methodology for calculating RWA on defaulted, non-impaired exposures, a fact that increased RWA consumption. The increase in the size of the Corporate Loan portfolio is the most important driver for the absolute increase in the RWA in 2010.

The total RWA for the retail exposure class increased by 16% compared to 2009, mainly due to two factors. Firstly, the risk parameters used in the Basel II Advanced IRB model have become more conservative, causing an increase in RWA. Secondly, the expiration of two own securitisations has increased the pool of mortgages that get a retail exposure class treatment under Basel II.

The RWA consumption of the securitisation exposure class increased by 18%. As for the corporate class, this shift is also due to the increase in the size of the Securitisation portfolio through new investments mainly in the Liquidity Investments Portfolio, as well as the retained positions in NIBC's newly issued securitisations.

The increase of 7% in the RWA of the equity exposure class is due to the increase in the size of the Equity Investments portfolio, predominantly by appreciation of the existing portfolio. Finally, the RWA for the sovereign exposure increased marginally, from zero to 2 million.

On the other hand, RWA for institutions decreased by 9%. The decrease of the institutions exposure class is related to the decrease in the size of NIBC's Debt Investments portfolio.

Breakdown of credit risk exposures

Table 3 shows a breakdown of EAD between exposure classes and exposure types under both the AIRB and the Standardised approach, as at 31 December 2010. Table 4 shows a similar breakdown during 2010 on average.

Table 3 Breakdown of credit EAD types by exposure class, 31 December 2010

IN EUR MILLIONS				
Exposure Class	On-Balance	Off-Balance	Derivatives	Total
AIRB APPROACH				
- of which corporate	7,401	1,574	459	9,434
- of which retail	5,064	1	0	5,066
- of which securitisations	1,388	2	71	1,461
- of which equities	469	71	0	540
SUBTOTAL	14,323	1,649	530	16,502
STANDARDISED APPROACH				
- of which institutions	1,722	118	469	2,309
- of which sovereign	1,644	0	0	1,644
- of which corporate	318	79	228	625
- of which retail	507	0	0	507
- of which equities	4	0	0	4
- of which other	62	0	0	62
SUBTOTAL	4,257	196	698	5,151
TOTAL	18,580	1,845	1,228	21,653

Small differences are possible in the table due to rounding

Table 4 Breakdown of credit EAD types by exposure class, average 2010

IN EUR MILLIONS				
Exposure Class	On-Balance	Off-Balance	Derivatives	Total
AIRB APPROACH				
- of which corporate	7,150	1,314	431	8,895
- of which retail	4,816	4	0	4,819
- of which securitisations	1,220	1	63	1,284
- of which equities	432	89	0	521
SUBTOTAL	13,618	1,407	494	15,519
STANDARDISED APPROACH				
- of which institutions	2,157	109	885	3,151
- of which sovereign	1,754	0	0	1,754
- of which corporate	417	66	198	681
- of which retail	542	0	0	542
- of which equities	27	0	0	27
- of which other	77	0	0	77
SUBTOTAL	4,974	175	1,082	6,231
TOTAL	18,591	1,582	1,576	21,750

Small differences are possible in the table due to rounding

Table 5 shows the breakdown of EAD between regions. The geographical distribution of NIBC's assets corresponds to the company's strategy for focus in North Western Europe, with the Netherlands, the UK and Germany accounting for more than 80% of the total EAD. This percentage increases to 90% when the rest of Europe is included. With respect to corporate exposures, the Asia/Pacific region mainly contains NIBC's exposures to the shipping and oil & gas sectors. Exposures to the oil & gas sector are also located in North America, as well as in the region 'Other', mainly in the United Arab Emirates and Brazil.

Table 5 Breakdown of EAD per region, 31 December 2010

IN EUR MILLIONS								
Exposure Class	The Netherlands	United Kingdom	Germany	Rest of Europe	Asia / Pacific	North America	Other	Total
AIRB APPROACH								
- of which corporate	3,178	1,886	1,604	1,148	910	356	353	9,434
- of which retail	5,066	0	0	0	0	0	0	5,066
- of which securitisations	813	157	45	303	3	124	17	1,461
- of which equities	444	8	16	44	0	28	0	540
SUBTOTAL	9,500	2,051	1,665	1,495	913	508	369	16,502
STANDARDISED APPROACH								
- of which institutions	520	862	115	378	50	329	54	2,309
- of which sovereign	1,624	0	0	15	0	0	4	1,644
- of which corporate	377	89	97	33	0	28	0	625
- of which retail	23	0	484	0	0	0	0	507
- of which equities	1	0	0	0	0	2	1	4
- of which other	62	0	0	0	0	0	0	62
SUBTOTAL	2,608	951	697	426	50	359	60	5,151
TOTAL	12,109	3,002	2,362	1,921	963	867	429	21,653
TOTAL (in %)	56%	14%	11%	9%	4%	4%	2%	100%

Small differences are possible in the table due to rounding

Table 6 shows the breakdown of EAD between industry sectors. The sector with the highest EAD is retail markets (30% of total EAD), which contains NIBC's Residential Mortgage portfolios in the Netherlands and Germany, and securitisation notes of residential mortgage-backed securities.

The next largest sector is financial services (15% of total EAD), which contains all of NIBC's institutions exposure class, as well as a few corporate exposures. More than half of the corporate EAD in this sector relates to a loan to an investment-grade financial institution, collateralised by a pool of prime Dutch residential mortgages.

The commercial real estate sector (12% of total EAD) is spread over a variety of property financing. The main real estate class is residential commercial property financing, which accounts for almost half of the commercial real estate sector in the corporate exposure class. This type of financing significantly reduces the concentration risk in the underlying collateral pool. Other types of financing include offices, retail properties, hotel financing and construction financing. About 13% of the commercial real estate portfolio consists of financing of miscellaneous properties, including mixed use and industrial properties. In terms of geographical distribution, approximately 95% of the commercial real estate portfolio is located in the Netherlands and Germany, and the remainder in other EU countries.

The sector government/central banks (7% of total EAD) is made up exclusively of NIBC's sovereign exposures. The vast majority of these exposures are related to cash placed with the Dutch Central Bank and the Dutch State Treasury Agency. NIBC has zero sovereign exposure to Greece, Italy, Ireland, Spain and Portugal.

Exposures to the shipping industry (7% of total EAD) include the four main shipping sub-sectors tankers, bulk carriers, container boxes and container vessels, which account for approximately 80% of the entire Shipping portfolio. The remainder of this portfolio includes, among others, financing of car and LNG carriers. Shipping exposures are well diversified between different countries, of which European Union countries (including the Netherlands, the UK and Germany) account for approximately one third of Shipping portfolio's EAD, Asia/Pacific for approximately 40% and North America for almost 15%. More than two thirds of the entire exposure of NIBC to the Asia/Pacific region relates to Shipping assets; the remainder relates to oil & gas project finance.

Table 6 Breakdown of EAD per industry sector, 31 December 2010

IN EUR MILLIONS														
Exposure Class	Retail Markets	Financial Services	Commercial Real Estate	Infra-structure	Government / Central Banks	Shipping	Wholesale / Retail/Leisure	Oil & Gas	Manu-facturing	Services	Agriculture & Food	TMT	Other	Total
AIRB APPROACH														
- of which corporate	0	806	1,939	2,122	0	1,534	714	849	602	427	210	168	63	9,434
- of which retail	5,066	0	0	0	0	0	0	0	0	0	0	0	0	5,066
- of which securitisations	815	0	403	0	0	0	0	0	0	0	0	0	243	1,461
- of which equities	0	40	39	106	0	17	152	0	37	38	0	38	74	540
SUBTOTAL	5,881	846	2,382	2,228	0	1,550	866	849	640	464	210	206	380	16,502
STANDARDISED APPROACH														
- of which institutions	0	2,309	0	0	0	0	0	0	0	0	0	0	0	2,309
- of which sovereign	0	30	0	0	1,614	0	0	0	0	0	0	0	0	1,644
- of which corporate	0	76	227	12	0	20	14	0	18	9	17	6	225	625
- of which retail	507	0	0	0	0	0	0	0	0	0	0	0	0	507
- of which equities	0	4	0	0	0	0	0	0	0	0	0	0	0	4
- of which other													62	62
SUBTOTAL	507	2,420	227	12	1,614	20	14	0	18	9	17	6	287	5,151
TOTAL	6,388	3,266	2,609	2,240	1,614	1,570	880	849	658	473	227	212	667	21,653
TOTAL (in %)	30%	15%	12%	10%	7%	7%	4%	4%	3%	2%	1%	1%	3%	100%

Small differences are possible in the table due to rounding

Other important industry sectors in NIBC's corporate exposure class are infrastructure, wholesale/retail/leisure and oil & gas, which together account for 18% of total EAD. These industry sectors contain exposures that

mainly stem from the business lines of Infrastructure & Renewables, Oil & Gas Services, Corporate Lending and Leveraged Finance. From a geographical point of view, all these business lines are concentrated in North Western Europe; as also mentioned previously, Oil & Gas Services also has exposures in North America, Asia/Pacific and the 'Other' region, mainly in the United Arab Emirates and Brazil.

Table 7 provides a breakdown of credit EAD per maturity. More than 45% of all of NIBC's credit risk exposures will mature after the next 5 years.

Table 7 Breakdown of credit risk EAD per maturity, 31 December 2010

IN EUR MILLIONS					
Exposure Class	≤ 1 year	> 1 year - ≤ 2 years	> 2 years - ≤ 5 years	> 5 years	Total
AIRB APPROACH					
- of which corporate	1,260	673	3,714	3,787	9,434
- of which retail	0	1	21	5,043	5,066
- of which securitisations	137	233	681	410	1,461
- of which equities	540	0	0	0	540
SUBTOTAL	1,938	907	4,416	9,240	16,502
STANDARDISED APPROACH					
- of which institutions	572	345	776	615	2,309
- of which sovereign	1,455	114	74	0	1,644
- of which corporate	183	71	209	161	625
- of which retail	507	0	0	0	507
- of which equities	0	0	1	3	4
- of which other	0	0	0	62	62
SUBTOTAL	2,718	530	1,062	841	5,151
TOTAL	4,656	1,437	5,478	10,082	21,653

Small differences are possible in the table due to rounding

Calculation of Risk Weighted Assets

AIRB approach

Ratings and rating process in the AIRB approach

The AIRB approach for the corporate and retail exposure classes has been adopted by NIBC and approved by DNB since 1 January 2008. The ratings framework consists of the calculation of 3 main parameters: *Probability of Default (PD)*, *Loss Given Default (LGD)* and *Exposure at Default (EAD)*.

The PD, LGD and EAD that are calculated through NIBC's internal models are used for the calculation of *expected loss (EL)* and Pillar-1 regulatory capital (**RC**). Internal ratings enable an objective comparison of the credit risk of different types of assets, making them an essential tool for the commercial and risk management departments to determine whether a transaction fits NIBC's strategy and portfolio, as well as to determine an appropriate pricing. *Economic Capital (EC)*, *risk-adjusted return on capital (RAROC)* and stress testing are additional areas, within Pillar 2, which make use of the above-mentioned parameters, although the methodologies for both EC and stress testing differ from those employed in Pillar 1. In particular, a market risk instead of a credit risk approach is used for a number of portfolios in Pillar 2. NIBC has developed a variety of

stress test scenarios, both on total portfolio and sub-portfolio level, to evaluate the impact of the scenarios on its RWAs and Tier-1 ratio. For more information on the differences between NIBC's calculations under Pillar 1 and Pillar 2, refer to the chapter on ICAAP.

NIBC enforces strict separation of responsibilities with respect to its internal rating methodologies and rating process, model development, model validation and internal audit. The roles and responsibilities of each involved unit are explicitly set out in internal policies and manuals, also in conformity with the stipulations of Basel II with respect to model governance.

In addition to these three internally calculated parameters, a fourth parameter which influences the calculation of the Pillar-1 RC is the maturity.

This section explains how the PD, LGD and EAD are applied within the AIRB corporate and retail framework of NIBC.

Corporate

NIBC applies its internally-developed credit rating methodology since 2000. This methodology consists of two elements: a counterparty credit rating that reflects the probability of default of the borrower, and an anticipated loss element that expresses the potential loss on the facility in the event of default of the borrower. All counterparties are reviewed at least once a year.

The basis for both the PD and the LGD methodologies is the application of expert judgement on a number of rating indicators. From a risk perspective, NIBC considers its corporate exposures to fall within four broad financing types (corporate lending, asset finance, acquisition finance and project finance), and for each of these financing types the relevant credit drivers and parameters are captured in the rating models.

In terms of counterparty credit rating, the credit quality is concentrated in the 5 and 6 categories in NIBC's internal rating scale (BB and B categories respectively in external rating agencies' scales). The fact that NIBC's corporate exposures are concentrated in sub-investment grade ratings is counterbalanced by the fact that almost all exposures have some form of collateralisation. Exposures can be collateralised by mortgages on real estate and ships, by (lease) receivables, liens on machinery and equipment, or by third-party guarantees and other similar agreements. As a result, NIBC's LGDs are concentrated in those LGD categories that correspond to recoveries in the range of 80% and 90%, which are relatively high for the banking industry.

