Translation by Danske Bank of a decision dated 19 January 2015 from the Danish Financial Supervisory Authority (*Finanstilsynet*).

The board of directors and the executive board of
Danske Bank A/S

19 January 2015

Control of compliance with accounting rules (control review) of Danske Bank A/S's annual report for 2013

The Danish Financial Supervisory Authority (FSA) has conducted a partial[1] control review of Danske Bank A/S's (Danske Bank's) annual report for 2013. It was done as a step in the control of financial companies' annual and interim reports conducted by the FSA in pursuance of section 83(2) of the Danish Securities Trading Act.[2]

The annual report for 2013, published in accordance with section 27(7) of the Danish Securities Trading Act, comprises the annual financial statements for the parent company and the group. The consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRSs) as adopted by the EU, and in accordance with the IFRS Executive Order for Financial Institutions,[3] and the parent company financial statements have been prepared in accordance with the Danish Executive Order on IFRS Application at Financial Institutions.[4]

The annual report for 2013 was audited by KPMG Statsautoriseret Revisionspartnerselskab, which issued an unqualified opinion with no emphasis of matter.

In letters of 4 June 2014 and 25 July 2014, the FSA requested statements from the bank regarding its goodwill impairment testing and information about market shares in the management's report. The bank replied in its letters of 27 June 2014 and 22 August 2014. In continuation of this, a meeting was held with the bank on 24 September 2014. At the meeting – and by e-mail of 20 October 2014 – the FSA requested supplementary statements, which the FSA received from the bank on 4 November 2014.

On 25 November 2014, the FSA submitted a draft decision to Danske Bank A/S for comments. In continuation of this, meetings were held with the bank on 1 December, 8 December, 9 December and 11 December 2014. For the purpose of these meetings and as a result of the discussions, the bank submitted a number of additional statements and calculations to the FSA.

On that basis, the FSA submitted a new draft decision for comments in a letter of 16 December 2014. The bank replied in a letter of 18 December 2014.

[1] The control review focuses only on a limited part of the annual report for 2013. It should therefore be noted that the review of the annual report cannot be considered exhaustive.
[2] Executive Order No. 831 of 12 June 2014.
[3] Executive Order No. 1306 of 16 December 2008.
[4] Executive Order No. 281 of 26 March 2014.

Decision

In the opinion of the FSA, Danske Bank's annual report for 2013 contains the following errors:

1. Information about goodwill
   Note 19 in the annual report on intangible assets lacks a great deal of information required under IAS 36.134, including:
   - i) Information about all key assumptions, i.e. the assumptions to which the recoverable amounts of the individual cash-generating units are most sensitive,
   - ii) A description of management's approach to determining the values assigned to each key assumption, and
   - iii) Sensitivity information for the key assumptions in cases where a reasonably likely change in a key assumption will cause a unit's carrying amount to exceed the recoverable amount.

2. Incorrect statement of market share
   In the management's report, the information provided on the market share for personal customers in Denmark is incorrect and non-compliant with section 187(2) and (3) of the Danish Financial Business Act (cf. subsection (1)). The bank stated that its market share was rising; in fact, however, the market share on the market in question had fallen.

In light of the upcoming presentation of the bank's annual report for 2014, pursuant to section 197 of the Danish Financial Business Act and section 83(3) of the Danish Securities Trading Act, the FSA regarding (i) above **orders** the bank to rectify the matter in the annual report for 2014 by providing the following information about goodwill regarding 2013 in the annual report for 2014 and to state that the matter has been rectified as a result of an order issued by the FSA. The information must be given for each cash-generating unit for which the carrying amount of goodwill is significant in comparison with the total carrying amount of goodwill:

- Information about all key assumptions, i.e. the assumptions to which the bank's impairment testing is most sensitive (IAS 36.134(d)(i)),
- A description of management's approach to determining the values assigned to each key assumption, including whether those values are consistent with external sources of information/reflect past experience (IAS 36.134(d)(ii)),
- Sensitivity information for the key assumptions in cases where a reasonably likely change in the key assumption will cause a unit's carrying amount to exceed the recoverable amount (IAS 36.134(f)).

Regarding (ii) above, pursuant to section 197(1) of the Danish Financial Business Act and section 83(3) of the Danish Securities Trading Act, the FSA **reprimands** Danske Bank for issuing incorrect information in the management's report of the annual report for 2013.

On the basis of the statements received from and discussions with the bank, the FSA has taken note of the fact that the impairment testing in the annual report for 2013 does not reflect significant goodwill impairment but, on the other hand, that a goodwill impairment charge needs to be recognised in the annual report for 2014.

