Consolidated Financial Statements

31 December 2021

Kvika banki hf. • Katrínartún 2 • 105 Reykjavík • Iceland • Reg. no. 540502-2930

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Endorsement and Statement
by the Board of Directors and the CEO

These are the audited Consolidated Financial Statements of Kvika banki hf. ("Kvika" or the "Bank") and its subsidiaries (together the "Group") for the year 2021.

The Group operates four business segments, Insurance, Asset Management, Commercial Banking and Investment Banking. The Group provides businesses, investors and individuals with comprehensive investment banking, insurance services and asset management services, as well as selected banking services. At the end of December 2021 the Group had ISK 528 billion of assets under management, compared to ISK 527 billion at year end 2020. The relatively small increase in assets under management during the year can by explained by the divestment of large closed-end funds, which offsets the increase in funds under management and private banking. The Bank is listed on the main list of Nasdaq OMX Iceland.

Merger with TM hf. and Lykill fjármögnun hf.

At the end of March 2021, the previously announced tripartite merger with TM hf. ("TM") and Lykill fjármögnun hf. ("Lykill") was concluded and as at end of March 2021, the Group's operations include insurance services through the subsidiary TM tryggingar hf. TM's shareholders received, in return for their shares in TM, 2,509,934,076 shares in Kvika. The payment was made by issuance of new share capital at end of March 2021. In accordance with IFRS 3, Business Combinations, the purchase price of TM and Lykill has been allocated to identifiable assets and liabilities acquired. The purchase price allocation process resulted in the recognisition of goodwill amounting to ISK 21 billion. Refer to note 3 for further information on the merger.

Following the merger, the Financial Supervisory Authority of the Central Bank ("FME") has designated the Group as a financial conglomerate as defined in Article no. 3 of Act no. 61/2017 on Additional Supervision of Financial Conglomerates. As a result of this designation, the Group's capital adequacy is now calculated as the solvency ratio of a financial conglomerate. Solvency measures the Group's ability to take on setbacks, thus indicating its financial strength.

Acquisition of Netgíró hf. and Aur app ehf.

During the first quarter of 2021 the Group concluded the acquisitions of Netgíró hf. ("Netgíró") and Aur app ehf. ("Aur"). Netgíró is a provider of "buy now pay later" services and Aur is a leading financial technology services company. Both companies have an extensive client base and the acquisitions are in line with Kvika's policy of utilising technological solutions to modernize financial services. Refer to note 3 for further information on the acquisitions.

Operations during 2021

Profit before taxes for the year amounted to ISK 10,487 million (2020: ISK 2,339 million), corresponding to an annualised 34.7% return on weighted tangible equity, based on the tangible equity position at the beginning of the year adjusted for changes in share capital and transactions with treasury shares during the year The Covid-19 pandemic continues to have an effect, especially with regards to operational complexity. However, for the year, it has not had a large impact on the Group's operations and income generating segments. The Group's net operating income during the year was ISK 21,997 million (2020: ISK 8,666 million). Net interest income amounted to ISK 4,646 million (2020: ISK 1,800 million). Net fee income amounted to ISK 6,828 million (2020: ISK 5,956 million). Net premiums and claims amounted to ISK 4,247 million (not part of the Group's operations in 2020). Other operating income amounted to ISK 6,276 million (2020: ISK 910 million). Administrative expenses during the year amounted to ISK 11,635 million (2020: ISK 5,724 million). The figures in the consolidated income statement for the year do not include the operations of TM, Lykill or Aur for the first quarter as the business combinations took place at end of March. Furthermore, they do not include the operations of Netgíró for January as the business combination took place at end of January.

According to the Consolidated Statement of Financial Position, equity at the end of the year amounted to ISK 78,368 million (31.12.2020: ISK 19,208 million) and total assets amounted to ISK 246,240 million (31.12.2020: ISK 123,196 million).

The Group's solvency ratio at 31.12.2021 was 1.57, with a regulatory minimum requirement of 1.0. There is no comparative figure as this is the first year that the Group calculates a solvency ratio.

The Bank's Board of Directors propose that no dividend will be paid in the year 2022 on 2021 operations.

Operational outlook

Following the successful merger with TM and Lykil, and the acquisitions of Aur and Netgíró, Kvika's financial position has never been stronger. The Bank enjoys a combination of financial strength, diversified business units and identifiable growth opportunities. The four business units of the Group: Insurance, Asset Management, Commercial Banking and Investment Banking are all highly profitable and we expect them to continue to strengthen. The pending acquisition of Ortus Secured Finance (OSF), will further add to the diversification of the income streams of the group. It is therefore expected that the strong and stable profitability of Kvika will continue this year, although it should be noted that market conditions in 2021 were unusually favourable.

Our balance sheet strength and capital position has increased in the last year and it is expected that this trend will continue. The maintenance of a strong capital position and liquidity is a priority and this year there will be an emphasis on increasing the Bank's debt issuance, both in Iceland and internationally, in addition to growing the retail deposit base in ISK. Kvika has considerable excess capital and due to the high profitability of the Group its capital base is constantly growing. As has been communicated to the market, it is expected that this excess capital will be partially returned to shareholders in the form of dividends and share buybacks, but the aim will also be to maintain strong capital ratios. That will enable the Group to take advantage of both external and internal growth opportunities in a sensible manner, with focus on further diversification and granularity of the Bank's loan book.

This year there will be clear focus on taking advantage of the numerous growth opportunities Kvika has. In the UK we expect to support in a sensible manner the growth of OSF, and increase its profitability with more efficient funding, which Kvika's ownership brings. It is expected that Kvika's fintech platforms will continue to grow at a high rate and there will be an emphasis on offering clients further products and services from across the group. The aim is also that TM will strengthen its position in the insurance market and in particular increase its relatively small market share in life and health insurance.

Endorsement and Statement
by the Board of Directors and the CEO

Economic outlook

The Icelandic economy is experiencing rebound in gross domestic product from 6.5% contraction in 2020 due to the Covid-19 pandemic. Gross domestic product in the first three quarters of 2021 was stronger than initially forecasted and it is anticipated that growth in GDP will be in the area of 5% in 2021 or 1% higher than officially forecasted. Unemployment has been falling and is reaching pre-pandemic level of 5% where part-time benefits and other government measures introduced early in the pandemic have now been abolished to a large extent. The labour market has historically been flexible and as unemployment returns to pre-pandemic levels, as the tourism gains more momentum and consumer confidence increases, labour shortages may occurr as the output gap closes. Inflation has been rising and peaked at 5.7% year-on-year at the end of 2021 mainly attributable to price increases due to devolopment in global commodity prices, shipping costs, housing prices and wage growth. Inflation is set to remain above 5.0% in 2022 but forecasted to not going below 4% until 2023, accounting for 10% appreciation of the ISK to trade-weigted basket of currencies and upcoming negotions on collective wage agreements. Commodity exports such as seafood and energy (aluminium) have rebounded due to increased commodity prices as well has the international sector (not reliant on natural resources) seen strong demand. In the short-term the outlook is promising in tourism as it is set to keep growing over the next years. Main uncertainty in the economic recovery is the development of the pandemic globally since Iceland is heavily dependent on foreign trade.

Share capital and shareholders

The Bank's issued share capital amounted to ISK 4,907 million as at 31 December 2021 (31.12.2020: ISK 2,141 million). At the end of the year the Bank held ISK 117 million treasury shares (31.12.2020: no treasury shares). The shares were acquired through a share buy-back programme. The Bank's share capital was increased by a nominal value of ISK 2,766 million during the year.

The Bank had 2,820 shareholders at year-end 2021 (2020: 990), none of which held more than 10% of shares in the Bank (2020: 0). The ten largest shareholders are as follows:

Shareholder	31.12.2021	31.12.2020
Lífeyrissjóður verzlunarmanna	8.20%	7.57%
Lífeyrissjóður starfsmanna ríkisins A-deild	6.28%	5.86%
Stoðir hf.	6.11%	8.24%
Gildi - lífeyrissjóður	4.61%	0.29%
Arion banki hf.	4.40%	2.18%
Birta lífeyrissjóður	4.33%	2.30%
Stapi lífeyrissjóður	3.08%	0.28%
Lífsverk lífeyrissjóður	2.47%	2.89%
Brú Lífeyrissjóður starfsmanna sveitarfélaga	2.14%	0.23%
Bóksal ehf.	2.02%	-
	43.63%	29.85%

Further information about the shareholders of the Bank is provided in note 73.

Risk management

The objective of risk management is to promote a good and efficient culture of risk awareness within the Group and to increase the understanding of employees and management on the Group's risk taking, in addition to an assessment process related to risk and capital position. An emphasis is placed on being up to speed on the latest developments and adoption of rules related to risk management, such as regarding capital- and liquidity management. The Group is faced with various kinds of risk that relate to its operations as a financial conglomerate and arise from its day-to-day operations. An active risk management entails analysing risk, measuring it and taking actions to limit it, as well as monitoring risk factors across the Group. The Group’s risk management, and its main operations, are described in the notes accompanying the Consolidated Financial Statements. Refer to notes 46-63 on analysis of exposure to various types of risk.

Corporate governance

Kvika is obliged to observe recognised corporate governance guidelines, pursuant to Par. 7 of Article 54 of Act No. 161/2002, on Financial Undertakings. The Bank complies with the Guidelines on Corporate Governance issued jointly in February 2021 by the Chamber of Commerce, NASDAQ Iceland and the Confederation of Icelandic Employers in most respects. The only deviation from the guidelines is that Kvika has not appointed a nomination committee nor decided how one should be appointed as further discussed in an appendix to these financial statements, which contains a corporate governance statement. Kvika has twice been recognized as a company which has achieved excellence in corporate governance following a formal assessment based on the Icelandic Guidelines on Corporate Governance issued by the Icelandic Chamber of Commerce, SA – Business Iceland and Nasdaq Iceland, first in 2018 and again in 2021. The recognition applies for three years at a time unless there have been significant changes to the Board of Directors or the ownership of the Bank. The Board of Directors intends to have such an assessment carried out on a regular basis and maintain the aforementioned recognition.

In accordance with the Bank´s articles of association, five members and two alternate members are elected to the Board of Directors each year at the Annual General Meeting. The eligibility of members of the Board is subject to statutory law. It is the Bank´s policy concerning election of the Board of Directors that the Board collectively has sufficient knowledge, competency and experience to understand the Bank´s operations, including the main risk factors. The ratio of each gender of members of the Board and alternate members shall be at least 40%. The election of Board members is furthermore governed by the provisions of the Act on Public Limited Liability Companies No. 2/1995 and the Act on Financial Undertakings No. 161/2002.

Endorsement and Statement
by the Board of Directors and the CEO

The Bank´s articles of association may be amended at lawfully convened shareholders´ meetings, provided that the notice of the meeting specifies that proposals for such amendments are scheduled and outlines the main substance of the amendments. An amendment takes effect only if approved by at least 2/3 of the votes cast and by shareholders controlling at least 2/3 of the shares represented at the meeting. However, the provisions of the articles of association regarding the voting rights of shareholders and equality among them cannot be amended except with the consent of all the shareholders who are subject to the curtailment of rights, cf. paragraph 3 of Article 94 of the Act on Public Limited Liability Companies No. 2/1995.

The Board of Directors emphasizes good corporate governance and adherence to accepted guidelines on corporate governance. The Board has laid down comprehensive rules in which the authority of the Board is defined and its scope of work in conjunction with the CEO. They address e.g. competence of Board members to participate in individual decisions, confidentiality and information disclosure between the CEO and the Board. All of the Board members are independent of the Bank and it´s major shareholders and there are no executive directors on the Board. The Bank aims to promote gender equality and two out of five board members are women.

Kvika has not established a specific policy on the diversity of its Board of Directors, Executive Committee and senior management with regard to age, gender or educational and professional background. Reasons for this are discussed thoroughly in the Statement on the Corporate Governance of Kvika.

The Board determines compensation for the CEO. The Board of Directors has delegated certain tasks to three separate subcommittees, the Risk Committee, Audit Committee and Remuneration Committee. In accordance with the Bank's articles of association, at least three members have been appointed to each committee, thereof at least two Board members. It is not permitted to appoint employees of the Bank to any subcommittee. Members shall have the necessary experience and knowledge for each committee's tasks according to applicable laws and rules. Each committee has incorporated procedural rules which have been confirmed by the Board of Directors.

The Board of Directors determines the risk policy and risk appetite of the Group with rules on risk management of the financial conglomerate of Kvika, which define risk factors in Kvika’s operations, including their nature and acceptable volume.

The CEO reports to the Board and verifies the effectiveness of internal controls and risk management in the Consolidated Financial Statements. Internal controls and risk management applied in the preparation of the Consolidated Financial Statements are organised with a view to preventing any significant deficiencies in the accounting process. Kvika’s Board of Directors and control units regularly verify the effectiveness of internal controls and risk management.

The Risk Committee has an advisory and supervisory role for the Bank’s Board of Directors, among other things, in determining its risk policy and risk appetite. The Audit Committee is intended to play an advisory and supervisory role for the Bank’s Board of Directors by, among other things, ensuring the quality of financial statements and other financial information from the Bank and the independence of its auditors. The Audit Committee supervises accounting procedures and the effectiveness of internal controls as well as internal and external auditing. The main aspects of internal and external control and the Bank’s management in connection with the accounting process are described in detail in the Statement on the Corporate Governance of Kvika.

Further information about the Bank's corporate governance can be found in an appendix to these financial statements which contains a corporate governance statement. A copy of the statement is available on the Bank's website, www.kvika.is.

Sustainability and non-financial reporting

A new strategy for the Group was approved in 2021. One of the guiding principles of the new strategy is sustainability and social responsibility. In addition, one of the seven key goals of Kvika, as outlined in the strategy, is to have a real and measurable impact on Iceland’s carbon footprint and climate issues in general. Long-term thinking remains Kvika’s value, and the value of simplicity and courage have now also been added.

Responsible decision making is discussed in Kvika‘s code of conduct, which reflects the Bank´s values and strategy. The code of conduct is approved by Kvika‘s Board of Director and formally certified by its employees. The Bank has also issued a code of conduct for suppliers and important suppliers are asked to formally acknowledge the code.

The Bank has issued a social responsibility policy which outlines the group’s vision and focus on social responsibility, including Kvika’s objectives, obligations, and commitments. Kvika´s ownership policies state that sustainability and social issues are, among other issues, coordinated throughout the Group. In 2021 Kvika established a committee for social responsibility and sustainability, and a new position of a project manager of sustainability. The committee and the project manager of sustainability follow through on the relevant activities at a group level.

Kvika is involved in various collaboration in sustainability and offers diverse community grants. Kvika became a member of the UN Principles for Sustainable Investments (UN PRI) in autumn 2020 on behalf of the Group and has since then worked on the implementation of the principles into the operation.

Kvika is a commercial bank that puts emphasis on fintech solutions. By emphasizing using digital technology, Kvika supports environmental protection, with simpler and more ecologically friendly processes, products, and services. Among green products and services the Bank established in 2021 are green car loans of Lykill, now one of Kvika´s brands, and green deposit accounts of the brand Audur, both of which fall under the terms of the Bank´s Green Financing Framework. In addition, Kvika issued its first green bond in December 2021.

In accordance the Act on Annual Accounts, no 3/2006, Kvika provides information on its progress, scope, and impacts, notably on the environment, society. and human resources, in a summary with the Board of Director´s statement. The summary also covers Kvika’s approach to human rights, corruption, and bribery, as well as other factors that are included in, and affect, Kvika’s social responsibility, cf. article 66 (d) of the Act on Annual Accounts. The summary with the Board´s statement refers to Kvika’s sustainability report for 2021 for more detailed information on the Group´s non-financial performance.

Kvika’s sustainability report follows Nasdaq’s ESG Reporting Guide 2.0 and, to a limited extent, the GRI Standards. This is the first time the Group issues a sustainability report in this format. The sustainability report can be found on Kvika’s website www.kvika.is and will also be submitted to the registry of annual accounts, as part of the Group's non-financial disclosures.

Endorsement and Statement
by the Board of Directors and the CEO

Statement by the Board of Directors and the CEO

The Consolidated Financial Statements of Kvika banki hf. for the year 2021 have been prepared in accordance with International Financial Reporting Standards as adopted by the EU, and additional requirements, as applicable, in the Act on Annual Accounts no. 3/2006, the Act on Financial Undertakings no. 161/2002 and rules on accounting for credit institutions no. 834/2003.

To the best of our knowledge these Consolidated Financial Statements give a true and fair view of the Group's assets, liabilities and financial position as at 31 December 2021 and the financial performance of the Group and changes of cash flows for the year 2021. Furthermore, in our opinion the Consolidated Financial Statements and the Endorsement of the Board of Directors and the CEO give a fair view of the development and performance of the Group's operations and its position and describe the principal risks and uncertainties faced by the Group.

In our opinion, the Consolidated Financial Statements of Kvika banki hf. for the year 2021 identified as "254900WR3I1Z9NPC7D84-2021-12-31-en.zip" are prepared in all material respects, in compliance with the European Single Electronic Format Regulation (ESEF).

The Board of Directors and the CEO of the Bank have today discussed the Consolidated Financial Statements for the year 2021, and confirm them by the means of their signatures.

Reykjavík, 24 February 2022.

Board of Directors

Sigurður Hannesson
Chairman

Guðmundur Þórðarson
Deputy Chairman

Helga Kristín Auðunsdóttir

Ingunn Svala Leifsdóttir

Guðjón Reynisson

Chief Executive Officer

Marinó Örn Tryggvason

Independent Auditor's Report

To the Board of Directors and Shareholders of Kvika banki hf.

Opinion

We have audited the consolidated financial statements of Kvika banki hf. for the year ended December 31, 2021 which comprise, the consolidated statement of comprehensive income, the consolidated statement of financial position, the consolidated statement of changes in equity, the consolidated statement of cash flows for the year then ended and the notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of Kvika banki hf. as at December 31, 2021, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and additional requirements, as applicable, in the Act on Annual Accounts, the Act on Financial Undertakings and rules on accounting for credit institutions.

Our opinion in this report on the consolidated financial statements is consistent with the content of the additional report that has been submitted to the company´s audit committee in accordance with the EU Audit Regulation 537/2014 Article 11.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the consolidated Financial Statements section of our report. We are independent of Kvika banki hf. in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in Iceland, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA. This includes that, based on the best of our knowledge and belief, no prohibited services referred to in the EU Audit Regulation 537/2014 Article 5.1 has been provided to the audited company or, where applicable, its parent company or its controlled companies within the EU . We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key Audit Matters	**How the matter was addressed in our audit**
Business combination	
On 30 March 2021, Kvika banki hf and TM hf. merged together. As detailed in note 3, the purchases price was ISK 49.4 billion. Following a purchase price allocation, ISK 5.0 billion of intangible assets were recognized, resulting in the recognition of ISK 21 billion of goodwill recognized in connection with the acquisition. The business combination with TM hf. was recognized as of 30 March 2021 in the consolidated financial statements and one of the subsidiary of TM hf. (TM tryggingar hf.) now represent the new insurance segment in the consolidated financial statements. The business combination required complex management judgment in applying IFRS 3, including determining the acquirer and valuation of recognized identifiable assets and liabilities. Due to the complexity involved, we consider the business combination to be a key audit matter.	Based on our risk assessment we have reviewed internal controls that address the accounting for business combinations and tested the reasonableness of the key assumptions. We have engaged our internal valuation specialist to assess and challenge management´s assumptions used in its fair value models for identifying and measuring identifiable assets and liabilities, including: • Challenging assumptions used to measure the valuation of identifiable assets and liabilities recognized and lifetime of intangible assets. • Testing valuation models, including mathematical accuracy and obtaining supporting evidence for future cash flow projections, estimates and key assumptions. • Considered the impact of reasonable possible changes in key assumptions and performed sensitivity calculations to quantify the impact of potential downside changes to Management´s models. We have also reviewed the disclosures presented in note 3 to the financial statements to confirm compliance with the provisions within IFRS 3.

