

Annexes

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Updated version of Financial Business Act (section 1) & Mortgage-Credit Loans and Mortgage-Credit Bonds etc. Act (section 2)

(Unofficial translation)

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Executive order on the Issue of Bonds, the Balance Principle and Risk Management

(Unofficial translation)

Annex 1

Unofficial translation. Only the Danish document has legal validity

Extract from bill no 577 of 6 June 2007

Amending the Financial Business Act and Various Other Acts
(Covered Bonds)

Section 1

The Financial Business Act, see Consolidation Act No. 286 of 4 April 2006, as amended by section 1 of Act No. 527 of 7 June 2006, section 3 of Act No. 108 of 7 February 2007 and section 5 of Act No. 181 of 28 February 2007, is amended as follows:

1. In section 1(4), second sentence, “sections 360,” shall be amended to read: “section 152a(2), second sentence, section 360,”.

2. The following shall be inserted after section 16:

“**16a. (1)** The Danish FSA (‘the FSA’) may license commercial banks and mortgage banks to issue covered bonds.

(2) Commercial banks and mortgage banks with a licence under subsection (1) hereof and the ship financing institution with a licence under section 2c of the Danish Act on a Ship Financing Institution (*lov om et skibsfinansieringsinstitut*) shall have the exclusive right to issue covered bonds. Mortgage banks with a licence under subsection (1) hereof shall also have the exclusive right to issue covered mortgage bonds.

(3) Bonds issued by credit institutions that have been granted a licence in another country within the European Union, or in a country with which the Community has entered into an agreement for the financial area may also be designated covered bonds provided that they satisfy the conditions of Annex VI, Part 1, points 68-71, of the Directive relating to the taking up and pursuit of the business of credit institution.

(4) The FSA shall lay down detailed rules on

- 1) the assets in which the lending commercial bank or mortgage bank may place payments received until settlement takes place, and
- 2) the lending commercial bank’s or mortgage bank’s verification of separation and settlement to the issuing commercial bank or mortgage bank.

16b. (1) A commercial bank or a mortgage bank may fund loans secured by mortgages on real estate by covered bonds or covered mortgage bonds issued by another commercial bank or mortgage bank.

(2) The FSA shall approve the issue of covered bonds or covered mortgage bonds under subsection (1) hereof.

16c. If a loan is to be funded by covered bonds or covered mortgage bonds issued by another commercial bank or mortgage bank, such funding arrangement shall appear from the loan agreement concluded between the lending commercial bank or mortgage bank and the borrower. The loan agreement shall also state that the lending and issuing institutions may exchange information on the borrower, see section 120b.

16d. (1) If a commercial bank or a mortgage bank grants a loan secured by a mortgage on real estate on the basis of covered bonds or covered mortgage bonds issued by another commercial bank or mortgage bank, such loan and the related mortgage shall be assigned to the issuing institution to hold as its own.

(2) Assignment according to subsection (1) hereof cannot be avoided pursuant to sections 67, 70 or 72 of the Danish Insolvency Act (*konkursloven*). However, avoidance may be effected pursuant to the said provisions if the assignment did not specifically appear to be ordinary.

16e. If a commercial bank or a mortgage bank grants a loan secured by a mortgage on real estate on the basis of covered bonds or covered mortgage bonds issued by another commercial bank or mortgage bank, the borrower may discharge his liabilities by payment to the lending commercial bank or mortgage bank, unless the issuing commercial bank or mortgage bank separately notifies him otherwise.

16f. (1) The lending commercial bank or mortgage bank shall keep payments received which relate to loans secured by mortgages on real estate on the basis of another commercial bank's or mortgage bank's issue of covered bonds or covered mortgage bonds separate from the other funds of the institution.

(2) The lending commercial bank or mortgage bank shall verify the separation of funds on a regular basis.

(3) The lending commercial bank or mortgage bank shall settle payments received with the issuing institution according to a predetermined plan.

(4) The FSA shall lay down detailed rules on the verification and settlement with the issuing institution.

16g. If the lending commercial bank or mortgage bank is declared bankrupt, payments encompassed by section 16f, see section 16b(1), which the lending commercial bank or mortgage bank has received, but not yet settled, shall accrue to the issuing commercial bank or mortgage bank and shall not be included in the insolvent estate."

3. The following shall be inserted after section 120a:

"120b. A lending commercial bank or mortgage bank may disclose information on a borrower to the issuing commercial bank or mortgage bank if a loan agreement has been concluded stating that the loan may be funded by covered bonds or covered mortgage bonds issued by another commercial bank or mortgage bank. Information may be exchanged between the lending commercial bank or mortgage bank and the commercial bank or mortgage bank issuing the covered bonds or covered mortgage bonds by which the loan is funded to the extent necessary for the purpose of risk

management and management of the portfolio in the register or the portfolio in a series or groups of series with series reserve fund.”

4. The following shall be inserted after section 152 before the heading “Special regulations for mortgage banks regarding the placement and liquidity of funds”:

“**152a. (1)** Commercial banks licensed to issue covered bonds shall establish and maintain a group of assets that must be kept separate from the other assets of the bank. The total value of the assets shall correspond at least to the value of the covered bonds issued at all times, and the mortgage collateral of the individual loan shall comply with the relevant lending limit at all times.

(2) If the value of the assets referred to in subsection (1) hereof no longer corresponds at least to the value of the covered bonds issued or does not comply with the relevant lending limit, the commercial bank shall promptly provide additional collateral to satisfy the requirement and shall notify the FSA thereof. For loans offered in Denmark, the duty to provide additional collateral and the related expenses cannot be imposed on the borrowers whose decreasing property values prompted the requirement for additional collateral.

(3) If the commercial bank fails to provide additional collateral under subsection (2) hereof, all bonds issued in the relevant register, see section 152g(1), shall lose their designation covered bonds. If subsequently the bonds again satisfy the requirements for covered bonds, the FSA may allow such bonds to be re-designated covered bonds.

(4) The provision of collateral under subsection (2) hereof cannot be avoided pursuant to sections 70 or 72 of the Insolvency Act. However, avoidance may be effected pursuant to the said provisions if the provision of collateral did not specifically appear to be ordinary.

152b. (1) Commercial banks licensed to issue covered bonds may raise loans to satisfy the requirement for the provision of additional collateral.

(2) The loan agreement shall state the register, see section 152g(1), for which the loan funds raised according to subsection (1) hereof are to be applied as additional collateral.

(3) Loan funds raised under subsection (1) hereof shall be placed in the asset types referred to in section 152c. As from the time when the loan is raised, the assets shall be placed in a separate account, a separate custody account or otherwise marked as deriving from the relevant loan.

152c. (1) The following types of assets may be included as collateral for the issue of covered bonds:

- 1) Loans secured by registered mortgages on real estate, see section 152d.
- 2) Loans secured by liens on ships registered in the Danish Ship Register, the Danish International Ship Register or any other internationally recognised ship register offering equivalent security, see section 152f, and loans for the purpose of funding the building or renovation of ships granted without liens on ships.
- 3) Bonds or instruments of debt issued by or guaranteed by central governments, central banks, public entities, regional or local authorities in a country within the European Union or in a country with which the Community has entered into an agreement for the financial area.