Counterparty credit ratings and probability of default

The *counterparty credit rating (CCR)* reflects the counterparty's capacity to meet its financial obligations in full and in time. CCRs do not incorporate any recovery issues, as these are captured through the LGD internal estimates.

NIBC's uses a through-the-cycle CCR rating scale, which consists of 10 grades (1-10). Most of these grades are further divided in notches, by the addition of a plus or minus sign to show the relative standing within the rating grade. NIBC uses a total of 22 notches, each of which is mapped to the rating scale of the main international rating agencies. Each notch carries a PD, which quantifies the likelihood that the counterparty will go into default in the next one year. The CCRs 9 and 10 are assigned to counterparties that have already defaulted and therefore carry a PD of 100%. Furthermore, CCRs are assigned a rating outlook. This assesses the potential direction of the CCR over the medium term. In determining a rating outlook, consideration is given to any changes in the economic and/or fundamental business conditions.

The general methodology for determining a CCR is based on several qualitative and quantitative rating indicators, such as the analysis of the business and financial profile of the counterparty, a cash flow analysis, a sovereign risk analysis, a peer-group analysis and a rating benchmark based on third-party models. Expert judgement is applied at the end of the rating process and determines what the final rating of the counterparty will be, taking into account the rating indicators of the various models.

The performance of the CCR methodology is back-tested annually in order to ensure that consistency is kept throughout the portfolio and to measure the discriminatory power and the ranking ability of the CCRs. Furthermore, NIBC regularly benchmarks its CCRs with external parties. The last benchmark took place in 2009 and generated satisfactory results.

Loss given default

Whereas CCRs are assigned on a counterparty level, LGD ratings are facility-specific. The LGD ratings reflect the loss that can be expected on a facility in a downturn scenario, if a counterparty defaults. NIBC's internal LGD scale consists of 7 grades (A-F) and 10 notches, each of which represents a different degree of recovery prospects and loss expectations.

NIBC's LGD philosophy is similar to the approach for CCRs. The LGD methodology is also based on a combination of qualitative and quantitative rating indicators that include, among others, the assessment of the available collateral and/or guarantees, the seniority of the loan, the applicable jurisdiction, and the quality of the counterparty's assets. Once the various LGD drivers have been assessed, the final LGD rating is based upon expert judgement.

As is the case for CCRs, the maintenance of NIBC's LGD models involves benchmarking and back-testing. NIBC is a founding member of the *Pan-European Credit Data Consortium (PECDC)*, the largest international loan loss data pooling entity. This enables NIBC to exchange anonymous loss data with other large international banks for the purposes of enhancing LGD modelling capabilities, sharing of best practices, LGD calibration and benchmarking.

Exposure at default and credit conversion factor

A third element of the AIRB approach is the calculation of the EAD. It is defined as the amount that is expected to be outstanding at the moment a counterparty defaults. Counterparties typically tend to utilise their credit lines more intensively when approaching default, which implies that the amount outstanding at default is expected to be higher than the current outstanding amount.

In order to quantify the additional expected utilisation, NIBC applies a *credit conversion factor (CCF)* on the undrawn portion of every credit facility. The main driver for the value of the CCF is the type of the credit facility (e.g. committed or uncommitted facility, loan, guarantee, derivative, etc.). NIBC produces its own internal estimates of CCF, based on the utilisation of defaulted credit facilities at the time of default and one year prior to default, which are a combination of internal defaulted facilities and defaulted facilities from the PECDC data pool. These internal estimates are then benchmarked anonymously to external estimates from other PECDC member banks.

Overview of AIRB corporate exposures

Table 8 provides an overview of corporate AIRB EAD types, broken down by NIBC rating grade (equivalent ratings of external rating agencies are provided in parentheses). The table also provides the average PD and LGD, weighted against EAD. As assets with a rating of 9/10 have already defaulted, the notion of LGD as used

for non-defaulted assets is no longer applicable. Losses are therefore estimated through a separate impairment model, in order to determine the impairment amounts.

In the course of 2010 and at the request of the regulator, NIBC implemented a more refined methodology for the calculation of RWA for the defaulted EAD. Whereas RWA and RC for the non-defaulted corporate exposures are calculated based on the standard Basel AIRB formula, the RWA and RC for the defaulted corporate exposures are a function of the impairment amount, if present, and the proportion of the impairment amount to the defaulted EAD. The introduction of this methodology caused an increase in the RWA and RC for the corporate exposure class, in line with NIBC's wish for more conservative capital calculations on its defaulted exposures in times of an economic downturn.

Despite the general economic conditions, 2010 showed a relatively stable quality in CCRs. The average weighted CCR in the corporate exposure class (excluding defaulted assets) was 6+ on NIBC's internal rating scale (equivalent to B+ in the rating scales of external rating agencies), both at 31 December 2010 and at 31 December 2009. On the contrary, the weighted-average LGD improved from 22% at 31 December 2009 to 19.7% at 31 December 2010.

Table 8 Breakdown of corporate AIRB EAD by weighted average PD, weighted average LGD and EAD type, 31 December 2010

IN EUR MILLIONS						
Rating Scale	WA PD	WA LGD	On-balance	Off-balance	Derivatives	Total
1/2 (AAA/AA)	0.03%	5.36%	60	11	1	72
3 (A)	0.11%	9.09%	510	0	8	518
4 (BBB)	0.35%	17.76%	835	407	117	1,359
5 (BB)	1.18%	18.27%	2,290	665	193	3,148
6 (B)	3.46%	22.62%	2,296	467	118	2,880
7 (CCC)	13.00%	29.81%	433	23	23	479
8 (CC/C)	28.92%	23.80%	60	0	0	61
9/10 (D)	100.00%	n.a.	916	1	0	917
TOTAL	2.61%	19.70%	7,401	1,574	459	9,434

Small differences are possible in the table due to rounding

Retail

The AIRB approach applies to NIBC's Dutch Residential Mortgage portfolio. The calculation of PD, LGD and EAD is performed by a Basel II AIRB model developed internally, which has been in use since 2006. The PD estimates are dependent on a variety of factors, of which the key factors are debt-to-income and loan-to-value ratios. Minor factors that play a role in the PD estimates are several other mortgage loan characteristics, borrower characteristics and payment performance information. The PD scale is based on a continuous scale ranging from 0 - 100%.

The LGD estimates are based on a downturn scenario comparable to the downturn in the Dutch mortgage market in the 1980s. In this case, the indexed collateral value is stressed in order to simulate the proceeds of a (forced) sale of the collateral. The stress is dependent on the location of the collateral and its absolute value. Together with assumptions about cost and time to foreclosure, an LGD is derived. The LGD estimate also takes into account whether a mortgage loan has a *Dutch government guarantee (NHG guarantee)*, for which the LGD

estimate will be lower in comparison to a mortgage loan without the NHG guarantee. The LGD estimate is also based on a continuous scale.

The EAD is set equal to the net exposure (outstanding balance minus built-up savings value) for all mortgage loans, except for non-amortising (in this case, interest-only loans). For the non-amortising loans, 3 months of accrued interest is added to the EAD.

The validation of these estimates is performed on historical data and is carried out on a yearly basis. For the PD and LGD, the estimates are back tested against realised defaults and realised losses. In this way, it is ensured that the model still functions correctly in a changing economic environment.

Overview of AIRB retail exposures

Table 9 provides an overview of retail AIRB EAD types, broken down by PD buckets. The table also provides the average PD and LGD, weighted against EAD. Note that the numbers in this table refer to the Dutch Residential Mortgage portfolio of NIBC.

Table 9 Breakdown of retail AIRB EAD by weighted average PD, weighted average LGD and EAD type, 31 December 2010

IN EUR MILLIONS					
PD bucket	WA PD	WA LGD	On-balance	Off-balance	Total
0.1% - 0.2%	0.13%	9.61%	1,288	0	1,288
0.3% - 0.4%	0.30%	15.28%	1,742	1	1,743
0.5% - 0.6%	0.50%	23.75%	1,178	0	1,178
0.7% - 0.9%	0.71%	28.32%	487	0	487
1% - 2%	1.08%	33.77%	183	0	183
2% - 5%	4.32%	16.30%	67	0	67
5% - 99%	17.91%	26.61%	80	0	80
100%	100.00%	24.56%	40	0	40
TOTAL			5,065	1	5,066

Equities

NIBC uses the simple risk weight approach for equity investments. Under this approach, the RWA is calculated by multiplying the exposure amount by 190% for private equity exposures in sufficiently diversified portfolios, 290% for exposures traded on listed exchanges and 370% for other exposures. The total EAD for equities amounts to EUR 544 million, of which EUR 540 million attracts a 370% risk weight (non-listed companies).

Securitisations

NIBC uses the IRB approach for securitisation exposures, both for purchased securitisations as well as for retained notes of own securitisations. Under the IRB approach, the RWA is calculated by multiplying the exposure amount by the appropriate risk weight. The risk weight depends upon the external rating, the granularity of the pool and the seniority of the pool. Alternatively, for retained notes of own securitisations, NIBC uses the IRB capital charge had the underlying exposures not been securitised (KIRB). This is applicable in the case where the capital requirement under the KIRB approach is lower than the capital requirement under the IRB approach for the securitisation exposure class. More detailed risk information about NIBC's securitisation exposures can be found in the securitisations section.

Table 10 Risk weights of securitisation EAD, 31 December 2010

IN EUR MILLIONS								Total
Risk weight	<10%	10% - 20%	25% - 50%	60% - 100%	250% - 650%	1250% or deducted		
Retained	126	97	106	52	13	95	489	
Purchased	390	213	90	91	49	138	972	
TOTAL	516	310	196	143	62	233	1,461	

Small differences are possible in the table due to rounding

Standardised Approach

For the calculation of RWA under the Standardised approach, the book value of the on-balance sheet (drawn) exposure is multiplied by a risk weight, depending on the exposure type and the external rating. The off-balance sheet (undrawn) exposures are multiplied by both a risk weight and a credit conversion factor. The risk weights are prescribed in the CRD (Annex VI, part 1):

- Almost all of NIBC's sovereign exposures are exposures with a zero risk weight. The vast majority of these exposures are related to cash placed with the Dutch Central Bank and the Dutch State Treasury Agency. NIBC has zero sovereign exposure to Greece, Italy, Ireland, Spain and Portugal.
- The risk weight for institutions is mostly either 20% (all short-term investment-grade exposures and long-term exposures with a rating equal to or higher than AA-) or 50% (long-term exposures with a rating between BBB- and A+). All exposures with a 10% risk weight are related to covered bonds.
- The corporate exposure class carries a risk weight of 100%. It mainly contains non-rateable exposures and derivatives to corporate counterparties.
- The retail exposure consists of the German Residential Mortgage portfolio. Part of the exposure, which is fully secured by residential property, receives a 35% risk weight and the other part receives a 100% risk weight.

Overview of Standardised portfolios

Tables 11 and 12 provide a breakdown of EAD and RWA, respectively, by exposure class, together with the applicable risk weight.

Table 11 Standardised EAD per risk weight, 31 December 2010

IN EUR MILLIONS									Total
Exposure Class	0%	10%	20%	35%	50%	100%	150%	Other	
Institutions	3	165	1,280	0	861	0	0	0	2,309
Sovereign	1,641	0	0	0	3	0	0	0	1,644
Corporate	0	0	0	0	0	625	0	0	625
Retail	0	0	0	438	0	69	0	0	507
Equities	0	0	1	0	0	3	0	0	4
Other	0	0	0	0	0	62	0	0	62
TOTAL	1,644	165	1,281	438	864	759	0	0	5,151

Table 12 Standardised RWA per risk weight, 31 December 2010

IN EUR MILLIONS									
Exposure Class	0%	10%	20%	35%	50%	100%	150%	Other	Total
Institutions	0	17	256	0	430	0	0	0	703
Sovereign	0	0	0	0	2	0	0	0	2
Corporate	0	0	0	0	0	625	0	0	625
Retail	0	0	0	153	0	69	0	0	222
Equities	0	0	0	0	0	3	0	0	3
Other	0	0	0	0	0	62	0	0	62
TOTAL	0	17	256	153	432	759	0	0	1,617

Credit risk mitigation

Institutions

The exposures to financial institutions are either related to *over-the-counter* (OTC) derivative transactions, or to debt investments (in tradable securities), or to cash management activities (money-market and repo transactions), or to credit derivatives. Details about credit risk management for OTC derivative transactions can be found in the section about counterparty credit risk. NIBC only enters into repo transactions if they are secured by highly-rated bonds. Some debt investments of financial institutions are secured by collateral (covered bonds) or benefit from state guarantees.

Corporate

An important element in NIBC's credit approval process is the assessment of collateral. Almost all exposures in the corporate exposure class have some form of collateralisation, with the main exception of IM loan exposures. IM loans may contain equity characteristics such as attached warrants or conversion features; examples of this exposure include mezzanine loans, convertible loans and shareholder loans, which are typically unsecured instruments.

Collateralised exposures can be secured by mortgages on real estate and vessels, by receivables, lease receivables or liens on machinery and equipment, or by third-party guarantees and other similar agreements. An exposure is deemed to be collateralised, fully or partly, if such assets are legally pledged in support of the exposure.