Independent Auditor's Report

Impairment charges for loans	
The group gross loans amounted ISK 72,925 million at year end and the total allowance for the group amounted to ISK 1,343 million against loans at amortized cost, unused credit facilities and guarantees at 31 December 2021. Measurement of loan impairment charges is considered a key audit matter as the determination of assumptions for expected credit losses is highly subjective due to the level of judgement applied by management. The most significant judgements are: • Assumptions used in the expected credit loss models to incorporate forward looking information. • Timely identification of exposures with significant increase in credit risk and credit impaired exposures. • Valuation of collateral and assumptions of future cash flows on manually assessed credit-impaired exposures. • Management overlays for particular exposures, which are not appropriately captured in the expected credit loss model. Management has provided further information about expected credit losses and provisions for guarantees in notes 23, 50 and 89 to the consolidated financial statements.	Based on our risk assessment and industry knowledge, we have examined the impairment charges for loans and provisions for undrawn loan commitments and guarantess and evaluated the methodology applied as well as the assumptions made according to the description of the key audit matter. During our audit we have evaluated whether the groups expected credit loss models are compliant to IFRS 9. Our examination included the following elements: • Testing of key controls over assumptions used in the expected credit loss models. • Substantively testing the valuation of collateral with particular focus on management overlays applied to collateral value. • Reviewed the PD (proabability of default) model from CreditInfo and how it has been calibrated to represent the banks portfolio. • Testing the appropriateness of forward looking information and how they have been applied in the expected credit loss models. We have evaulated whether disclosure in the consolidated financial statement are in accordance with IFRS.
Measurement of liabilities under insurance contracts	
Liabilities under insurance contracts for the Group amounted to ISK 22,434 million at 31 December 2021. There of claims provision amounted to ISK 16,493 million. Measurement of claims provision is deemed a key audit matter as the determination of assumptions for the measurement of claims provision requires Management to apply judgements about future events. Changes in assumptions and the methodology applied may have a material impact on the measurement of claims provision. Management has provided further information about liabilities under insurance contracts in note 33 and 104 to the consolidated financial statements.	Based on our risk assessment, we have examined the valuation of claims provision and evaluated the methodology applied and the assumptions made. Our examination included the following elements, where we also made use of our internationally qualified actuaries: • Testing of key controls over the actuarial models, data collection and analysis and the assumptions-setting processes. • Performed substantive testing on reported claims and estimated whether the liability was sufficiently recognized. • Evaluated managements first estimates of claims when further information is missing. • Evaluated management methodology and calculations of IBNR. • Reconcliations of reported and IBNR claims at year end. In addition we have evaluated whether disclosures in the consolidated financial statements are in accordance with IFRS.

Other information

The Board of Directors and the CEO are responsible for the other information. The other information comprises the report of board of directors, Statement of the Corporate Governance and Non-Financial information.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon, except the confirmation regarding report of the board of directors as stated below.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

In accordance with Paragraph 2 article 104 of the Icelandic Financial Statement Act no. 3/2006, we confirm to the best of our knowledge that the accompanying report of the board of directors includes all information required by the Icelandic Financial Statement Act that is not disclosed elsewhere in the financial statements.

Independent Auditor's Report

Responsibilities of the Board of Directors and the CEO for the Consolidated Financial Statements

The Board of Directors and the CEO are responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and additional requirements, as applicable, in the Act on Annual Accounts, the Act on Financial Undertakings and rules on accounting for credit institutions, and for such internal control as the Board of Directors and the CEO determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Board of Directors and the CEO are responsible for assessing Kvika banki hf.'s ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Board of Directors and the CEO either intends to liquidate the company or to cease operations, or has no realistic alternative but to do so.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.
As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of Kvika banki hf.'s internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated and separate financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Board of Directors and the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Board of Directors and the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

In addition to our work as the auditors of Kvika banki hf., Deloitte has provided the firm with permitted additional services such as review of interim financial statements, other assurance engagements and consultation on tax matters. Deloitte has in place internal procedures in order to ensure its independence before acceptance of additional services. Deloitte has provided to the audit commitee written confirmation that Deloitte is independent of Kvika banki hf.

From the matters communicated with the Board of Directors and the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Independent Auditor's Report

Report on other legal and regulatory requirements

Report on European single electronic format (ESEF Regulation)

As part of our audit of the consolidated financial statements of Kvika banki hf. we performed procedures to be able to issue an opinion on whether the consolidated financial statements of Kvika banki hf. for the year 2021 with the file name "254900WR3I1Z9NPC7D84-2021-12-31-en.zip" is prepared, in all material respects, in compliance with laws no. 20/2021 disclosure obligation of issuers of securities and the obligation to flag relating to requirements regarding European single electronic format regulation EU 2019/815 which include requirements related to the preparation of the consolidated financial statements in XHTML format and iXBRL markup.

Management is responsible for preparing the consolidated financial statements in compliance with laws no. 20/2021 disclosure obligation of issuers of securities and the obligation to flag. This responsibility includes preparing the consolidated financial statements in a XHTML format in accordance to EU regulation 2019/815 on the European single electronic format (ESEF regulation).

Our responsibility is to obtain reasonable assurance, based on evidence that we have obtained, on whether the consolidated financial statements is prepared in all material respects, in compliance with the ESEF Regulation, and to issue a report that includes our opinion. The nature, timing and extent of procedures selected depend on the auditor's judgement, including the assessment of the risks of material departures from the requirement set out in the ESEF regulation, whether due to fraud or error.

In our opinion, the consolidated financial statements of Kvika banki hf. for the 2021 with the file name "254900WR3I1Z9NPC7D84-2021-12-31-en.zip" is prepared, in all material respects, in compliance with the ESEF Regulation.

Deloitte was appointed auditor of Kvika banki hf. by the general meeting of shareholders on 21 April 2021. Deloitte have been elected since the general meeting 2016.

Kópavogur, 24 February 2022.

Deloitte ehf.

Pálína Árnadóttir

State Authorized Public Accountant

Kvika banki hf. Amounts are in ISK thousands

Consolidated Income Statement
For the year 2021

	Notes	2021	2020
Interest income		7,084,596	3,719,984
Interest expense		(2,438,481)	(1,919,810)
Net interest income	5	4,646,115	1,800,174
Fee and commission income		7,224,480	6,149,794
Fee and commission expense		(396,739)	(194,136)
Net fee and commission income	6	6,827,741	5,955,659
Earned premiums, net of reinsurers' share		11,808,210	0
Claims incurred, net of reinsurers' share		(7,560,809)	0
Net premiums and claims	7	4,247,400	0
Net financial income	8	5,671,978	832,595
Share in loss of associates, net of income tax	26	(27,566)	(7,427)
Other operating income		631,391	85,048
Other operating income		6,275,803	910,215
Net operating income		21,997,059	8,666,048
Administrative expenses	10-13	(11,634,885)	(5,723,554)
Net impairment	14	138,842	(317,468)
Revaluation of contingent consideration		(97,548)	(286,058)
Revaluation of investment properties	27	83,095	0
Profit before taxes		10,486,563	2,338,969
Income tax	15	347,634	28,277
Special tax on financial activity	16	(35,454)	(16,613)
Special tax on financial institutions	17	(135,299)	(77,402)
Profit for the year		10,663,444	2,273,231

	Notes	2021	2020
Attributable to the shareholders of Kvika banki hf.		10,734,181	2,348,621
Attributable to non-controlling interest	25	(70,737)	(75,390)
Profit for the year		10,663,444	2,273,231
Earnings per share	18		
Basic earnings per share (ISK per share)		2.62	1.10
Diluted earnings per share (ISK per share)		2.56	1.02

The notes on pages 16 to 77 are an integral part of these Consolidated Financial Statements.

Kvika banki hf. Amounts are in ISK thousands

Consolidated Statement of Comprehensive Income
For the year 2021

	Notes	2021	2020
Profit for the year		10,663,444	2,273,231
Changes in fair value of financial assets through OCI, net of tax		(108,180)	20,887
Realized net gain transferred to the Income Statement, net of tax		11,522	948
Changes to reserve for financial assets at fair value through OCI		(96,657)	21,834
Exchange difference on translation of foreign subsidiaries		12,238	48,935
Other Comphrehensive income that is or may be reclassified subsequently to profit and loss		(84,419)	70,769
Total comprehensive income for the year		10,579,025	2,344,000

	Notes	2021	2020
Attributable to the shareholders of Kvika banki hf.		10,649,762	2,419,390
Attributable to non-controlling interest		(70,737)	(75,390)
Total comprehensive income for the year		10,579,025	2,344,000

The notes on pages 16 to 77 are an integral part of these Consolidated Financial Statements.

Kvika banki hf. Amounts are in ISK thousands

Consolidated Statement of Financial Position
As at 31 December 2021

Assets	Notes	31.12.2021	31.12.2020
Cash and balances with Central Bank	19	38,645,894	28,945,030
Fixed income securities	20	40,046,651	28,785,033
Shares and other variable income securities	21	22,683,295	5,072,830
Securities used for hedging	22	22,085,696	19,620,240
Loans to customers	23	71,587,646	29,322,972
Derivatives	24	2,734,216	389,671
Investment in associates	26	67,000	42,240
Investment properties	27	1,100,000	1,016,905
Intangible assets	28	31,455,409	3,562,621
Operating lease assets	29	1,458,621	0
Property and equipment		405,695	162,373
Deferred tax assets	15,30	3,177,763	835,816
Reinsurance assets	33	749,383	0
Other assets	31	10,042,553	5,440,092
Total assets		246,239,821	123,195,821

Liabilities			
Deposits	32	78,669,807	59,924,683
Technical provision	33	22,434,447	0
Borrowings	34	17,261,048	26,424,340
Issued bills	35	0	2,003,608
Issued bonds	36	32,597,716	5,568,085
Subordinated liabilities	37	3,371,766	2,077,225
Short positions held for trading	38	1,323,631	1,520,547
Short positions used for hedging	39	1,280,868	731,987
Derivatives	24	3,008,401	1,750,346
Current tax liabilities		347,068	341
Deferred tax liabilities	30	899,942	236,186
Other liabilities	40	6,677,507	3,750,472
Total liabilities		167,872,201	103,987,820

Equity			
Share capital	41	4,790,139	2,141,002
Share premium		50,316,002	4,290,521
Other reserves		9,613,793	5,014,902
Retained earnings		13,696,745	7,740,546
Total equity attributable to the shareholders of Kvika banki hf.		78,416,678	19,186,971
Non-controlling interest	25	(49,058)	21,030
Total equity		78,367,620	19,208,001
Total liabilities and equity		246,239,821	123,195,821

The notes on pages 16 to 77 are an integral part of these Consolidated Financial Statements.

Kvika banki hf. Amounts are in ISK thousands

Consolidated Statement of Changes in Equity
For the year 2021

1 January 2021 to 31 December 2021	Notes	Share capital	Share premium	Other reserves: Option reserve	Other reserves: Warrants reserve	Other reserves: Deficit reduction reserve	Other reserves: Fair value reserve	Other reserves: Translation reserve	Other reserves: Restricted retained earnings	Retained earnings	Total share-holders' equity	Non-controlling interest	Total equity
Equity as at 1 January 2021		2,141,002	4,290,521	0	149,462	3,103,697	27,293	54,520	1,679,930	7,740,546	19,186,971	21,030	19,208,001
Profit for the year										10,734,181	10,734,181	(70,737)	10,663,444
Changes in fair value of financial assets through OCI							(108,180)				(108,180)		(108,180)
Realized net gain transferred to the Income Statement							11,522				11,522		11,522
Translation of foreign operations													
Exchange difference on translation of foreign subsidiaries								11,589			11,589	649	12,238
Total comprehensive income for the year		0	0	0	0	0	(96,657)	11,589	0	10,734,181	10,649,113	(70,088)	10,579,025
Restricted retained earnings									4,777,983	(4,777,983)	0		0
Prior year adjustment							(5,459)				(5,459)		(5,459)
Transactions with owners of the Bank													
Capital increase		2,766,392	48,673,652								51,440,045	0	51,440,045
Own shares acquired through business combination		(6,400)	(126,720)								(133,120)		(133,120)
Treasury shares acquired as part of a buy-back programme ..		(117,256)	(2,741,165)								(2,858,422)		(2,858,422)
Transactions with own shares		6,400	126,720								133,120		133,120
Stock options	72			4,430							4,430		4,430
Warrants exercised	42		92,994		(92,994)						0		0
Equity as at 31 December 2021		4,790,139	50,316,002	4,430	56,468	3,103,697	(74,823)	66,109	6,457,912	13,696,745	78,416,678	(49,058)	78,367,620

The notes on pages 16 to 77 are an integral part of these Consolidated Financial Statements.

Kvika banki hf. Amounts are in ISK thousands

Consolidated Statement of Changes in Equity
For the year 2020

				Other reserves									
1 January 2020 to 31 December 2020	**Notes**	**Share capital**	**Share premium**	**Option reserve**	**Warrants reserve**	**Deficit reduction reserve**	**Fair value reserve**	**Trans-lation reserve**	**Restricted retained earnings**	**Retained earnings**	**Total share-holders' equity**	**Non-controlling interest**	**Total equity**
Equity as at 1 January 2020		1,945,366	3,115,992	7,687	206,501	3,103,697	0	5,586	778,191	6,292,189	15,455,209	59,974	15,515,183
Profit for the year										2,348,621	2,348,621	(75,390)	2,273,231
Changes in fair value of financial assets through OCI							20,887				20,887		20,887
Realized net gain transferred to the Income Statement							948				948		948
Translation of foreign operations											0		0
Exchange difference on translation of foreign subsidiaries								48,935			48,935		48,935
Total comprehensive income for the year		0	0	0	0	0	21,834	48,935	0	2,348,621	2,419,390	(75,390)	2,344,000
Restricted retained earnings									901,739	(901,739)	0		0
Adjustments for tax effects							5,459				5,459		5,459
Transactions with owners of the Bank													
Capital increase		195,637	1,108,806								1,304,443	36,446	1,340,889
Stock options	72			2,471							2,471		2,471
Stock options excercised			8,683	(10,158)						1,475	0		0
Warrants exercised			57,038		(57,038)						0		0
Equity as at 31 December 2020		2,141,002	4,290,521	0	149,462	3,103,697	27,293	54,520	1,679,930	7,740,546	19,186,971	21,030	19,208,001

The notes on pages 16 to 77 are an integral part of these Consolidated Financial Statements.

Kvika banki hf. Amounts are in ISK thousands

Consolidated Statement of Cash Flows
For the year 2021

Cash flows from operating activities	Notes	2021	2020
Profit for the year		10,663,444	2,273,231
Adjustments for:			
Indexation and exchange rate difference		89,214	(1,458,673)
Share in (profit) loss of associates, net of income tax		27,566	7,427
Depreciation and amortisation		1,966,889	301,238
Net interest income		(4,646,115)	(1,800,174)
Net impairment		(138,842)	334,773
Income tax		(329,374)	(28,277)
Investment properties, fair value change		(83,095)	0
Other adjustments		(71,925)	87,851
		7,477,762	(282,605)
Changes in:			
Fixed income securities		3,833,960	(20,660,571)
Shares and other variable income securities		(5,042,426)	(1,413,622)
Securities used for hedging		(2,465,456)	4,654,529
Loans to customers		(2,802,876)	1,109,130
Derivatives - assets		(763,439)	870,162
Operating lease assets		946,974	0
Other assets		1,558,140	(500,618)
Deposits		18,479,161	8,255,394
Technical provision		(276,730)	0
Short positions		351,965	1,012,619
Derivatives - liabilities		1,215,432	468,005
Other liabilities		(380,224)	538,821
		14,654,481	(5,666,153)
Interest received		6,555,029	3,440,541
Interest paid		(1,905,378)	(1,653,626)
Net cash from (to) operating activities		26,781,893	(4,161,843)
Cash flows from investing activities			
Acquisition of intangible assets	28	(458,271)	(354,053)
Acquisition of property and equipment		(160,551)	0
Proceeds from the sale of property and equipment		0	169,536
Dividend from assoiciates		3,750	7,500
Acquisition of subsidiary and associates, net of cash		(845,239)	0
Net sale (investment) in associates		0	363,000
Lease receivable payments		19,915	28,430
Net cash (to) from investing activities		(1,440,397)	214,413
Cash flows from financing activities			
Borrowings		(12,377,785)	5,672,370
Issued bills		(5,291,000)	(1,941,697)
Subordinated liabilities		(1,258,799)	0
Increase in capital		1,994,343	1,361,462
Aquired own shares		(2,858,421)	0
Decrease in warrants		0	(57,018)
Lease payments		(299,701)	(197,076)
Net cash (to) from financing activities		(20,091,363)	4,838,040
Net increase in cash and balances with Central Bank		5,250,133	890,610
Cash and balances with Central Bank at the beginning of the year		28,945,030	26,818,231
Change in cash and cash equivalents due to acquisition of subsidiary		4,586,420	0
Effects of exchange rate fluctuations on cash and balances with Central Bank		(135,688)	1,236,189
Cash and balances with Central Bank at the end of the year	19	38,645,894	28,945,030

The notes on pages 16 to 77 are an integral part of these Consolidated Financial Statements.

Kvika banki hf. Amounts are in ISK thousands

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Notes to the Consolidated Financial Statements

General information

1. Reporting entity

Kvika banki hf. ("Kvika" or the "Bank") is a limited liability company incorporated and domiciled in Iceland, with its registered office at Katrínartún 2, Reykjavík. The Bank operates as a bank based on Act No. 161/2002, on Financial Undertakings, and is supervised by the Financial Supervisory Authority of the Central Bank ("FME"). At end of March 2021, a tripartite merger with TM hf. and Lykill fjármögnun hf. was concluded and as at end of March 2021, the Group's operations include insurance services through the subsidiary TM tryggingar hf.

The Consolidated Financial Statements for the year ended 31 December 2021 comprise Kvika banki hf. and its subsidiaries (together referred to as the Group). The Group operates four business segments, Asset Management, Corporate Banking, Insurance Services and Investment Banking. The Group provides businesses, investors and individuals with comprehensive investment banking, insurance services and asset management services as well as selected banking services.

The Consolidated Financial Statements were approved and authorised for issue by the Board of Directors and the CEO on 24 February 2022.

2. Basis of preparation

a. Statement of compliance

The Consolidated Financial Statements have been prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union and additional requirements, as applicable, in the Act on Annual Accounts no. 3/2006, the Act on Financial Undertakings no. 161/2002 and rules on accounting for credit institutions no. 834/2003.

b. Basis of measurement

The Consolidated Financial Statements have been prepared using the historical cost basis except for the following:
- fixed income securities are measured at fair value;
- shares and other variable income securities are measured at fair value;
- securities used for hedging are measured at fair value;
- certain loans to customers which are measured at fair value;
- derivatives are measured at fair value;
- investment properties are measured at fair value;
- certain receivables are measured at fair value;
- shared based payment is accounting for in accordance with IFRS 2;
- contingent consideration is measured at fair value;
- short positions are measured at fair value; and
- technical provision is measured in accordance with IFRS 4.

c. Functional and presentation currency

The Consolidated Financial Statements are prepared in Icelandic Krona (ISK), which is the Bank's functional currency. All financial information has been rounded to the nearest thousand, unless otherwise stated.

The Group's assets and liabilities which are denominated in other currency than ISK are translated to ISK using the exchange rate as at the end of day 31 December 2021.

d. Going concern

The Bank's management has assessed the Group's ability to continue as a going concern and is satisfied that the Group has the resources to continue its operations.

e. Estimates and judgements

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

The estimates and underlying assumptions are based on historical result and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources.

The estimates and underlying assumptions are reviewed on an on-going basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period and future periods if the revision affects both current

Information about areas of estimation uncertainty and critical judgements made by management in applying accounting policies that can have a significant effect on the amounts recognised in the Consolidated Financial Statements is provided in note 118.

f. Relevance and importance of notes to the reader

In order to enhance the informational value of the Condensed Interim Consolidated Financial Statements, the notes are evaluated based on relevance and importance for the reader. This can result in information, that has been evaluated as neither important or relevant for the reader, not being presented in the notes.

The COVID-19 pandemic and the challenges it created had an impact on the operation and assets of the Group during the years 2020 and 2021. This impact is best quantified in its effect on the Bank's loan portfolio. For further details see notes 50 and 89.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

3. Business combinations

a. Merger of Kvika banki, TM hf. and Lykill fjármögnun hf.