- 4) Bonds or instruments of debt issued by or guaranteed by central governments, central banks, public entities, regional or local authorities in a country outside the European Union with which the Community has not entered into an agreement for the financial area, multilateral development banks or international organisations, if a calculation of the risk-weighted items weights the non-subordinated and unsecured debt of the issuers concerned by 0%, see Annex VI of the Directive relating to the taking up and pursuit of the business of credit institution.
- 5) Bonds or instruments of debt issued by entities referred to in nos. 3 and 4 hereof and where a calculation of the risk-weighted items weights the issuer's non-subordinated and unsecured debt at 20%, see Annex VI of the Directive relating to the taking up and pursuit of the business of credit institutions. It is a condition that the value by which these assets are included does not exceed 20% of the nominal value of the issuer's outstanding covered bonds.
- 6) Bonds or instruments of debt issued by credit institutions, if a calculation of the risk-weighted items weights the non-subordinated and unsecured debt of the relevant credit institutions at 20%, see Annex VI of the Directive relating to the taking up and pursuit of the business of credit institutions. Bonds or instruments of debt issued by a credit institution in a country within the European Union or in a country with which the Community has entered into an agreement for the financial area that have an original term of 100 days or less may be included if a calculation of the risk-weighted items weights the non-subordinated and unsecured debt of the relevant credit institution at not more than 50%, see Annex VI of the Directive relating to the taking up and pursuit of the business of credit institutions. The value by which the assets referred to in the first and second sentences hereof are included may not exceed 15% of the nominal value of the issuer's outstanding covered bonds. The 15% limit shall apply to the entire credit institution exposure according to this no. and no. 7. Receivables arising in connection with mortgage payments on and repayments of loans secured by mortgages on real estate shall not be included in the 15% limit..
- 7) Other non-subordinated receivables from and guarantees provided by credit institutions as referred to in no. 6 hereof. It is a condition that the value at which these receivables and guarantees are included does not exceed 15% of the nominal value of the issuer's outstanding covered bonds. The 15% limit shall apply to the total credit institution exposure according to no. 6 and this no. Receivables arising in connection with mortgage payments on and repayments of loans secured by mortgages on real estate, shall not be included in the 15% limit..

(2) A covered bond may not be issued with both real estate and ships as collateral.

(3) The FSA may authorise the use of assets as collateral for the issue of covered bonds other than those referred to in subsection (1) hereof and may set other limits for the proportion of the collateral for the bond issue which the relevant types of assets may account for, if such authorisation is in accordance with the Directive relating to the taking up and pursuit of the business of credit institutions.

152d. (1) For loans secured by registered mortgages on real estate and granted on the basis of the issue of covered bonds, the terms, repayment profiles and lending limits stipulated in sections 3-5 of the Danish Mortgage Credit Loans and Mortgage Credit Bonds etc. Act (*lov om realkreditlån og realkreditobligationer m.v.*), shall apply, but see subsections (2) and (3) hereof.

(2) For loans secured by registered mortgages on real estate and granted on the basis of the issue of covered bonds for properties covered by section 5(1) of the Mortgage Credit Loans and Mortgage

Credit Bonds etc. Act, sections 3 and 4 of the Mortgage Credit Loans and Mortgage Credit Bonds etc. Act shall not apply if the lending limit does not exceed 75%.

(3) For loans secured by registered mortgages on real estate and granted on the basis of the issue of covered bonds for commercial properties encompassed by section 5(3)(ii) and (iii), of the Mortgage Credit Loans and Mortgage Credit Bonds etc. Act, the lending limit of 60% may be raised to 70%, if additional collateral of not less than 10% is provided for the part of the loan that exceeds 60% of the value of the property. For loans for properties encompassed by section 5(2) of the Mortgage Credit Loans and Mortgage Credit Bonds etc. Act, the lending limit of 70% may be used only if additional collateral of not less than 10% is provided for the part of the loan that exceeds 60% of the value of the property.

(4) Fixtures and fittings encompassed by section 38 of the Danish Registration of Property Act (*tinglysningsloven*) may be included in a valuation of the property.

(5) Fittings installed in a commercial property for the purpose of its operation may be included in the valuation. The livestock belonging to an agricultural property may also be included in the valuation to the extent that the livestock forms part of the continuous production. With regard to the mortgaging of agricultural properties, the value of the livestock forming part of the continuous production may be included in the value of land and buildings by not more than 30%.

152e. (1) Loans secured by mortgages on real estate and granted on the basis of the issue of covered bonds shall be secured by a separate mortgage and may not be granted against collateral provided in the form of mortgages registered to the mortgagor and letters of indemnity, but see subsections (2) and (3) hereof. The mortgage shall state that it may serve as security for a loan funded by the issue of covered bonds.

(2) Mortgages on real estate registered before 1 July 2007 may serve as security for loans funded by the issue of covered bonds.

(3) The FSA may grant exemptions from subsection (1) hereof for loans granted for real estate located outside Denmark, the Faeroe Islands and Greenland.

152f. For loans secured by liens on ships, the commercial bank may grant loans of up to 70% of the value fixed for the ship used as collateral. The term of loans granted may not exceed 15 years at the date of disbursement of the loan. For building loans, the term may not exceed four years counting from the date of the first disbursement. When fixing the term of loans, due consideration must be paid to the average life of the type, age and condition, etc., of the relevant ship.

152g. (1) Commercial banks shall keep registers of assets covered by sections 152a and 152b and of financial instruments that satisfy the conditions of subsection (2) hereof. A commercial bank may keep one or more registers. A register may not include assets secured on both real estate and ships.

(2) Financial instruments may be included in a register of assets only if they are used for hedging risks between the assets in the register on the one side and the covered bonds issued on the other side and where the agreement on the financial instrument specifies that the commercial bank's suspension of payments, bankruptcy or failure to observe the obligation to provide additional collateral according to section 152a(2) does not constitute a breach..

(3) Registered assets, including financial instruments, shall serve to satisfy the holders of the covered bonds and the counterparties with whom the agreements on the financial instruments have been concluded, and subsequently to satisfy loans raised under section 152b(1).

(4) The commercial bank shall report to the FSA which assets, etc., are included in the register. The FSA, or the party duly authorised by the FSA, shall verify the existence of the said assets.

152h. The FSA shall lay down detailed rules on the

- 1) valuation of covered bonds issued and the ongoing calculation of the value of the assets relative to the covered bonds;
- 2) valuation of the assets securing the issue of covered bonds, see section 152c(1);
- 3) conditions on which building loans for the building or renovation of ships may be granted, see section 152c(1), no. 2;
- 4) organisation, registration and verification of the existence of assets registered, see section 152g;
- 5) granting of loans funded by the issue of covered bonds secured by mortgages on real estate by commercial banks in cases where there is no clean registered mortgage and in such cases what alternative collateral may be provided; and
- 6) limitation of risks in connection with the issue of covered bonds, including interest rate risks, currency risks and option risks.”

5. The following shall be inserted after “Mortgage bonds” in section 162(1), no. 3: “, covered mortgage bonds and covered bonds issued by mortgage banks, commercial banks or the ship financing institution”.

6. In section 171(1) and section 172(1), “section 124(1) and (4),” shall be amended to read: “section 124(1) and (4)-(6),”.

7. In section 173(1) and section 174(1), “section 125(2) and (7)” shall be amended to read: “section 125(1) and (7)-(9)”.

8. The following shall be inserted in section 224 as a new subsection after subsection (2):

“(3) If a commercial bank or mortgage bank is licensed to issue covered bonds, such licence may be withdrawn if:

- 1) the commercial bank seriously or repeatedly violates sections 152a-152g or rules laid down pursuant to section 16a(4) or section 152h;
- 2) the mortgage bank seriously or repeatedly violates sections 33a-33e of the Mortgage Credit Loans and Mortgage Credit Bonds etc. Act or rules laid down pursuant to section 16a(4) of this Act or section 33 of the Mortgage Credit Loans and Mortgage Credit Bonds etc. Act; or
- 3) the issue of covered bonds has not been commenced within 12 months of the FSA having granted a licence to the institution.”

Subsections (3) and (4) shall then become subsections (4) and (5).

9. In section 226(1), “sections 223-225” shall be amended to read: “section 223; section 224(1), (2), (4) and (5) and section 225”.

10. In section 226(2), “section 224(2) and (3)” shall be amended to read: “section 224(2) and (4)”.

11. The following shall be inserted after section 247 before the heading “Special regulations for insurance companies regarding restoration and other measures”:

“**247a. (1)** If the FSA withdraws the licence of a commercial bank under section 224(1), no. 1 or 2; if the FSA according to section 234(1) or the commercial bank files a petition for bankruptcy; or if the commercial bank is declared bankrupt following a petition filed by other parties, the FSA shall decide that the repayment from the commercial bank to the holders of the covered bonds issued by the commercial bank shall be subject to administration. In situations encompassed by section 224(3), no. 1, the FSA may also decide that the commercial bank’s repayment to the holders of the covered bonds issued by the bank shall be subject to administration. At the same time, the FSA shall appoint an administrator to administer the repayment to the holders of covered bonds in cooperation with any co-administrators.