Regarding other issues about which the FSA has inquired, the FSA takes note of the bank's comments and explanations.

The FSA directs the bank's attention to the fact that, pursuant to section 34(2) of the Danish Securities Trading Act (cf. section 27(1)), the bank is obliged to disclose inside information immediately after the occurrence of the circumstances or event, even though the circumstances or event has not been formalised. Similarly, significant changes to inside information which have already been published must be published immediately after the occurrence of the changes and through the same channel as the one used for publishing the original information. The FSA also points out that, pursuant to section 27(6) of the Danish Securities Trading Act, an issuer may postpone the publishing of inside information to avoid damage to justified interests. Use of this provision is subject to such postponement not misleading the public and to ensuring that such information is treated as confidential. If the bank chooses to postpone the publishing of inside information, the FSA must be informed immediately.

Complaints procedure

In accordance with section 372(1) of the Danish Financial Business Act and section 88(1) of the Danish Securities Trading Act, the decision made by the FSA may be brought before the Danish Company Appeals Board by e-mail to ean@erst.dk or by ordinary mail to Dahlerups Pakhus, Langelinie Allé 17, P.O. Box 2000, DK-2100 Copenhagen Ø, no later than four weeks after the bank has received the decision.

According to section 7 of the Danish Executive Order on the Company Appeals Board, complaints to the Company Appeals Board are subject to a fee of DKK 4,000. However, if the complaint does not concern the complainant's current or future business matters, the fee is DKK 2,000. According to section 15(4) of the executive order, the Board or its chairman on its behalf may decide to refund part of or the whole fee paid if the complainant's claim is upheld wholly or in part. The fee is refunded if the complaint is rejected.

Publication

Pursuant to section 354a(1) of the Danish Financial Business Act and section 84c(1) of the Danish Securities Trading Act, the FSA and the bank are required to publish the decision.

Summary and assessment

For the sake of clarity, each item is presented as follows:

- Summary
- The assessment of the FSA

The legal basis is set out in appendix 1.

1. General

In its letters of 4 June 2014 and 25 July 2014, the FSA requested that Danske Bank A/S submit statements on its impairment testing of goodwill, information on markets shares in its management's report and information on remuneration.

The bank replied in letters dated 27 June 2014 and 22 August 2014. A meeting was held with the bank on 24 September 2014. At the meeting and in an e-mail dated 20 October 2014, the FSA requested further statements, which were received from the bank in its reply dated 4 November 2014.

On 25 November 2014, the FSA submitted a draft decision to Danske Bank A/S for comments. In continuation of this, meetings were held with the bank on 1 December, 8 December, 9 December and 11 December 2014. For the purpose of these meetings and as a result of the discussions, the bank submitted a number of additional statements and calculations to the FSA.

On that basis, the FSA submitted a new draft decision for comments in a letter of 16 December 2014. The bank replied in a letter of 18 December 2014.

2. Information about goodwill

2.1 Summary

Under IAS 36.134(d)(iii), the length of the budget period must be stated in the annual report, and if a period longer than five years is used, an explanation of why this is justifiable must appear in the annual report.

In its annual report for 2013, the bank did not state the length of the budget period. In addition, the bank used a subsequent “normalisation period” without giving a justification for it, for which the FSA requested an explanation in a letter of 4 June 2014.

Concerning the information lacking about the period used for the budgets for goodwill impairment tests, the bank explained, in a letter of 27 June 2014, that the length of the budget and normalisation periods was omitted in the annual report for 2013 since, according to the bank’s assessment, it was information that was inessential since the use of a normalisation period affected neither the result of the impairment test nor the sensitivity analysis. This is because the assumptions in the normalisation period had come to approach those of the terminal period. The omission occurred as a step in the bank’s overall effort to increase the overview of the notes by reducing the extent of insignificant information.

In IAS 36.134, there are a number of information requirements about goodwill and the goodwill impairment testing. The information must be given for each cash-generating unit for which the carrying amount of goodwill is significant in comparison with the total carrying amount of goodwill:

In its review of the annual report, the FSA found that the bank omitted to give the following information:

a) Information about all assumptions to which the bank’s impairment testing is most sensitive (key assumptions) (IAS 36.134(d)(i)),
b) A description of management’s approach to determining the values assigned to each key assumption, including whether those values are consistent with external sources of information/reflect past experience (IAS 36.134(d)(ii)),
c) Sensitivity information for the key assumptions in cases where a reasonably likely change in the key assumption will cause a unit’s carrying amount to exceed the recoverable amount (IAS 36.134(f)).