In general, NIBC requests collateral to protect its interests. NIBC ascribes value to collateral provided that the collateral is sufficiently liquid, that documentation is effective and that enforcing NIBC's legal rights to the collateral will be successful. The type and quantity of the collateral depends on the type of transaction, the counterparty and the risks involved. The most significant types of collateral securing the corporate exposure class are tangible assets, such as real estate, vessels, rigs, *floating, production, storage & offloading* (FPSO) units and equipment.

NIBC initially values collateral based on fair market value when structuring a transaction, and evaluates the collateral and its value (semi-) annually during the lifetime of the exposure. NIBC typically seeks confirmation from independent third-party experts that its interests are legally enforceable. Exposures in the shipping and oil & gas sectors are secured by assets such as ships and drilling vessels. The commercial real estate portfolio is primarily collateralised by mortgages on financed properties. Collateral value is estimated using third-party

appraisers, whenever possible, or valuation techniques based on common market practice. Other corporate exposures are, to a large extent, collateralised by assets such as inventory, debtors, and third-party credit protection (e.g. guarantees). The value of these types of collateral can be more difficult to determine, therefore such collateral is attributed a nil value.

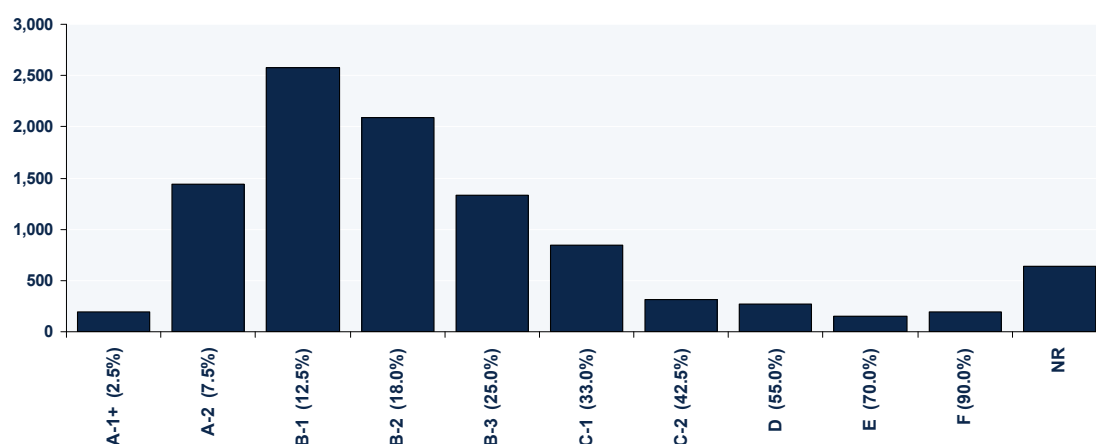
Graph 1 shows the distribution of corporate EAD per internal LGD rating. Note that the corporate exposures of the graph refer to non-defaulted exposures, given that the LGD is a measure of anticipated loss from the facilities of a non-defaulted counterparty. Once a counterparty enters default, then the impairment amount is a more meaningful measure of the loss. More information on impairment amounts can be found in the next section.

LGD ratings are facility-specific. As described in previous sections, an LGD rating reflects the loss that can be expected in a downward scenario on a facility, if a counterparty defaults. NIBC's internal LGD scale consists of 7 grades (A-F) and 10 notches, each of which represents a different degree of recovery prospects and loss expectations. In graph 1 the letters on the horizontal axis refer to NIBC's LGD grades and notches, whereas the numbers inside the parentheses refer to the loss percentage assigned to each LGD rating. NR stands for not rateable. NR is assigned to entities to which NIBC's corporate rating tools were not applicable at the time of rating. Exposures in the NR category fall under the Standardised approach.

The LGD methodology is based on a combination of qualitative and quantitative rating indicators that include, among others, the assessment of the realisable collateral value, guarantees, the seniority of the exposure, the applicable jurisdiction, and the quality of the counterparty's assets. Once the various LGD drivers have been assessed, the final LGD rating is based upon expert judgement. The assessment of the available collateral is the basis for NIBC's LGD analysis. In determining the realisable collateral value, which is based upon recent appraisals, NIBC applies a number of haircuts on the collateral's fair market value. These haircuts are mainly driven by the type of collateral, how liquid it is, the business cycle of the industry, the costs for forced collateral sales and other work-out costs.

NIBC's LGDs are concentrated in those LGD categories that correspond to recoveries in the range of 80% and 90%, which are relatively high for the banking industry.

Graph 1 Breakdown Corporate EAD (in EUR millions) per LGD rating, 31 December 2010



Retail

Dutch residential mortgage portfolio

Credit losses are mitigated in a number of different ways:

- The underlying property is pledged as collateral;
- Under Dutch law NIBC has full recourse to the borrower;
- 15% of the Dutch Own Book portfolio and 43% of the Dutch Securitised portfolio are covered by the NHG programme; and
- Approximately 43% of the Dutch portfolio has been securitised.

For the portfolio not covered by the NHG programme, the underlying property is the primary collateral for any mortgage loan granted, though savings and investment deposits may also serve as additional collateral.

A measurement for potential losses, taking into account indexation of house prices and seasoning, is achieved by calculating the *loan-to-indexed-market-value (LTiMV)*. The indexation is made by using the index of the Dutch Land Registry Office (Kadaster), which is based on market observables. For the part of the portfolio not covered by the NHG programme, only 13% has an LTiMV above 100%. For the remainder of the portfolio, the indexed collateral value is sufficient to cover the entire loan balance outstanding.

German residential mortgage portfolio

As is the case in the Netherlands, the underlying property is the primary collateral for any mortgage loan granted. In contrast to the Dutch market, most of the mortgage loans contain an annuity repayment, leading to a lower outstanding balance during the lifetime of the loan. The majority of the underlying collateral for the German portfolio is located in former West Germany.

Overview of impaired and past-due exposures

Sovereign and Institutions

In 2010 NIBC did not take any impairments on these exposure classes.

Corporate

Credit officers and CRM monitor the quality of corporate counterparties on a regular basis. On a quarterly basis, the entire portfolio is assessed for impairment. All existing impairments are reviewed as well.

NIBC considers a range of factors that have a bearing on the future cash flows that it expects to receive from the defaulted exposure, including the business prospects of the borrower and its industry sector, the realisable value of collateral held, the level of subordination relative to other lenders and creditors, and the likely cost and likely duration of any recovery process. Judgements are made in the process including, among other, the determination of expected future cash flows and their timing, the market value of collateral, and market discount rates. Furthermore, NIBC's judgements change with time as new information becomes available, or as recovery strategies evolve, resulting in frequent revisions to individual impairments, on a case-by-case basis.

NIBC calculates an impairment amount by taking certain factors into account, particularly the available collateral securing the loan and, if present, the corporate derivative exposure. The amount of loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future losses that have not been incurred). If collateral is present, then the present value of the future cash flows includes the foreclosure value of collateral.

Table 8 in the section *Calculation of Risk Weighted Assets* presented a breakdown of the corporate exposure class in NIBC's internal rating scale. Counterparties with a default rating (9/10) represent a total EAD of EUR 917 million, but this does not necessarily mean that all these counterparties carry an impairment amount. Reasons for not always taking an impairment amount for a defaulted counterparty may be e.g. over-collateralisation or NIBC's expectation of future cash-flow generation. IBNR stands for *incurred but not reported*.

When a default occurs (in line with the Basel II definition²), then the entire EAD of the borrower is classified as defaulted. On the contrary, if an impairment amount is taken against a facility, only the EAD of that particular facility is classified as impaired.

Tables 13 and 14 show a breakdown of the impairment amounts (EUR 153 million) of the corporate exposure class per region and industry sector as at 31 December 2010. The column labelled *Impaired EAD Corporate* shows the EAD of those facilities carrying an impairment amount (EUR 350 million). The difference between the impaired EAD on facility level and the impairment amount can be explained by the presence of collateral or NIBC's expectation of future cash-flow generation.

The impact of the credit crisis on the corporate exposures was felt in 2010 as in previous years but impairments remained at acceptable levels. Additions to impairments were significantly lower in 2010 than in 2009. However, the impact of the crisis differed between the various segments. Most new impairments were taken on the commercial real estate exposures, but other parts of the corporate exposures carry either no impairments (e.g. oil & gas) or negligible amounts (e.g. shipping). Other corporate exposures that had experienced increased impairments in 2008 and 2009 showed signs of stabilisation and/or upward credit migrations, as is the case of leveraged finance and corporate lending exposures.

Table 13 Breakdown of impairments on corporate exposure class per region, 31 December 2010

IN EUR MILLIONS			
Region	Total EAD Corporate	Impaired EAD Corporate	Impairment
The Netherlands	3,555	288	119
United Kingdom	1,975	37	15
Germany	1,701	25	16
Rest of Europe	1,181	0	0
Asia / Pacific	910	0	0
North America	384	0	0
Other	353	0	0
IBNR			3
TOTAL	10,059	350	153

² According to the Basel II definition, a default is determined on borrower level. A default is indicated by using a 9 or 10 rating in NIBC's internal rating scale. A default is considered to have occurred with respect to a particular obligor when either or both of the two following events have taken place: i. The bank considers that the obligor is unlikely to pay its credit obligations to the banking group in full, without recourse by the bank to actions such as realising security (if held). ii. The obligor is past due more than 90 days on any material credit obligation to the banking group.

Table 14 Breakdown of impairments on corporate exposure class per industry sector, 31 December 2010

IN EUR MILLIONS			
Industry sector	Total EAD Corporate	Impaired EAD Corporate	Impairment
Commercial Real Estate	2,166	156	35
Infrastructure	2,134	7	3
Shipping	1,553	3	0
Financial Services	882	74	39
Oil & Gas	850	0	0
Wholesale/Retail/Leisure	728	41	30
Manufacturing	621	24	20
Services	435	44	23
Agriculture & Food	228	1	0
TMT	174	0	0
Other	288	0	0
IBNR			3
TOTAL	10,059	350	153

The amounts in arrear are reported to the TC every two months. Payments might be be overdue for various reasons. However, late payments that are not yet received are not automatically assumed to be uncollectible.

Table 15 presents the corporate EADs with a past-due amount. The past-due amounts between 1 and 5 days may be caused by various operational reasons. The EAD of EUR 440 million that appears as having an amount in arrear for above 90 days is collateralised by granular multi-family residential real estate.

Table 15 EAD with a past-due amount, corporate exposure class, 31 December 2010

IN EUR MILLIONS	Corporate EAD
1 - 5 days	202
6 - 30 days	10
31 - 60 days	17
61 - 90 days	19
SUBTOTAL LESS THAN 90 DAYS	248
Over 90 days	440
No payment arrear	9,371
TOTAL	10,059

Retail

As the residential mortgage portfolios in the Netherlands and Germany are on accounting classification fair value through profit or loss, the notion of impairments is not applicable on NIBC's retail exposure class. An increase in defaults and losses was observed in both 2009 and 2010 compared to previous years, due to market circumstances. The defaults and actual credit losses in the Dutch and German portfolio have, nevertheless, been extremely low in the past years. In 2010, the loss incurred on the Dutch residential mortgage portfolio was EUR 5.4 million. The German residential mortgage portfolio experienced losses for the first time in 2010, which amounted to EUR 95 thousand.

Table 16 shows an overview of the retail EAD with an amount in arrear at 31 December 2010. The table also shows those EADs with technical past-due amounts. These amounts contain those borrowers with an amount in arrear below EUR 250.

Table 16 EAD with amounts in arrear, retail exposure class, 31 December 2010

IN EUR MILLIONS	Retail EAD
Technical past-due amounts	9
1 - 30 days	110
31 - 60 days	28
61 - 90 days	15
SUBTOTAL LESS THAN 90 DAYS	162
Over 90 days	43
No payment arrear	5,368
TOTAL	5,573

Equities

NIBC determines an impairment on the equity investments available for sale held in NIBC's investment portfolio, if there has been a significant or prolonged decline in the fair value below the original cost (including previous impairment losses). NIBC uses expert judgement in determining what is 'significant' or 'prolonged' by evaluating, among other factors, whether the decline is outside the normal range of volatility in the asset's price. In addition, impairment may be appropriate when there is evidence of deterioration in the financial health of the company of which the securities NIBC holds, a decline in industry or sector performance, adverse changes in technology, operational problems or insufficient cash flows.

Tables 17 and 18 present an overview of impairments on equity exposures per region and industry sector respectively. The columns labelled *Impaired EAD Equity after impairment* present the remaining EAD after the impairment has been taken. This remainder EAD can, therefore, be smaller than the impairment amount. The impairment amount of EUR 59 million in Table 18 relates mainly to NIBC's equity participations in a German financial institution and a fund investment.