(2) When the repayment from a commercial bank to the holders of covered bonds issued by the commercial bank becomes subject to administration, the FSA shall ensure that the decisions to commence administration and appoint an administrator are registered with or otherwise made public by the Danish Commerce and Companies Agency. The administration estate shall also notify the borrowers that future payments relating to the individual borrower’s instalment and interest payments on the loan may be effected in full discharge to the administration estate only.

(3) The administrator may appoint one or more co-administrators with knowledge of matters relevant for the administration.

(4) The administration estate shall pay fees to administrators and any other expenses in connection with the administration. The amount of fees shall be fixed according to negotiations with the FSA.

(5) The administration estate shall be subject to supervision by the FSA.

247b. (1) At the beginning of the administration, the registered assets, see section 152g(1), shall promptly be transferred to the administration estate. The administration estate represented by the administrator shall be entitled to dispose of the said assets. For investment securities, this shall be registered at a central securities depository; for rights in real estate, this shall be registered in the Land Register; and for ships, this shall be registered in a ship register.

(2) If a commercial bank is declared bankrupt, the liquidator shall immediately transfer the assets referred to in subsection (1) hereof to the administrator.

(3) The administrator shall have the registered assets valued in accordance with the provisions laid down pursuant to section 152h, no. 2.

(4) The administration estate cannot be closed until repayment has been made of all the bonds, for which the registered assets have been provided as collateral, and the financial instruments have matured.

(5) If a commercial bank is declared bankrupt after administration has commenced, the said bankruptcy shall have no effect on the administration estate.

(6) The administrator shall manage the assets received from the commercial bank, and may require all material necessary for the administration from the bank, possibly with the assistance of a bailiff.

247c. If a commercial bank is declared bankrupt, or the bank fails to observe the obligation to provide additional collateral under section 152a(2), the holders of the covered bonds or the lenders under section 152b(1) cannot claim such bankruptcy or failure to constitute a cause for early repayment of payment obligations. Nor shall the borrowers of loans granted on the basis of covered bonds be caused to forfeit their right, if any, to repay the loan, in full or in part, in accordance with the terms of repayment that apply to the loans.

247d. (1) If a commercial bank is declared bankrupt, the registered assets, including financial instruments, calculated after deduction of expenses for the administrator, shall be used to pay claims from the holders of covered bonds and counterparties on the financial instruments secured by the registered assets and agreements. Then loans raised by the commercial bank for the purpose of providing additional collateral, see section 152b(1), shall be paid. Any excess funds shall be included in the insolvent estate, see section 32 of the Insolvency Act.

(2) The individual holders of covered bonds, counterparties on the financial instruments and lenders under section 152b(1) cannot raise any claims against the estate. However, on behalf of the administration estate, the administrator may prove claims against the estate of amounts required according to the valuation to satisfy the holders of the covered bonds, counterparties on the financial instruments and lenders under section 152b as well as any claims of interest accrued on the said claims from issue of the bankruptcy order, in order to satisfy the bondholders, counterparties on financial instruments and lenders under section 152b.

(3) If the registered funds are insufficient to satisfy the holders of the covered bonds and counterparties on the registered financial instruments and to cover any debt raised by the commercial bank for the purpose of providing additional collateral, see section 152b(1), the administrator may prove as ordinary claims any remaining uncovered claims against the commercial bank's assets available for distribution at the closing and dissolution of the administration estate.

(4) Any excess registered funds cannot be transferred to another register, but shall be transferred to the insolvent estate.

(5) No set-off by a creditor as referred to in section 42 of the Insolvency Act may be made to satisfy a claim owing to the commercial bank and relating to loans raised on the basis of covered bonds issued by the bank.

247e. If the commercial bank is declared bankrupt, proceeds from loans raised by the bank for the purpose of satisfying the requirement for provision of additional collateral, see section 152a(2), which do not form part of a register, shall serve to cover the holders of the covered bonds and counterparties on financial instruments of the register for the purpose of which the loan was raised to provide additional collateral. Any excess funds shall be disbursed to the lender.

247f. (1) Holders of bonds having lost the designation covered bonds, see section 152a(3), first sentence, and counterparties on the registered agreements on financial instruments secured by the registered assets and agreements, shall retain the position assigned to holders of covered bonds and

financial counterparties according to Danish insolvency law, see section 247d(1), first sentence. The same applies to loans raised by the commercial bank for the purpose of providing additional collateral, see section 152b.

(2) The administrator shall prove any remaining claims as ordinary claims against the insolvent estate of the commercial bank.

(3) The provisions of section 152a(1), first sentence, sections 152b-152h and sections 247a-247e shall apply correspondingly to bonds having lost the designation covered bonds, see section 152a(3), and the related financial instruments.”

12. In section 253(1), “section 224(1), nos. 1 and 2 and (4)” shall be amended to read: “section 224(1), nos. 1 and 2 and (5)”.

13. In section 373(1), the following shall be inserted after “section 11(1)-(4);”: “section 16a(2); section 16b(2);”.

14. In section 373(2), the following shall be inserted after “Any person violating the provisions in”: “section 16c; section 16d(1); section 16f(1)-(3);”.

15. In section 373(2), “sections 122, 123, 158, 159 and 167” shall be amended to read: “sections 122 and 123; section 152a(1), first sentence; section 152c(2); section 152e(1); section 152g(1), first and third sentences, (2) and (4); sections 158, 159 and 167”.

16. In section 373(2), the following shall be inserted as the second sentence:

“Similar punishment shall apply to any violation of the duty to notify under section 152a(2), first sentence.”

17. In Annex 3, the following shall be inserted after no. 1 as a new number:

“2) Granting of loans without mortgages on real estate to public authorities or against a guarantee from a public authority to undertake primary liability.”

Nos. 2 and 3 shall then become nos. 3 and 4.

Section 2

Act No. 454 of 10 June 2003 on Mortgage Credit Loans and Mortgage Credit Bonds etc., as amended by section 105 of Act No. 90 of 31 January 2007, shall be amended as follows:

1. The following shall be inserted as a footnote to the title of the Act:

"1) The Act contains provisions implementing parts of Directive 2006/48/EC of 14 June 2006 of the European Parliament and the Council relating to the taking up and pursuit of the business of credit institution (recast) (OJ 2006 No. L 177, p. 1)."

2. The following shall be inserted in section 1(1), first sentence, after "This Act shall apply to mortgage bonds": ", covered mortgage bonds, covered bonds".

3. Section 2(1) shall be drafted as follows:

"Mortgage loans shall be granted against recorded mortgages on real estate according to the rules stipulated in this Part. Loans may be granted without mortgages on real estate to public authorities or against a guarantee from a public authority to undertake primary liability as mentioned in section 152c(1), nos. 3-5, of the Financial Business Act."

4. Section 6 shall be repealed.

5. The following shall be inserted in *section 8* as a new subsection after subsection (5):

"(6) To the extent that a loan is granted on the basis of covered mortgage bonds and covered bonds, the loan may be disbursed before final registration, see subsections (1)-(5) hereof, if collateral is provided in accordance with section 152c(1), nos. 3-7, of the Financial Business Act. In the event that the collateral provided takes the form of a guarantee from a commercial bank, the guarantee shall be covered by the 15% limit stipulated in section 152c(1), nos. 6-7, of the Financial Business Act."

Subsection (6) shall then become subsection (7).

6. In *section 8(6)*, which shall become subsection (7), "(1)-(5)" shall be amended to "(1)-(6)".

7. Section 19 shall be drafted as follows:

19. Mortgage bonds issued before 1 July 2007 shall be negotiable homogenous debt instruments admitted for trading in regulated markets in countries within the European Union or countries with which the Community has entered into an agreement for the financial area, or corresponding markets in other countries."