Re (a) and (b): In the bank's annual report for 2013, the bank presented a table entitled "Impairment test assumptions", in which the bank stated the values used for growth in the terminal period and the required rate of return before tax (the discount rate).

In addition, the bank states as follows with respect to the interest rate level:

"The difficult market conditions for the Group's banking units continued. Low money market rates kept earnings at a low level. The Group expects a period of modest growth and low money market rates before economies will normalise. Normalised interest rate levels are expected to increase net profit. If the economies do not normalise as expected, or future regulations increase costs more than expected, intangible assets may be impaired. Owing to the expectations for the budget period, around 57% of the net present value of future cash flows is expected to be generated in the terminal value [sic]."

Furthermore, the bank stated in its reply of 27 June 2014 that interest margins, growth in deposits and lending and impairment levels have special significance for the cash flow estimates.

Re (c): For all key assumptions, according to IAS 36.134(f), a great deal of information should be given if a reasonably likely change in the key assumption will cause a unit's carrying amount to exceed the recoverable amount.

Information must be given about the amount: (i) whereby the unit's recoverable amount exceeds the carrying amount; (ii) information about the value that is assigned to the key assumption; and (iii) the amount whereby the value that is assigned to the key assumption must be changed after the incorporation of any subsequent effects of the change in the other variables that are used to measure the recoverable amount so that the unit's recoverable amount comes to correspond to the carrying amount.

This information must be given about all key assumptions and for each cash-generating unit when a reasonably likely change in the key assumption will result in a need for impairments.

In connection with the hearing on the draft decision submitted for comments on 25 November 2014, the bank recognised that the disclosures in the notes in the annual report for 2013 could be elaborated. See the bank's presentation of 1 December 2014.

In its reply of 18 December 2014 regarding hearing on the draft decision, the bank stated that the FSA's draft decision, in addition to growth in the terminal period and the required rate of return, defined interest rate developments, interest margin, growth in deposits and lending and loan impairment charges as key assumptions. To this the bank noted:

"As appears from the enclosed overview and extracts from the annual reports for 2013 of a wide range of large European and Nordic banks, there is no practice for defining key assumptions other than required rate of return, growth and earnings. Accordingly, there is no practice for providing information about specific assumptions such as interest margins and loss ratios. We consider such assumptions to be confidential and competition-sensitive information. Therefore, we do not consider it fair if Danske Bank, as the only bank in Europe, would be required to publish such information."

2.2 The assessment of the FSA

The FSA finds that the bank did not provide information about all key assumptions (IAS 36.134(d)(i)). Key assumptions are those to which the recoverable amounts of the individual units are most sensitive.

Considering that the bank states directly in its annual report for 2013 that the values in use calculated are sensitive to changes in interest rates and that the FSA has also determined this in the review of the bank's impairment tests and at subsequent discussions with the bank and in a review of the bank's calculations, it is assessed that the trend in interest rates, including the interest margin, is a key assumption in the bank's budgets. Since the bank has deposits that carry a very low interest rate or an interest rate of 0% and calculates the interest margin on deposits as the difference between the date-to-day rate and the rate offered to customers, the bank's deposit margins are particularly sensitive to changes in interest rate levels.

The FSA also finds, partly on the basis of the bank's reply and partly on the basis of the FSA's review and discussions with the bank regarding the impairment tests, that the growth in both deposits and lending (which track GDP growth in the budget period) and the loan impairment charges for each cash-generating unit are key assumptions.

As regards the key assumptions – interest rate levels, including interest margins, growth in deposits and lending (GDP growth) and impairment levels – the bank did not, according to the FSA, include information about management's method of calculating the key assumptions and did not specify whether it is in accordance with external sources or historical experience (IAS 36.134(d)(ii)).

The bank's reply of 18 December 2014 states that there is no practice for providing information about specific assumptions such as interest margins and loss ratios.

In this connection, the FSA notes that IAS 36.134(f) requires the value of a specific assumption to be disclosed (that is, in connection with sensitivity information for the individual cash-generating units) only in the case(s) in which a reasonably likely change in a key assumption leads to impairment of goodwill. Otherwise, IAS36.134(d)(i) and (ii) requires only the disclosure of a description of the individual key assumptions and the method of calculating the value. Furthermore, the FSA notes that the disclosure requirement in IAS 36.134(d)(i) and (ii) covers only key assumptions in the budget period, while the requirements [sic] for the required rate of return and growth in the terminal period are subject to other disclosure requirements in the standard (IAS 36.134(d)(iv) and (v).