Table 17 Breakdown of impairments on equity exposure class per region, 31 December 2010

IN EUR MILLIONS			
Region	Total EAD Equity after impairment	Impaired EAD Equity after impairment	Impairment
The Netherlands	445	0	8
Rest of Europe	44	7	6
North America	30	19	39
Germany	16	0	20
United Kingdom	8	0	2
Asia / Pacific	0	0	0
Other	1	0	0
TOTAL	544	26	75

Table 18 Breakdown of impairments on equity exposure class per industry sector, 31 December 2010

IN EUR MILLIONS			
Industry Sector	Total EAD Equity after impairment	Impaired EAD Equity after impairment	Impairment
Wholesale/Retail/Leisure	152	0	2
Infrastructure	106	0	0
Financial Services	45	19	59
Commercial Real Estate	39	0	0
Services	38	0	0
TMT	38	0	0
Manufacturing	37	7	6
Shipping	17	0	0
Oil & Gas	0	0	0
Agriculture & Food	0	0	0
Other	74	0	8
TOTAL	544	26	75

Small differences are possible in the table due to rounding

Securitisations

As of 1 July 2008, NIBC reclassified all its securitisation exposures from fair value through profit or loss to amortised cost, with the exception of synthetics and equity tranches, as IFRS does not allow such an accounting treatment for these products. Synthetics are still classified as fair value through profit or loss, while equity tranches were reclassified as available for sale (fair value through equity). Therefore, impairments for the securitisation exposures only refer to the period after 30 June 2008 and only for the portion that is on accounting classification at amortised cost. The impairment amount takes the carrying value as reference. This carrying value is the market value as at 30 June 2008, adjusted for 'pull-to-par' effects. For equity exposures, the impairment amount is equal to the difference between the carrying value prior to the impairment and the current market value. For the other tranches, the impairment amount is equal to the difference between the carrying value and the expected cash flows, discounted by the original effective yield, if positive.

Table 19 shows a breakdown of impairments on securitisations per collateral type. The column labelled *Impaired EAD Securitisation after impairment* presents the remaining EAD after the impairment has been taken. The total impairment amount on the Securitisations portfolio as at 31 December 2010 was EUR 149 million.

Table 19 Breakdown of impairments on securitisation exposure class per collateral type, 31 December 2010

IN EUR MILLIONS	Total EAD Securitisation after impairment	Impaired EAD Securitisation after impairment	Impairment
ABS	17	0	0
CDO/CLO	191	6	29
CMBS	326	1	9
RMBS	510	0	1
OTHER	6	0	0
TOTAL WESTERN EUROPEAN SECURITISATIONS	1,050	7	39
NL - RMBS AAA	289	0	0
TOTAL SECURITISED TREASURY LIQUIDITY INVESTMENTS	289	0	0
TOTAL SECURITISATION EXPOSURE NIBC BANK	1,339	7	39
US CDO ¹	29	0	0
US CMBS	15	0	0
US CRE-CDO	62	3	110
US RMBS	16	0	0
TOTAL US SECURITISATIONS NIBC HOLDING	122	3	110
TOTAL SECURITISATIONS NIBC HOLDING	1,461	10	149

¹ Concerns EU CDO exposure with predominantly US collateral.

Expected loss versus realised losses

NIBC regularly reviews the methodology and assumptions used for estimating both the amount and timing of future cash flows, to reduce any differences between loss estimates (*Expected Loss, EL*) and actual loss (*Realised Loss, RL*) experience. The EL is a statistical measure that is based on the calculated PD, LGD and EAD, and it represents the average loss that NIBC expects to incur. The RL is the actual loss that NIBC has experienced at the end of a given year.

As already mentioned in the section on impairments, the impact of the credit crisis on the corporate exposures was felt in 2010 as in previous years but impairments remained at acceptable levels. Additions to impairments were significantly lower in 2010 than in 2009. However, the impact of the crisis differed between the various segments.

With respect to corporate exposures, most new impairments were taken on the commercial real estate exposures, but other parts of the corporate exposures carry either no impairments (e.g. oil & gas) or negligible amounts (e.g. shipping). Other corporate exposures that had experienced increased impairments in 2008 and 2009 showed signs of stabilisation and/or upward credit migrations, as is the case of leveraged finance and corporate lending exposures.

With respect to retail exposures, an increase in defaults and losses was observed in both 2009 and 2010 compared to previous years, due to market circumstances. The defaults and actual credit losses in the Dutch and German portfolio have, nevertheless, been extremely low in the past years. Specifically the German residential mortgage portfolio experienced losses for the first time in 2010.

Table 20 shows the average losses in basis points in 2010 and 2009. Losses are attributed to the year in which the counterparty became defaulted according to the Basel II definition. The losses are based on the actual write-off on the loans and on the outstanding impairment (31 December 2010) in case the default was unresolved at year-end. Consequently, average losses are not necessarily constant, given that impairments change over time. The losses are related to the non-defaulted portfolio at the start of the year, containing on- and off-balance sheet amounts.

Table 20 shows that the realised loss for the corporate exposure class is higher than the expected loss. This is due to the fact that NIBC's internal AIRB models produce through-the-cycle ratings.

Table 20 Expected Loss (EL) versus Realised Loss (RL)

Exposure Class	2010		2009	
	EL	RL	EL	RL
Corporate	0.59%	0.97%	0.43%	0.71%
Retail	0.24%	0.08%	0.20%	0.05%

Counterparty Credit Risk

This paragraph deals with counterparty credit risk. NIBC defines counterparty credit risk as the credit risk resulting from OTC derivative transactions, where there is none or limited initial investment, such as *interest rate swaps (IRS)*, *credit default swaps (CDS)* and *foreign exchange (FX)* transactions.

NIBC is exposed to counterparty credit risk from derivative transactions both with corporate clients as well as with financial institutions. For both types of counterparties, counterparty credit risk is measured similarly, being the sum of the positive replacement value and add-on. The add-on reflects the potential future change in the marked-to-market value during the remaining lifetime of the derivative contract. All derivative transactions are legally covered by *International Swaps and Derivatives Association (ISDA)* agreements. Derivative transactions with corporate clients are concluded as part of the relationship management. Capital and credit limits for corporate clients are allocated on a one-obligor basis. The credit risk resulting from counterparty credit risk is monitored in conjunction with other exposures (e.g. loans) to these clients, and in the majority of cases the collateral of the loan is also applicable to the derivative exposure.

For nearly all its financial counterparties, NIBC has mitigated the counterparty credit risk by using a *Credit Support Annex (CSA)*. Under this annex, the credit exposures after netting are mitigated by the posting of (cash) collateral. Limits for financial counterparties cover money-market, repo and derivative exposures and are based upon a combination of external ratings, market developments like CDS spreads, and expert judgement. In line with market practice, *credit value adjustments (CVA)* are incorporated into the derivative valuations to reflect the risk of default of the counterparty. The CVA is calculated at the counterparty level as the sum of the present value of the expected loss (PD x LGD x expected exposure profile) estimated over the lifetime of all outstanding OTC derivative contracts. Table 21 shows the breakdown of EAD, RWA and capital requirement for derivatives at 31 December 2010.

Table 21 Breakdown of EAD, RWA and capital requirement for derivatives, 31 December 2010

IN EUR MILLIONS	EAD	RWA	Capital requirement
AIRB APPROACH			
- of which corporate	459	233	19
- of which securitisations	71	48	4
STANDARDISED APPROACH			
- of which corporate	228	228	18
- of which institutions	470	137	11
TOTAL DERIVATIVES	1,228	646	52

As discussed above, the EAD for derivatives is based on the sum of the positive replacement value (marked-to-market value) and applicable add-on. For corporate exposures using the AIRB approach, the PD is derived from the CCR, and the LGD is set equal to the facility weighted-average LGD. For institutions and corporate exposures for which the Standardised approach is used, the risk weight of the counterparty is used in the calculation of the RWA.

Table 22 Gross and net fair value exposure from derivative contracts

IN EUR MILLIONS	2010
Gross exposure	3,318
Netting benefits	(2,390)
Reduction from collateral	(142)
Net current exposure	786

NIBC uses credit derivatives both to protect its Debt Investments portfolio as well as to create credit exposures, although the latter is significantly reduced as part of the de-risking policy that NIBC started implementing in 2007. Tables 23 and 24 show the breakdown of all CDS contracts:

Table 23 Breakdown of CDS contracts by exposure class (nominal amounts)

IN EUR MILLIONS		
CDS contract exposure class	Sold protection	Bought protection
Sovereign	0	0
Institutions	54	0
Corporate	48	69
Securitisations	30	0
TOTAL	132	69

Table 24 Breakdown of CDS contracts by name type (nominal amounts)

IN EUR MILLIONS		
CDS contract name type	Sold protection	Bought protection
Single name	84	6
Multiple name	48	63
TOTAL	132	69

Market Risk

NIBC defines market risk as the current and prospective threat to its earnings and capital as a result of movements in market prices. Market risk, therefore, includes price risk, interest rate risk and foreign exchange risk, both within and outside the Trading portfolio. For fixed-income products, market risk also includes credit spread risk, which is the risk due to movements of underlying credit curve. The predominant market risk drivers for NIBC are interest rate risk and credit spread risk.

The trading portfolio of NIBC is the result of customer-driven transactions and limited trading for its own account in interest-rate risk products. Interest rate risk outside the Trading portfolio of NIBC is limited to centrally managed mismatch positions. For all other banking activities, only residual positions are allowed, given that the basic principle of NIBC is to hedge the interest rate risk from assets, liabilities and off-balance sheet instruments. Given the policy of limited trading activities within NIBC, the capital requirements are, in general, small. FX risk arises primarily from principal investments, customer-driven loans and funding or mismatch positions in foreign currencies. The general principle is to hedge FX risk completely, although small residual positions, e.g. from profits in foreign currencies, are allowed.

Market risk RWA and capital requirement for 31 December 2010 and 2009 are given in table 25. The RWA in 2010 increased compared to 2009 because of the higher risk profile of the Trading portfolio at the end of 2010. This should be regarded more as incidental rather than as a structural increase in RWA.

Table 25 Breakdown of RWA and capital requirement for market risk

IN EUR MILLIONS	31 December 2010		31 December 2009	
	RWA	Capital requirement	RWA	Capital requirement
- of which trading portfolio VaR	213	17	54	4
- of which FX Standardised approach	31	3	44	4
TOTAL MARKET RISK	244	20	98	8

Governance

The objectives of the market risk function are to measure, report and control the market risk of NIBC, both inside and outside the Trading portfolio. For this purpose, a common framework applies across the whole institution. For all books with interest or credit spread risk, limits are defined and positions are monitored daily. The risk management and control function is independent of the trading activities. The market risk position is reported to the ALCO once every two weeks. Any requests for new limits also have to be approved by the ALCO. Any significant breach of market risk limits is reported to the CRO on a daily basis. The income statement of the trading portfolio is also monitored daily.

The risk appetite for interest rate risk is set, among others, by the *value-at-risk (VaR)* limits. For the Trading portfolio a VaR limit (99% confidence level, one-day holding period) of EUR 3 million is set; for each of the Mismatch portfolios a VaR limit of EUR 7 million applies and the VaR on consolidated basis should be below of EUR 15 million.

Measurement methods

NIBC uses multiple risk measures to capture all aspects of market risk. These include interest *basis point value* (BPV), credit BPV, interest VaR and credit VaR. These measures are calculated on a daily basis for the major currencies and are reviewed by the Market Risk department:

- Interest and credit BPV measure the sensitivity of the market value for a change of one basis point in each time bucket of the interest rate and credit spread, respectively. During 2010, NIBC updated its interest rate risk methodology by introducing multiple curves for each repricing frequency (overnight, 1 month, 3 months and 6 months) both for discounting and calculating forward rates;
- The interest VaR, credit spread VaR and total VaR measure the threshold value, which daily marked-to-market losses with a confidence level of 99% will not exceed, based upon four years of historical data for weekly changes in interest rates, credit spreads and both simultaneously. For the Trading portfolio, additional VaR scenarios based upon daily historical market data and a 10-day holding period are used, both for limit-setting as well as for the calculation of the capital requirement. Not only is the use of daily market data for the Trading portfolio a regulatory requirement, but this portfolio only contains liquid plain vanilla interest rate products. For these products, reliable daily market data are available. Outside the Trading portfolio, however, less liquid positions are kept, for which reliable daily market data, especially for credit spreads, are not available;
- As future market price developments may differ from those that are contained by the four-year history, the risk analysis is complemented by a wide set of scenarios, including scenarios intended as stress testing and vulnerability identification, both based on historical events and on possible future events.

Stress testing

In addition to the VaR, NIBC has defined a number of stress tests. These stress tests consist both of historical events as well as potential extreme market conditions, which have not (yet) materialised. Market risk stress tests are conducted and reported daily, both on portfolio as well as on a consolidated level. Below some examples of stress tests are mentioned:

- Historical interest rate spike 1994, where long-term interest rates rose by 275 basis points in Europe and by 250 basis points in the US.
- Credit crisis 2008, where credits spreads rose significantly.
- Hypothetical scenario, where interest rates shift by -100 basis points or + 100 basis points.
- Hypothetical scenario, where credit spreads rise significantly.

Regulatory capital for market risk in the Trading portfolio

Since 2008, NIBC has received supervisory approval to use the Internal Models Approach (IMA) for market risk in the Trading portfolio. Annex VII, part B of the European directive 2006/48/EC sets the requirements for systems and controls regarding exposures in the Trading portfolio. NIBC complies in all material aspects with these requirements. As given in table 25, the total capital requirement for market risk at the end of 2010 equalled EUR 20 million.