8. Section 20(1) shall be drafted as follows:

"Funds raised by the issue of mortgage bonds or covered mortgage bonds or other securities may solely be used for lending against mortgages on real estate or lending to public authorities or against a guarantee from a public authority to undertake primary liability, but see subsections (2) and (3) hereof. However, additional collateral may be provided for covered mortgage bonds pursuant to section 33d(1) hereof."

9. Section 21 shall be drafted as follows:

21. The FSA shall lay down detailed rules on limitation of risks in connection with the issue of mortgage bonds, covered mortgage bonds, covered bonds and other securities, including interest rate risks, currency risks and option risks."

10. The following shall be inserted in section 26 as a new subsection after subsection (3):

"(4) Financial instruments may be included as assets or liabilities in a series or group of series with a series reserve fund only if they are used for hedging risks between the assets relating to the series on the one side and the mortgage bonds, covered mortgage bonds and covered bonds issued on the other side, where the agreement on the financial instrument specifies that the mortgage bank's suspension of payments, bankruptcy or failure to observe the obligation to provide additional collateral according to section 33d(1) does not constitute a breach."

Subsection (4) shall then become subsection (5).

11. In section 27(1), first sentence, section 29(1), section 31, second sentence, section 32(1), first sentence, and section 32(2), first and third sentences, the following shall be inserted after "mortgage bonds": ", covered mortgage bonds, covered bonds".

12. In section 27(1), the following shall be inserted after the second sentence:

"Then the debt incurred by the mortgage bank for the purpose of providing additional collateral, see section 33e hereof, shall be covered."

13. The following shall be inserted in section 27 as subsection (3):

"(3) If a mortgage bank is declared bankrupt, counterparties on the financial instruments concluded to hedge risks in a series or group of series of mortgage bonds, covered mortgage bonds or covered bonds, see section 26(4) hereof, shall rank equally with the holders of mortgage bonds, covered mortgage bonds or covered bonds in the said series or group of series according to Danish insolvency law, see subsection (1), first sentence, and sections 31 and 32 hereof."

14. The following shall be inserted after section 27:

"**27a.** Holders of bonds having lost the designation covered mortgage bonds or covered bonds, see section 33d(2) hereof, and counterparties on the financial instruments shall retain the position assigned to holders of covered mortgage bonds, covered bonds and financial counterparties according to insolvency law. The same shall apply to cover of debt incurred by the mortgage bank for the purpose of providing additional collateral, see section 33e hereof.

(2) The provisions of sections 27b and 28-33 shall apply correspondingly to bonds having lost the designation covered mortgage bonds or covered bonds and the related financial instruments.

27b. If the mortgage bank is declared bankrupt, proceeds from loans raised by the bank for the purpose of satisfying the requirement for provision of additional collateral, see section 33d(1) hereof, and not included in a series or group of series, shall serve to cover the holders of covered bonds or covered mortgage bonds and counterparties on the financial instruments in the series or group of series for the purpose of which the loan was raised to provide additional collateral. Any excess funds shall be disbursed to the lender."

15. Section 28 shall be drafted as follows:

If a mortgage bank is declared bankrupt, holders of mortgage bonds, covered mortgage bonds, covered bonds and other securities or lenders under section 33e(1) cannot submit such bankruptcy as a cause for early repayment of payment obligations. Nor shall the mortgage bank's borrowers forfeit their right to repay mortgage loans or loans granted on the basis of issue of covered mortgage bonds or covered bonds in full or in part, in accordance with the special repayment terms that apply to the loan.

(2) In the event that a mortgage bank fails to observe the obligation to provide additional collateral under section 33d(1) hereof, holders of the covered mortgage bonds or covered bonds or lenders under section 33e(1) cannot submit such failure as a cause for early repayment of payment obligations.."

16. The following shall be inserted in section 32(1), second sentence, after "With the consent of the appointed supervisory authority, the mortgage-credit institution": "conclude agreements on financial instruments"

17. The following shall be inserted in section 32(3), third sentence, after "The liquidator may": "conclude agreements on financial instruments"

18. The following shall be inserted after section 33:

"Part 4a

Covered mortgage bonds and covered bonds

33a. Mortgage banks shall be entitled to fund lending, see section 2(1) hereof, by issuing covered mortgage bonds, provided that the bank is licensed to do so under section 16a(1) of the Financial Business Act.

(2) Loans funded by covered mortgage bonds shall be granted in separate series with a series reserve fund.

(3) The value of the assets covering the covered mortgage bonds issued shall always correspond at least to the value of the covered mortgage bonds issued, and the mortgage collateral of the individual loan shall comply with the relevant lending limit at all times.

33b. Mortgage banks may fund lending secured by the asset types listed in section 152c(1), nos. 1 and 3-7, of the Financial Business Act by issuing covered bonds, provided that the bank is licensed to do so under section 16a(1) of the Financial Business Act. Section 152c(3) of the Financial Business Act shall apply correspondingly.

(2) Loans funded by covered bonds shall be granted in separate series with a series reserve fund.

(3) The value of the assets covering the covered bonds issued shall always correspond at least to the value of the covered bonds issued, and the mortgage collateral of the individual loan shall comply with the relevant lending limit at all times.

33c. For loans funded by covered mortgage bonds or covered bonds, the terms, repayment profiles and lending limits stipulated in sections 3-5 hereof shall apply.

(2) For loans funded by covered mortgage bonds or covered bonds secured on real estate covered by section 5(1) hereof, sections 3 and 4 shall not apply if the lending limit does not exceed 75%.

(3) For loans funded by covered mortgage bonds or covered bonds for commercial properties encompassed by section 5(3), nos. 2 and 3 hereof, the lending limit of 60% may be raised to 70%, if additional collateral of not less than 10% is provided for the part of the loan that exceeds 60% of the value of the property. For loans funded by covered mortgage bonds or covered bonds for properties encompassed by section 5(2) hereof, the lending limit of 70% may be used only if additional collateral of not less than 10% is provided for the part of the loan that exceeds 60% of the value of the property.

(4) Fixtures and fittings encompassed by section 38 of the Danish Registration of Property Act (*tinglysningsloven*) may be included in the valuation of real estate.

(5) Fittings installed in a commercial property for the purpose of its operation may be included in the valuation. The livestock belonging to an agricultural property may also be included in the valuation to the extent that the livestock forms part of the continuous production. With regard to the mortgaging of agricultural properties, the value of the livestock forming part of the continuous production may be included in the value of land and buildings by not more than 30%.

(6) Loans secured by mortgages on real estate and granted on the basis of the issue of covered mortgage bonds or covered bonds shall be secured by a separate mortgage and may not be granted against collateral provided in the form of mortgages registered to the mortgagor and letters of indemnity, but see subsections (7) and (8) hereof. The mortgage shall state that it may serve as security for a loan funded by the issue of covered mortgage bonds or covered bonds.

(7) Mortgages on real estate registered before 1 July 2007 may serve as security for loans funded by the issue of covered mortgage bonds or covered bonds. Notwithstanding the first sentence hereof, mortgages registered to the mortgagor and letters of indemnity may not serve as security for loans funded by the issue of covered mortgage bonds.

(8) For loans funded by the issue of covered bonds, exemptions may be granted from the requirement of section 11(1), first sentence, that the borrower shall own the real estate and from the requirement of section 23(1) that the borrower shall be personally liable for the loan.

(9) The FSA may grant exemptions from subsection (6) hereof for loans granted for real estate located outside Denmark, the Faeroe Islands and Greenland.

33d. If the value of the assets referred to in sections 33a(3) and 33b(3) hereof no longer corresponds at least to the value of the covered mortgage bonds or covered bonds issued or does not comply with the relevant lending limits, the mortgage bank shall promptly provide additional collateral to satisfy the requirement and shall notify the FSA thereof. Additional collateral shall be provided in the form of the types of assets listed in section 152c(1), nos. 1 and 3-7, of the Financial Business Act. Section 152c(3) of the Financial Business Act shall apply correspondingly. For loans offered in Denmark, the obligation to provide additional collateral and the related expenses cannot be imposed on the borrowers whose decreasing property values prompted the requirement for additional collateral.