In March 2021, the tripartite merger of Kvika banki hf. ("Kvika"), TM hf. ("TM") and Lykill Fjármögnun hf. ("Lykill") was concluded. In the merger TM and Lykill were dissolved without settlement of debts, the three companies were combined and are TM and Lykill thereby a part of the Bank as at 30 March 2021 and their subsidiaries are part of the Group's Consolidated Financial Statements from that day. The activities and operations of TM and Lykill have been integrated with those of the Bank and the merged company operates under the name Kvika banki hf. During the years 2020 and 2021, the Bank incurred transaction costs related to the merger amounting to ISK 40 million which were expensed as operating expenses.

The transaction is a good strategic fit and allows for loan diversification for the Group. It is anticipated that cost synergies will result in considerably lower funding costs and reduced operating expenses for the activities of Lykill and TM. For more information, reference is made to stock exhange releases and investor presentations that Kvika has published.

The consideration transferred, to the previous owners of TM, was in the form of shares in the merged company in exchange for their shares in TM. TM's shareholders received, in return for their shares in TM, 2,509,934,076 shares in Kvika. The payment was made by issuance of new share capital at end of March 2021. The fair value of the Kvika shares transferred was based on the listed share price of the Bank at 30 March 2021, being 19.7 per share. Kvika is the acquirer in the business combination as, among other things, the majority of the Group‘s senior management and board of directors consists of management and directors from Kvika.

In accordance with IFRS 3, Business Combinations, the purchase price of TM and Lykill was allocated to identifiable assets and liabilities acquired. The purchase price allocation ("PPA") of TM and Lykill has been finalised and recognised goodwill amounts to ISK 20,984 million. The following table summarises the recognised amounts of assets and liabilities acquired by the Group on the acquisition date, 30 March 2021, as well as fair value changes made as a part of the PPA.

Identifiable assets acquired and liabilities assumed **Assets**	**Book value at acquisition date**	**Fair value changes**	**Total**
Cash and cash equivalents	4,476,923		4,476,923
Fixed income securities	15,649,175		15,649,175
Shares and other variable income securities	12,899,937		12,899,937
Loans to customers	39,384,339		39,384,339
Operating lease assets	1,784,025		1,784,025
Investment where investment risk is borne by life-insurance policyholders	93,883		93,883
Derivatives	1,581,106		1,581,106
Intangible assets	750,648	4,607,739	5,358,387
Property and equipment	793,195		793,195
Deferred tax assets	1,088,721	937,495	2,026,216
Other assets	11,706,807		11,706,807
Total	90,208,760	5,545,234	95,753,994
Liabilities			
Borrowings	6,457,110	233,548	6,690,658
Issued bills	3,253,058		3,253,058
Issued bonds	24,241,920		24,241,920
Subordinated liabilities	2,358,610		2,358,610
Technical provision for life-insurance policies where investment risk is borne by policyholders	93,883		93,883
Derivatives	42,623		42,623
Deferred tax liabilities	694,715	297,348	992,063
Technical provision	27,169,612		27,169,612
Other liabilities	2,449,848		2,449,848
Total	66,761,377	530,896	67,292,273

Total identifiable net assets	28,461,721
Acquisition price	49,445,701
Calculated goodwill on acquisition	20,983,981

The figures in the consolidated income statement for the year 2021 do not include the operations of TM or Lykill during January through March as the merger took place at end of March. If the merger had occurred on 1 January 2021, it is estimated that the consolidated net operating income would have been ISK 24,971 million and the consolidated profit before tax for the year would have been ISK 12,004 million.

Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

3. Business combinations (cont.)

b. Acquisition of Netgíró hf.

In January 2021, the Group acquired 80% of the shares in Netgíró hf. ("Netgíró") and is Netgíró a part of the Group and Consolidated Financial Statements from the end of January 2021. The Group is now the sole owner of Netgíró as before the acquisition, it owned 20% of the shares in the company. The 20% share which the Group previously owned was at end of 2020 held at a fair value in line with the purchase price for the remaining share. The consideration transferred, to the previous owners of Netgíró, was in the form of a cash payment of ISK 325 million. During the years 2020 and 2021, the Bank incurred transaction costs related to the acquisition amounting to ISK 16 million which were expensed as operating expenses.

Netgíró is a provider of "buy now pay later" services. The transaction is a good strategic fit and is in line with Kvika's policy of utilising technological solutions to modernize financial services. The acquisition also allows for loan diversification for the Group, and synergies in terms of improved funding costs.

In accordance with IFRS 3, Business Combinations, the purchase price of Netgíró was allocated to identifiable assets and liabilities acquired. The purchase price allocation ("PPA") of Netgíró has been finalised and recognised goodwill amounts to ISK 221 million. The following table summarises the recognised amounts of assets and liabilities acquired by the Group on the acquisition date, 31 January 2021, as well as fair value changes made as a part of the PPA.

Identifiable assets acquired and liabilities assumed	**Book value at**	**Fair value**	
Assets	**acquisition date**	**changes**	**Total**
Cash and cash equivalents	35,843		35,843
Loans to customers	2,655,867		2,655,867
Property and equipment	4,335		4,335
Intangible assets	409,372	623,072	1,032,444
Deferred tax assets	112,300		112,300
Other assets	285,884		285,884
Total	3,503,602	623,072	4,126,674
Liabilities			
Borrowings	3,320,809		3,320,809
Deferred tax liabilities	0	133,911	133,911
Other liabilities	486,644		486,644
Total	3,807,454	133,911	3,941,365
Total identifiable net assets			185,309
Acquisition price			406,000
Calculated goodwill on acquisition			220,691

As a part of the acquisition, the Group provided Netgíró with funding to repurchase cash flow from loans which it had sold. The presentation in the table above reflects this.

The figures in the consolidated income statement for the period do not include the operations of Netgíró in January 2021 as the merger took place at end of January 2021. If the merger had occurred on 1 January 2021, it is estimated that the consolidated net operating income would have been ISK 22,075 million and the consolidated profit before tax for the year would have been ISK 10,492 million.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

3. Business combinations (cont.)

c. Acquisition of Aur app ehf.

In March 2021, the Group acquired Aur app ehf. ("Aur") and is Aur a part of the Group and Consolidated Financial Statements from 31 March 2021. The consideration transferred, to the previous owners of Aur, was in the form of a cash payment of ISK 453 million. During the year 2021, the Bank incurred transaction costs related to the acquisition amounting to ISK 8 million which were expensed as operating expenses.

Aur is a leading financial technology services company with an extensive client base. The acquisition is in line with Kvika's policy of utilising technological solutions to modernize financial services.

In accordance with IFRS 3, Business Combinations, the purchase price of Aur was allocated to identifiable assets and liabilities acquired. The purchase price allocation ("PPA") of Aur has been finalised and recognised goodwill amounts to ISK 109 million. The following table summarises the recognised amounts of assets and liabilities acquired by the Group on the acquisition date, 31 March 2021, as well as fair value changes made as a part of the PPA.

Identifiable assets acquired and liabilities assumed	**Book value at**	**Fair value**	
Assets	**acquisition date**	**changes**	**Total**
Cash and cash equivalents	75,302		75,302
Intangible assets	38,132	419,570	457,702
Deferred tax assets	0	33,069	33,069
Other assets	3,925		3,925
Total	117,359	452,639	569,998
Liabilities			
Deferred tax liabilities	0	83,914	83,914
Other liabilities	142,263		142,263
Total	142,263	83,914	226,177
Total identifiable net assets			343,821
Acquisition price			453,239
Calculated goodwill on acquisition			109,418

The figures in the consolidated income statement for the period do not include the operations of Aur for January through March 2021 as the merger took place at end of March 2021. If the merger had occurred on 1 January 2021, it is estimated that the consolidated net operating income would have been ISK 22,035 million and the consolidated profit before tax for the year would have been ISK 10,497 million.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

Segment information

4. Business segments

Segment reporting is based on the same principles and structure as internal reporting to the CEO and the Board of Directors. Segment performance is evaluated on profit before cost allocation and tax.

Reportable segments

Following business combinations during the year 2021, the Group has changed the structure of its internal reporting and reportable segments. The Group now defines four reportable operating segments; Insurance, Asset Management, Commercial Banking and Investment Banking. The figures for the year 2021 reflect the current operating segment structure for the whole year and comparison amounts for the previous year have been restated accordingly.

- Insurance
  The TM insurance group offers its customers comprehensive insurance services, including life insurance.
- Asset Management
  Products and services offered include asset management involving both domestic and foreign assets, private banking, and private pension plans. The management of a broad range of mutual funds, investment funds and institutional investor funds is include in this segment through the operations of Kvika eignastýring hf. and Gamma Capital Management hf.
- Commercial Banking
  Commercial Banking offers various forms of banking services and related advisory services, in addition to providing specialised lending services. Included in this operating segment is Lykill, the leasing operations of the Group, and the Group's fintech operations, such as Auður, Netgíró and Aur.
- Investment Banking
  Investment Banking consists of Capital Markets, Corporate Finance and Kvika Securities Limited. The functions of Market Making and Treasury are also included in the segment although they are a part of Kvika's Finance division.

Supporting units consist of the functions carried out by the Bank's support divisions, such as Risk Management, Finance, IT and Operations, etc. The information presented relating to the supporting units does not represent an operating segment.

2021	Insurance	Asset Management	Commercial Banking	Investment Banking	Supporting units	Total
Net interest income	205,437	(654)	3,365,277	1,081,026	(4,971)	4,646,115
Net fee and commission income	(14,483)	3,700,385	857,867	2,233,452	50,520	6,827,741
Net premiums and claims	4,247,400	-	-	-	-	4,247,400
Net financial income	3,399,270	79,056	655,736	1,537,915	-	5,671,978
Share in profit of associates	0	(2,184)	(27,881)	-	2,498	(27,566)
Other operating income	84,510	7,078	517,837	2,646	19,319	631,391
Net operating income	7,922,134	3,783,682	5,368,836	4,855,040	67,367	21,997,059
Salaries and related expenses	(1,163,622)	(1,149,644)	(665,856)	(1,289,582)	(2,010,955)	(6,279,660)
Other operating expenses	(1,595,644)	(95,716)	(1,417,256)	(746,619)	(1,499,990)	(5,355,225)
Net impairment	(8,245)	-	149,572	-	(2,484)	138,842
Revaluation of contingent consideration	-	(97,548)	-	-	-	(97,548)
Revaluation of investment properties	-	-	83,095	-	-	83,095
Profit (loss) before cost allocation and tax	5,154,623	2,440,773	3,518,391	2,818,839	(3,446,063)	10,486,563
Net segment revenue from external customers	7,922,134	3,794,627	6,156,740	4,055,845	67,713	21,997,059
Net segment revenue from other segments	-	(10,945)	(787,904)	799,195	(346)	0

2020	Insurance	Asset Management	Commercial Banking	Investment Banking	Supporting units	Total
Net interest income	-	(58,208)	1,638,335	220,233	(186)	1,800,174
Net fee and commission income	-	3,467,718	639,258	1,852,277	(3,594)	5,955,659
Net premiums and claims	-	-	-	-	-	-
Net financial income	-	44,368	91,400	696,826	-	832,595
Share in profit of associates	-	10,428	(17,855)	-	-	(7,427)
Other operating income	-	(4,942)	97,041	1,935	(8,986)	85,048
Net operating income	-	3,459,363	2,448,180	2,771,271	(12,766)	8,666,048
Salaries and related expenses	-	(1,099,252)	(269,758)	(1,024,285)	(1,229,688)	(3,622,983)
Other operating expenses	-	(202,014)	(453,196)	(538,557)	(906,803)	(2,100,570)
Net impairment	-	(142,069)	(173,296)	(1,108)	(994)	(317,468)
Revaluation of contingent consideration	-	(286,058)	-	-	-	(286,058)
Profit (loss) before cost allocation and tax	-	1,729,970	1,551,929	1,207,321	(2,150,251)	2,338,969
Net segment revenue from external customers	-	3,459,369	2,440,427	2,701,519	64,734	8,666,048
Net segment revenue from other segments	-	(6)	7,753	69,753	(77,500)	-

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

Income statement

5. Net interest income

Interest income is specified as follows:

	2021	2020
Cash and balances with Central Bank	98,077	394,169
Derivatives	1,358,756	735,015
Loans to customers	4,985,407	2,433,211
Fixed income securities (FVOCI)	459,687	140,067
Other interest income	182,670	17,522
Total	7,084,596	3,719,984

Interest expense is specified as follows:

	2021	2020
Deposits	688,525	763,176
Borrowings	325,855	647,679
Issued bills	34,334	73,266
Issued bonds	866,116	134,078
Subordinated liabilities	385,960	206,285
Derivatives	10,557	6,175
Other interest expense*	127,136	89,150
Total	2,438,481	1,919,810

* Thereof are lease liabilities' interest expense amounting to ISK 39 million (2020: ISK 22 million).

During the year 2021, ISK 112 million were expensed in one-off costs related to refinancing debt which was acquired in relation to the merger with Lykill. Additionally, interest expenses related to issued bonds was reduced by ISK 184 million as a result of the fair value measurement of liabilities assumed from Lykill.

Total interest income recognised in respect of financial assets not carried at fair value through profit or loss amounts to ISK 5,021 million (2020: ISK 2,634 million). Total interest expense recognised in respect of financial liabilities not carried at fair value through profit or loss amounts to ISK 2,432 million (2020: ISK 1,913 million).

6. Net fee and commission income

Fee income and expenses are presented on a net fee basis, as presented in internal reporting to management for decision making purposes, and broken down by business segments. The business segments are representative of the nature and types of activity from which the Group generates fee income from. A description of each business segment is provided in note 4. As discussed in that note, the Group changed the structure of its internal reporting and reportable segments during 2021. The figures for the year 2021 reflect this structure and the comparison amounts have been restated accordingly.

Net fee and commission income by business segment	2021	2020
Insurance	(14,483)	0
Asset Management	3,700,385	3,467,718
Commercial Banking	857,867	639,258
Investment Banking	2,233,452	1,852,277
Supporting units	50,520	(3,594)
Total	6,827,741	5,955,659

7. Net premiums and claims

Net premiums and claims is specified as follows:

Earned premiums, net of reinsurers' share	2021
Premiums written	8,048,480
Premiums written, reinsurers' share	(315,788)
Change in provision for unearned premiums	4,484,240
Change in provision for unearned premiums, reinsurers' share	(408,723)
Total	11,808,210

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

7. Net premiums and claims (cont.)

Claims incurred, net of reinsurers' share	**2021**
Claims paid	(8,126,007)
Claims paid, reinsurers' share	853,013
Change in provision for claims due to insurance operations	245,620
Change in risk margin	5,075
Change in provision for claims, reinsurers' share	(538,510)
Total	(7,560,809)
Net premiums and claims	4,247,400
Combined ratio	84.1%

Insurance operations became part of the Group's operations following the merger with TM hf. at end of the first quarter of 2021. As a result, the operating figures only relate to period 01.04.2021 to 31.12.2021. Furthermore, there are no comparative figures as insurance operations were not part of the consolidated financial statements for the year 2020.

8. Net financial income

Net financial income is specified as follows:

	2021	**2020**
Net gain on financial assets and financial liabilities mandatorily measured at fair value through profit or loss		
Fixed income securities	607,723	399,893
Shares and other variable income securities	4,647,213	474,696
Derivatives	388,524	28,163
Loans to customers	(36,956)	6,684
Unwinding, interest and exchange rate change of technical provision	488	0
Foreign currency exchange difference	64,987	(76,841)
Total	5,671,978	832,595

9. Foreign currency exchange difference

Foreign currency exchange difference is specified as follows:

	2021	**2020**
(Loss) gain on financial instruments at fair value through profit and loss	(148,309)	228,247
Gain (loss) on other financial instruments	213,295	(305,088)
Total	64,987	(76,841)

10. Administrative expenses

Administrative expenses are specified as follows:	**2021**	**2020**
Salaries and related expenses	6,279,660	3,622,983
Other operating expenses	3,627,764	1,758,834
Depositors' and Investors' Guarantee Fund contributions	31,718	35,366
Depreciation and amortisation	1,243,431	133,907
Depreciation of right of use asset	452,312	172,463
Total	11,634,885	5,723,554

11. Salaries and related expenses

Salaries and related expenses are specified as follows:	**2021**	**2020**
Salaries	4,675,858	2,816,240
Performance based payments excluding share-based payments	275,830	34,175
Share-based payment expenses	4,389	2,471
Pension fund contributions	642,849	380,309
Tax on financial activity	306,555	162,627
Other salary related expenses	374,179	227,161
Total	6,279,660	3,622,983
Average number of full time employees during the year	316	144
Total number of full time employees at year-end	331	160

The figures for 2020 do not include employees of TM hf. and its subsidiaries, Lykill fjármögnun hf. and TM tryggingar hf., nor for Netgíró hf. or Aur app ehf. At the beginning of 2021, these companies had 179 full time employees and Kvika and its subsidiaries had 160, or 339 in total.

According to Act No. 165/2011, passed in 2011, banks and other financial institutions providing VAT exempt services, must pay a tax based on salary payments, called tax on financial activity. The current tax rate is 5.50% (2020: 5.50%).

Notes to the Consolidated Financial Statements

12. Employment terms of the Board of Directors and management

Salaries and benefits paid to the Board of Directors, the CEO and Managing Directors, including the Deputy CEO, of the Bank for their work for companies within the Group, and their shareholding in the Bank, are specified as follows:

			31.12.2021			31.12.2020
	Salaries and benefits	Number of shares	Warrants & options	Salaries and benefits	Number of shares	Warrants & options
Marinó Örn Tryggvason, CEO	63,756	3,427	7,390	51,397	2,093	14,667
Sigurður Hannesson, Chairman of the Board and member of the Risk and Remuneration committees	17,461	8,550	0	11,673	8,550	0
Guðmundur Þórðarson, Deputy Chairman of the Board and chairperson of the Risk committee	10,002	66,750	0	8,299	133,500	0
Guðjón Karl Reynisson, Board member and chairperson of the Remuneration committee	9,379	10,411	0	8,472	10,411	0
Helga Kristín Auðunsdóttir, Board member and member of the Audit committee	8,916	0	0	0	0	0
Ingunn Svala Leifsdóttir, Board member and chairperson of the Audit committee	3,159	0	0	0	0	0
Hrönn Sveinsdóttir, member of the Audit committe and former Board member	4,759	0	0	8,299	500	0
Inga Björg Hjaltadóttir, member of the Audit committe and former Board member	5,579	0	0	10,163	0	0
Kristín Friðgeirsdóttir, former Board member and former member of the Audit committee	1,229	0	0	0	0	0
Albert Þór Jónsson, former alternate Board member	489	0	0	489	0	0
Kristín Pétursdóttir, former Board member and former member of the Risk and Remuneration committees	0	0	0	3,968	0	0
Kristín Guðmundsdóttir, former alternate Board member and former member of the Risk and Audit committees	0	0	0	1,755	0	0
Managing Directors (2021: 7 (on average: 6.75), 2020: 6 (on average: 6))	380,996	47,971	29,564	283,518	31,804	73,333
Total	505,725	137,108	36,954	388,032	186,858	88,000

Salaries and benefits are substantially all short-term employee benefits. Salaries and benefits paid to members of the Board of Directors include compensation for their participation in Board committees.

The CEO and the managing directors received performance based payments in 2021. Following the merger with TM and Lykill in 2021, the number of managing directors of the Bank increased by one, and as a result the salaries and benefits figures for managing directors for 2021 and 2020 are not directly comparable.

Figures for shares, share options and warrants are in thousands and include shares held by companies owned by or under the control of the respective parties as at 31 December 2021 and 31 December 2020. If the holdings are held indirectly through companies, then the pro rata ownership of the aforementioned persons has been included.

The Bank has defined the Deputy CEO and two Managing Directors as Key Employees, as defined in Act No. 161/2002 on Financial Undertakings. Furthermore the Bank has approved and published internal rules covering the qualification requirements, evaluation process and conduct of Key Employees, in accordance with requirements set forth by the Financial Supervisory Authority of the Central Bank.

The Bank has adopted a remuneration policy which covers three remuneration components, base pay, performance based incentive scheme and other benefits, including pension fund contributions. Further information about the remuneration policy is provided in notes 70-72.