VaR

Although trading positions change daily, Graph 2 shows that the average level of risk during 2009 was maintained in the first three quarters of 2010. Only towards the end of 2010 did the level of risk increase

significantly compared to the period before. The higher risk position at year-end 2010 also explains the higher capital requirement.

Throughout 2010, the portfolio consisted solely of interest rate-driven exposures. Activities comprise short-term (up to two years) interest position-taking, money-market and bond futures trading and swap spread position taking. The interest rate risk between positions in swaps and bond futures is also taken into account in the VaR. The portfolio is also used for facilitating derivative transactions with corporate clients. As a further insight in the risk characteristics of the Trading book, table 26 shows the key statistics of the VaR numbers for the Trading portfolios in 2010. At the end of 2010, trading activities rebounded from the very low volumes since the beginning of 2009, but still largely within the predefined limits. The VaR also increased as a result of the change in methodology as described previously.

Graph 2 Development of VaR in the Trading portfolio during 2009 and 2010



Table 26 Key risk statistics, Trading portfolio 2010

IN EUR THOUSANDS	Interest rate	
	BPV	VaR
Max*	(126)	1,769
Average	(63)	706
Min*	27	219
YEAR-END 2010	(69)	1,210

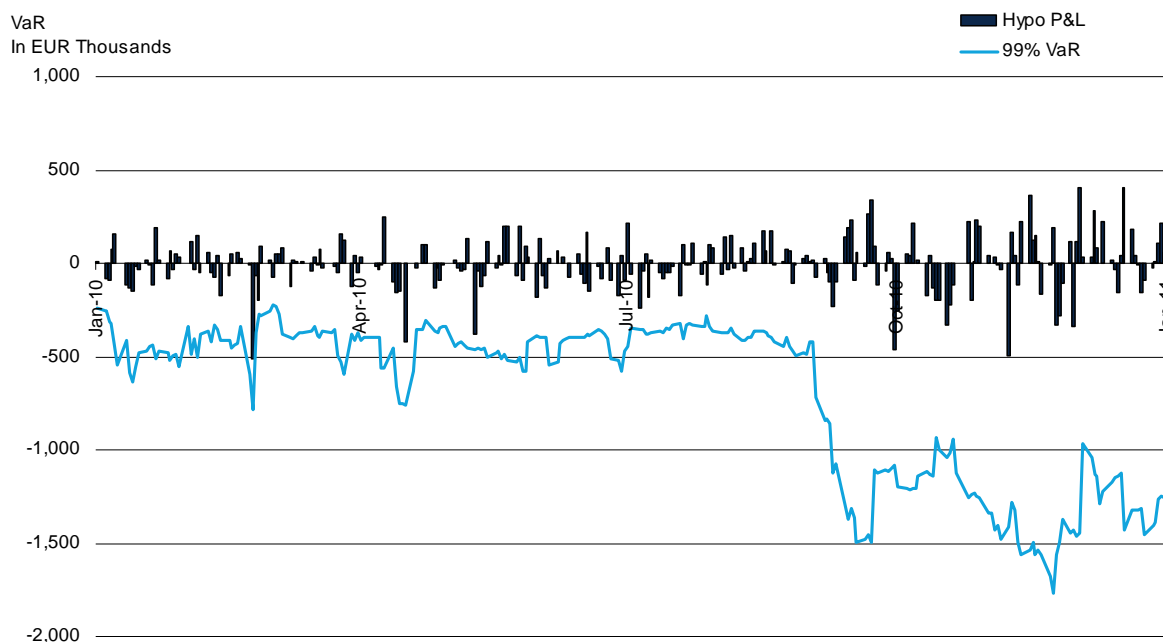
* Min: value closest to zero, Max: value farthest from zero

Back testing

Back testing for the Trading portfolios is conducted in accordance with the guidelines of the Basel Committee on Banking Supervision. For the Trading book, the one-day 99% VaR is back tested with the hypothetical *profit or loss* (P&L). The hypothetical P&L is calculated based upon the end-of-day trading position and the change in

market rates from the trading day to the next business day using full revaluation. Graph 3 shows the hypothetical P&L and 99% VaR figures for 2010. The total number of outliers during this period amounted to zero.

Graph 3 Back test results of the Trading portfolio during 2010



Market risk outside the Trading portfolio

Interest rate risk in the Mismatch portfolios

Strategic interest rate risk position is concentrated in the Mismatch portfolios. In 2010, NIBC maintained its positions in both the USD and EUR mismatch portfolio. These portfolios exclusively contain swap positions, with which a view on future interest rate developments is taken.

Interest rate risk in the Banking book

Apart from the Trading portfolio and the Mismatch portfolios, interest rate risk is also contained in the following portfolios (henceforth collectively referred to as 'Banking book'):

- Debt Investments portfolio;
- Residential Mortgage portfolio; and
- Residual Interest Rate Risk portfolio.

The interest rate risk in these portfolios is significantly below the risk contained in the Mismatch portfolios, as it is the policy of NIBC to hedge the interest rate risk in these portfolios.

NIBC uses an economic value approach to model interest rate risk in the Banking book. Corporate loans and deposits are modelled based upon the contractual re-pricing date, without prepayment. For mortgages, a dedicated prepayment model is used, where prepayment depends upon the remaining interest period and which is calibrated regularly using realised historical prepayments. On-demand retail savings are modelled as

zero coupon bonds with approximately equal notional amounts and a maturity ranging from one to nine months. All cash flows are discounted by applying a swap curve plus the appropriate credit spread curve.

Table 27 shows the interest rate sensitivity from an economic perspective for EUR, USD and GBP. For the other currencies the interest rate risk is minimal. The impact of a larger interest rate movement (parallel shock of plus or minus 100 basis points) is shown in table 28.

Table 27 Interest rate sensitivity, 31 December 2010

IN EUR THOUSANDS	BPV			Total
	Trading	Mismatch	Banking	
EUR	(8)	(412)	182	(238)
USD	(61)	(244)	(50)	(355)
GBP	0	0	5	5
Other	0	0	6	6
TOTAL	(69)	(656)	143	(582)

Table 28 Effect of an interest rate shock on economic value, 31 December 2010

IN EUR THOUSANDS		
Interest rate shock	-100bp	+100bp
EUR	23,908	(22,971)
USD	36,771	(35,788)
GBP	(938)	1,025
Other	(956)	902
TOTAL	58,785	(56,832)

Credit spread risk

Within Treasury, credit spread risk is mainly concentrated in the Debt Investments portfolio and comprises investments in financial institutions and sovereign entities, securitised products and enhanced investments. NIBC's total credit spread sensitivity at 31 December 2010 (-0.541 million EUR/bp) has not changed much compared to 31 December 2009 (-0.450 million EUR/bp). The distribution of credit spread risk over the different portfolios is almost equally split between the Securitisation portfolio (48%) and the portfolios containing investments in financial institutions and state-guaranteed bonds (52%).

Foreign exchange risk

As stated previously, it is the policy of NIBC to hedge its currency risk as much as possible. NIBC uses the Standardised approach for the calculation of regulatory capital for currency risk. At year-end 2010, the capital requirement for FX risk was EUR 3 million.

Operational Risk

Operational risk is the risk of direct or indirect loss resulting from inadequate or failed processes or systems, from human error or external events including legal risk. This is the definition of the Basel Committee on Banking Supervision. NIBC has chosen to include reputation and strategic business risk as operational risk. Operational Risk Management is concerned with all operational risks that affect NIBC's reputation, operational earnings and/or have adverse effects on capital value.

The objective of Operational Risk Management is laid down in the operational risk policy and the means and responsibilities for managing operational risk are laid down in the operational risk framework. The framework sets out the roles and responsibilities for management supervision, as well as those tools and methods used within the bank for identifying, measuring, reporting, monitoring, and controlling operational risk. 'Sound Practices for the Management and Supervision of Operational Risk', published by the Basel Committee on Banking Supervision, has been used in the development of the operational risk framework to ensure robust and effective management and supervision. The framework is based on the principle that NIBC's Managing Board and Supervisory Board and senior management are actively involved in risk management, and that the bank's risk management framework is independent, conceptually sound and implemented with integrity.

Operational risk is managed both at group and division level. The Managing Board provides consistency and oversight of significant operational issues, and oversees the adoption of best practice across the bank. At the division level and below, managers are responsible for adherence to the operational risk policy and operational risk management framework, which includes oversight of all operational risks specific to the business and reporting of operational risk events and losses.

The Operational Risk Management department monitors and manages operational risk at group level, develops policy and provides methodology and tools. The tools utilised by managers give an integrated view of the risk self-assessment, control identification, action planning, and event and loss registration and support the constant process of evaluating and reducing operational risk, and planning mitigation measures. The dynamics of NIBC's risk profile are managed by the Operational Risk Management department through the New Product Approval Process that ensures that NIBC has the operational capability to provide a new product or service and ensures the client suitability of its offerings.

NIBC has sought to build operational risk management into all its business processes. Operational risk is monitored on a daily basis and self-assessments are performed semi-annually. The year-end self-assessments form the basis for NIBC's 'In Control Report' section of the Annual Report. 'In control' reporting seeks to ensure that the operational risk management policy framework is integrated into the daily activities of all employees and that it forms an integral part of the internal control system.

The capital requirement under the Standardised Approach is the sum of the requirement per individual business line. Within each business line, gross income is the indicator that serves as a proxy for the scale of business operations and as such, the likely scale of operational risk exposure within each of these business lines.

The capital requirement for each business line is calculated by multiplying the average gross income of the past three years by a factor assigned to that business line. This factor serves as a proxy for the industry-wide

relationship between the operational risk loss experience for a given business line and the aggregate level of gross income for that business line.

The calculation is used to determine the regulatory capital requirement for operational risk and is performed annually by NIBC's Finance department. Table 29 shows the amount of RWA and the capital requirement for operational risk as at year-end 2010 and 2009. Both RWA and the capital requirement have more than halved in 2010. On the one hand, this relates to a less conservative calculation methodology that is allowed by the regulation, whereby negative operational income can be taken into account within operational sectors. On the other hand, it relates to the dataset on which operational risk calculations are based. As the average gross income for the past three years is used and the dataset is refreshed every year, the oldest year is dropped and the most recent year is added. The year that was dropped was 2006, during which NIBC had a higher average gross income than 2009, which was the new year added in the dataset.

Table 29 Breakdown of RWA and capital requirement for operational risk

IN EUR MILLIONS	2010		2009	
	RWA	Capital requirement	RWA	Capital requirement
Standardised approach	313	25	704	56
TOTAL OPERATIONAL RISK	313	25	704	56

Liquidity Risk

NIBC defines liquidity risk as the inability of the company to fund its assets and meet its obligations as they become due, at acceptable cost.

One of the cornerstones of NIBC's liquidity risk management framework is to maintain a comfortable liquidity position. The credit and liquidity crisis made liquidity risk management even more important. NIBC was able to maintain a sound liquidity position in the difficult times of the credit crisis due to the prudent and conservative liquidity and funding policy in the past, as well as by diversifying funding sources. Following the funding diversification of the past years, further expansion of the online retail savings programme NIBC Direct, as well as renewed RMBS issuance, were the major funding initiatives undertaken in 2010. In addition, NIBC was able to maintain its liquidity buffers of highly liquid assets and collateralised funding capacity.

Stress scenario

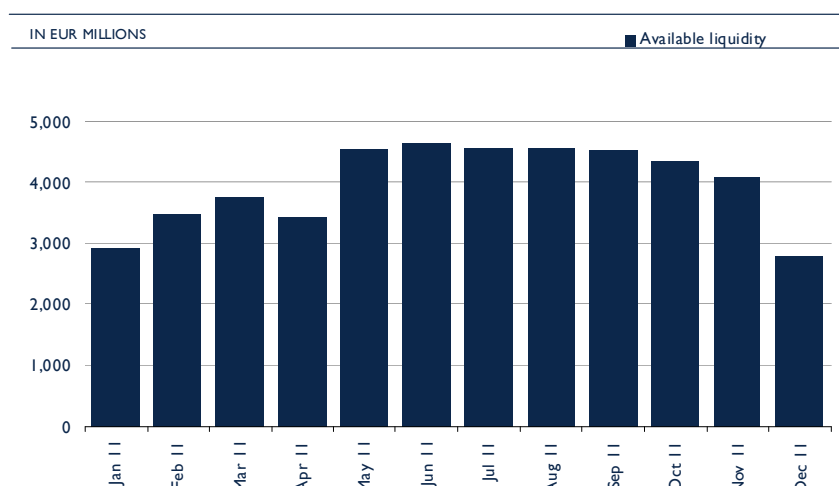
Based on projections prepared by the business units and reviewed by risk management, and the current asset and liability maturity profiles, a liquidity stress test is prepared and presented once every two weeks to the ALCO, in order to create continuous monitoring of the liquidity position. The outcome of this 12-month liquidity stress test was positive at 31 December 2009 and at 31 December 2010, implying positive liquidity buffers for a 12-month period following these dates.