(2) In the event that the mortgage bank fails to provide additional collateral pursuant to subsection (1), first sentence, hereof, all bonds issued in the relevant series with a series reserve fund shall lose the designation covered mortgage bonds or covered bonds. Bonds having lost the designation covered mortgage bonds may be designated mortgage bonds, provided that they comply with the statutory requirements for mortgage bonds.

(3) If subsequently the bonds again satisfy the requirements for covered mortgage bonds or covered bonds, the FSA may allow such bonds to be re-designated covered mortgage bonds or covered bonds.

(4) The provision of collateral under subsection (1) hereof cannot be avoided pursuant to section 70 or 72 of the Insolvency Act. However, avoidance may be effected pursuant to the said provisions if the provision of collateral did not specifically appear to be ordinary.

33e. Mortgage banks licensed to issue covered bonds may raise loans to satisfy the requirement for the provision of additional collateral.

(2) The loan agreement shall state the series or group of series with a series reserve fund to which the loan funds raised according to subsection (1) hereof may be allocated.

(3) Loan funds raised according to subsection (1) hereof shall be placed in the asset types referred to in section 152c(1), nos. 1 and 3-7, of the Financial Business Act. As from the time when the loan is raised, the assets shall be placed in a separate account, a separate custody account or otherwise be marked as deriving from the relevant loan. When the assets are used as additional collateral, they shall be included in the relevant series or group of series with a series reserve fund.

33f. The FSA shall lay down detailed rules on the

- 1) valuation of the issued covered mortgage bonds or covered bonds and the ongoing calculation of the value of the assets relative to the covered mortgage bonds or the covered bonds, and
- 2) valuation of the assets securing the issue of covered mortgage bonds or covered bonds."

19. The following shall be inserted after section 36:

"**36a.** The Minister for Economic and Business Affairs shall lay down detailed rules on the use of digital communication, including electronic signatures, in connection with the exchange of information pursuant to this Act between citizens and undertakings on the one side and the public authorities on the other as well as on storage of information."

20. In section 39(1), "section 2(1) and (2), first sentence" shall be amended to "section 2(1)".

21. The following shall be inserted in section 39 as a new subsection after subsection (1):

"(2) Violation of section 2(2), first sentence, section 26(4), section 33a(2), section 33b(2) and section 33c(6) hereof shall be punishable by fine. Similar punishment shall apply to any violation of the duty to notify under section 33d(1), first sentence, hereof."

Subsections (2)-(4) shall then become subsections (3)-(5).

Annex 2

(Unofficial translation)

Executive Order no 718 of 21 June 2007 on the Issue of Bonds, the Balance Principle and Risk Management

Pursuant to section 152h(1), no. 6, and section 373(4), of the Danish Financial Business Act (*lov om finansiel virksomhed*), see Consolidation Act No. 381 of 19 April 2007, as amended by Act No. 577 of 6 June 2007, section 20(2), section 21, section 26(5), and section 39(3), of the Mortgage Credit Loans and Mortgage Credit Bonds etc. Act (*lov om realkreditlån og realkreditobligationer m.v.*), see Act No. 454 of 10 June 2003, as amended by Act No. 577 of 6 June 2007, and section 5(4), no. 6, and section 14(2), of the Danish Act on a Ship Financing Institution (*lov om et skibsfinansieringsinstitut*), see Consolidation Act No. 745 of 19 July 2005, as amended by Act No. 577 of 6 June 2007, the following provisions shall apply:

Part 1

Scope and definitions

1. This Executive Order shall apply to:

- 1) the issue by commercial banks of covered bonds in registers,
- 2) the issue by mortgage banks of mortgage bonds, covered mortgage bonds, covered bonds and other securities with preferential status, see section 1 of the Act on Mortgage Credit Loans and Mortgage Credit Bonds etc., in series with a series reserve fund, groups of series with a joint series reserve fund or in the bank as such, and
- 3) the issue by a ship financing institution of debentures, bonds issued by Danish Ship Finance and covered bonds in capital centres or in the bank as such.

2. Undertakings licensed to issue mortgage bonds, covered mortgage bonds, covered bonds and other securities with preferential status, debentures and bonds issued by Danish Ship Finance shall comply with a balance principle. Compliance with the balance principle shall be ensured by compliance with the provisions of either Part 2 or Part 3.

(2) Undertakings covered by subsection (1) above shall be entitled to choose which balance principle to apply to each register, series with a series reserve fund, group of series with a joint series reserve fund or capital centre. For mortgage banks and ship financing institutions, the bank or institution shall be considered a separate series with a series reserve fund or a separate capital centre, respectively.

(3) Compliance with the balance principle pursuant to Part 2 or Part 3, see subsection (2), shall appear from the basic prospectus or prospectus supplement for series or other bond issues opened after 1 July 2007. For bonds comprised by the transitional scheme concerning weighting in connection with the capital adequacy calculation according to the recast Credit Institution Directive 2006/48/EC, this must take place by 31 December 2007.

3. In the event that a mortgage bank or ship financing institution chooses to comply with the balance principle pursuant to the provisions of Part 2, see section (2)1, the provisions of subsections (2)-(4) shall be observed.

(2) The undertaking shall have sound liquidity. The liquidity shall amount to at least 10% of the undertaking's given undrawn credit lines on call loans granted on overdraft terms that have not been financed by a bond issue.

(3) The undertaking's liquidity shall include the following:

- 1) Operating cash.
- 2) Fully safe and liquid demand deposits with credit institutions and insurance companies.
- 3) Portfolio of safe, easily marketable, uncharged securities and credit instruments.

(4) In the event that the requirement in subsection (2) has not been satisfied, and this is not remedied within eight days of the undertaking failing to meet the requirements, the undertaking shall immediately inform the Danish Financial Supervisory Authority (FSA) thereof. The FSA shall stipulate a deadline for the undertaking's satisfaction of the requirement.

4. Commitments arising from financial instruments for hedging purposes with credit institutions as the counterparty shall be included in the general 15% limit for all credit institution claims according to the recast Credit Institution Directive 2006/48/EC. Any failure to comply with this limit shall immediately be offset by provision of additional collateral by way of assets covered by section 152c(1), nos. 3-4, of the Financial Business Act.

(2) In order to be included as cover, financial instruments used to hedge risks between assets and issued bonds shall be concluded with a counterparty qualifying for a 20% weighting pursuant to Schedule 3, No. 11(a), of the Executive Order on Capital Adequacy (*bekendtgørelse om kapitaldækning*). The requirement relating to counterparty weighting shall be satisfied on an ongoing basis.

(3) In the event that the hedging pursuant to subsection (2) concerns another part of the undertaking itself, the following shall be required:

- 1) Initial provision of collateral for the total hedging with the counterparty pursuant to an ISDA Credit Support Annex. Such collateral shall account for at least 2.5 per thousand of the total principal amounts converted into DKK on outstanding derivatives for a counterparty having at a minimum an AA rating, and at least 5 per thousand for a counterparty having at a minimum an A rating. The rating shall be made by a credit rating agency approved by the FSA.
- 2) The provision of collateral shall be unilateral, i.e. the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre shall not provide collateral vis-à-vis the counterparty.
- 3) The accepted provision of collateral shall be assets covered by section 152c(1), nos. 3 and 4.
- 4) Continuous daily monitoring of the market values of the derivatives.
- 5) In the event that the market value of the derivatives causes the initial collateral provided to decrease by 20%, the counterparty shall settle with the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre in order to restore the initial collateral.

(4) The FSA may demand the provision of additional collateral or that all derivative agreements concluded by the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre with another part of the undertaking as the counterparty, see subsection (3), shall be transferred and set up with another counterparty, in the event that the counterparty's rating falls below an A rating.