13. Auditor's fees

Remuneration to the Group's auditors is specified as follows:

	2021	2020
Audit of annual accounts	83,724	67,009
Review of interim accounts	28,350	11,180
Other audit related services	14,934	3,436
Total	127,008	81,625
Thereof to the auditors of the Bank	71,249	50,320

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

14. Net impairment

	2021	2020
Net change in impairment of loans	124,089	(158,956)
Net change in impairment of other assets	(10,730)	(147,346)
Net change in impairment of loan commitments, guarantees and unused credit facilities	25,483	(11,166)
Total	138,842	(317,468)

15. Income tax

The Bank and some of its subsidiaries will not pay income tax on its profit for 2021 due to the fact that Group has a tax loss carry forward that offsets the calculated income tax. Following business combinations during the first half of 2021, the tax loss carry forward has increased considerably and as at 31 December it amounts to ISK 23 billion for the Group. A substantial part of the tax loss carry forward is utilisable until end of year 2028. Management is of the opinion that the Group's operations in the years to come will result in taxable results which will be offset with the tax loss carry forward. The Group has therefore recognised a part of the tax loss carry forward as a deferred tax asset in the consolidated statement of financial position. The deferred tax asset is reviewed at each reporting date. Refer to note 30 for more information on the deferred tax asset.

Income tax is recognised based on the tax rates and tax laws enacted during the current year, according to which the domestic corporate income tax rate was 20.0% (2020: 20.0%). Companies within the Group, which operate outside of Iceland, recognise income tax in accordance with the applicable tax laws in the country where they are resident.

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

Reconciliation of effective tax rate:

		2021		2020
Profit before tax		10,486,563		2,338,969
Income tax using the domestic corporation tax rate	20.0%	(2,097,313)	20.0%	(467,794)
Non-deductible expenses	0.1%	(7,395)	0.0%	(1,137)
Non-taxable income	(17.8%)	1,862,182	(12.6%)	293,712
Recognition of tax losses	(11.1%)	1,159,050	(10.8%)	252,325
Effects due to merger	6.0%	(632,952)	0.0%	0
Other changes	(0.6%)	64,062	2.1%	(48,830)
Effective income tax	(3.3%)	347,634	(1.2%)	28,277

Profit before tax amounts to ISK 10,487 million. Income tax amounts to ISK 348 million, resulting in an effective tax rate of -3.3%. This is substantially different from the Icelandic corporate tax rate of 20%, mainly due to non-taxable income from shares and revaluation of the deferred tax asset.

16. Special tax on financial activity

The special tax on financial activity is an additional income tax which becomes effective when the income tax base exceeds ISK 1,000 million. It is levied on the same entities as the tax on financial activity according to Act No. 90/2003. The tax rate is set at 6.0% (2020: 6.0%) and the tax is not a deductible expense for income tax purposes. The tax is presented separately in the consolidated income statement.

17. Special tax on financial institutions

According to Act No. 155/2010 on Special Tax on Financial Institutions, certain types of financial institutions, including banks, must pay annually a tax based on the carrying amount of their liabilities as determined for tax purposes in excess of ISK 50 billion at year-end. The tax rate is set at 0.145% (2020: 0.145%) and the tax is not a deductible expense for income tax purposes. The tax is presented separately in the consolidated income statement.

18. Earnings per share

The calculation of basic earnings per share is based on earnings attributable to shareholders and a weighted average number of shares outstanding during the year. The diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Bank has issued warrants and stock options that have a dilutive effect.

	2021	2020
Net earnings attributable to equity holders of the Bank	10,734,181	2,348,621
Weighted average number of outstanding shares	4,104,785	2,141,002
Adjustments for warrants and stock options	90,703	161,879
Total	4,195,488	2,302,882
Basic earnings per share (ISK)	2.62	1.10
Diluted earnings per share (ISK)	2.56	1.02

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

Statement of Financial Position

19. Cash and balances with Central Bank

Cash and balances with Central Bank are specified as follows:

	31.12.2021	31.12.2020
Deposits with Central Bank	16,611,434	21,379,857
Cash on hand	14,651	11,649
Balances with banks	16,093,533	3,405,876
Foreign treasury bills	2,564,841	1,739,281
Included in cash and cash equivalents	35,284,459	26,536,663
Restricted balances with Central Bank - average maintenance level	0	0
Restricted balances with Central Bank - fixed reserve requirement	1,235,491	952,636
Receivables from Central Bank	2,125,945	1,455,730
Total	38,645,894	28,945,030

The Bank holds mandatory reserve deposit accounts with the Central Bank of Iceland in compliance with the Central Bank's Rules on Minimum Reserve Requirements No. 585/2018. Under these rules the reserve requirement is divided into two parts: a fixed reserve requirement bearing no interest and an average maintenance level requirement bearing the same interest as that on deposit-taking institutions' current accounts with the Central Bank. The mandatory reserve deposit with the Central Bank and the receivables from the Central Bank are not available for the Group to use in its daily operations.

20. Fixed income securities

Fixed income securities are specified as follows:

Mandatorily measured at fair value through profit or loss	31.12.2021	31.12.2020
Listed government bonds and bonds with government guarantees	5,343,444	2,890,226
Listed bonds	8,492,751	1,412,239
Unlisted bonds	4,907,093	1,535,801
Measured at fair value through other comprehensive income		
Listed government bonds and bonds with government guarantees	18,127,222	18,962,079
Listed treasury bills	2,997,628	3,984,688
Listed bonds	178,512	0
Total	40,046,651	28,785,033

21. Shares and other variable income securities

Shares and other variable income securities are specified as follows:

Mandatorily measured at fair value through profit or loss	31.12.2021	31.12.2020
Listed shares	5,523,914	892,423
Unlisted shares	8,907,091	2,338,138
Unlisted unit shares in bond funds	3,824,181	1,448,126
Unlisted unit shares in other funds	4,428,108	394,143
Total	22,683,295	5,072,830

22. Securities used for hedging

Securities used for hedging are specified as follows:

	31.12.2021	31.12.2020
Listed government bonds and bonds with government guarantees	126,113	7,115,854
Listed bonds	1,699,621	2,147,393
Listed shares	18,745,871	9,890,103
Unlisted unit shares	1,514,091	466,891
Total	22,085,696	19,620,240

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

23. Loans to customers

The breakdown of the loan portfolio by individuals and corporates is specified as follows:

	Individuals		Corporates		Total	
31.12.2021	Gross carrying amount	Book value	Gross carrying amount	Book value	Gross carrying amount	Book value
Loans to customers at amortised cost	31,285,094	30,771,742	39,114,914	38,291,634	70,400,008	69,063,377
Loans to customers at FV through profit or loss	650,814	650,814	1,873,455	1,873,455	2,524,269	2,524,269
Total	31,935,908	31,422,557	40,988,369	40,165,089	72,924,277	71,587,646

	Individuals		Corporates		Total	
31.12.2020	Gross carrying amount	Book value	Gross carrying amount	Book value	Gross carrying amount	Book value
Loans to customers at amortised cost	5,015,213	4,992,943	22,100,559	21,586,179	27,115,772	26,579,121
Loans to customers at FV through profit or loss	608,034	608,034	2,135,817	2,135,817	2,743,851	2,743,851
Total	5,623,247	5,600,976	24,236,376	23,721,996	29,859,623	29,322,972

The Group presents finance lease receivables as part of loans to customers at amortised cost. As at 31 December 2021, the book value of finance lease receivables amounted to ISK 16,139 million. Finance leases became part of the Group's statement of financial position following the merger with Lykill during the year 2021. Reference is made to note 3 for further information on the merger.

24. Derivatives

Derivatives are specified as follows:

	Notional		Carrying value	
31.12.2021	**Assets**	**Liabilities**	**Assets**	**Liabilities**
Interest rate derivatives	14,353,716	13,087,145	1,799,162	0
Currency forwards	8,260,384	9,306,104	54,740	126,212
Bond and equity total return swaps	23,328,516	25,873,506	336,233	2,882,189
Equity options	453,594	0	544,081	0
Total	46,396,210	48,266,754	2,734,216	3,008,401

	Notional		Carrying value	
31.12.2020	**Assets**	**Liabilities**	**Assets**	**Liabilities**
Interest rate derivatives	3,176,798	3,102,368	74,429	0
Currency forwards	2,698,140	2,740,401	0	42,261
Bond and equity total return swaps	21,918,514	23,386,919	108,771	1,577,177
Equity options	130,343	3,860	206,470	130,909
Total	27,923,795	29,233,548	389,671	1,750,346

25. Group entities

The main subsidiaries held directly or indirectly by the Group are listed in the table below.

Entity	**Nature of operations**	**Domicile**	**Share 31.12.2021**	**Share 31.12.2020**
Aur app ehf.	Financial technology services	Iceland	100%	-
FÍ Fasteignafélag GP ehf.	Real estate fund management	Iceland	100%	100%
GAMMA Capital Management hf.	Fund management	Iceland	100%	100%
Kvika eignastýring hf.	Asset management	Iceland	100%	100%
M-Investments ehf.	Holding company	Iceland	100%	100%
Netgíró hf.	Consumer lending operations	Iceland	100%	20%
Rafklettur ehf.	Holding company	Iceland	100%	100%
TM líftryggingar hf.	Insurance services	Iceland	100%	-
TM tryggingar hf.	Insurance services	Iceland	100%	-
AC GP 3 ehf.	Fund management	Iceland	80%	80%
Kvika Securities ltd.	Business consultancy services	UK	100%	100%

During the first quarter of 2021, the Group acquired a number of new subsidiaries. Reference is made to note 3 for more information on the acquisitions.

Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

26. Investment in associates

a. Investment in associates is accounted for using the equity method and is specified as follows:

Entity	Nature of operations	Domicile	Share 31.12.2021	Share 31.12.2020
Kjölfesta GP ehf.	Holding company	Iceland	-	50%
Gláma fjárfestingar slhf.	Holding company	Iceland	24%	24%
Moberg d. o. o.	Digital solutions provider	Croatia	40%	-

The Group does not consider its associates material, neither individually nor as a group. During the second quarter of 2021, the Group sold all its shareholding in Kjölfesta GP ehf. During the fourth quarter of 2021 the Group acquired a 40% stake in Moberg d. o. o., a digital solutions provider.

b. Changes in investments in associates are specified as follows:

	31.12.2021	31.12.2020
Balance at the beginning of the year	42,240	776,490
Acquisition of shares in associates	67,000	0
Dividend received	(3,750)	(7,500)
Disposal of shares in associates	(10,924)	(719,323)
Share in (loss) profit of associates, net of income tax	(27,566)	(7,427)
Total	67,000	42,240

27. Investment properties

Investment properties are specified as follows:	31.12.2021	31.12.2020
Balance at the beginning of the year	1,016,905	1,016,553
Additions	0	352
Revaluation of investment properties	83,095	0
Total	1,100,000	1,016,905

In October 2017, the Group acquired investment properties through one of its subsidiaries, Rafklettur ehf. The intention is to either earn rental income or capital appreciation or both. The book value of investment properties is based on the most recent appraisal values by licensed real estate agents, current listing prices and/or recent transactions for comparable real estates or valuation models based on gross income multipliers. During 2021, the Group received rental income amounting to ISK 81 million (2020: ISK 77 million) and incurred direct operating expenses of ISK 13 million (2020: ISK 15 million).

28. Intangible assets

Intangible assets are specified as follows:

31.12.2021	Goodwill	Customer relationships	Brands	Software and other	Total
Balance as at 1 January 2021	2,943,881	0	0	618,740	3,562,621
Additions during the period	0	0	0	458,271	458,271
Additions through business combinations	21,314,091	2,391,991	2,439,788	2,017,629	28,163,498
Amortisation	0	(136,181)	(99,523)	(493,278)	(728,982)
Balance as at 31 December 2021	24,257,972	2,255,810	2,340,265	2,601,362	31,455,409
Gross carrying amount	24,257,972	2,391,991	2,439,788	3,270,240	32,359,991
Accumulated amortisation and impairment losses	0	(136,181)	(99,523)	(668,878)	(904,582)
Balance as at 31 December 2021	24,257,972	2,255,810	2,340,265	2,601,362	31,455,409

31.12.2020	Goodwill	Customer relationships	Brands	Software and other	Total
Balance as at 1 January 2020	2,943,881	0	0	339,375	3,283,256
Additions during the period	0	0	0	354,053	354,053
Amortisation	0	0	0	(74,688)	(74,688)
Balance as at 31 December 2020	2,943,881	0	0	618,740	3,562,621
Gross carrying amount	2,943,881	0	0	794,340	3,738,221
Accumulated amortisation and impairment losses	0	0	0	(175,600)	(175,600)
Balance as at 31 December 2020	2,943,881	0	0	618,740	3,562,621

Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

28. Intangible assets (cont.)

b. Impairment testing

Assets with indefinite useful life, such as goodwill, are not amortised but are subject to annual impairment testing as described in note 98. Goodwill is allocated to cash generating units ("CGUs") for the purpose of impairment testing. The allocation is made to those CGUs or groups of CGUs that are expected to benefit from the business combinations in which the goodwill arose. Goodwill has been allocated to three CGUs, Asset Management, Commercial Banking and Insurance. The goodwill allocated to Commerical Banking and Insurance, following business combinations during the year 2021, is a based on a preliminary estimate. The allocation will be finalised during the year 2022.

The goodwill impairment tests were performed at the end of 2021. Their results show that the recoverable values exceed the carrying values of goodwill. In addition to the base case testing, additional scenarios were tested where some key inputs had been stressed. In all scenarios tested the results show that there is sufficient headroom and that there are no triggers indicating that impairment is necessary.

The following table shows the key assumptions used in the estimation of the recoverable amount. The recoverable amounts are calculated by discounting the estimated future growth rate of the CGUs. The time value of money and price of uncertainty, calculated as the weighted average cost of capital ("WACC"), are based on external market information about market risk, interest rates and CGU specific elements like country risk.

31.12.2021	Future growth rate	Discount rate	Book value
Asset Management	3.5%	10.1%	2,943,881
Commercial Banking	3.5%	11.1%	13,013,764
Insurance	3.0%	11.2%	8,300,327
Total goodwill			24,257,972

31.12.2020	Future growth rate	Discount rate	Book value
Asset Management	3.5%	9.4%	2,943,881
Total goodwill			2,943,881

29. Operating lease assets

Operating lease assets are specified as follows:

	31.12.2021
Balance as at 1 January 2021	0
Additions through business combinations	1,784,025
Additions	233,914
Disposals	(319,763)
Depreciation	(239,555)
Balance as at 31 December 2021	1,458,621
Gross carrying amount	2,226,907
Accumulated depreciation	(768,286)
Balance as at 31 December 2021	1,458,621

There are no comparative figures as operating lease assets were part of business combinations during the period. Reference is made to note 3 for more information on business combinations.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

30. Deferred tax assets and liabilities

Deferred tax assets	3,177,763	835,816
Deferred tax liabilities	(899,942)	(236,186)
Net	2,277,821	599,630

The Group's deferred tax assets (liabilities) are attributable to the following items:

	31.12.2021	31.12.2020
Property and equipment	270,609	(56,575)
Intangible assets	(563,719)	0
Other items	(225,954)	(172,014)
Tax losses carried forward	2,796,884	828,219
Total	2,277,821	599,630

At year end 2021, tax losses carried forward amount to ISK 22.7 billion, and are set to expire as follows:

	Tax losses
Tax losses 2012, expiring in 2022	467,499
Tax losses 2013, expiring in 2023	1,511,014
Tax losses 2015, expiring in 2025	1,242,589
Tax losses 2017, expiring in 2027	453,436
Tax losses 2018, expiring in 2028	18,137,597
Tax losses 2020, expiring in 2030	909,209
Total	22,721,343

31. Other assets

Other assets are specified as follows:

	31.12.2021	31.12.2020
Accounts receivable	7,599,584	3,646,962
Unsettled transactions	984,264	630,192
Right of use asset and lease receivables	800,087	478,995
Investment where investment risk is borne by life-insurance policyholders	111,172	0
Receivables at fair value	30,202	327,210
Sundry assets	517,245	356,733
Total	10,042,553	5,440,092

Right of use asset and lease receivables are specified as follows:

	31.12.2021	31.12.2020
Right of use asset and lease receivables at the beginning of the year	478,995	622,415
Additions during the period	453,937	11,152
Additions through business combinations	301,665	0
Disposal	(175,404)	0
Indexation	37,716	18,023
Depreciation and lease receivable installment	(296,822)	(172,596)
Total	800,087	478,995

Right of use asset and lease receivables mostly consist of real estates for the Group's own use. The Group has entered into sublease contracts for parts of the real estates which it does not use for its operations.

32. Deposits

Deposits are specified as follows:

	31.12.2021	31.12.2020
Demand deposits	63,858,051	46,775,812
Time deposits	14,811,756	13,148,871
Total	78,669,807	59,924,683

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

33. Technical provision

Technical provision is specified as follows:

	31.12.2021
Claims provision	16,492,994
Premium provision	5,311,124
Risk margin	630,329
Technical provisions, total	22,434,447

The Group buys reinsurance primarily as excess of loss treaties to protect itself against extreme events, but certain lines are protected by quota share treaties.

Reinsurer's share:	
Claims provision	635,419
Premium provision	113,964
Reinsurer's share, total	749,383

Own technical provision:	
Claims provision	15,857,575
Premium provision	5,197,160
Risk margin	630,329
Own technical provision (net), total	21,685,065

The estimated claims provisions are reported less estimated salvage value of the assets that were damaged. The total salvage value at end of December 2021 is immaterial.
There are no comparative figures as the technical provision was a part of business combinations during the year. Reference is made to note 3 for more information on business combinations.

Development of claims provisions from 1.4.2021 to 31.12.2021:	**Total**	**Reinsurer's share**	**Own share**
Claims provisions at 1.4.2021	16,764,649	(1,173,928)	15,590,720
Paid claims in the period due to older accident years	(3,967,947)	310,640	(3,657,306)
Exchange rate change of claims provisions due to older accident years	4,150	0	4,150
Unwinding and interest rate change of claims provisions due to older accident years	(30,185)	0	(30,185)
Change in settlement cost allocation due to older accident years	(210,595)	0	(210,595)
Change in assessment of claims provisions due to older accident years	(66,201)	(114,159)	(180,360)
Change in Claims provisions for claims incurred in 2021	3,999,123	342,028	4,341,151
Claims provisions at 31.12.2021	16,492,994	(635,419)	15,857,575
Change in claims provisions due to insurance operations	(245,620)	538,510	292,890
Proportional change in assessment of claims for older accident years	(0.4%)	9.7%	(1.2%)

The positive development of own claims provision contributes to a decrease in combined ratio of 1.4%.

Development of premium provisions from 1.4.2021 to 31.12.2021:	**Total**	**Reinsurer's share**	**Own share**
Premium provisions at 1.4.2021	9,769,559	(522,428)	9,247,131
Exchange rate change of premium provisions	25,806	(258)	25,547
Change in the provision for unearned premiums	(4,484,240)	408,723	(4,075,518)
Premium provisions at end of year	5,311,124	(113,964)	5,197,160

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

33. Technical provision (cont.)

Unwinding, interest and exchange rate change from 1.4.2021 to 31.12.2021:	Total	Reinsurer's share	Own share
Unwinding and interest rate change of claims provisions due to older accident years	(30,185)	0	(30,185)
Exchange rate change of claims provisions	4,150	0	4,150
Change in the provision for unearned premiums	25,806	(258)	25,547
Total unwinding, interest and exchange rate change of technical provisions	(229)	(258)	(488)

34. Borrowings

Borrowings are specified as follows:

	31.12.2021	31.12.2020
Money market deposits	17,261,048	26,424,340
Total	17,261,048	26,424,340

Money market deposits typically have a principal of ISK 5-500 million and maturity between 1 day and 6 months and pay fixed interest rates.

The Bank has not had any defaults of principal, interest or other breaches with respect to its debt issued and other borrowed funds.