In addition to the 12-month liquidity stress analysis described below, NIBC also conducts liquidity analyses over longer periods once every two weeks. These analyses assume a possible growth in the size of the books in combination with new funding initiatives as the ones mentioned. The outcome of, for example, a 36-month liquidity analysis shows again a positive buffer throughout the period.

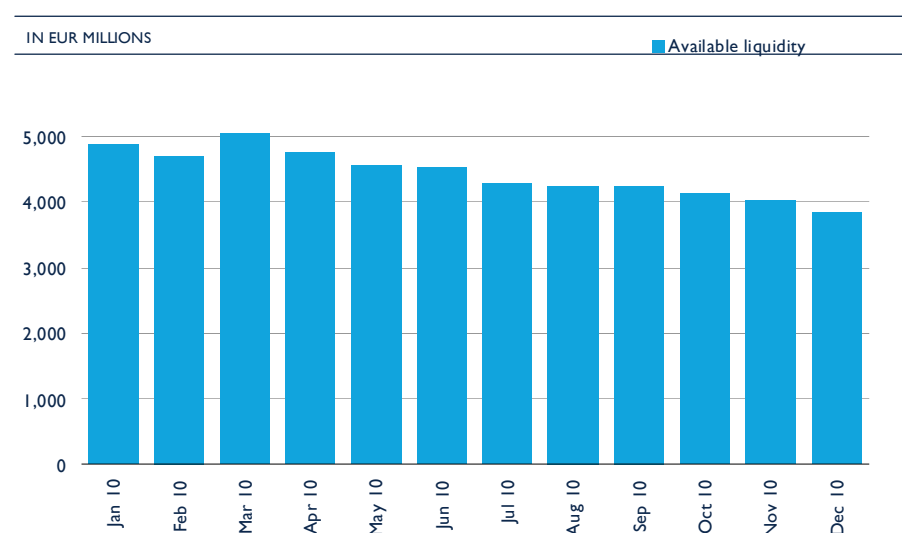
Graphs 4 and 5 show the strong liquidity buffer in the stress scenario at year-end 2010 and year-end 2009 and focuses on the next 12 months. The available liquidity, as presented in the graphs, consists of:

- A projected pool of cash plus liquidity buffers of highly liquid assets and collateralised funding capacity, minus a buffer for intraday payments and potential CSA collateral cash outflows, at each month end;
- A reduction to the available pool created by maturing liabilities and other projected outflows (e.g. from new business); and
- An increase in the available pool created by maturing assets.

Graph 4 Stress scenario, short-term analysis, 31 December 2010



Graph 5 Stress scenario, short-term analysis, 31 December 2009



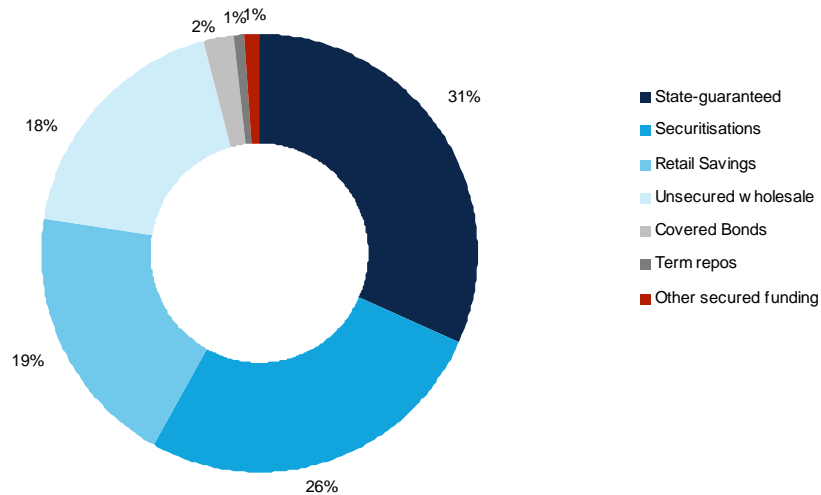
Both forecasts of the 12-month liquidity stress test at 31 December 2009 and at 31 December 2010 show that the outcome of the stress test after 12 months is positive in both years.

At the end of 2010, a large buffer of cash, highly liquid assets and collateralised funding capacity is available to cover the expiring funding in 2011. Due to a restructuring of a part of the collateralised funding capacity, the realised liquidity buffer at the end of 2010 was lower than originally forecast at the beginning of 2010, however this is only a temporary effect. After this restructuring, in March 2011 and the following months the liquidity buffers will again reach the level as expected at the end of 2009. Thereafter the liquidity buffer of NIBC in this liquidity stress declines at the end of 2011 to a still comfortably high level. This decline is mainly caused by maturing funding including the first government-guaranteed issue of NIBC. Note that this liquidity stress test does not assume new funding initiatives. In 2011, initiatives as, for example, an increase in retail savings and certain forms of secured funding, will contribute to the liquidity of NIBC.

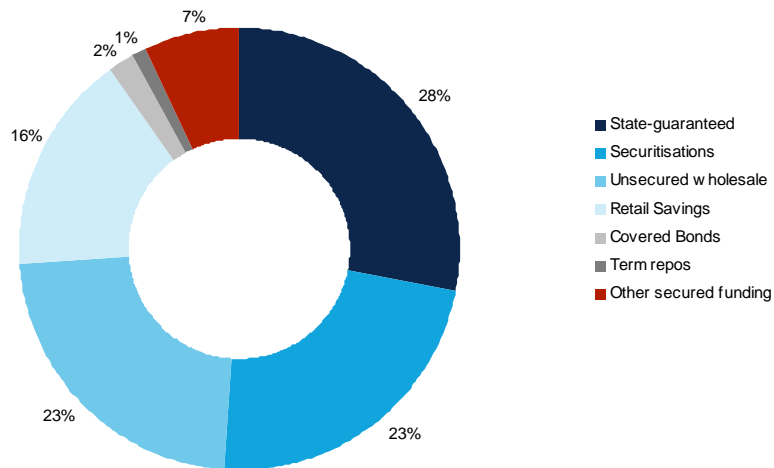
Funding

NIBC further diversified its funding base by the initiatives mentioned earlier. An overview of the Funding portfolio at 31 December 2010 and 31 December 2009 is shown in graphs 6 and 7. In contrast to previous years, the consolidated securitisations are included in the funding portfolio.

Graph 6 Breakdown of total Funding portfolio, 31 December 2010 (EUR 21,216 million)



Graph 7 Breakdown of total Funding portfolio, 31 December 2009 (EUR 23,132 million)



Securitisation Exposures

Overview and strategy

NIBC as originator

NIBC has been active in the securitisation and structuring market for over 10 years. The types of collateral for these securitisations include residential mortgages, commercial mortgages, leveraged loans and securitisations. NIBC's *Dutch Residential Mortgage Backed Securities (RMBS)* programme was established in 1997. NIBC's residential mortgage programme was later extended with the Sound and Essence issues. In 2003, NIBC started its North Westerly *Collateralised Loan Obligations (CLO)* programme. In 2004, NIBC became the collateral manager of its first US *Collateralised Debt Obligations (CDO)* transaction. In 2006, NIBC launched its introductory *Commercial Mortgage-Backed Securities (CMBS)* transaction under its MESDAG programme. In addition, NIBC has acted as arranger and lead manager on a number of third-party transactions. Table 30 gives an overview of the cumulative nominal amounts at 31 December 2010 of which NIBC was originator:

Table 30 Cumulative nominal amounts of NIBC's securitisations

IN EUR MILLIONS	Traditional originator	Total
UNDERLYING ASSET		
Residential mortgages	5,315	5,315
Commercial mortgages	2,329	2,329
CLO	3,346	3,346
TOTAL	10,990	10,990

As at 31 December 2010, there were no synthetic originated securitisations in NIBC's Securitisations portfolio.

Objectives

NIBC's objectives in relation to securitisation activities are:

- Transfer of credit risk;
- Obtain funding, reduce funding cost and diversify funding sources;
- Offer its real estate clients access to the capital markets;
- Earn management fees on the assets under management;
- Generate fee income by structuring third-party transactions; and
- Earn fees on ancillary roles in securitisations.

Roles and involvement

NIBC has fulfilled the following roles in the securitisation process:

- Arranger (structuring) of both third-party and proprietary securitisation transactions;
- Underwriter in securitisation transactions involving both third-party and proprietary transactions;
- Collateral manager for a number of managed CDO/CLO transactions;
- Swap counterparty for a number of residential and commercial mortgage securitisations;
- Liquidity facility provider for a number of residential and commercial mortgage securitisations;
- Calculation agent and principal paying for number of residential and commercial mortgage securitisations;

- Company administrator for a number of securitisations; and
- Investor in securitisations.

Securitisation activity in 2010

After two years during which NIBC only structured a number of asset-backed securities as collateral for collateralised funding purposes (which are not included in the quantitative disclosures, as credit risk transfer with regard to the exposures securitised has not been recognised for the purposes of Pillar-1 capital requirements), NIBC approached the securitisation market with two new issues for the first time since the financial crisis erupted in 2007. Both within the RMBS programme *Dutch MBS* and the *Essence* programme, new transactions (Dutch MBS XV and Essence III respectively) were issued successfully in 2010. On the other hand, NIBC called both the Dutch MBS X and Dutch MBS XI transactions at their first scheduled call date.

Names of the External Credit Assessment Institutions used for securitisations

NIBC uses Fitch, Moody's and Standard & Poor's to rate its securitisations. Most of the RMBS securitisations are rated by Fitch and Moody's. For the other type of securitisations, Standard & Poor's is also one of the rating agencies.

Accounting policy

NIBC consolidates securitisation *Special Purpose Entities (SPE)* in its financial statements when:

- It will obtain the majority of the benefits of the activities of an SPE;
- It retains the majority of the residual ownership risks related to the assets in order to obtain the benefits from its activities;
- It has decision-making powers to obtain the majority of the benefits; and
- The activities of the SPE are being conducted on NIBC's behalf according to NIBC's specific business needs so that it obtains the benefits from the SPE operations. Such an evaluation is necessarily subjective.

NIBC does not consolidate SPEs that it does not control.

NIBC as investor

Next to its role as originator of securitised products, NIBC has also been active as an investor in securitised products. In 2007, NIBC's perspective on the securitisation market changed and a policy of active de-risking was implemented for both the Western European and North American portfolio. As part of this policy, the complete North American RMBS portfolio was closed and the remaining North American portfolio (consisting of CMBS and CRE-CDO) was transferred from NIBC Bank to NIBC Holding. The Western European portfolio was also significantly reduced in size but remained within NIBC Bank.

At the end of 2009, NIBC set up a Liquidity Investments portfolio. This portfolio was set up to invest part of NIBC's excess liquidity in the securitisation market. Investments are limited to AAA-rated RMBS transactions backed by Dutch collateral, and are eligible to be pledged as collateral with the *European Central Bank (ECB)*. Apart from this strict mandate, each investment is pre-approved by both the Market Risk and Financial Markets Credit Risk departments. In 2010, NIBC further increased its investments under this mandate.

Securitisation exposures at NIBC Bank

Under this heading, several overviews regarding the securitisation exposures (retained and purchased) of NIBC Bank are presented, detailing underlying collateral type, credit quality and vintage. The numbers in this section are slightly different from those in the risk notes of the Annual Report, because the IFRS rules for consolidating securitisation exposures differ from Pillar 3 classifications under the securitisation framework, especially for derivative exposures. Table 31 provides an overview of NIBC Bank's exposures in securitisations at 31 December 2010.

Table 31 EAD of Securitisations portfolio at NIBC Bank, 31 December 2010

IN EUR MILLIONS	Investor	Originator	Total
ABS	17	13	30
CDO/CLO	138	52	191
CMBS	156	170	326
RMBS	245	252	497
OTHER	4	2	6
TOTAL WESTERN EUROPEAN SECURITISATIONS	561	489	1,050
NL - RMBS AAA	289	0	289
TOTAL SECURITISED TREASURY LIQUIDITY INVESTMENTS	289	0	289
TOTAL SECURITISATION EXPOSURE NIBC BANK	850	489	1,339

Small differences are possible in the table due to rounding

Credit quality of Securitisations portfolio

The credit quality is based on an internal composite, following Basel II guidelines, including external ratings from Standard & Poor's, Moody's and Fitch. The non-rated portion of the portfolio relates to first-loss positions in both NIBC's own securitisations as well as third-party securitisations, which have been marked down to between 1% and 10% of their nominal value at 31 December 2010.