(5) The 15% limit of subsection (1) shall not apply to the undertaking's investment of the following funds from the undertaking's lending activities:

- 1) Investment of forward payments from the debtor until payments can be made to the creditor (prepaid funds).

- 2) Investment of repayment amounts from the debtor until the bonds issued can be cancelled or drawn or a new disbursement of a new loan secured by mortgages on real estate can be made within three months of the next repayment date (immediate repayment at par funds).
- 3) Investment of proceeds from a bond issue to refinance the maturity of bonds until such bonds mature (refinancing funds).
- 4) Investment of proceeds from a bond issue to hedge fixed-price agreements until the loans can be disbursed (pre-issue funds).
- 5) Land registration guarantees, if the lending undertaking has received a registered mortgage containing an endorsement pertaining only to the existing loans to be discharged by the new loan, and it concerns submission of redemption amounts under binding redemption offers made to undertakings under the supervision of the FSA, the Danish Agency for Governmental Management, the State, local authorities or the Danish National Building Fund, provided that the submission is conditional upon the mortgages being extinguished and delivered to the lending undertaking.
- 6) Loss guarantees, provided that they do not constitute an effective claim on the credit institution.
- 7) Own issued bonds within the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre.
- 8) Other commitments from other transfers from or management of funds from debtors having raised loans secured on mortgages on real estate to the owners of issued bonds, until disbursement can be made.

5. Interest rate, currency and option risks shall not be assumed by a register, series with a series reserve fund, groups of series with a joint series reserve fund or a capital centre, but see sections 7-10, 13, 15-17, 26, 28, 29 and 31.

Part 2

General balance principle

Calculation of payments

6. Risks shall be calculated on the basis of the differences between future disbursements on issued mortgage bonds, covered mortgage bonds, covered bonds, other securities issued by mortgage banks, debentures, bonds issued by Danish Ship Finance and financial instruments to hedge differences in payments and the future payments on mortgages, loans to public authorities or guaranteed by a public authority, investments pursuant to section 4(5), other investments and financial instruments hedging differences in payments.

(2) When calculating the payment differences mentioned in subsection (1), payments shall be included on their due date. The undertaking may decide that differences in payments shall not cover payment surpluses arising when debtors make their payments or parts thereof earlier than the payments made by the undertaking to the holders of the underlying bonds, when the customer has no claim for interest rate compensation agreed upon in advance.

(3) In the calculation of the payments mentioned in subsection 1, future payment flows may be calculated on the basis of adequate internal models. The FSA may set requirements for the undertaking regarding such internal models. Interest margin earnings and contributions, etc., may be included in these payment flows, provided that they are included consistently over time and in all stress tests, see sections 7-10 and 12.

Stress tests

Interest rate risk

7. The interest rate risk shall be calculated as the highest reduction in the present value of differences in payments calculated pursuant to section 6 on the basis of six different assumptions regarding the development of the yield structure, see subsections (2) and (4).

(2) The interest rate risk shall be calculated using the following assumptions regarding the development of the yield structure:

- 1) A parallel shift in the yield structure causing all yields to increase by one percentage point.
- 2) A parallel shift in the yield structure causing all yields to decrease by one percentage point.

(3) The interest rate risk pursuant to subsection (2) shall not exceed:

- 1) 10% of the excess cover for commercial banks,
- 2) 1% of the capital adequacy requirement plus 2% of the additional excess cover for mortgage banks,
- 3) 1% of the capital adequacy requirement plus 5% of the additional excess cover for a ship financing institution.

(4) The interest rate risk shall be calculated using the following assumptions regarding the development of the yield structure:

- 1) A parallel shift in the yield structure causing all yields to increase by at least 2.5 percentage points.
- 2) A parallel shift in the yield structure causing all yields to decrease by at least 2.5 percentage points.
- 3) A parallel shift in the yield structure causing all yields to increase by one percentage point up to a term of three months, a parallel shift of the yield structure causing all yields to decrease by one percentage point over a term of ten years, and a continuous, proportional shift in the yield structure in the interval between three months and ten years.
- 4) A parallel shift in the yield structure causing all yields to decrease by one percentage point up to a term of three months, a parallel shift of the yield structure causing all yields to increase by one percentage point over a term of ten years, and a continuous, proportional shift in the yield structure in the interval between three months and ten years.

(5) The interest rate risk calculated pursuant to subsection (4) shall not exceed:

- 1) 100% of the excess cover for commercial banks,
- 2) 5% of the capital adequacy requirement plus 10% of the additional excess cover for mortgage banks,
- 3) 5% of the capital adequacy requirement plus 10% of the additional excess cover for a ship financing institution.

(6) The interest rate risk mentioned in subsections (2) and (4) means the interest rate risk calculated for each currency in which the undertaking experiences differences in payments. The undertaking shall not be entitled to offset interest rate risks resulting from different currencies.

(7) Notwithstanding subsection (6) above, the undertaking shall be entitled to offset an interest rate risk resulting from differences in payments in EUR against an interest rate risk resulting from differences in payments in DKK by up to 50% of the interest rate risk in that of the two currencies with the numerically lowest calculated interest risk.

(8) The undertaking shall be entitled to apply internal models for calculating the interest rate risk pursuant to subsections (2) and (4). The FSA may set requirements for the undertaking regarding such internal models.

8. In connection with the establishment or closing of a register, series with a series reserve fund, group of series with a joint series reserve fund or a capital centre, the interest rate risk may amount to a maximum of DKK 20 million, notwithstanding the limits provided in section 7.

Currency risk

9. The currency risk shall be calculated as the highest reduction in the present value of differences in payments calculated pursuant to section 6 on the basis of two different assumptions regarding the development of the exchange rate, see subsection (2).

(2) The currency risk shall be calculated using the following assumptions regarding the development of the exchange rate:

- 1) An increase in exchange rates of 10% for currencies within the EU, the EEA or Switzerland. For all other currencies, an increase in exchange rates of 50%.
- 2) A decrease in exchange rates of 10% for currencies within the EU, the EEA or Switzerland. For all other currencies, a decrease in exchange rates of 50%.

(3) The currency risk calculated pursuant to subsection (2) shall not exceed:

- 1) 10% of the excess cover for commercial banks,
- 2) 10% of the capital adequacy requirement plus 10% of the additional excess cover for EUR, and 1% of the capital adequacy requirement plus 1% of the additional excess cover for other currencies for mortgage banks,
- 3) 10% of the capital adequacy requirement plus 10% of the additional excess cover for a ship financing institution.

(4) The undertaking shall be entitled to apply internal models for calculating the currency risk pursuant to subsection (2). The FSA may set requirements for the undertaking regarding such internal models.

Option risk

10. Risks pertaining to hedging conditional (asymmetric) claims on debtors as well as term mismatch between conditional (asymmetric) claims on debtors and hedging options in a register, series with a series reserve fund, group of series with a joint series reserve fund or a capital centre shall be limited, see subsections (2)-(4).

(2) The option risk shall be measured on the basis of the vega risk parameter and calculated as the highest reduction in the present value of differences in payments calculated pursuant to section 6 on the basis of two different assumptions regarding the development of the volatility structure, see subsection (3).

(3) The option risk shall be calculated using the following assumptions regarding the development of the volatility structure:

- 1) An increase in the volatility structure of one percentage point.
- 2) A decrease in the volatility structure of one percentage point.

(4) The option risk calculated pursuant to subsection (3) shall not exceed:

- 1) 5% of the excess cover for commercial banks,
- 2) 0.5% of the capital adequacy requirement plus 1% of the additional excess cover for mortgage banks,
- 3) 0.5% of the capital adequacy requirement plus 1% of the additional excess cover for a ship financing institution.

(5) The option risk mentioned in subsection (2) shall mean the sum of the option risk calculated for each currency in which the undertaking experiences differences in payments. The undertaking shall not be entitled to offset option risks resulting from different currencies.

(6) Notwithstanding subsection (5) above, the undertaking shall be entitled to offset an option risk resulting from differences in payments in EUR against an option risk resulting from differences in payments in DKK by up to 50% of the option risk in that of the two currencies with the numerically lowest calculated option risk.