35. Issued bills

Issued bills are specified as follows:

	31.12.2021	31.12.2020
KVB 21 0322	0	598,488
KVB 21 0621	0	595,587
KVB 21 0921	0	809,534
Total	0	2,003,608

36. Issued bonds

Issued bonds are specified as follows:

Currency, nominal value	First issued	Maturity	Maturity type	Terms of interest	31.12.2021	31.12.2020
Unsecured bonds:						
KVB 20 01, ISK 5,000 million	2020	2023	At maturity	Floating, 1 month REIBOR + 0.85%	4,609,836	1,763,538
KVB 19 01, ISK 5,000 million	2019	2024	Amortizing	Floating, 1 month REIBOR + 1.50%	3,003,775	3,474,842
KVB 21 01, GBP 12 million	2021	2023	At maturity	Floating, 3 month LIBOR + 2.50%	2,117,105	0
KVB 21 02, ISK 5,400 million	2021	2027	At maturity	CPI-indexed, fixed 1.0%	5,589,138	0
Lykill 23 11, ISK 3,010 million	2020	2023	At maturity	Floating, 1 month REIBOR + 1.10%	2,575,197	0
KVIKA 24 1119, GBP 11,4 million	2021	2024	At maturity	Floating, 3 month LIBOR + 1.75%	2,007,693	0
KVIKA 24 1216 GB, ISK 4,500 mil.	2021	2024	At maturity	Floating, 3 month REIBOR + 0.90%	4,506,565	0
Asset backed bonds:						
Lykill 16 01, ISK 10,870 million	2016	2023	Amortizing	Floating, 1 month REIBOR + 1.10%	2,928,877	0
Lykill 26 05, ISK 5,130 million	2019	2026	Amortizing	CPI-indexed, fixed 3.30%	3,792,658	0
Lykill 24 06, ISK 1,570 million	2020	2024	Amortizing	Fixed, 2.80%	1,002,853	0
Lykill 23 09, ISK 1,000 million	2019	2023	Amortizing	Fixed, 5.20%	464,019	0
Total					32,597,716	5,238,381
Unlisted senior unsecured bonds, total					0	329,704
Total					32,597,716	5,568,085

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

37. Subordinated liabilities

a. Subordinated liabilities:

Currency, nominal value	First issued	Maturity	Maturity type	Terms of interest	31.12.2021	31.12.2020
KVB 15 01, ISK 1,000 million	2015	2025	At maturity	CPI-Indexed, fixed 7.50%	0	1,169,444
KVB 18 02, ISK 800 million	2018	2028	At maturity	CPI-Indexed, fixed 7.50%	960,156	907,781
TM 15 1, ISK 2,000 million	2015	2045	At maturity	CPI-Indexed, fixed 5.25%	2,411,610	0
Total					3,371,766	2,077,225

Following authorisation from the FME, the Group repaid KVB 15 01 on the interest payment date in August 2021.
At the interest payment date in the year 2023 for KVB 18 02, the Group has the right to repay the subordinated bond and on any subsequent interest payment dates until maturity.
At the interest payment date in May 2025 for TM 15 01, the annual interest rate increases from 5.25% p.a. to 6.25% p.a. At the interest payment date in May 2025 for TM 15 01, the Group has the right to repay the subordinated bond and on any subsequent interest payment dates until maturity.

Subordinated liabilities are financial liabilities in the form of subordinated capital which, in case of the Group's voluntary or compulsory winding-up, will not be repaid until after the claims of ordinary creditors have been met. In the calculation of the capital ratio, they are included within Tier 2 and are a part of the equity base. The amount eligible for Tier 2 capital treatment is amortised on a straight-line basis over the final 5 years to maturity or up to 20% a year. The Group may only retire subordinated liabilities with the permission of the FME.

b. Subordinated liabilities are specified as follows:

	31.12.2021	31.12.2020
Balance at the beginning of the year	2,077,225	1,999,530
Redemption of KVB 15 01	(1,258,799)	0
Additions through business combinations	2,358,610	0
Paid interest	(113,125)	(115,000)
Paid interests due to indexation	(14,763)	(9,922)
Accrued interests and indexation	322,618	202,617
Total	3,371,766	2,077,225

38. Short positions held for trading

Short positions held for trading are specified as follows:

	31.12.2021	31.12.2020
Listed government bonds and bonds with government guarantees	608,965	559,382
Listed bonds	714,665	961,165
Total	1,323,631	1,520,547

39. Short positions used for hedging

Short positions used for hedging are specified as follows:

	31.12.2021	31.12.2020
Listed government bonds and bonds with government guarantees	1,280,868	731,987
Total	1,280,868	731,987

40. Other liabilities

Other liabilities are specified as follows:

	31.12.2021	31.12.2020
Salaries and salary related expenses	1,481,030	490,576
Lease liability	1,041,121	477,691
Accounts payable and accrued expenses	974,515	324,385
Unsettled transactions	875,985	1,217,659
Withholding taxes	694,281	361,088
Contingent consideration	483,486	386,001
Special taxes on financial institutions and financial activities	170,753	97,664
Reinsurance liabilities	142,407	0
Technical provision for life-insurance policies where investment risk is borne by policyholders	111,172	0
Expected credit loss allowance for loan commitments, guarantees and unused credit facilities	6,720	31,371
Other liabilities	696,038	364,037
Total	6,677,507	3,750,472

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

40. Other liabilities (cont.)

Lease liability is specified as follows:

	31.12.2021	31.12.2020
Lease liability at the beginning of the year	477,691	616,521
Additions during the period	452,001	39,449
Additions through business combinations	373,413	0
Installment	(299,701)	(197,076)
Indexation	37,716	18,796
Total	1,041,121	477,691

41. Share capital

a. Share capital

The nominal value of shares issued by the Bank is ISK 1 per share. All currently issued shares have a nominal value of ISK 1 per share, and are fully paid. The holders of shares are entitled to receive dividends as approved by the general meeting and are entitled to one vote per nominal value of ISK 1 at shareholders' meetings. Reference is made to the Bank's Articles of Association for more information about the share capital.

	31.12.2021	31.12.2020
Share capital according to the Bank's Articles of Association	4,907,395	2,141,002
Nominal amount of treasury shares	117,256	0
Authorised but not issued shares	413,325	546,480

b. Changes made to the nominal amount of share capital

The Bank's share capital was increased by ISK 256,458,363 in nominal value during the year 2021 in order to serve the exercising of issued warrants. In addition to that, the share capital was increased by ISK 2,509,934,076 in nominal value in relation to the merger with TM hf. and Lykill fjármögnun hf.

c. Share capital increase authorisations

According to the Bank's Articles of Association dated 20 December 2021, the Board of Directors is authorised to increase the share capital of the Bank by up to ISK 100 million through subscription for new shares. This authorisation is based on temporary provision I to the Articles of Association and is valid until 15 March 2022.

Temporary provision II to the Articles of Association authorises the Board of Directors to issue warrants and increase the share capital accordingly. Pursuant to this temporary provision the Board of Directors is authorised to increase share capital by up to ISK 77 million to serve warrants issued under this provision. This authorisation is valid until 21 April 2026.

Temporary provision IV to the Articles of Association authorises the Board of Directors to issue warrants and increase the share capital accordingly. According to section A of temporary provision IV the Board of Directors is currently authorised to increase share capital by up to ISK 60 million to serve issued warrants. According to section B of temporary provision IV the Board of Directors is furthermore granted a conditioned authorisation to increase the share capital, currently by an additional amount of ISK 107 million to serve issued warrants. The authorisation under section B of temporary provision IV is directly linked to the Board of Directors' authorisation under section A of temporary provision I.

The aforementioned authorisation under section B of temporary provision IV currently stands at ISK 57 million. However, should the Board of Directors utilise its authorisation according to section A of temporary provision I and increase the Bank's share capital by ISK 100 million, the authorisation under section B of temporary provision IV will increase from ISK 57 million to ISK 107 million, as stipulated in the provision. The Board of Directors' authorisation under temporary provision IV to increase share capital thus currently totals ISK 117 million but can increase to ISK 167 million by the usage by the Board of Directors of its authorisation pursuant to section A of temporary provision I. This authorisation is valid until 31 December 2022.

Temporary provision IV to the Articles of Association authorises the Board of Directors to increase the share capital of the Bank in stages by up to ISK 70 million in nominal value, for the purposes of fulfilling stock option agreements in accordance with the Bank's stock option plan which has been approved by Iceland Revenue and Customs as provided for in Art. 10 of the Income Tax Act, No. 90/2003. This authorisation is valid until 31 December 2024.

A copy of the Bank's Articles of Association, including the temporary provisions, is available on the Bank's website, www.kvika.is, reference is made to them for more information.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

42. Warrants

The Bank has issued warrants for shares in the total nominal amount of ISK 138,758,320 as at 31 December 2021. The number of owners of these warrants is 60 and they purchased the warrants for a total consideration of ISK 56,468,129. The purchase price of the warrants was determined using market standard methodology and a valuation from an independent appraiser as applicable. Should the owners of the warrants exercise their warrants, the Bank is obliged to issue new shares and sell to the warrant owners at a predefined price, usually referred to as strike price. If all the warrants would be exercised, the Bank's share capital would increase to 5,046,153,256, and the newly issued shares would represent 2.7% of the Bank's total issued capital, post dilution.

Issue Date	Nominal amount	Purchase price of warrants	Annual increase of strike price	Strike price at expiry date	Exercise period
September 2017	23,000,019	7,148,756	7.5%	7.74	Sept. 2020 - Sept. 2022
September 2017	91,966,634	27,456,206	7.5%	7.74	Sept. 2021 - Sept. 2022
May 2018	1,166,667	505,167	7.5%	10.75	Dec. 2021 - Dec. 2022
April 2019	1,000,000	944,000	7.5%	15.36	Dec. 2020 - Dec. 2022
April 2019	16,125,000	15,222,000	7.5%	15.36	Dec. 2020 - Dec. 2022
August 2019	5,500,000	5,192,000	7.5%	15.36	Dec. 2021 - Dec. 2022
Total	138,758,320	56,468,129			

43. Solvency of a financial conglomerate

The FME has designated the Group as a financial conglomerate as defined in Article no. 3 of Act no. 61/2017 on Additional Supervision of Financial Conglomerates. As a result of this designation, the Group's capital adequacy is now calculated as the solvency ratio of a financial conglomerate. The Group furthermore calculates the consolidated capital adequacy ratio for entities not belonging to the insurance sector by excluding the insurance activities from calculation of risk weighted assets and capital base. The Group similarly calculates the solvency ratio of entities solely belonging to the insurance sector.

Solvency measures the Group's ability to take on setbacks, thus indicating its financial strength. The available capital and capital requirements of the Group is calculated as a financial conglomerate according to Articles 16, 17 and 18 of Act on Additional Supervision of Financial Conglomerates No. 61/2017. The Group's solvency ratio is 1.57, with a regulatory minimum requirement of 1.0.

Solvency ratio of the Group as a financial conglomerate is specified as follows:

	31.12.2021
Available capital	
Own Funds eligible for non insurance activities	32,496,219
Own Funds eligible for insurance activities	14,121,233
Total	46,617,452
Solvency requirement for insurance activities	
Solvency Capital Requirements (SCR)	9,986,019
Own funds requirement for non insurance activities	
Statutory minimum capital requirement (Pillar I)	7,680,858
Additional capital requirements (Pillar II)	6,816,762
Minimum capital requirement for non insurance activities	14,497,620
Additional capital protection buffers	5,280,590
Total	19,778,210
Solvency	46,617,452
Solvency requirement (SCR)	9,986,019
Own funds requirement for non insurance activities	19,778,210
Minimum solvency of financial conglomerate	29,764,229
Solvency ratio	1.57

There are no comparative figures as the Group has not previously been required to calculate the solvency ratio for as a financial conglomerate.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

44. Capital adequacy ratio (CAR)

The capital adequacy ratio of the Group, excluding entities which belong to the insurance sector, calculated in accordance with Article 84 of Act No. 161/2002 on Financial Undertakings, was 33.8%. The minimum requirement from the FME is 15.1%. The ratio is calculated as follows:

Own funds eligible for non insurance activities	31.12.2021	31.12.2020
Total equity	78,367,620	19,208,001
Expected dividends according to Dividend Policy	0	0
Capital eligible as CET1 Capital	78,367,620	19,208,001
Goodwill and intangibles	(25,564,998)	(3,562,621)
Shares in other financial institutions	(20,441,123)	(259,829)
Subordinated fixed income securities	0	(117,250)
Deferred tax asset	(3,177,763)	(835,816)
Common equity Tier 1 capital (CET 1)	29,183,736	14,432,485
Tier 2 capital	3,312,483	2,012,387
Deductions from Tier 2 capital	0	(227,952)
Total own funds	32,496,219	16,216,919
Risk weighted exposures		
Credit risk	70,135,184	40,070,248
Market risk	4,051,492	3,617,483
Operational risk	21,824,053	13,621,015
Total risk weighted exposures	96,010,729	57,308,746
Capital ratios		
Capital adequacy ratio (CAR)	33.8%	28.3%
CET1 ratio	30.4%	25.2%
Minimum Capital adequacy ratio requirement	15.1%	15.1%
Minimum Capital adequacy ratio requirement including supervisory buffers	20.6%	20.6%
Minimum CET 1 ratio requirement including supervisory buffers	14.0%	14.0%

The FME supervises the Bank on a consolidated basis and, as such, receives information on the capital adequacy of, and sets capital requirements for, the Bank as a whole. The Bank's regulatory capital calculations for credit risk and market risk are based on the standardised approach and the capital calculations for operational risk are based on the basic indicator approach.

Minimum capital requirement is based on the Bank's Internal Capital Adequacy Assessment Process (ICAAP) and is reviewed by the FME through the Supervisory Review and Evaluation Process (SREP). The Bank's minimum regulatory capital requirement, based on the SREP from 2019, is 15.1%. The FME has notified the Bank that a new SREP process will be conducted in 2022. The minimum regulatory capital requirement including the additional capital buffers is 20.6% as at 31 December 2021.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

45. Solvency of insurance activities

The Group calculates solvency capital and capital requirements for entities which belong to the insurance sector. The available capital and required capital is calulated in accordance with Articles 88 and 96 of the Act on Insurance Activity No. 100/2016. This brings the solvency ratio for entities which belong to the insurance sector to 1.41. Solvency capital requirements according to law is the minimum insurance companies have to meet.

	31.12.2021
Own funds eligible for insurance activities solvency	
Equity eligible for insurance activities	22,163,820
Goodwill and intangibles	(5,888,497)
Difference between net technical provision in the financial statements and solvency rules	350,979
Proposed dividend payment	(2,500,000)
Non-controlling interest	(5,069)
Total	14,121,233
Solvency requirement	
Life insurance risk	326,634
Health insurance risk	1,390,074
Non-life insurance risk	4,956,453
Market risk	7,478,337
Counterparty default risk	962,624
Multifaceted effects	(4,259,005)
Risk due to intangible assets	0
Base Solvency Capital Requirements (Basic SCR)	10,855,118
Operational risk	627,562
Adjustment for the loss-absorbing capacity of deferred taxes	(1,496,661)
Solvency Capital Requirements (SCR)	9,986,019
Solvency	14,121,233
Solvency requirement (SCR)	9,986,019
Solvency ratio	1.41
Eligible items to meet the minimum capital	14,121,233
Minimum required capital (MRC)	3,818,920
Minimum required capital ratio	3.70

There are no comparative figures as insurance services became a part of the Group's operations through business combinations during the year 2021. Reference is made to note 3 for more information on business combinations.

Notes to the Consolidated Financial Statements

Risk management

46. Risk management framework

a. Board of Directors

The Bank's Board of Directors is responsible for the Group's corporate governance, including the establishment and oversight of the Group's risk management framework and risk appetite setting. In that respect, the Board of Directors has set a policy on the Group's corporate governance. In order to ensure harmonized and good governance on a consolidated basis, the Bank's Board of Directors further sets out ownership policies for subsidiaries that are considered an important part of the Group's operations. According to the ownership policies, the Boards of Directors of the relevant subsidiaries shall always provide the Bank with all information necessary for it to carry out its supervisory role and the services that the Bank provides to the relevant subsidiaries. Further, as risk management must be co-ordinated on a group-wide basis, those subsidiaries, shall provide risk management with all necessary information to enable the Bank to be able to fulfil its obligations as parent company of the Group. The head of risk management and the Bank's compliance officer can request a direct audience with the Boards of Directors of those subsidiaries. Risk management policies are reviewed regularly to reflect changes in market conditions and the Group's activities. The Group, through training and management standards and procedures, continuously aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

b. Board of Directors sub-committees

The Bank's Board of Directors has established three sub-committees, the Risk Committee, Audit Committee and Remuneration Committee. In accordance with the Bank´s articles of association, three members have been appointed to each committee, thereof at least two Board members. It is not permitted to appoint employees of the Bank to any committee. Members shall have the necessary experience and knowledge for each committee´s tasks according to applicable laws and rules. Each committee has incorporated procedural rules which have been confirmed by the Board of Directors.

The Risk Committee is intended to perform a consultative and supervisory role for the Bank’s Board of Directors, including for the formation of the Bank’s risk policy and risk appetite. The Risk Committee supervises the arrangement and activity of risk management, credit risk, market risk, liquidity risk, operational risk, reputational risk and other risk as applicable.

The Audit Committee is intended to perform a consultative and supervisory role for the Bank’s Board of Directors, including to ensure the quality of the annual accounts and other financial information of the Bank and the independence of the Bank’s auditors. The Audit Committee monitors the work process for the preparation of financial statements, the functioning of internal controls as well as internal and external auditing.

The Remuneration Committee is intended to perform a consultative and supervisory role for the Bank’s Board of Directors in connection with the Bank’s remuneration and that they support the objectives and interests of the Bank.

c. CEO

The CEO is responsible for the effective implementation through the corporate governance structure and committees. The CEO has established three committees, which are responsible for developing and monitoring risk management policies in their specified areas.

d. Committees

The Bank operates three committees that are involved in risk management: an Asset and Liability Committee (ALCO), a Credit Committee and an Operations Committee.

ALCO supervises the management of the Bank's balance sheet, assets and liabilities. This involves determining the most efficient division between returns and risk and allocating funds to the Bank's business units.

The Credit Committee addresses matters regarding the Bank's loan activities and is responsible for and makes decisions on the investments and sale of unlisted assets, such as unlisted securities and financial instruments, shares in private limited companies and other companies, and as regards other divisions than Treasury and Market Making, the investment and sale of unit share certificates in funds for collective investment. The committee is responsible for the approval of larger loans and is the primary forum for the discussion of the Bank's credit rules, including credit limits for relevant divisions of the Bank.

The Operations Committee is responsible for supervision and implementation of the Bank's security and quality policies. The security policy mainly addresses data security and operational security in IT systems, physical security for the personnel and proper access controls and monitoring in the Bank's premises. The quality work is aimed at upholding proper quality in work processes, IT systems and services to support performance and profitability, lower operational risk and increase the customer experience.

e. Risk management

The purpose of the Bank's risk management unit is to identify, quantify, control and report on the risks that the Group is exposed to in its daily activities. The unit also participates in drafting the overall risk policy and has representatives on the ALCO committee, Credit committee and the Operations committee. The unit’s main activities include monitoring and managing credit risk, market risk, liquidity risk and operational risk. The Board of Directors sets the rules and guidelines regarding the Group's risk policy and the obligations of risk management and credit control. The division reports regularly on the Group’s positions and exposure to risk to the Board of Directors, the CEO and to the ALCO committee.

f. Compliance Officer

The compliance function is an independent function that operates under the CEO, and the appointment of the Compliance Officer and his deputy is confirmed by the Board. The compliance function monitors the Bank's compliance risk on a permanent basis and that the measures, policies and procedures that have been put in place so that the Bank complies with its obligations are adequate and effective. The Compliance Officer is also responsible for coordinating and monitoring the Bank's compliance with applicable anti-money laundering and terrorist financing laws and regulations.

Notes to the Consolidated Financial Statements

46. Risk management framework (cont.)

g. Internal Audit

Internal Audit is responsible for providing an objective opinion on the Group’s operations, as well as advice which aims to increase the Group’s value and to strengthen risk management and internal control. The Internal Audit’s main task, is to estimate whether adequate processes and systems are in place, and whether they are relevant and efficient. The Internal Auditor is recruited by the Board of Directors and is located accordingly in the hierarchy. Its operations cover all units of operations, including the subsidiaries TM tryggingar hf., TM líftryggingar hf., Kvika eignastýring hf., Gamma Capital Management hf. and Kvika Securities Ltd. According to the letter of appointment, the internal auditor has direct access to the Boards' of Directors of the Bank's subsidiaries.