Table 32 Rating distribution of Securitisations portfolio (investor), 31 December 2010

IN EUR MILLIONS	AAA	AA	A	BBB	BB	Below BB	Total
ABS	9	3	3	0	1	1	17
CDO/CLO	0	9	58	43	7	20	138
CMBS	56	20	34	12	17	16	156
RMBS	55	32	43	47	15	53	245
OTHER	3	1	0	0	0	0	4
TOTAL WESTERN EUROPEAN SECURITISATIONS	123	66	138	103	41	90	561
NL - RMBS AAA	289	0	0	0	0	0	289
TOTAL SECURITISED TREASURY LIQUIDITY INVESTMENTS	289	0	0	0	0	0	289
TOTAL SECURITISATION EXPOSURE (INVESTOR)	412	66	138	103	41	90	850

Small differences are possible in the table due to rounding

Table 33 Rating distribution of retained positions in the Securitisations portfolio (originator), 31 December 2010

IN EUR MILLIONS	Derivatives	AAA	AA	A	BBB	BB	Below BB	Total
ABS	13	0	0	0	0	0	0	13
CDO/CLO	0	0	0	41	3	3	5	52
CMBS	6	9	8	71	4	0	73	170
RMBS	51	127	11	22	13	10	17	252
OTHER	0	0	0	0	0	0	2	2
TOTAL WESTERN EUROPEAN SECURITISATIONS	71	135	19	134	20	13	96	489
NL - RMBS AAA	0	0	0	0	0	0	0	0
TOTAL SECURITISED TREASURY LIQUIDITY INVESTMENTS	0	0	0	0	0	0	0	0
TOTAL SECURITISATION EXPOSURE (ORIGINATOR)	71	135	19	134	20	13	96	489

Small differences are possible in the table due to rounding

Vintage of Securitisations portfolio

NIBC's Securitisations (investor) portfolio has a fairly favourable vintage with just below 55% stemming from 2005 and earlier, albeit this percentage can differ among collateral classes. The more recent vintages are mostly related to the investments made under the Liquidity Investments mandate.

Table 34 Vintage of Securitisations portfolio (investor), 31 December 2010

IN EUR MILLIONS	RMBS	CMBS	CDO/CLO	ABS	OTHER	LIQUIDITY	Total
2010	50	0	0	0	0	43	93
2009	0	0	0	0	0	21	21
2008	0	0	0	0	0	9	9
2007	1	18	29	0	0	52	100
2006	47	68	30	0	0	26	171
2005	29	43	17	3	0	37	130
2004	71	27	52	3	3	33	189
2003	24	0	5	10	0	31	70
2002	12	0	4	0	0	14	30
2001	8	0	0	0	0	23	31
2000	4	0	0	0	0	0	4
1999	0	0	0	0	1	0	1
1998	0	0	0	1	0	0	1
TOTAL	245	156	138	17	4	289	850

Small differences are possible in the table due to rounding

Table 35 Vintage of Securitisations portfolio (originator), 31 December 2010

IN EUR MILLIONS	RMBS	CMBS	CDO/CLO	ABS	OTHER	LIQUIDITY	Total
2010	143	0	0	0	2	0	145
2009	0	0	0	0	0	0	0
2008	0	0	0	0	0	0	0
2007	17	156	0	0	0	0	173
2006	0	14	2	0	0	0	16
2005	78	0	11	0	0	0	89
2004	13	0	17	0	0	0	30
2003	13	0	23	0	0	0	36
2002	0	0	0	0	0	0	0
2001	0	0	0	0	0	0	0
2000	0	0	0	0	0	0	0
1999	0	0	0	0	0	0	0
1998	0	0	0	0	0	0	0
TOTAL	265	170	52	0	2	0	489

Small differences are possible in the table due to rounding

Securitisation exposures at NIBC Holding

In 2007, the US Securitisations portfolio was sold from NIBC Bank to NIBC Holding. This section gives the characteristics of this portfolio. Tables 36 and 37 present the rating distribution and vintage of the US Securitisations portfolio in **NIBC Holding** as at 31 December 2010.

Table 36 Rating distribution of US Securitisations portfolio (investor), 31 December 2010

IN EUR MILLIONS	AAA	AA	A	BBB	BB	Below BB	Total
US CDO	0	11	5	12	0	0	29
US CMBS	0	4	3	8	0	1	15
US CRE-CDO	0	2	6	11	7	36	62
US RMBS	1	7	0	6	2	1	16
TOTAL US SECURITISATIONS NIBC HOLDII	1	24	14	36	9	39	122

Small differences are possible in the table due to rounding

Table 37 Vintage of US Securitisations portfolio, 31 December 2010

IN EUR MILLIONS	US CDO	US CMBS	US CRE CDO	US RMBS	Total
2010	0	0	0	1	1
2009	0	0	0	0	0
2008	0	0	1	1	1
2007	0	0	13	0	13
2006	4	5	32	1	42
2005	14	3	8	6	30
2004	2	0	9	7	19
2003	9	0	0	0	9
2002	0	1	0	0	1
2001	0	6	0	0	6
2000	0	0	0	0	0
1999	0	0	0	0	0
1998	0	0	0	0	0
TOTAL	29	15	62	16	122

Small differences are possible in the table due to rounding

Internal Capital Adequacy Assessment Process

The *Internal Capital Adequacy Assessment Process (ICAAP)* of each institution refers to the process with which risks and related capital are internally measured, allocated and managed, and by which the adequacy of capital available is assessed.

The internal capital requirements of NIBC under the ICAAP are based upon an internal Economic Capital framework. In addition to this, NIBC has an extensive framework of historical and theoretical stress scenarios that analyse the impact of severe shocks in the credit risk or market risk environment. The outcomes of these stress scenarios are compared to the available Economic Capital as well as the calculated Economic Capital usage.

Economic capital

Economic Capital (EC) is the amount of capital that NIBC allocates as a buffer against potential losses from business activities, based upon its internal assessment of risks. It differs from Basel II regulatory capital, as NIBC sometimes assesses the specific risk characteristics of its business activities in a different way than the general regulatory method. Relating the risk-based EC of each business to its profit results in the calculation of its RAROC. EC and RAROC are key tools used in support of the capital allocation process according to which shareholders' equity is allocated as efficiently as possible based on expectations of both risk and return. The usage of EC is reported once every two weeks to the ALCO. The ALCO adjusts the maximum allocation level of EC to and within each business, taking into account business expectations and the desired risk profile. EC allocation is based on a one-year risk horizon, using a 99.95% confidence level (increased from 99.90% in 2009). This confidence level means that there is a probability of 0.05% that losses in a period of one year will be larger than the allocated EC.

EC methodology

NIBC uses the business model of each activity as the basis for determining the EC approach. If the business model of an activity is trading, distribution, or investment for a limited period of time, a market risk approach is used based upon historical simulation, increased with add-ons for, among other, specific risk and prepayment risk. A business model equal to 'buy-to-hold' or investment to maturity means that a credit risk approach is applied based upon estimations of PD and LGD. Add-ons for operational risk and country risk are also calculated. In addition, NIBC allocates EC for business risk, reputation risk and model risk on a group-wide level.

The EC approach differs from the regulatory capital approach, in which only the trading books are assigned a market risk approach. Activities that have a business model equal to distribution or investment for a limited period of time are, in some cases, assigned a credit risk approach in the regulatory capital framework due to Basel II regulations or regulatory industry practice. For these business model categories, NIBC applies a market risk approach in the EC framework similar to the trading activities, as for all of these activities the market price becomes relevant at a certain point in time. Risks and EC are therefore monitored accordingly.

The main differences between the EC and regulatory capital framework exist for the Residential Mortgage portfolio, the Securitisations portfolio and NIBC's interest rate mismatch position. EC is determined by a market risk approach for these activities because of their business model. The regulatory capital approach for these portfolios is either included in credit risk (mortgages and securitisations) or not included at all within Basel II Pillar 1 (mismatch position). As EC methodology may differ significantly among financial institutions, it is more appropriate to compare the regulatory capital ratios for the purpose of industry comparison of market risk and credit risk exposures.

EC usage

EC is allocated to all business activities in the form of limits set by the ALCO. The amount of EC usage of each business is then calculated, based on the risk of its activities.

- For the Corporate Loan portfolio, which uses a major part of EC, EC usage is calculated using a credit risk approach based upon the Basel II regulatory capital formula and an add-on for concentration risk;
- For the Debt Investments and Trading portfolios (including the interest rate mismatch positions that represent the strategic long-term investments of NIBC's capital) and the Residential Mortgage portfolio, a market risk approach is used to determine EC usage. Historical data are used to simulate scenarios from which EC is calculated.
- For the Investment Management Loan portfolio, EC usage is calculated by applying a credit risk approach based upon the Basel II regulatory capital formula; and
- For the Equity Investment portfolio, fixed percentages are used.

Table 38 shows the EC usage per business activity. At the beginning of 2010, the EC framework started taking into account diversification effects between the different risk types (credit, market and operational risk), next to diversification effects within market risk that were already part of NIBC's EC methodology. Within the market risk EC calculation, NIBC takes diversification effects into account between credit spread and interest rate risk. Diversification derives from the fact that not all risks will occur at the same time. Therefore, the sum of EC within or between risks on a stand-alone basis will be higher than the amount of EC if these risks are combined. This reduction of EC is defined as diversification.

Table 38 EC usage per business activity

IN EUR MILLIONS	31 December 2010	31 December 2009	Difference
Corporate Loan portfolio	548	493	11%
Investment Management Loans and Equity Investment portfolio	231	185	25%
Total credit and investment risk	779	678	15%
Residential Mortgage portfolio	312	262	19%
Debt Investments and Trading portfolio	537	438	23%
<i>of which: mismatch positions</i>	160	252	-37%
Market risk diversification effects	(266)	(115)	131%
Total market risk	583	585	0%
Operational and other risk	114	71	62%
Reputation risk	100	100	0%
Business risk	100	100	0%
Model risk	20	20	0%
Total other risk	334	291	15%
Diversification effects between risk types	(415)	-	N/A
TOTAL DIVERSIFIED ECONOMIC CAPITAL	1,281	1,554	-18%

The changes in the usage of EC at year-end 2010 are owed to a variety of factors. The most notable ones are due to methodology changes, such as the introduction of diversification between different risk types, the confidence level increase from 99.90% to 99.95%, the change in market risk EC approach (from scaling the weekly VaR figures for a one-year horizon) towards historical simulation (sampling historical weekly changes to arrive at a one-year horizon and 99.95% confidence level), and the addition of specific risk within market risk.

Apart from the above changes, the changes in EC usage can also be explained as follows:

- The increase of 11% noted for the Corporate Loan portfolio was mainly the result of the increase in the size of the portfolio, as well as the introduction of EC for unexpected losses on non-impaired defaulted loans.
- The increase of 25% in the IM Loans and Equity Investment portfolios are due to positive revaluations of the Equity Investments portfolio.
- With respect to market risk, 2010 was the first year in which NIBC adopted the historical simulation methodology described earlier to calculate EC for portfolios with a market risk approach. This methodology change led to an increase in EC for the Residential Mortgage and Debt Investments portfolios. Also a larger short-term liquidity portfolio of highly liquid assets (part of the Securitisations portfolio) that reflects NIBC's cash surplus, contributed to the rise in EC usage. Moreover, credit-spread tightening in 2010 led to a higher fair value of debt investments and subsequently, to a higher EC. In addition, NIBC now includes, as mentioned, a specific risk add-on to account for rating migration risk and default risk of market risk positions.
- Diversification effects within market risk have increased based on the 2010 market data.
- The EC usage of the interest rate mismatch position decreased by 37%, mainly due to the methodology change, the amortisation of the strategic mismatch positions, as well as due to relatively shorter maturities of the strategic mismatch positions.
- Economic capital for operational risk differs from the regulatory capital calculation due to differences in methodology (e.g. differences in the confidence level and timing of adjustments of parameters).

Stress scenarios

The event risk framework is part of the Pillar 2 framework for Basel II within NIBC. On a quarterly basis, results of the event risk analysis are presented to the ALCO and to the Risk Policy Committee, providing senior management and the Supervisory Board members with information that can be taken into account in decisions regarding risk appetite. At NIBC, stress scenarios focus on vulnerability testing of portfolios, assessing the impact of extreme events and benchmarking EC calculations. Several scenarios based on both historical events, as, for example, the Asian crisis or the internet bubble, and hypothetical scenarios as, for example, a severe recession or stagflation, are applied.

Capital Base Components

The capital base, also referred to as regulatory capital, is calculated in accordance with the Dutch legislation and the EU Capital Requirements Directive. The available regulatory capital is based on capital contributed by subsidiaries covered by prudential consolidation accounts, which should be available, without restrictions or time constraints, to cover risks and absorb potential losses. All amounts are included net of tax charges.

The available regulatory own funds at NIBC are classified under two main categories, being Tier-1 capital and Tier-2 capital. The two main components in the regulatory own funds are core equity and subordinated debt. Profit of the year is included in the Tier-1 capital after deductions for proposed dividend. The key terms and conditions of each of these categories are summarised below.

The capital ratio is calculated by dividing the regulatory capital with risk weighted assets.

Tier-1 capital

Tier-1 capital is composed of eligible capital, eligible reserve, innovative hybrid Tier-1 capital and non-innovative hybrid Tier-1 capital after deduction of eligible items.

Eligible capital

Eligible capital consists of share capital, share premium and repurchased own shares (treasury shares are deducted).

Eligible reserve

Eligible reserve consists primarily of retained earnings, minority interest and net profit from current year. Retained earnings are earnings from previous years. Minority interest reflects the equity of minority shareholders in a subsidiary. Net profit is included after verification by the external auditor.