(7) The undertaking shall be entitled to apply internal models for calculating the option risk pursuant to (2). The FSA may set requirements for the undertaking regarding such internal models.

Liquidity risk

11. Interest payments to the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre, see section 6, shall be higher than interest payments from the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre, see section 6, over a current period of 12 months.

(2) Excess cover and liquidity investments, provided that they have been made in safe and liquid securities, claims on central governments and central banks in zone A countries or contributions to credit institutions in zone A countries may be included as interest payments to the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre.

(3) The requirement in subsection (1) shall not apply to structures where loans and funding by definition have been matched in respect of payments from the establishment of the loan and subsequent refinancing, and where any capital gains or losses are equalised by compensation or an increase of the borrower's interest payments up to the maturity of the loan or the next refinancing. In addition to interest, interest-related payments and disbursements may also be included for such structures.

12. The present value of future payments into the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre calculated pursuant to section 6 shall always be higher than the present value of the future disbursements from the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre calculated pursuant to section 6.

Special provisions governing mortgage banks

13. The interest rate risk with regard to the assets, liabilities and off-balance sheet items of the mortgage bank, excluding section 6, shall not exceed 8% of the capital base of the mortgage bank.

(2) The interest rate risk in subsection (1) shall mean the interest rate risk calculated pursuant to section 7(1)-(2) and (6)-(8).

14. The issue of bonds and other securities may be made as an advance issue of fixed-price agreements concluded, or as a bloc issue based on estimated lending activities.

(2) Excess funds from a bloc issue shall not exceed the budgeted gross volume of loans for the subsequent 6-month period in each individual series with a series reserve fund. This provision shall not apply to bloc issues made on the basis of planned repurchases with a view to re-funding an already existing funding arrangement. Such bloc issues shall not have a term exceeding 6 months, after which period any excess bonds shall be cancelled.

15. The currency risk with regard to the assets, liabilities and off-balance sheet items of the mortgage bank, excluding section 6, shall not exceed 10% of the capital base of the mortgage bank.

(2) The currency risk in subsection (1) shall mean the currency risk calculated pursuant to section 9(1), (2) and (4).

16. If an undertaking is able to document that risks resulting from differences in payments on a specified part of the loans granted in accordance with previous requirements regarding the balance principle, comply with the balance principle provisions of the present Part, the FSA may permit that continuous calculation regarding this part of the portfolio is not carried out.

Special provisions governing a ship financing institution

17. The interest rate risk with regard to the assets, liabilities and off-balance sheet items of a ship financing institution, excluding section 6, shall not exceed 8% of the capital base of the ship financing institution.

(2) The interest rate risk mentioned in subsection (1) shall mean the interest rate risk calculated pursuant to section 7(1), (2) and (6)-(8).

Part 3

Specific balance principle

Definitions

18. The terms used in this Part shall be defined as follows:

- 1) Immediate repayment at par: Immediate repayment of a loan at par value.
- 2) Safe and liquid securities: Listed claims on mortgage banks or similar credit institutions in zone A countries, claims on central governments and central banks in zone A countries as well as listed claims on multinational development banks. As regards such claims, an exchange into cash can take place without significant effect on the price of the claims in question.
- 3) Conditional imbalances: Imbalances of an option-like nature.

Issue of bonds and other funding

19. No undertaking shall be allowed to grant:

- 1) index-linked loans based on the issue of nominal bonds and other nominal securities, or vice versa, or
- 2) index-linked loans based on the issue of bonds and other securities which are to be indexed by an index other than the one used in connection with the loan granted.

(2) The requirements of subsection (1) may be deviated from if, in connection with use of derivative financial instruments, the undertaking fully hedges any differences between payment sequences.

20. No undertaking shall be entitled to grant callable loans on the basis of the issue of non-callable bonds or other securities.

(2) The provisions in subsection (1) shall not be deviated from through the use of derivative financial instruments.

21. The issue of bonds and other securities may be made as an advance issue of fixed-price agreements concluded, or as a bloc issue based on estimated lending activities.

(2) Repayment of loans by bonds other than the underlying bonds cannot exceed 15% of the nominal value of the undertaking's issued bonds in the register, series with a series reserve fund, group of series with a joint series reserve fund or the capital centre..

(3) In the event of repayment in accordance with subsection (2), the bonds used to repay the loans in question shall be bonds issued with a payment sequence that as closely as possible matches the payment sequence of the loans repaid.

(4) Subsection (2) shall not apply to immediate repayments at par.

(5) Excess funds from a bloc issue shall not exceed the budgeted gross volume of loans for the subsequent 90-day period in each individual register, series with a series reserve fund or capital centre. This provision shall not apply to bloc issues made on the basis of planned repurchases with a view to re-funding an already existing funding arrangement. Such bloc issues shall not have a term exceeding 90 days, after which period any excess bonds shall be cancelled.

(6) Excess funds, including funds deriving from immediate repayments at par and funds deriving from more frequent repayment dates on the lending side than on the bond side or any other liquidity surpluses caused by payments exceeding disbursements, see section 23(1), shall, until they can be re-lent, disbursed, or the underlying bonds are repaid, be invested in safe and liquid securities, see section 18, no. 2, or be placed as deposits with zone A credit institutions subject to a period of notice of up to 12 months and be kept separate from other funds.

22. Options and similar derivative instruments that offer asymmetric returns included in the calculation of future differences in payments within the framework of the balance principle, see section 23(1), shall have a maximum term of four years as from the time when the agreement was made with the borrower.

Calculation of payments and liquidity provisions

23. It shall be possible to calculate the differences between future disbursements on issued mortgage bonds, covered mortgage bonds, covered bonds, other securities issued by mortgage banks, debentures, bonds issued by Danish Ship Finance and financial instruments hedging differences in payments and the future payments on mortgages, loans to public authorities or guaranteed by a public authority, investments pursuant to section 4(5), other investments and financial instruments hedging differences in payments, see section 21(6), on a daily, cumulative, discounted basis for all future payments and disbursements.

(2) Disbursements, see subsection (1), shall mean payments on bonds and other securities as well as financial instruments. Payments, see subsection (1), shall mean repayments on mortgages less direct contributions and contributions in the form of significant interest margin earnings and less other administration fees, as well as payments on financial instruments and investments, see section 21(6).

(3) When calculating the payments mentioned in subsection (1), they shall be included on their due date.

24. When calculating the payments mentioned in section 23, future payment flows may be calculated on the basis of adequate financial models.

25. Seen in proportion to the undertaking's capital base, a future liquidity deficit of the undertaking arising from disbursements exceeding payments received, see section 23(1), shall not exceed:

- 1) 25% in years 1-3,
- 2) 50% in years 4-10 and
- 3) 100% as from year 11.

(2) The undertaking's liquidity deficits mentioned in subsection (1) shall not comprise liquidity deficits offset by liquidity investments, provided that such investments are made in safe and liquid

securities, see section 18, no. 2, or as deposits in zone A credit institutions subject to a period of notice of up to 12 months.

Provisions governing interest rate risk

26. The interest rate risk assumed by the undertaking due to the differences in payments mentioned in section 23(1), including interest rate risk on excess funds in connection with investment of such funds, see section 21(6), shall not exceed an amount corresponding to 1% of the capital base of the undertaking. Differences in payments shall not cover payment surpluses arising when debtors make their repayments or parts thereof earlier than the payments made by the undertaking to the holders of the underlying bonds, when the customers have no claim for compensatory payments.