47. Hedging

Securities held as a hedge against derivatives positions of customers make up a part of the Group's portfolio of assets. The Group hedges currency exposure between the Group's loan portfolio and debts to the extent possible, but does not apply hedge accounting.

48. Credit risk - overview

a. Definition

One of the Group's primary sources of risk is counterparty credit risk. Credit risk is defined as the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

b. Management

The risk management unit is responsible for managing and reporting on credit risk. The Group uses a variety of tools and processes to manage credit risk, including collaterals, hedges and loan portfolio management.

c. Credit approval process

The originating department prepares a proposal for each larger loan or credit line which is presented to the credit committee for approval. The proposal consists of a basic description of the client, the purpose of the loan, a simple credit assessment and arguments for or against granting the loan. The committee decides whether there is need for further credit assessment and on what terms the loan may be granted. For smaller loans the originating department optains a general credit approval from the credit committee with respect to the process, terms, credit limits and total amount of the specific lending type.

A more thorough credit assessment may be conducted if considered appropriate and can include an assessment of a borrower's fundamental credit strength as well as the value of any collateral. To assess the borrower's capacity to meet his or her obligations the committee can request stress test analysis of the borrower's cash flow or call for third party assessments.

d. Collateral

Securing loans with collateral is a traditional method to reduce credit risk. The Group uses different methods to reduce credit risk by obtaining collateral from customers where appropriate. Such collateral gives the Group right to the collateralised assets for current and future obligations incurred by the customer.

The Group places emphasis on pricing loans according to the value and quality of pledged collateral. The Group applies appropriate haircuts on all collateral in order to ensure proper risk mitigation. For all collateral in listed securities, the Group maintains the right to liquidate collateral in case its market value falls below a predefined limit.

To a very large extent the Group's loan portfolio consists of senior loans, most of which are highly collateralised.

e. Credit rating, control and provisioning

The risk management unit is responsible for credit rating and reviewing the loan portfolio. In case of any significant delay of payments or defaults the unit carefully analyses the underlying assets and loan documents and organizes the process of collection.

The Group monitors the value of collateral by listed securities on a real time basis, and takes prompt action when necessary.

f. Loan portfolio management

To ensure an effective diversification of the loan portfolio the board has set a limit framework defining maximum exposure as a ratio of the Group’s equity and/or the total size of the loan portfolio. These limits include limitation on joint exposure to associated clients, exposure to individual and associated industries, single regions and countries etc. It is the responsibility of risk management to monitor that these limits are not being violated and to report discrepancies to the credit committee.

g. Impairment

Provisioning for loan impairments is estimated on the basis of expected loss models assessing the portfolio as a whole as well as individual lending. Risk management suggest a level of provisioning for the portfolio, based on the expected loss assessment. Risk management reassess impairments in the event of collateral decay, delayed payments, indication of increased risk, or other early warning signs. Provisions require approval from the credit committee. Refer to note 89 for more information on the Group's impairment policy.

h. Derivatives

The Group offers derivative contracts in the form of swap contracts on highly liquid securities. On the day when the contract is entered into, the Group purchases the underlying security and hedges its exposure to price changes. Collateral is in the form of cash or listed, highly liquid securities. The risk management sets rules about the level of collateralisation and monitors the compliance to these rules. Contracts are closed if required levels of collateralisation are not met.

i. Securities used for hedging

The Group hedges itself for market risk of derivative contracts by purchasing the underlying securities at the commencement of the contract. Since the contracts require delivery of the underlying securities to the customer on the settlement day, the credit risk towards the issuer is immaterial.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

49. Maximum exposure to credit risk

The maximum exposure to credit risk for on-balance sheet and off-balance sheet items, before taking into account any collateral held or other credit enhancements, is specified as follows:

31.12.2021 On-balance sheet exposure	Public entities	Financial institutions	Corporate customers	Individuals	31.12.2021
Cash and balances with Central Bank	22,552,361	16,093,533			38,645,894
Fixed income securities	27,881,492	5,800,281	6,364,877		40,046,651
Loans to customers	14,708	150	40,150,231	31,422,557	71,587,646
Derivatives		2,131,645	595,510	7,061	2,734,216
Other assets	541,252	2,395,982	4,182,883	2,122,349	9,242,466
	50,989,813	26,421,592	51,293,502	33,551,966	162,256,873
Off-balance sheet exposure					
Loan commitments			2,819,754	333,034	3,152,788
Financial guarantee contracts			512,901		512,901
Maximum exposure to credit risk	50,989,813	26,421,592	54,626,156	33,885,000	165,922,562

31.12.2020 On-balance sheet exposure	Public entities	Financial institutions	Corporate customers	Individuals	31.12.2020
Cash and balances with Central Bank	25,539,154	3,405,876			28,945,030
Fixed income securities	26,040,694	1,685,377	1,058,961		28,785,033
Loans to customers			23,721,996	5,600,976	29,322,972
Derivatives		130,709	258,962		389,671
Other assets	364,393	2,105,031	2,491,673		4,961,097
	51,944,241	7,326,993	27,531,592	5,600,976	92,403,802
Off-balance sheet exposure					
Loan commitments			1,771,209	366,050	2,137,260
Financial guarantee contracts			1,245,885		1,245,885
Maximum exposure to credit risk	51,944,241	7,326,993	30,548,685	5,967,027	95,786,947

50. Credit quality of financial assets

The book value of financial assets which fall under the impairment requirements of IFRS 9 are presented net of expected credit losses ("ECL") in the statement of financial position. The ECL are recalculated for each asset on at least a quarterly basis. The assessment of ECL is based upon calculations being derived from models on PD, LGD and EAD. Furthermore, the assessment is based upon management's assumptions regarding the development of macroeconomic factors over the coming year. The assumptions for macroeconomic development are decided for three scenarios: a base case, an upside case and a downside case, including a probability weight for each scenario. The assumptions are used for calculations of the probability weighted ECLs. The amount of ECL to be recognized is dependent on the Group's definition of significant increase in credit risk, which controls the impairment stage each asset is allocated to. The factors that are used to measure significant increase in credit risk include comparison of changes in PD values, annualized lifetime PD values, days past due and watch list.

The COVID-19 pandemic had an impact on the Group's loan portfolio during the years 2020 and 2021. This is mainly reflected in the effect of macro-economic variables on the probability of default and has therefore a homogenous impact on the whole portfolio. All scenarios were negatively impacted when the pandemic started. The negative impact however reduced in 2021 while the weights of the negative outlook economic scenario slightly decreased. The negative outlook economic scenario now weighs 30% and the positive outlook only weighs 10% in the total outcome. However, the pandemic has not had a significant effect on asset value. Due to the fact that the loan portfolio is in general well secured, changes to loss given default are minimal, which offsets the negative effect of increased probability of default.

Economic measures by the Icelandic government softened and delayed the impact of the pandemic. This means that borrower defaults which would otherwise have occurred already, have been delayed and possibly avoided. Even though the public restrictions are planned to be fully lifted in coming weeks the local economy as well as the world economy is expected to be affected by the aftermath of the pandemic, which appears e.g. in goods shortage, high inflation rates and undesirable unemployment rates. This is accounted for in the expected credit loss approach mandated in IFRS 9, meaning the Group does not expect to incur further significant losses due to impairments and write offs as the pandemic unwinds, all other things being equal.

In general, the Group’s debtors have been able to adapt to the changes in the economic reality due to COVID-19.

Because the economic scenario driven changes in the probability of default has a significant and homogenous impact on all customers and as the adaptability of debtors varies, the Group has put a greater emphasis on expert review to counter the effect of the pandemic's amplification of the inherent homogeneity prediction error in the model, i.e. to better reflect the heterogeneity of the Group's debtors.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

50. Credit quality of financial assets (cont.)

The following table shows the macro economic values for the variables used in the expected credit loss model. The Group utilises an economic forecast which is aligned with requirements for the calculation of expected credit loss.

		Scenarios	
Model parameters 31.12.2021	**Base case**	**Upside**	**Downside**
Unemployment rate	4.3%	3.6%	5.0%
Inflation CPI index	5.7%	5.4%	5.8%
Assigned weight	60.0%	10.0%	30.0%

		Scenarios	
Model parameters 31.12.2020	**Base case**	**Upside**	**Downside**
GDP growth	-5.5%	-3.0%	-9.5%
Unemployment rate	10.0%	7.5%	11.0%
Assigned weight	50.0%	5.0%	45.0%

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

50. Credit quality of financial assets (cont.)

a. Breakdown of loans to customers by industry and information on collateral and other credit enhancements

The Group applies the same valuation methods to collateral held as other comparable assets held by the Group. For other types of assets the Group uses third party valuation where possible. Haircuts are applied to account for liquidity and other factors which may affect the collateral value of the asset or other credit enhancement.

					Allocated collateral										
31.12.2021	**Claim due to value**	**Impairment expected credit loss**	**Carrying amount**	**%**	**Total collateral**	**Deposits**	**Listed securities and liquid funds**	**Unlisted securities and other funds**	**Residential real estate**	**Commercial real estate**	**Automobiles**	**Industrial equipment**	**Guarantees**	**Other**	**Unsecured claim value**
Public entities	14,863	(155)	14,708	0.0%	12,094	0	0	0	0	0	7,109	0	0	4,985	3,578
Financial institutions	186	(35)	150	0.0%	947	0	0	0	0	0	947	0	0	0	0
Corporate															
Service activities	8,456,811	(247,535)	8,209,276	11.5%	15,651,650	14,947	174,157	4,014,414	0	357,702	7,981,939	1,901,548	0	1,206,943	938,771
Construction	7,917,387	(322,606)	7,594,781	10.6%	15,033,846	72,849	0	0	5,273,648	3,604,444	2,805,676	2,641,503	0	635,726	137,565
Activities of holding companies	6,139,170	(12,842)	6,126,328	8.6%	17,448,909	33,420	1,159	10,009,915	2,057,402	4,552,973	109,251	102,295	178,500	403,993	382,487
Real estate activities	5,672,433	(23,272)	5,649,161	7.9%	14,962,837	123,210	1,281,231	2,620,852	4,748,147	5,557,610	522,141	75,810	16,000	17,835	109,875
Activities of holding comp. - Securities	2,692,571	(330)	2,692,241	3.8%	7,278,984	192,983	6,781,355	304,646	0	0	0	0	0	0	10,337
Wholesale and Retail Trade	3,266,183	(39,934)	3,226,249	4.5%	5,808,339	428,926	0	680,000	0	483,601	2,153,630	1,050,763	0	1,011,419	523,089
Other	6,828,764	(176,570)	6,652,195	9.3%	12,894,412	5,652	450,718	1,427,675	212,449	3,071,002	1,981,879	2,249,651	194,500	3,300,888	3,253,774
Individual	31,935,908	(513,375)	31,422,557	43.9%	44,164,668	41,690	2,221,224	823,646	6,589,474	402,206	32,743,905	1,157,983	0	184,542	6,215,381
Total	72,924,277	(1,336,655)	71,587,646	100.0%	133,256,687	913,676	10,909,844	19,881,148	18,881,119	18,029,538	48,306,477	9,179,552	389,000	6,766,330	11,574,857

					Allocated collateral										
31.12.2020	**Claim due to value**	**Impairment expected credit loss**	**Carrying amount**	**%**	**Total collateral**	**Deposits**	**Listed securities and liquid funds**	**Unlisted securities and other funds**	**Residential real estate**	**Commercial real estate**	**Automobiles**	**Industrial equipment**	**Guarantees**	**Other**	**Unsecured claim value**
Financial institutions	0	0	0	0.0%	0	0	0	0	0	0	0	0	0	0	0
Corporate															
Activities of holding companies	5,028,991	(91,502)	4,937,489	16.8%	14,109,569	9,899	168,644	9,471,872	734,690	3,282,905	0	0	441,560	0	128,644
Construction	5,778,115	(212,899)	5,565,216	19.0%	9,133,191	37	0	0	4,035,845	5,057,309	0	0	0	40,000	81,946
Financial activities	1,717,763	(50,193)	1,667,570	5.7%	744,727	90,343	81,632	228,239	32	0	0	0	0	344,480	1,228,197
Real estate activities	3,669,211	(39,552)	3,629,659	12.4%	8,110,745	3,711	145,905	1,626,221	2,486,304	3,821,735	0	0	26,750	120	234,779
Activities of holding compa. - Securities	2,997,582	(2,355)	2,995,226	10.2%	10,623,797	280,488	9,440,256	903,054	0	0	0	0	0	0	10,952
Service activities	2,012,081	(33,463)	1,978,618	6.7%	5,078,184	136,242	42,470	3,979,506	0	365,769	0	0	0	554,197	76,211
Other	3,032,633	(84,414)	2,948,219	10.1%	8,707,910	29,267	36,825	2,597,023	385,150	2,268,093	0	0	67,500	3,324,053	150,248
Individual	5,623,247	(22,271)	5,600,976	19.1%	9,747,097	24,298	2,842,506	33,032	6,688,262	82,000	0	0	0	77,000	308,698
Total	29,859,623	(536,650)	29,322,972	100.0%	66,255,220	574,284	12,758,237	18,838,945	14,330,282	14,877,811	0	0	535,810	4,339,851	2,219,674

Collatarel value is shown as the market- or accounting value of collateral allocated to exposures. Other collateral includes financial claims, inventories and receivables. For larger unsecured claim values, the Bank is in general covered by covenants in the loan agreement, e.g. with a negative pledge or other ring fencing.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

50. Credit quality of financial assets (cont.)

b. Credit quality of financial assets by credit quality band

The following tables show financial assets subject to the impairment requirements of IFRS 9 broken down by credit quality bands where band i denotes the lowest and iv the highest credit risk. Assets serviced by debtors already recognised as being in default by the rating agency are shown outside credit quality bands. Assets measured at fair value through profit or loss are not subject to the impairment requirements of IFRS 9 but are nevertheless included in the tables in order to give a more complete picture of the credit quality of loans to customers and reconcile the tables to the carrying amount on the balance sheet. Exposures which are non-rated relate to Legal Entities not rated by rating agency or Individuals where individual rating has not been obtained. Probability of default for these exposures is based on average probability for similar exposures and is furthermore individually assessed by credit specialists.

31.12.2021

Loans to customers:	**Stage 1**	**Stage 2**	**Stage 3**	**FVTPL**	**Total**
Credit quality band I	47,608,198	527,551	5,254	995,247	49,136,251
Credit quality band II	6,501,676	649,356	408		7,151,440
Credit quality band III	2,726,307	3,561,501	4,480		6,292,288
Credit quality band IV	386,107	1,167,598	1,897		1,555,602
In default	62,259	269,872	1,959,308	127,217	2,418,657
Non-rated	3,748,503	1,003,618	216,115	1,401,804	6,370,040
Gross carrying amount	61,033,049	7,179,496	2,187,463	2,524,269	72,924,277
Expected credit loss	(211,083)	(293,663)	(831,885)		(1,336,631)
Book value	60,821,966	6,885,833	1,355,578	2,524,269	71,587,646

Loan commitments, guarantees and unused credit facilities:	**Stage 1**	**Stage 2**	**Stage 3**	**FVTPL**	**Total**
Credit quality band I	1,808,577	0			1,808,577
Credit quality band II	87,689	0			87,689
Credit quality band III	1,029,809	1,000	10		1,030,819
Credit quality band IV	44,741	134,415			179,156
In default	1,000		2,636		3,636
Non-rated	470,753	828	7,535	76,694	555,811
Total off-balance sheet amount	3,442,569	136,243	10,182	76,694	3,665,688
Expected credit loss	(4,940)	(130)	(1,649)		(6,720)
Net off-balance sheet amount	3,437,629	136,113	8,533	76,694	3,658,969

31.12.2020

Loans to customers:	**Stage 1**	**Stage 2**	**Stage 3**	**FVTPL**	**Total**
Credit quality band I	14,899,136	436,960	20,849	1,022,457	16,379,402
Credit quality band II	3,859,240	389,944		233,126	4,482,310
Credit quality band III	1,161,890	555,021	229,771	17,999	1,964,680
Credit quality band IV	1,740,690	393,737	1,285		2,135,712
In default	28,455	2,676	552,915	862,234	1,446,280
Non-rated	2,824,445	14,311	4,448	608,034	3,451,238
Gross carrying amount	24,513,856	1,792,649	809,267	2,743,851	29,859,623
Expected credit loss	(306,203)	(72,222)	(158,226)		(536,650)
Book value	24,207,653	1,720,426	651,042	2,743,851	29,322,972

Loan commitments, guarantees and unused credit facilities:	**Stage 1**	**Stage 2**	**Stage 3**	**FVTPL**	**Total**
Credit quality band I	2,417,243	0	39,771		2,457,014
Credit quality band II	331,257	155,937			487,193
Credit quality band III	56,703	40,276	8,000		104,979
Credit quality band IV	1,089	4,709			5,798
In default	2,591		10,689	2,801	16,081
Non-rated	80,827	154,053		77,200	312,080
Total off-balance sheet amount	2,889,709	354,974	58,460	80,001	3,383,144
Expected credit loss	(14,830)	(13,631)	(2,911)		(31,371)
Net off-balance sheet amount	2,874,879	341,344	55,548	80,001	3,351,773

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

50. Credit quality of financial assets (cont.)

c. Breakdown of loans to customers into not past due and past due

31.12.2021	**Claim value**	**Expected credit loss**	**Carrying amount**
Not past due	69,602,189	(727,673)	68,874,516
Past due 1-30 days	1,362,406	(96,311)	1,266,095
Past due 31-60 days	797,031	(19,728)	777,303
Past due 61-90 days	76,257	(13,221)	63,036
Past due 91-180 days	209,085	(44,399)	164,687
Past due 181-360 days	627,918	(251,984)	375,935
Past due more than 360 days	249,390	(183,316)	66,074
Total	72,924,277	(1,336,631)	71,587,646

31.12.2020	**Claim value**	**Expected credit loss**	**Carrying amount**
Not past due	28,909,071	(442,622)	28,466,450
Past due 1-30 days	537,707	(9,705)	528,002
Past due 31-60 days	32,831	(71)	32,760
Past due 61-90 days	71,310	(2,416)	68,894
Past due 91-180 days	49,403	(2,443)	46,959
Past due 181-360 days	17,012	(15,472)	1,541
Past due more than 360 days	242,288	(63,922)	178,366
Total	29,859,623	(536,650)	29,322,972

d. Allowance for expected credit loss on loans to customers and loan commitments, guarantees and unused credit facilities

The following tables show changes in the expected credit loss allowance of loans to customers and for loan commitments, guarantees and unused credit facilities during the period.