The FSA's finds that the bank did not include some sensitivity information as IAS 36.134(f) specifies that information must be disclosed if a reasonably likely change in a key assumption will cause a unit's carrying amount to exceed its recoverable amount.

According to the rules, the sensitivity analysis must show the value by which a key assumption must change in order for a need for impairments to arise. When this sensitivity information is calculated, the subsequent effects on the other variables must be taken into account. Considering the fact that there is a complex correlation between the key assumptions and the other (key) variables in the bank's cash flow projections, a reader of the financial statements cannot, on the basis of the information received, assess, for each key assumption, whether the sensitivity to reasonably likely changes as well as the effect between the variables together result in impairment of goodwill.

It is the FSA's assessment that there is a need for more sensitivity information about more key assumptions than the bank presented in its annual report for 2013, since the FSA's review of the impairment tests as well as discussions with the bank on the impairment tests and the bank's additional calculations have shown that the calculated values in use are very sensitive to changes in the assumptions, including the subsequent effects on other (key) assumptions.

In this connection, the FSA notes that the bank provided this information only as a total for all the cash-generating units, but that, according to the standard, sensitivity information must be given for each cash-generating unit if the amount of goodwill is material in relation to the total value of goodwill.

The FSA finds that it is a deviation from the rules that the bank in note 19 on goodwill in its annual report for 2013 did not include the information listed above.

Total goodwill in the bank's annual report for 2013 amounted to 12.7% of equity capital and 0.6% of the group's total assets and is thus assessed to be a significant accounting item. Since this involves a note that is related to a significant accounting item, it is considered to be an error when material, required information is omitted.

In this assessment, the FSA has emphasised that much information is lacking and that the users of the financial statements may therefore have difficulty assessing on what basis the bank estimated the calculated values [sic] for the individual cash-generating units and thus on what basis the impairment tests were carried out. An impairment test is associated with uncertainty because the values are based only on management's estimates, so it is assessed that the information that is lacking is essential for the user of the financial statements.

Overall, it is thus the FSA's assessment that it is an error that the bank did not include the required information about goodwill in its annual report for 2013. Considering the fact that the bank is not ordered to provide corrective/supplementary information for its annual report for 2013, but is ordered to rectify the matter in the 2013 annual report in its annual report for 2014 because the bank is about to release this report, the note on goodwill for 2014 must include the information that is lacking about goodwill regarding the annual report for 2013.

In this connection, the FSA notes that, when the bank includes information for 2013 in its annual report for 2014 to rectify the matter in the 2013 annual report, it must base its materiality assessment on the carrying amounts for 2013 when it determines the cash-generating units for which information is to be included.

3. Incorrect statement of market share

3.1 Summary

In the annual report for 2013, Danske Bank described the trend in its market share of lending to personal customers. The following is stated in the management's report, p. 19: "Realkredit Danmark's share of net new mortgage lending and our share of new bank lending in Denmark increased."

Moreover, the following is stated on p. 21: “There was an unsatisfactory customer churn in Denmark during the year, but we saw a slight increase in our market share of bank lending in Denmark and increased our share of net new mortgage lending at Realkredit Danmark.”

Since the FSA, through the reports received about lending and guarantees to personal customers at Danish banks, could not conclude that Danske Bank had in fact increased its market share of bank lending to personal customers in Denmark, the FSA requested, in a letter of 4 June 2014, that the bank disclose the calculation of the market share mentioned above.

In a letter of 27 June 2014, the bank wrote that the statements about the bank’s market shares on pp. 19 and 21 were wrong, since the bank, during the preparation of the draft annual report for 2013, used an internally calculated market share for October that, because of a regrettable error, was included in the final annual report for 2013. These figures showed a slightly rising market share for bank lending to personal customers. If the bank had used the market share in the MFI[5] statistics at the end of 2013, it would have shown a decline in the market share from 29.3% to 27.5%.

Danske Bank explained further in its letter of 27 June 2014 that in the future it will stop the calculation of the internally calculated market share and that it will calculate the market share exclusively on the basis of the MFI reporting to the Danish central bank. In addition, the bank will begin to disclose the period for the calculation of the market shares in the annual and interim reports in the first quarter of 2014 [sic].

The bank also stated that it became aware of the error immediately after the release of the annual report for 2013. The bank assessed that the error was not of a nature that necessitated a change in the annual report for 2013.