(2) Interest rate risks shall be calculated for each individual currency in which the undertaking experiences differences in payments; the risk being calculated as the largest fall in the present value of the differences in payments calculated in the following six ways:

- 1) An assumed parallel shift in the yield structure causing all yields to increase by one percentage point.
- 2) An assumed parallel shift in the yield structure causing all yields to decrease by one percentage point.
- 3) For all conditional imbalances, see section 18, no. 3, a parallel yield increase of three percentage points is assumed, and changes in the present value of the differences in payments are divided by three. For all other differences in payments, a parallel yield increase of one percentage point is assumed where no division is made. The two calculated changes in present value shall be added together.
- 4) For all conditional imbalances, see section 18, no. 3, a parallel yield decrease of three percentage points is assumed, and changes in the present value of the differences in payments are divided by three. For all other differences in payments, a parallel yield decrease of one percentage point is assumed where no division is made. The two calculated changes in present value shall be added together.
- 5) An assumed parallel shift in the yield structure causing all yields to increase by one percentage point up to a term of three months, a parallel shift of the yield structure causing all yields to decrease by one percentage point over a term of ten years, and a continuous, proportional shift in the yield structure in the interval between three months and ten years.
- 6) An assumed parallel shift in the yield structure causing all yields to decrease by one percentage point up to a term of three months, a parallel shift of the yield structure causing all yields to increase by one percentage point over a term of ten years, and a continuous, proportional shift in the yield structure in the interval between three months and ten years.

(3) The interest rate risk mentioned in subsection (1) means the sum of the interest rate risk calculated in compliance with subsection (2) for each currency in which the undertaking experiences differences in payments. Interest rate risks in different currencies cannot be set off against each other.

(4) In the calculation of the interest rate risk according to subsection (2), the interest rate risk shall be calculated on the basis of adequate financial models.

Registers or series with a series reserve fund

27. For each individual register, series with a series reserve fund, including the institution as such, or groups of series with a joint series reserve fund, sections 21, 25 and 26 shall apply with regard to the excess cover of the register, the capital adequacy requirement plus additional excess

cover in the series with a series reserve fund, or the capital adequacy requirement plus additional excess cover in the group of series with a joint series reserve fund. For series with joint and several liability, however, no liquidity deficit in the series calculated in accordance with section 23(1) shall exceed 1% of the capital adequacy requirement plus additional excess cover in the series.

(2) In connection with the establishment of a register, a series with a series reserve fund or a group of series with a joint series reserve fund, the liquidity deficit or interest rate risk shall not – irrespective of the limits stipulated in sections 25 and 26 – exceed DKK 20 million. In connection with establishment of a series with a series reserve fund or a group of series with a joint series reserve fund, notwithstanding the provision of section 21(5), excess funds from a bloc issue shall not for a period of up to 12 months after this executive order has entered into force exceed the budgeted gross volume of loans for the subsequent 6-month period in each individual series with a series reserve fund or group of series with a joint series reserve fund.

(3) Subsection (1) shall not apply to series with a series reserve funds, except for the institution as such, in which no new loans are granted after 1 January 2001. For series with joint and several liability, however, no liquidity deficit in the series calculated in accordance with section 23(1) shall exceed 1% of the capital adequacy requirement plus additional excess cover in the series. Moreover, for other series with a series reserve fund, no liquidity deficit calculated in accordance with section 23(1) shall exceed 8% of the capital adequacy requirement plus additional excess cover in the series.

(4) In the event that series according to subsection (3), set up under previous legislation, are being terminated and where, consequently, the limits for liquidity deficits for series cannot be observed, this provision may be disregarded. The FSA shall immediately be notified hereof.

Interest rate risk with regard to the securities portfolio, etc.

28. The interest rate risk with regard to the assets, liabilities and off-balance sheet items of the undertaking, exclusive of the items mentioned in section 23(1), shall not exceed 8% of the capital base of the undertaking.

(2) The interest rate risk mentioned in subsection (1) shall mean a calculation of the change in the present value when the market yield changes by one percentage point. The calculation shall be made both for the market yield plus one percentage point and for the market yield less one percentage point. The interest rate risk is then that of the two results where the present value – in the event of a change in the market yield by one percentage point – expresses a deterioration of the present value in relation to the present value at the market yield.

(3) When calculating the interest rate risk pursuant to subsection (2), the calculation requirements stipulated in section 26(3) and (4) shall apply.

Currency risk

29. The currency risk with regard to the assets, liabilities and off-balance sheet items of the undertaking shall not exceed 0.1% of the capital base of the undertaking. The currency risk shall be calculated by means of exchange rate indicator 2.

(2) Net positions in foreign currencies not included in exchange rate indicator 2 shall not exceed DKK 30 million for each individual currency.

Reporting requirements

30. If an undertaking is able to document that any risks resulting from differences in payments, see section 23(1), on a specified part of the loans granted in accordance with previous balance

principle requirements, comply with the balance principle provisions of the present Executive Order, the FSA may permit that continuous calculation of liquidity imbalances and interest rate risks is not carried out regarding this part of the portfolio.

Special provisions governing a ship financing institution

31. Only section 18, nos. 2 and 3, sections 19, 20(1), 22-24, 26, 28 and 29(2) shall apply to a ship financing institution, but see subsection (5).

(2) The requirements of section 20(1) may be deviated from if, in connection with use of derivative financial instruments, the undertaking fully hedges any differences between payment sequences.

(3) The undertaking may issue bonds as an advance issue of fixed-price agreements concluded or as a bloc issue based on the undertaking's loan offers made and the estimated lending activities.

(4) Excess funds from a bloc issue shall not exceed the sum of the undertaking's loan offers made and the undertaking's core capital, see section 129 of the Financial Business Act, see section 17(1) of the Executive Order on a Ship Financing Institution.

(5) Excess funds, see section 21(6), shall, until they can be re-lent, disbursed, or the underlying bonds are repaid, be kept separate from other funds and invested:

- 1) in safe and liquid securities, see section 18, no. 2, or
- 2) as deposits in credit institutions having their registered office in zone A subject to a period of notice of up to 12 months.

(6) A future liquidity deficit of the undertaking arising from disbursements exceeding payments received, see section 23(1), shall not exceed the undertaking's capital base.

(7) The liquidity deficits mentioned in subsection (6) for the undertaking shall not comprise liquidity deficits that are offset by liquidity investments, provided that such investments are made in safe and liquid securities, see section 18, no. 2, or as deposits in credit institutions having their registered office in zone A subject to a period of notice of up to 12 months.

(8) The currency risk relating to the undertaking's assets, liabilities and off-balance sheet items shall not exceed 2% of the capital base of the undertaking, see section 128 of the Financial Business Act, see section 17(1) of the Executive Order on a Ship Financing Institution, plus the total currency risk on write-downs of foreign-currency lending. The currency risk shall be calculated by means of exchange rate indicator 2.

(9) In special circumstances, the FSA may permit that the limit mentioned in subsection (8) and section 29(2) is temporarily exceeded.

Part 4

Reports

32. In connection with presentation of the financial statements, the undertaking shall issue a statement to the effect that all the provisions of this Executive Order have been complied with.

(2) Not later than 20 working days after the end of the first, second and third quarters, the undertaking shall report information on forms prepared by the FSA for the purpose of the FSA's verification of whether the requirements of sections 7, 9, 10, 13, 15, 17, 25, 26 and 28 have been satisfied. The year-end reporting shall be made not later than 30 working days after the end of the year. The forms are available at the FSA's website.

(3) The reports shall be available on a machine-readable or electronic medium and be approved by the undertaking's executive board.

Part 5

Commencement and sanctions

33. Violation of section 2(1) and (3), section 3(1), (2) and (4), section 4 (1)-(4), sections 5-12, section 13(1), section 14(2), section 15(1), section 17(1), section 19(1), section 20(1), section 21(2), (3), (5) and (6), section 22, section 23(1) and (3), section 25(1), section 26(1), (2), and (4), section 27, section 28(1) and (2), section 29, section 31(2)-(8) and section 32 shall be punishable by a fine.

(2) Undertakings, etc. (legal persons) shall be held criminally liable according to the rules laid down in Part 5 of the Danish Penal Code.

34. This Executive Order shall enter into force on 1 July 2007.

(2) At the same time, Executive Order No. 1190 of 17 December 2003 on Mortgage Banks' Issue of Bonds, the Balance Principle, Interest Rate and Currency Risks shall be repealed.

Danish Financial Supervisory Authority

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