31.12.2021

Expected credit loss allowance total

	Stage 1	**Stage 2**	**Stage 3**	**Total**
Transfers of financial assets:				
Balance as at 1 January 2021	321,032	85,853	161,137	568,022
Transfer to Stage 1 - (Initial recognition)	34,178	(29,997)	(4,181)	0
Transfer to Stage 2 - (significantly increased credit risk)	(47,041)	47,041		0
Transfer to Stage 3 - (credit impaired)	(40,441)		40,441	0
Net remeasurement of loss allowance	(96,561)	70,239	(5,768)	(32,090)
New financial assets, originated or purchased	191,888	161,773	764,301	1,117,962
Derecognitions and maturities	(147,031)	(41,115)	(42,547)	(230,693)
Write-offs			(79,850)	(79,850)
Balance as at 31 December 2021	216,023	293,794	833,534	1,343,351

Expected credit loss allowance for loans to customers

	Stage 1	**Stage 2**	**Stage 3**	**Total**
Transfers of financial assets:				
Balance as at 1 January 2021	306,203	72,222	158,226	536,650
Transfer to Stage 1 - (Initial recognition)	22,686	(18,946)	(3,740)	0
Transfer to Stage 2 - (significantly increased credit risk)	(47,022)	47,022		0
Transfer to Stage 3 - (credit impaired)	(40,439)		40,439	0
Net remeasurement of loss allowance	(80,142)	70,417	(6,232)	(15,958)
New financial assets, originated or purchased	190,271	161,773	763,828	1,115,872
Derecognitions and maturities	(140,474)	(38,824)	(40,786)	(220,084)
Write-offs			(79,850)	(79,850)
Balance as at 31 December 2021	211,083	293,663	831,885	1,336,631

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

50. Credit quality of financial assets (cont.)

Expected credit loss allowance for loan commitments, guarantees and unused credit facilities

	Stage 1	Stage 2	Stage 3	Total
Transfers of financial assets:				
Balance as at 1 January 2021	14,830	13,631	2,911	31,371
Transfer to Stage 1 - (Initial recognition)	11,492	(11,051)	(440)	0
Transfer to Stage 2 - (significantly increased credit risk)	(19)	19		0
Transfer to Stage 3 - (credit impaired)	(3)		3	0
Net remeasurement of loss allowance	(16,419)	(178)	464	(16,132)
New financial assets, originated or purchased	1,617		472	2,089
Derecognitions and maturities	(6,558)	(2,291)	(1,761)	(10,609)
Balance as at 31 December 2021	4,940	130	1,649	6,720

31.12.2020

Expected credit loss allowance total

	Stage 1	Stage 2	Stage 3	Total
Transfers of financial assets:				
Balance as at 1 January 2020	182,670	102,932	132,170	417,771
Transfer to Stage 1 - (Initial recognition)	12,232	(10,477)	(1,755)	0
Transfer to Stage 2 - (significantly increased credit risk)	(16,824)	16,824		0
Transfer to Stage 3 - (credit impaired)	(6,259)	(6,410)	12,669	0
Net remeasurement of loss allowance	(17,377)	16,843	2,269	1,735
New financial assets, originated or purchased	244,086	46,596	33,894	324,576
Derecognitions and maturities	(77,496)	(80,455)	(8,110)	(166,061)
Write-offs			(10,000)	(10,000)
Balance as at 31 December 2020	321,032	85,853	161,137	568,022

Expected credit loss allowance for loans to customers

	Stage 1	Stage 2	Stage 3	Total
Transfers of financial assets:				
Balance as at 1 January 2020	167,078	100,185	129,416	396,679
Transfer to Stage 1 - (Initial recognition)	11,599	(10,020)	(1,579)	0
Transfer to Stage 2 - (significantly increased credit risk)	(11,256)	11,256		0
Transfer to Stage 3 - (credit impaired)	(5,965)	(6,410)	12,375	0
Net remeasurement of loss allowance	(17,562)	10,944	1,598	(5,019)
New financial assets, originated or purchased	234,351	44,753	32,486	311,589
Derecognitions and maturities	(72,043)	(78,486)	(6,071)	(156,599)
Write-offs			(10,000)	(10,000)
Balance as at 31 December 2020	306,203	72,222	158,226	536,650

Expected credit loss allowance for loan commitments, guarantees and unused credit facilities

	Stage 1	Stage 2	Stage 3	Total
Transfers of financial assets:				
Balance as at 1 January 2020	15,592	2,746	2,754	21,092
Transfer to Stage 1 - (Initial recognition)	633	(457)	(176)	0
Transfer to Stage 2 - (significantly increased credit risk)	(5,568)	5,568		0
Transfer to Stage 3 - (credit impaired)	(294)		294	0
Net remeasurement of loss allowance	186	5,899	670	6,755
New financial assets, originated or purchased	9,735	1,844	1,408	12,987
Derecognitions and maturities	(5,453)	(1,970)	(2,039)	(9,462)
Balance as at 31 December 2020	14,830	13,631	2,911	31,371

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

51. Loan-to-value

a. General

The loan-to-value ratio (LTV) is the ratio of the gross amount of the loan to the value of the collateral, if any. The general creditworthiness of a customer is viewed as the most reliable indicator of credit quality of a loan. Besides collateral included in the LTV ratios the Group uses other risk mitigation measures, such as guarantees, negative pledge, cross-collateral and collateralization of non-quantifiable assets.

b. Breakdown

The breakdown of loans to customers by LTV is specified as follows:

	31.12.2021	%	31.12.2020	%
Less than 50%	20,182,991	28.2%	12,579,973	42.9%
51-70%	18,411,393	25.7%	7,450,150	25.4%
71-90%	18,175,877	25.4%	3,101,307	10.6%
91-100%	3,063,469	4.3%	1,870,641	6.4%
100-125%	2,706,342	3.8%	48,476	0.2%
125-200%	201,953	0.3%	13,996	0.0%
Greater than 200%	670,667	0.9%	198,961	0.7%
No or negligible collateral:				
Purchased short-term retail claims	0	0.0%	2,027,605	6.9%
Other loans with no collateral	8,174,954	11.4%	2,031,863	6.9%
Total	71,587,646	100.0%	29,322,972	100.0%

52. Collateral against exposures to derivatives

The Group applies the same valuation methods to collateral held as other comparable assets held by the Group. Haircuts are applied to account for liquidity and other factors which may affect the collateral value of the asset.

	Deposits	Fixed income securities	Variable income securities	Real estate	Other fixed assets	Other	31.12.2021
Financial institutions	2,201,519	118,222	737,598				3,057,340
Corporate customers	715,724	19,382	907,511				1,642,617
Individuals	79,757	5,307	22,613				107,678
Total	2,997,001	142,911	1,667,723	0	0	0	4,807,635

	Deposits	Fixed income securities	Variable income securities	Real estate	Other fixed assets	Other	31.12.2020
Financial institutions	587,322	413,397					1,000,720
Corporate customers	176,327	121,815	640,596				938,738
Individuals	20,164	26,064	24,598				70,825
Total	783,813	561,276	665,194	0	0	0	2,010,283

Amounts have been adjusted to exclude collateral in excess of claim value, i.e. overcollateralisation.

53. Large exposures

In accordance with regulation no. 233/2017 on Prudential Requirements, total exposure towards a customer is classified as a large exposure if it exceeds 10% of the financial institution's Tier 1 capital (see note 44).

According to the regulation a single exposure, net of risk adjusted mitigation, cannot exceed 25% of the eligible Tier 1 capital. Single large exposures net of risk adjusted mitigation take into account the effects of collateral and other credit enhancements held by the financial institution, and other credit enhancements, in accordance with regulation no. 233/2017.

		31.12.2021		31.12.2020
Large exposures before risk adjusted mitigation	**Number**	**Amount**	**Number**	**Amount**
10-20% of capital base	2	8,732,707	0	0
20-25% of capital base	0	0	0	0
Exceeding 25% of capital base	0	0	0	0
Total	2	8,732,707	0	0
Thereof nostro accounts with foreign banks with a rating of investment grade or higher	2	8,732,707	0	0
Large exposures net of risk adjusted mitigation	2	8,732,707	0	0

No single large exposure net of risk adjusted mitigation exceeds 25% of capital base in accordance with the regulation no. 233/2017.

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Notes to the Consolidated Financial Statements

54. Insurance risk

As discussed in note 3, the Group acquired TM hf., an insurance company, during the first quarter of 2021. As a result of the acquisition, insurance risk is now a key risk which is actively monitored and measured by the Group's risk management division.

Insurance risk is a risk, other than financial risk, transferred from the holder of a contract to the issuer, such as financial loss due to accident, damage, theft, illness, disability or death. The Group compensates certain losses of customers against payment of a premium. A premium is paid at the beginning of the period covered by the insurance protection, the loss is incurred at a later point and settlement can then take some time, which varies based on the nature of the loss and the circumstances. Premium and estimated indemnity must be secured until payment takes place. Premiums must cover all claim cost, operating cost and reasonable mark-up taking into account yield. Specific risk arises as premiums are predetermined but the service is provided at a later point and is undefined at the beginning. This risk is specific for insurance operation and is defined as insurance risk.

Insurance risk is divided into two groups, premium risk and risk of claims outstanding in order to segregate between incurred and future claims.

Premium risk is the risk that future claims, in addition to related expenses, will be higher than anticipated at the time premiums for current insurance contracts were decided and the insurance cover the Group guaranteed thus underestimated. The risk consists in main respect in that the frequency or severity of claims and benefits are greater than estimated. This may be caused by inaccurate assumptions but also temporary effect from individual large claims. Nature of claims can be different from expected or have changed due to developments in society.

The Group monitors frequency of claims and distribution of single claims amounts within each category and responds to changes in pricing or product development if necessary. Premium risk is reduced by distributing the risk between insurance groups and by making reinsurance contracts for significant claims.

Outstanding claim risk is the risk that existing but not settled claims will be higher than estimated. Negative development can be caused by the fact that notified but unsettled claims have been undervalued and that claims not yet notified prove to be higher or more than estimated. This applies to both actual indemnification to the claimant and related expenses, such as clearance of ruins and cost of expert services in evaluations and settlements of claims.

The Group's outstanding claims is based on the evaluation of final cost of all unsettled claims. Significant uncertainty in that evaluation is inevitable. A period of time can pass from when a loss incurs until a claim is notified to the Group as the loss had not been discovered or the claimant was not aware of its right to compensation. Though a damage is known its consequences can remain unknown until later, it is not completely clear what is damaged in an asset damage until repair has begun and permanent consequences of accidents are unclear until long after the accident. Consequences of a damage may at first have been under or overestimated. There are also some cases where notified claims do not end in compensation by the Group, either because no loss was incurred, the claim did not fall under the terms of the insurance contract or that the claim did not reach the minimum own risk of the insured.

Own technical provision classified to line of insurance operations	**31.12.2021**
Fire and other damage to property insurance	2,105,022
Marine, aviation and transport insurance	847,645
Motor vehicle liability insurance	10,639,438
Other motor insurance	1,199,425
General liability, credit and suretyship insurance	2,701,425
Income Protection Insurance	1,058,845
Workers' compensation insurance	2,717,221
Medical Expense Insurance	6,104
Life insurance	360,402
Sold reinsurances	49,539
Own technical provision total	21,685,065

There are no comparative figures as insurance services became a part of the Group's operations through business combinations during the year 2021. Reference is made to note 3 for more information on business combinations.

55. Liquidity risk

a. Definition

Liquidity risk is the risk that the Group will encounter difficulty in meeting contractual payment obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. This risk mainly arises from mismatches in the timing of cash flows. The Group has internal rules that require certain matching of the maturities of assets and liabilities. Furthermore, to ensure the ability to meet liquidity needs, the Group maintains a stock of highly liquid unencumbered assets, e.g. cash, treasury bills and treasury bonds.

b. Management

Liquidity is managed by treasury and monitored by risk management. Liquidity position is reported to the ALCO committee. The Central Bank of Iceland sets minimum requirements for the liquidity coverage ratio (LCR) and the net stable funding ratio (NSFR). The minimum 30 day LCR regulatory requirement is 100% for both LCR total and LCR in foreign currencies. For LCR in ISK the minimum requirement is 30% as of 1 January 2020, 40% as of 1 January 2022 and 50% as of 1 January 2023. The minimum regulatory requirement for NSFR total is 100%.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

55. Liquidity risk (cont.)

b. Management (cont.)

The FME has designated the Group as a financial conglomerate. LCR is not calculated for a financial conglomerate, instead the Group calculates LCR based on the consolidated statement of financial position excluding the insurance operations of TM tryggingar hf. The Group was in compliance with internal and external liquidity requirements throughout the years 2021 and 2020.

	31.12.2021	31.12.2020
NSFR total	130%	159%

	31.12.2021	31.12.2020
LCR total	290%	266%
LCR in ISK	182%	265%
LCR in foreign currencies	219%	179%

c. Maturity analysis of financial assets and financial liabilities

31.12.2021 **Financial assets by type**	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Gross inflow/ (outflow)**	**Carrying amount**
Non-derivative assets							
Cash and balances with Central Bank	36,735,621	1,173,420	738,000			38,647,041	38,645,894
Fixed income securities	18,391,127	3,115,221	10,453,037	7,127,439	959,827	40,046,651	40,046,651
Shares and other variable income securities	15,278,393	2,948,677	4,230,156	226,069		22,683,295	22,683,295
Securities used for hedging	22,085,696					22,085,696	22,085,696
Loans to customers	5,009,571	5,730,923	27,168,009	39,368,877	5,872,898	83,150,279	71,587,646
Reinsurance assets	66,660	78,751	240,729	351,169	12,073	749,383	749,383
Other assets	3,546,888	4,508,101	1,830,359	157,206		10,042,553	10,042,553
	101,113,957	17,555,093	44,660,289	47,230,760	6,844,798	217,404,897	205,841,117
Derivative assets							
Inflow	8,495,539	1,340,505	3,001,987	8,957,388		21,795,420	
Outflow	(8,151,488)	(1,350,233)	(1,162,801)	(8,648,207)		(19,312,729)	
	344,052	(9,728)	1,839,186	309,181	0	2,482,690	2,734,216

Financial liabilities by type	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Gross inflow/ (outflow)**	**Carrying amount**
Non-derivative liabilities							
Deposits	(65,385,245)	(6,620,835)	(5,409,417)	(1,369,701)	(58,840)	(78,844,038)	78,669,807
Technical provision	(2,569,878)	(2,291,356)	(7,004,287)	(10,217,641)	(351,284)	(22,434,447)	22,434,447
Borrowings	(2,975,625)	(9,783,251)	(2,955,884)	(1,619,785)		(17,334,545)	17,261,048
Issued bills						0	0
Issued bonds	(264,524)	(989,290)	(3,810,121)	(25,064,483)	(5,611,362)	(35,739,780)	32,597,716
Subordinated liabilities			(194,143)	(813,627)	(6,228,579)	(7,236,350)	3,371,766
Short positions held for trading	(1,323,631)					(1,323,631)	1,323,631
Short positions used for hedging	(1,280,868)					(1,280,868)	1,280,868
Other liabilities	(1,773,454)	(2,538,572)	(741,858)	(1,511,952)	(111,672)	(6,677,507)	6,677,507
	(75,573,225)	(22,223,304)	(20,115,711)	(40,597,189)	(12,361,737)	(170,871,167)	163,616,790
Derivative liabilities							
Inflow	12,935,075	3,788,518		3,167,699		19,891,293	
Outflow	(15,073,201)	(4,594,592)		(3,233,330)		(22,901,123)	
	(2,138,125)	(806,074)	0	(65,631)	0	(3,009,830)	3,008,401
Unrecognised financial items							
Loan commitments							
Inflow	265,888	621,243	1,958,828	369,626		3,215,585	
Outflow	(3,152,788)					(3,152,788)	
Financial guarantee contracts							
Inflow		49,798	87,475	316,571	59,057	512,901	
Outflow	(512,901)					(512,901)	
	(3,399,800)	671,041	2,046,302	686,196	59,057	62,797	
Summary							
Non-derivative assets	101,113,957	17,555,093	44,660,289	47,230,760	6,844,798	217,404,897	
Derivative assets	344,052	(9,728)	1,839,186	309,181		2,482,690	
Non-derivative liabilities	(75,573,225)	(22,223,304)	(20,115,711)	(40,597,189)	(12,361,737)	(170,871,167)	
Derivative liabilities	(2,138,125)	(806,074)		(65,631)		(3,009,830)	
Net assets (liabilities) excluding unrecognised items	23,746,658	(5,484,014)	26,383,765	6,877,120	(5,516,939)	46,006,589	
Net unrecognised items	(3,399,800)	671,041	2,046,302	686,196	59,057	62,797	
Net assets (liabilities)	20,346,858	(4,812,972)	28,430,067	7,563,316	(5,457,882)	46,069,386	

Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

55. Liquidity risk (cont.)

31.12.2020 **Financial assets by type**	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Gross inflow/ (outflow)**	**Carrying amount**
Non-derivative assets							
Cash and balances with Central Bank	28,059,712	890,470				28,950,182	28,945,030
Fixed income securities	5,600,838	117,250	19,802,625	3,264,320		28,785,033	28,785,033
Shares and other variable income securities	1,464,966		3,607,863			5,072,830	5,072,830
Securities used for hedging	19,620,240					19,620,240	19,620,240
Loans to customers	2,017,619	3,403,967	16,159,918	8,581,843	3,504,320	33,667,667	29,322,972
Other assets	1,474,195	1,027,270	715,537	2,223,090		5,440,092	5,440,092
	58,237,570	5,438,957	40,285,943	14,069,253	3,504,320	121,536,043	117,186,196
Derivative assets							
Inflow	1,056,236	778,870		76,798		1,911,904	
Outflow	(979,810)	(746,525)		(2,368)		(1,728,703)	
	76,426	32,345	0	74,429	0	183,200	389,671

Financial liabilities by type	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Gross inflow/ (outflow)**	**Carrying amount**
Non-derivative liabilities							
Deposits	(48,383,678)	(5,944,107)	(3,993,981)	(1,664,675)	(47,976)	(60,034,418)	59,924,683
Borrowings	(6,789,566)	(9,747,775)	(10,001,623)			(26,538,964)	26,424,340
Issued bills		(600,000)	(1,420,000)			(2,020,000)	2,003,608
Issued bonds	(82,395)	(164,111)	(1,073,859)	(4,529,066)		(5,849,431)	5,568,085
Subordinated liabilities			(150,788)	(1,741,109)	(1,060,762)	(2,952,658)	2,077,225
Short positions held for trading	(1,520,547)					(1,520,547)	1,520,547
Short positions used for hedging	(731,987)					(731,987)	731,987
Other liabilities	(923,315)	(1,317,466)	(1,098,735)	(410,956)		(3,750,472)	3,750,472
	(58,431,489)	(17,773,459)	(17,738,985)	(8,345,806)	(1,108,738)	(103,398,478)	102,000,947
Derivative liabilities							
Inflow	17,286,909	2,315,614	390,250			19,992,773	
Outflow	(18,111,337)	(3,092,010)	(411,675)			(21,615,021)	
	(824,428)	(776,395)	(21,425)	0	0	(1,622,248)	1,750,346
Unrecognised financial items by type							
Loan commitments							
Inflow	107,445	264,951	1,108,702	733,780		2,214,878	
Outflow	(2,137,260)					(2,137,260)	
Financial guarantee contracts							
Inflow	711,288	114,000	297,639	63,901	59,057	1,245,885	
Outflow	(1,245,885)					(1,245,885)	
	(2,564,411)	378,951	1,406,341	797,681	59,057	77,619	
Summary							
Non-derivative assets	58,237,570	5,438,957	40,285,943	14,069,253	3,504,320	121,536,043	
Derivative assets	76,426	32,345		74,429		183,200	
Non-derivative liabilities	(58,431,489)	(17,773,459)	(17,738,985)	(8,345,806)	(1,108,738)	(103,398,478)	
Derivative liabilities	(824,428)	(776,395)	(21,425)			(1,622,248)	
Net assets (liabilities) excluding unrecognised items	(941,921)	(13,078,552)	22,525,533	5,797,876	2,395,581	16,698,518	
Net unrecognised items	(2,564,411)	378,951	1,406,341	797,681	59,057	77,619	
Net assets (liabilities)	(3,506,331)	(12,699,601)	23,931,874	6,595,557	2,454,639	16,776,137	

Maturity analysis of financial assets and financial liabilities is based on contractual cash flows or, in the case of held for trading securities, expected cash flows. If an amount receivable or payable is not fixed, e.g. for inflation indexed assets and liabilities, the maturity analysis uses estimates based on current conditions.

Cash flows relating to unrecognised balance sheet items (unused loan commitments and financial guarantee contracts) are presented separately from financial assets and financial liabilities. Both contractual outflows and inflows are shown, to fully reflect the nature of these items.

It should be noted that the Group's expected cash flows sometimes vary considerably from the contractual cash flows, most significantly in that demand deposits from customers are expected to remain stable or increase in the long term. In this case the presentation used reflects the worst case scenario from the Group's perspective. Furthermore, the analysis does not consider any measures that could be taken to convert long-term assets to cash through sale.

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Notes to the Consolidated Financial Statements

56. Market risk

a. Definition

Market risk constitutes risk due to changes in the market prices of financial instruments and comprises interest rate risk, currency risk and other price risk. Notes 57-62 relate to market risk exposure.

b. Management

The Group has a strict policy on controlling market risk and to keep the exposure within set limits. The risk management unit monitors market risk limits on a daily basis and reports regularly to the ALCO committee and to the CEO.