3.2 The assessment of the FSA

According to section 186(1), second sentence, of the Danish Financial Business Act, the management’s report must contain a true and fair view of the matters that the report treats. For the management’s report to contain a true and fair view, according to section 187(1) of the Danish Financial Business Act, the information must be prepared so that it supports the users of the financial statements in their financial decisions, and the information must be reliable in relation to what the users of the financial statements normally expect (see section 187(2) and (3)).

It is in the FSA’s assessment a deviation from the rules that the bank, in its annual report, gives incorrect information about the bank’s market share in the management’s report.

In the period leading up to and immediately after the bank’s release of its annual report for 2013, there was considerable public interest in the trend in the bank’s market share of bank lending to personal customers in Denmark.

The trend in the market share for lending to personal customers gives the users of the financial statements information about the bank’s competitiveness in an important market for the bank.

[5] The figures that Danish banks report to the Danish central bank for MFI (Monetary Financial Institutions) statistics.

It is the FSA's assessment that the information about the bank experiencing a slight rise in its market share, although there was actually a decline in the market share, was erroneous information with material significance for the users of the financial statements. In this connection, the FSA has emphasised that the incorrect information appears in two places in the management's report.

The bank has stated that it has changed the procedure for the calculation of the market share so that a similar error will not occur in the future.

A copy of this decision has been sent to the bank's external auditors and group chief auditor.

Appendix 1 – Legal basis

IAS 36.134 provides as follows:
"An entity shall disclose the information required by (a)–(f) for each cash-generating unit (group of units) for which the carrying amount of goodwill or intangible assets with indefinite useful lives allocated to that unit (group of units) is significant in comparison with the entity's total carrying amount of goodwill or intangible assets with indefinite useful lives:

a) the carrying amount of goodwill allocated to the unit (group of units).
b) the carrying amount of intangible assets with indefinite useful lives allocated to the unit (group of units).
c) the basis on which the unit's (group of units') recoverable amount has been determined (i.e., value in use or fair value less costs of disposal).
d) if the unit's (group of units') recoverable amount is based on value in use:
    i) a description of each key assumption on which management has based its cash flow projections for the period covered by the most recent budgets/forecasts. Key assumptions are those to which the unit's (group of units') recoverable amount is most sensitive.
    ii) a description of management's approach to determining the value(s) assigned to each key assumption, whether those value(s) reflect past experience or, if appropriate, are consistent with external sources of information, and, if not, how and why they differ from past experience or external sources of information.
    iii) the period over which management has projected cash flows based on financial budgets/forecasts approved by management and, when a period greater than five years is used for a cash-generating unit (group of units), an explanation of why that longer period is justified.
    iv) the growth rate used to extrapolate cash flow projections beyond the period covered by the most recent budgets/forecasts, and the justification for using any growth rate that exceeds the long-term average growth rate for the products, industries, or country or countries in which the entity operates, or for the market to which the unit (group of units) is dedicated.
    v) the discount rate(s) applied to the cash flow projections.

[…..]

f) if a reasonably possible change in a key assumption on which management has based its determination of the unit's (group of units') recoverable amount would cause the unit's (group of units') carrying amount to exceed its recoverable amount:
    i) the amount by which the unit's (group of units') recoverable amount exceeds its carrying amount.
    ii) the value assigned to the key assumption.
    iii) the amount by which the value assigned to the key assumption must change, after incorporating any consequential effects of that change on the other variables used to measure recoverable amount, in order for the unit's (group of units') recoverable amount to be equal to its carrying amount."

Section 186(1) of the Danish Financial Business Act provides as follows:

"The annual financial statements and any consolidated financial statements shall give a true and fair presentation of the undertaking's and group's assets and liabilities, financial position and results. The management review shall contain a true and fair report of the matters dealt with in the review."

Section 187 of the Danish Financial Business Act provides as follows:
"(1) In order for the financial statements and consolidated financial statements to give a true and fair presentation, and for the management review to contain a true and fair report, cf. section 186, the requirements of subsections (2) and (3) shall be complied with.
(2) The annual report shall be prepared so as to support users of financial statements in their financial decisions. Such users are private individuals, undertakings, organisations and public authorities, etc., whose financial decisions must normally be expected to be affected by an annual report, including present and prospective members of the undertaking, creditors, employees, clients, alliance partners, the local community, authorities providing government grants, and fiscal authorities. As a minimum, the decisions in question concern

1) investment of the user's own resources,
2) the management's administration of the funds of the undertaking, and
3) the allocation of the funds of the undertaking.

(3) The annual report shall be prepared so as to disclose information about matters which are normally relevant to users, cf. subsection (2). The information disclosed must also be reliable in relation to users' normal expectations."