Innovative Tier-1 hybrid capital

Innovative Tier-1 hybrid instruments are deeply subordinated debt instruments, senior only to Shareholders' Equity. They have an indeterminate duration, but step up calls that could give an incentive exercise and have a relatively high capacity for loss absorption. These instruments must meet strict rules predefined by DNB.

Non-innovative Tier-I hybrid capital

Non-innovative Tier-1 hybrid instruments are deeply subordinated debt instruments, senior only to Shareholders' Equity. They have an indeterminate duration and a relatively high capacity for loss absorption. These instruments must meet strict rules predefined by DNB.

Deduction from Tier-I capital

Intangible assets

The deducted intangible assets contain goodwill.

Securitisation exposures

NIBC has purchased subordinated bonds issued by various securitisation entities. According to the CRD and Dutch legislation, the subordinated bonds are deducted from regulatory own funds. 50% should be deducted from Tier-1 capital and 50% should be deducted from Tier-2 capital.

AIRB provision excess of expected loss

An adjustment is made for the difference between EL and provision for the related exposures in the regulatory own funds. The negative difference (when EL amount is larger than the provision amount) is included in the regulatory own funds as shortfall. According to the rules in the CRD and Dutch legislation, the shortfall amount shall be deducted from the regulatory own funds. The deduction of 50% is from Tier-1 capital and the remaining 50% from Tier-2 capital.

Tier-2 capital

The Tier-2 capital is composed of subordinated debt instruments, revaluation reserve after deduction of eligible items. Tier-2 capital includes two types of subordinated debt instruments; perpetual and dated instruments. The total Tier-2 capital may not exceed 50% of the amount of Tier-1 capital and dated Tier-2 capital may not exceed 50% of Tier-1 capital. The limits are set after deductions.

The amount possible to include in the Tier-2 capital related to dated loan capital is reduced if the remaining maturity is less than five years. The outstanding amount in the specific issue is deducted by 20% for each year beyond five years.

Revaluation reserve

Revaluation reserve contains unrealized gains from equity holdings classified as available for sale and revaluation of property.

Deductions from Tier-2 capital

Securitisation exposures

NIBC has purchased subordinated bonds issued by various securitisation entities. According to the CRD and Dutch legislation, the subordinated bonds are deducted from regulatory own funds. 50% should be deducted from Tier-1 capital and 50% should be deducted from Tier-2 capital.

AIRB provision excess of expected loss

An adjustment is made for the difference between EL and provision for the related exposures in the regulatory own funds. The negative difference (when EL amount is larger than the provision amount) is included in the regulatory own funds as shortfall. According to the rules in the CRD and Dutch legislation, the shortfall amount shall be deducted from the regulatory own funds. The deduction of 50% is from Tier-1 capital and the remaining 50% from Tier-2 capital.

A summary of items included in the regulatory capital is as follows:

Table 39 Regulatory Capital components NIBC Holding N.V., 31 December 2010

IN EUR MILLIONS	2010	2009
TIER 1		
Called-up share capital	1,408	1,407
Share premium	535	535
Deduction of own shares (Treasury shares)	(3)	(5)
Eligible reserves	(338)	(323)
Net profit	33	(22)
Minority interests	19	19
Deduction of goodwill	(121)	(121)
CORE TIER-1 CAPITAL	1,533	1,490
Deduction of certain securitisation exposures not included in risk-weighted assets	(73)	(24)
Deduction excess of expected losses over impairment allowances	(31)	(31)
Innovative hybrid Tier-1 capital	75	89
Non-innovative hybrid Tier-1 capital	227	221
TOTAL TIER-1 CAPITAL	1,731	1,745
TIER-2		
Reserves arising from revaluation of property and unrealised gains on available foresale	31	30
Qualifying subordinated liabilities		
Undated loan capital	35	32
Dated loan capital	185	238
Deduction of certain securitisation exposures not included in risk-weighted assets	(73)	(24)
Deduction excess of expected losses over impairment allowances	(31)	(31)
TOTAL TIER-2 CAPITAL	147	245
TOTAL REGULATORY CAPITAL (capital base)	1,878	1,990

Changes in Core Tier-1 and Tier-1 capital

The core Tier-1 capital has increased by EUR 43 million and the main contribution is the net profit of the year (including proposed dividend) of EUR 33 million. Tier-1 capital has decreased by EUR 14 million; the main contribution is the increase of the deduction of securitisation exposures of EUR 73 million, due to non-investment grade ratings. 50% should be deducted from Tier-1 capital and 50% should be deducted from Tier-2 capital.

Changes in Tier-2 capital

The Tier-2 capital has decreased by EUR 98 million. The main reasons are the buy-back of dated loan capital for an amount of EUR 45 million and the increase of the deduction of securitisation exposures of EUR 73 million, see section above.

Capital Adequacy

The capital adequacy of NIBC is managed at NIBC Holding level.

The principal ratios for reviewing the capital adequacy of NIBC are the Tier-1 ratio and the BIS ratio. These ratios, which were implemented by the *Bank for International Settlements (BIS)*, are intended to promote comparability between financial institutions. They are based on the Basel II Accord.

NIBC monitors the developments in the ratios on a monthly basis, including comparison between the expected ratios and the actual ratios. These ratios indicate capital adequacy to mitigate on-balance credit risks, including off-balance sheet commitments, market risks, operational risks and other risk positions expressed as risk weighted items in order to reflect their relative risk. During the year ended 31 December 2010, NIBC complied amply with the capital requirements imposed by the Dutch Central Bank, which require a minimum Tier-1 ratio of 4% and a minimum BIS ratio of 8%.

Capital ratios

The Tier-1 ratio is defined as Tier-1 capital divided by *Risk Weighted Assets (RWA)*.

The BIS ratio is defined as Total Capital (which is the sum of Tier-1 capital and Tier-2 capital) divided by RWA.

NIBC's Tier-1 capital ratio stood at 14.0% at end-2010. This is a healthy position that also implies that NIBC can fulfil the tightened Basel III requirements that will be introduced in the coming years.

Tables 40 and 41 show the capital ratios, capital requirements and RWA for NIBC.

Table 40 NIBC Holding N.V. Capital ratios, Basel II actual

IN EUR MILLIONS	2010	2009
CAPITAL RATIOS		
Core Tier-1 ratio	12.4	13.2
Tier-1 ratio	14.0	15.5
BIS ratio	15.2	17.7

Table 4I Breakdown of EAD, capital requirements and RWA of NIBC Holding N.V.

IN EUR MILLIONS	2010			2009		
	EAD	RWA	Capital requirement	EAD	RWA	Capital requirement
CREDIT RISK	21,653	11,801	944	21,847	10,445	836
AIRB APPROACH						
- of which corporates	9,434	6,340	507	8,356	5,206	417
- of which retail	5,066	789	63	4,573	624	50
- of which securitisations	1,461	1,055	84	1,106	892	71
- of which equities	540	2,000	160	501	1,847	148
STANDARDISED APPROACH						
- of which institutions	2,309	703	56	3,993	775	62
- of which sovereigns	1,644	2	0	1,864	0	0
- of which corporates	625	625	50	737	737	59
- of which retail	507	222	18	576	248	20
- of which equities	4	3	0	49	24	2
- of which other	62	62	5	92	92	7
MARKET RISK		244	20		98	8
- of which trading book VaR		213	17		54	4
- of which FX Standardised approach		31	3		44	4
OPERATIONAL RISK		313	25		704	56
Standardised approach		313	25		704	56
TOTAL (including Basel I floor)	21,653	12,358	989	21,847	11,247	900

Small differences are possible in the table due to rounding

Appendix I

Scope of Application

NIBC financial consolidation scope is based on IFRS, which is determined in accordance with IAS 27 Consolidated and Separate Financial Statements, IAS 28 Investments in Associates, IAS 31, Interest in Joint Ventures, and SIC 12 Consolidation Special Purpose Entities.

Subsidiaries are all entities (including special purpose entities) controlled by NIBC Holding N.V. Control exists when the company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The existence and effect of potential voting rights that are currently exercisable or currently convertible are considered when assessing whether the company controls another entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

NIBC applies a policy of treating transactions with minority interests as transactions with parties external to the Group. Minority interests in the net assets and net results of consolidated subsidiaries are shown separately on the balance sheet and income statement.

A joint venture exists where NIBC has a contractual arrangement with one or more parties to undertake activities typically, though not necessarily, through entities that are subject to joint control. The Group's interests in jointly controlled entities are accounted for by proportionate consolidation. NIBC combines its share of the joint venture's individual income and expenses, assets and liabilities and cash flows on a line-by-line basis with similar items in NIBC's financial statements.

Associates are those entities over which NIBC has significant influence, but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights. Except as otherwise described below, investments in associates are accounted for by the equity method of accounting and are initially recognised at cost. The Group's investment in associates includes goodwill (net of any accumulated impairment loss) identified on acquisition.

With effect from 1 January 2007, all newly acquired investments in associates held by the venture capital organisation within the operating segment Merchant Banking, which is considered to be a venture capital organisation, as that term is used in IAS 28, are designated upon initial recognition as financial assets at fair value through profit or loss. These assets are initially recognised at fair value and subsequent changes in fair value are recognised in the income statement in the period of the change in fair value.

Tables 1-5 present the entities that form part of the capital base of NIBC Holding N.V.

Table 1 Group principal undertakings included in the capital base

Subsidiaries of NIBC Holding N.V.	Voting power	Domicile	Consolidation method
NIBC Bank N.V.	100%	The Netherlands	Purchase method
NIBC Venture Capital N.V.	100%	The Netherlands	Purchase method
NIBC Credit Management Inc.	100%	The United States	Purchase method
NIBC Investment Management N.V.	100%	The Netherlands	Purchase method
NIBC Investments N.V.	100%	The Netherlands	Purchase method

Table 2 Principal undertakings of NIBC Bank N.V. included in the capital base

Subsidiaries of NIBC Bank N.V.	Voting power	Domicile	Consolidation method
NIBC Bank Ltd	100%	Singapore	Purchase method
BV NIBC Mortgage Backed Assets	100%	The Netherlands	Purchase method
Parnib Holding N.V.	100%	The Netherlands	Purchase method
Counting House B.V.	100%	The Netherlands	Purchase method
NIBC Principal Investments B.V.	100%	The Netherlands	Purchase method

Table 3 Principal investments of NIBC N.V. in associates included in the capital base

Associates of NIBC Bank N.V.	Voting power	Domicile	Consolidation method
PE Express I B.V., Breskens	37.5%	The Netherlands	Equity method
PE Express II B.V., Breskens	37.5%	The Netherlands	Equity method
PE Express III B.V., Breskens	35%	The Netherlands	Equity method
PE Express IV B.V., Breskens	35%	The Netherlands	Equity method

Table 4 Prudential filter: subsidiaries treated as associates included in the capital base

Subsidiaries of NIBC Bank N.V.	Voting power	Domicile	Consolidation method
GRW Reinfurt GmbH	93.4%	Germany	Equity method
Olympia Nederland Holding B.V.	100.0%	The Netherlands	Equity method
Cyclomedia Technology B.V.	64.4%	The Netherlands	Equity method
NIBusker Holding B.V.	75.0%	The Netherlands	Equity method

Appendix 2

List of Abbreviations

ABS	Asset-Backed Securities
AIRB	Advanced Internal Ratings' Based (approach)
ALCO	Asset & Liability Committee
ALM/MR	Asset & Liability Management and Market Risk department
BIS	Bank for International Settlements
BPV	Basis-point Value
CCF	Credit Conversion Factor
CCR	Counterparty Credit Rating
CDO	Collateralised Debt Obligations
CDS	Credit Default Swap
CLO	Collateralised Loan Obligations
CMBS	Collateralised Mortgage-Backed Securities
CRD	Capital Requirements Directive
CRM	Credit Risk Management department
CRO	Chief Risk Officer
CSA	Credit Support Annex
CVA	Credit Value Adjustments
DA	Distressed Assets department
DNB	Dutch Central Bank
EAD	Exposure at Default
EC	Economic Capital
ECB	European Central Bank
ECC	Engagement and Compliance Committee
EL	Expected Loss
FMCR	Financial Markets Credit Risk department
FX	Foreign Exchange
FPSO	Floating, Production, Storage and Offloading
IC	Investment Committee
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards
IMA	Internal Model Approach
IRS	Interest Rate Swaps
ISDA	International Swaps and Derivatives Association
LGD	Loss Given Default
LTiMV	Loan-to-Indexed Market Value
NHG Guarantee	Dutch government guarantee
ORM	Operational Risk Management department
OTC	Over-the-Counter derivatives
P&L	Profit & Loss account

PD	Probability of Default
PECDC	Pan-European Credit Data Consortium
RAROC	Risk-Adjusted Return on Capital
RC	Pillar-1 Regulatory Capital
RL	Realised Loss
RMBS	Residential Mortgage-Backed Securities
RMC	Risk Management Committee
RP&R	Risk Policy and Reporting department
RWA	Risk Weighted Assets
SPE	Special Purpose Entity
SREP	Supervisory Review and Evaluation Process
TC	Transaction Committee
VaR	Value-at-Risk

NIBC Holding N.V.

Carnegieplein 4

2517 KJ The Hague, the Netherlands

P.O. Box 380

2501 BH The Hague, the Netherlands

www.nibc.com