57. Interest rate risk

a. Definition

The Group's exposure to interest rate risk is twofold. On the one hand, the Group has a proprietary portfolio of bonds, where market rates affect prices and any fluctuations are recognised in the income statement. On the other hand, the Group has mismatch in assets and liabilities with fixed interest terms. These include loans and swap contracts for securities on the asset side and borrowings and deposits on the liability side. This mismatch does not create an immediate effect on the income statement but nevertheless affects the Group's economic value.

Proprietary positions which are subject to interest rate risk fall under the scope of the Group's market risk management.

b. Management

The Group takes measures to minimise interest rate risk by matching the interest rate profile and duration of assets with the Group's liabilities as well as using derivative and non-derivative financial instruments to manage effectively the risk of an adverse impact on the Group's earnings.

58. Interest rate risk associated with trading portfolios

a. Breakdown

The breakdown of financial assets and liabilities in trading portfolios by the earlier of interest repricing time or maturity is specified as follows:

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	31.12.2021
Fixed income securities			91,531	894,288	1,446,062	2,431,880
Short positions - fixed income securities			(24,979)	(514,176)	(784,475)	(1,323,631)
Net imbalance	0	0	66,552	380,111	661,587	1,108,250

	Up to 1 month	1-3 months	3-12 months	1-5 years	Over 5 years	31.12.2020
Fixed income securities			995,943	2,512,237	193,801	3,701,981
Short positions - fixed income securities				(127,198)	(1,393,349)	(1,520,547)
Net imbalance	0	0	995,943	2,385,039	(1,199,548)	2,181,434

b. Sensitivity analysis

The Group performs monthly sensitivity analysis on financial assets and liabilities in trading portfolios that are subject to interest rate risk. The sensitivity analysis assumes a shift in the yield curves for all currencies. A parallel shift in yield curves would have the following impact on the Group's pre-tax profit and equity, assuming all other risk factors remain constant:

	Shift in basis points	31.12.2021 Downward	31.12.2021 Upward	31.12.2020 Downward	31.12.2020 Upward
Indexed	50	42,091	(42,091)	5,620	(5,620)
Non-indexed	100	(35,656)	35,656	31,700	(31,700)
Total		6,436	(6,436)	37,321	(37,321)

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Notes to the Consolidated Financial Statements

59. Interest rate risk associated with non-trading portfolios

a. Breakdown

The breakdown of financial assets and liabilities in non-trading portfolios by the earlier of interest repricing time or maturity is specified as follows:

31.12.2021

Financial assets	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Total**
Cash and balances with Central Bank	36,081,053	2,564,841				38,645,894
Fixed income securities	4,059,204	317,875	15,430,656	9,986,479	7,820,556	37,614,770
Loans to customers	59,696,220	2,603,372	4,651,287	4,285,008	351,759	71,587,646
Financial assets excluding derivatives	99,836,478	5,486,088	20,081,943	14,271,487	8,172,316	147,848,311
Effect of derivatives	23,328,516			15,129,226		38,457,742
Total	123,164,994	5,486,088	20,081,943	29,400,713	8,172,316	186,306,053

Financial liabilities	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Total**
Deposits	78,669,807					78,669,807
Borrowings	3,431,363	10,955,347	2,861,690	12,648		17,261,048
Issued bills						0
Issued bonds	264,089	983,646	3,707,789	22,324,381	5,317,811	32,597,716
Subordinated liabilities			(81,893)	1,344,948	2,108,711	3,371,766
Financial liabilities excluding derivatives	82,365,260	11,938,993	6,487,586	23,681,977	7,426,521	131,900,336
Effect of derivatives		12,339,360				12,339,360
Total	82,365,260	24,278,353	6,487,586	23,681,977	7,426,521	144,239,696
Total interest repricing gap	40,799,734	(18,792,265)	13,594,357	5,718,736	745,795	42,066,357

31.12.2020

Financial assets	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Total**
Cash and balances with Central Bank	27,205,748	1,739,281				28,945,030
Fixed income securities	17	99,156	17,593,356	7,297,972	92,550	25,083,052
Loans to customers	24,457,207	793,533	2,815,576	1,287,973	(31,316)	29,322,972
Financial assets excluding derivatives	51,662,972	2,631,970	20,408,932	8,585,946	61,234	83,351,054
Effect of derivatives	18,597,318	3,397,994		3,100,000		25,095,311
Total	70,260,290	6,029,964	20,408,932	11,685,946	61,234	108,446,365

Financial liabilities	**Up to 1 month**	**1-3 months**	**3-12 months**	**1-5 years**	**Over 5 years**	**Total**
Deposits	59,924,683					59,924,683
Borrowings	6,797,253	9,715,286	9,911,801			26,424,340
Issued bills		598,592	1,405,016			2,003,608
Issued bonds	82,908	164,653	640,449	4,680,075		5,568,085
Subordinated liabilities	1,168,852		64,711	843,662		2,077,225
Financial liabilities excluding derivatives	67,973,696	10,478,531	12,021,977	5,523,737	0	95,997,940
Effect of derivatives	3,102,368					3,102,368
Total	71,076,064	10,478,531	12,021,977	5,523,737	0	99,100,309
Total interest repricing gap	(815,774)	(4,448,567)	8,386,956	6,162,209	61,234	9,346,056

b. Sensitivity analysis

The Group performs monthly sensitivity analysis on financial assets and liabilities in non-trading portfolios subject to interest rate risk. The sensitivity analysis assumes a shift in the yield curves for all currencies. A parallel shift in yield curves would have the following impact on the Group's pre-tax profit and equity, assuming all other risk factors remain constant:

	Shift in		**31.12.2021**		**31.12.2020**
Currency	**basis points**	**Downward**	**Upward**	**Downward**	**Upward**
ISK, indexed	50	222,350	(216,040)	62,022	(60,635)
ISK, non-indexed	100	85,251	(92,544)	24,517	(36,416)
Other currencies	20	(7,936)	7,901	980	(1,139)
Total		299,665	(300,683)	87,519	(98,190)

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

60. Exposure towards changes in the CPI

a. Definition

Exposure towards changes in CPI is the risk that fluctuations in the Icelandic Consumer Price Index (CPI) will affect the balance and cash flow of indexed financial instruments.

The Group is exposed to inflation indexation of assets and liabilities denominated in ISK. All indexed assets and liabilities are valued according to the CPI measure at any given time and changes in CPI are recognised in the income statement.

b. Management

The Group controls its indexation risk through derivatives contracts and sales and purchases of indexed bonds, mostly government bonds, and thus keeps its exposure to the CPI within the limits set by the ALCO committee.

c. Balance of CPI linked assets and liabilities

The net balance of CPI linked assets and liabilities is specified as follows:

	31.12.2021	**31.12.2020**
Assets	36,414,405	11,877,087
Liabilities	(18,295,156)	(8,311,283)
Total	18,119,249	3,565,804

d. Sensitivity to changes in CPI

Given the net balance of CPI linked assets and liabilities, a 1% change in the CPI would, with other things constant, result in the following changes to the Group's pre-tax profit.

	31.12.2021		**31.12.2020**	
	-1%	1%	-1%	1%
Government bonds	(97,037)	97,037	(14,006)	14,006
Other fixed income securities	(87,163)	87,163	(6,810)	6,810
Loans to customers	(81,424)	81,424	(66,955)	66,955
Derivatives	(98,520)	98,520	(31,000)	31,000
Short positions	8,476	(8,476)	9,484	(9,484)
Deposits	58,158	(58,158)	55,629	(55,629)
Issued bonds	108,317	(108,317)	0	0
Subordinated liabilities	8,000	(8,000)	18,000	(18,000)
	(181,192)	181,192	(35,658)	35,658

The effect on equity would be the same.

61. Currency risk

a. Definition

Currency risk arises when financial instruments are not denominated in the functional currency of the respective Group entity and can affect both the Group's income statement and statement of financial position. A part of the Group's financial assets and liabilities is denominated in foreign currencies.

b. Management

Currency positions are monitored by risk management and reported to the ALCO committee. Any mismatch between assets and liabilities in each currency is monitored closely and managed within limits.

The Group is subject to limits set by the Central Bank of Iceland regarding the maximum open currency position. At 31 December 2021 and 31 December 2020 the Group's position in foreign currencies was within those limits.

c. Exchange rates

The following exchange rates have been used by the Group in the preparation of these financial statements:

	Closing 31.12.2021	**Average 2021**	**Closing 31.12.2020**	**Average 2020**
EUR/ISK	147.6	150.2	156.1	154.5
USD/ISK	130.4	127.1	127.2	135.3
GBP/ISK	175.7	174.7	173.6	173.7

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

61. Currency risk (cont.)

d. Breakdown of financial assets and financial liabilities denominated in foreign currencies

31.12.2021

Financial assets	**EUR**	**USD**	**GBP**	**DKK**	**Other currencies**	**Total**
Cash and balances with Central Bank	2,277,825	5,680,299	3,146,054	1,241,355	340,352	12,685,883
Fixed income securities	739,569	1,825,272	247,114			2,811,955
Shares and other variable income securities	1,670	1,907,258	2,368,725	834	101,149	4,379,636
Securities used for hedging	560,656	32,740	1,563		200,745	795,704
Loans to customers	1,432,801	64,955	1,886,376	23,274	132,863	3,540,269
Other assets	285,729	59,975	33,389	50,984	33,663	463,739
Financial assets excluding derivatives	5,298,251	9,570,499	7,683,221	1,316,446	808,771	24,677,187
Derivatives	3,764,406	491,375	422,187		19,266	4,697,234
Total	9,062,656	10,061,875	8,105,408	1,316,446	828,037	29,374,421

Financial liabilities	**EUR**	**USD**	**GBP**	**DKK**	**Other currencies**	**Total**
Deposits	3,330,163	7,437,554	1,320,108	1,201,927	246,671	13,536,423
Borrowings	43,260	652,726				695,986
Issued bonds			4,124,798			4,124,798
Technical provision	88,442	133,707	1,298	32,113	82,004	337,563
Other liabilities	383,973	96,248	49,046	1,754	98,030	629,052
Financial liabilities excluding derivatives	3,845,838	8,320,236	5,495,250	1,235,793	426,705	19,323,822
Derivatives	5,657,882	1,172,600	2,135,377			8,965,859
Total	9,503,721	9,492,836	7,630,627	1,235,793	426,705	28,289,682

Net currency position	**EUR**	**USD**	**GBP**	**DKK**	**Other currencies**	**Total**
Financial assets	9,062,656	10,061,875	8,105,408	1,316,446	828,037	29,374,421
Financial liabilities	(9,503,721)	(9,492,836)	(7,630,627)	(1,235,793)	(426,705)	(28,289,682)
Financial guarantee contracts	116,486					116,486
Total	(324,579)	569,039	474,781	80,652	401,332	1,201,226

31.12.2020

Financial assets	**EUR**	**USD**	**GBP**	**NOK**	**Other currencies**	**Total**
Cash and balances with Central Bank	1,448,060	1,781,860	93,064	45,420	1,230,660	4,599,063
Fixed income securities	468,294	(0)	244,143			712,436
Shares and other variable income securities		230,685	1,364,787		1	1,595,473
Securities used for hedging	302,728	9,541		143,181		455,449
Loans to customers	629,567		1,221,891		0	1,851,457
Other assets	316,061	552,657	321,743	150,022	1,654	1,342,137
Financial assets excluding derivatives	3,164,709	2,574,743	3,245,627	338,622	1,232,315	10,556,016
Derivatives	390,250	2,551,251	20,925		0	2,962,425
Total	3,554,959	5,125,993	3,266,551	338,622	1,232,315	13,518,441

Financial liabilities	**EUR**	**USD**	**GBP**	**NOK**	**Other currencies**	**Total**
Deposits	3,076,426	4,311,550	520,743	94,862	933,540	8,937,121
Borrowings	45,990					45,990
Issued bonds		329,704				329,704
Other liabilities	303,224	223,311	220,068	143,181	268,601	1,158,384
Financial liabilities excluding derivatives	3,425,640	4,864,565	740,811	238,042	1,202,141	10,471,199
Derivatives		130,909	2,256,150	74,640		2,461,699
Total	3,425,640	4,995,474	2,996,961	312,682	1,202,141	12,932,898

Net currency position	**EUR**	**USD**	**GBP**	**NOK**	**Other currencies**	**Total**
Financial assets	3,554,959	5,125,993	3,266,551	338,622	1,232,315	13,518,441
Financial liabilities	(3,425,640)	(4,995,474)	(2,996,961)	(312,682)	(1,202,141)	(12,932,898)
Financial guarantee contracts	176,393					176,393
Total	305,712	130,519	269,590	25,940	30,174	761,936

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

61. Currency risk (cont.)

e. Sensitivity to currency risk

Given the net currency position, a 10% change in the value of the ISK would, with other things constant, result in the following changes to the Group's pre-tax profit.

	31.12.2021		31.12.2020	
Assets and liabilities denominated in foreign currencies	**-10%**	**+10%**	**-10%**	**+10%**
EUR	(32,458)	32,458	30,571	(30,571)
USD	56,904	(56,904)	13,052	(13,052)
GBP	47,478	(47,478)	26,959	(26,959)
DKK	8,065	(8,065)	(1,201)	1,201
NOK	668	(668)	2,594	(2,594)
Other currencies	39,465	(39,465)	4,219	(4,219)
Total	120,123	(120,123)	76,194	(76,194)

The effect on equity would be the same.

62. Equity risk

a. Definition

Equity risk is the risk that the fair value of equties decreases as the result of changes in the value of shares and other variable income securities in the Group’s portfolio.

b. Sesitivity analysis of equity risk

The analysis below calculates the effect of possible movements in equity prices that affect the Consolidated Financial Statements. A negative amount in the table reflects a potential net reduction in the Consolidated Income Statement or equity, while a positive amount reflects a potential net increase. Investments in associates are excluded.

	31.12.2021		31.12.2020	
	-10%	**+10%**	**-10%**	**+10%**
Listed shares	(552,391)	552,391	(89,242)	89,242
Unlisted shares	(890,709)	890,709	(233,814)	233,814
Unlisted unit shares in funds	(825,229)	825,229	(184,227)	184,227
Total	(2,268,329)	2,268,329	(507,283)	507,283

63. Operational risk

a. Definition

Operational risk is the risk of direct or indirect loss from inadequate or failed internal processes or systems, from human error or external events that affect the Group's reputation and operational earnings.

b. Management

The individual business units within the Group are primarily responsible for managing their respective operational risk. The risk management unit is furthermore responsible for identifying, monitoring and reporting the Group's operational risk. Operational risk can be reduced through staff training, process re-design and enhancement of the control environment. The risk management unit monitors operational risk by tracking loss events, quality deficiencies, potential risk indicators and other early-warning signals. The unit takes an active role in internal control and quality management.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

Financial assets and financial liabilities

64. Accounting classification of financial assets and financial liabilities

The accounting classification of financial assets and financial liabilities is specified as follows:

31.12.2021 Financial assets	**Amortised cost**	**Fair value through OCI**	**Manda-torily at fair value through P/L**	**Total carrying amount**
Cash and balances with Central Bank	38,645,894			38,645,894
Fixed income securities		21,303,362	18,743,288	40,046,651
Shares and other variable income securities			22,683,295	22,683,295
Securities used for hedging			22,085,696	22,085,696
Loans to customers	69,063,377		2,524,269	71,587,646
Derivatives			2,734,216	2,734,216
Other assets	10,012,351		30,202	10,042,553
Total	117,721,622	21,303,362	68,800,966	207,825,950

Financial liabilities	**Amortised cost**	**Fair value through OCI**	**Manda-torily at fair value through P/L**	**Total carrying amount**
Deposits	78,669,807			78,669,807
Borrowings	17,261,048			17,261,048
Issued bills				0
Issued bonds	32,597,716			32,597,716
Subordinated liabilities	3,371,766			3,371,766
Short positions held for trading			1,323,631	1,323,631
Short positions used for hedging			1,280,868	1,280,868
Derivatives			3,008,401	3,008,401
Other liabilities	6,194,021		483,486	6,677,507
Total	138,094,357	0	6,096,387	144,190,744

31.12.2020 Financial assets	**Amortised cost**	**Fair value through OCI**	**Manda-torily at fair value through P/L**	**Total carrying amount**
Cash and balances with Central Bank	28,945,030			28,945,030
Fixed income securities		22,946,767	5,838,266	28,785,033
Shares and other variable income securities			5,072,830	5,072,830
Securities used for hedging			19,620,240	19,620,240
Loans to customers	26,579,121		2,743,851	29,322,972
Derivatives			389,671	389,671
Other assets	5,112,881		327,210	5,440,092
Total	60,637,033	22,946,767	33,992,067	117,575,867

Financial liabilities	**Amortised cost**	**Fair value through OCI**	**Manda-torily at fair value through P/L**	**Total carrying amount**
Deposits	59,924,683			59,924,683
Borrowings	26,424,340			26,424,340
Issued bills	2,003,608			2,003,608
Issued bonds	5,568,085			5,568,085
Subordinated liabilities	2,077,225			2,077,225
Short positions held for trading			1,520,547	1,520,547
Short positions used for hedging			731,987	731,987
Derivatives			1,750,346	1,750,346
Other liabilities	3,364,471		386,001	3,750,472
Total	99,362,412	0	4,388,881	103,751,293

Notes to the Consolidated Financial Statements

65. Financial assets and financial liabilities measured at fair value

a. Fair value hierarchy

The fair value of financial assets and liabilities that are traded in active markets are based on quoted market prices. For other financial instruments the Group determines fair value using various valuation techniques. IFRS 13 specifies a fair value hierarchy based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources whereas unobservable inputs reflect the Group's market assumptions. These two types of inputs result in the following fair value hierarchy:

- Level 1
  Inputs are quoted market prices (unadjusted) in active markets for identical instruments.

- Level 2
  Inputs are not quoted market prices but are observable either directly, i.e. as prices, or indirectly, i.e. derived from prices. This category includes financial instruments valued using quoted prices in active markets for similar instruments, quoted prices for similar or identical instruments in markets that are considered less than active and other instruments which are valued using techniques which rely primarily on inputs that are directly or indirectly observable from market data.

- Level 3
  Inputs are not observable or unobservable inputs have a significant effect on the valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments are required to reflect the differences between the instruments.

b. Valuation process

The Bank's Credit committee is responsible for fair value measurements of financial assets and financial liabilities classified as level 2 or level 3 instruments. The valuation is carried out by personnel from respective departments under supervision from Risk. The valuations are revised at least quarterly, or when there are indications of significant changes in the underlying inputs.

c. Valuation techniques

The Group uses widely recognised valuation techniques, including net present value and discounted cash flow models, comparison with similar instruments for which market observable prices exist, Black-Scholes and other valuation models.

Valuation techniques include recent arm's length transactions between knowledgeable, willing parties, if available, reference to the current fair value of other instruments that are substantially the same, the discounted cash flow analysis and option pricing models. Valuation techniques incorporate all factors that market participants would consider in setting a price and are consistent with accepted methodologies for pricing financial instruments. Periodically, the Group calibrates the valuation technique and tests it for validity using prices from any observable current market transactions in the same instrument, without modification or repackaging, or based on any available observable market data.

For more complex instruments, the Group uses proprietary models, which usually are developed from recognised valuation models. Some or all of the inputs into these models may not be market observable, and are derived from market prices or rates or are estimated based on assumptions. When entering into a transaction, the financial instrument is recognised initially at the transaction price, which is the best indicator of fair value, although the value obtained from the valuation model may differ from the transaction price. This initial difference, usually an increase in fair value, indicated by valuation techniques is recognised in income depending upon the individual facts and circumstances of each transaction and no later than when the market data becomes observable.

The value produced by a model or other valuation technique is adjusted to allow for a number of factors as appropriate, because valuation techniques cannot appropriately reflect all factors market participants take into account when entering into a transaction. Valuation adjustments are recorded to allow for model risks, bid-ask spreads, liquidity risks, as well as other factors. Management believes that these valuation adjustments are necessary and appropriate to fairly state financial instruments carried at fair value in the statement of financial position.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

66. Financial assets and financial liabilities measured at fair value

a. Fair value hierarchy classification

The fair value of financial assets and financial liabilities measured at fair value in the statement of financial position is classified into the fair value hierarchy as follows:

31.12.2021

Financial assets	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
Mandatorily measured at fair value through profit and loss				
Fixed income securities	13,186,221	4,762,529	794,538	18,743,288
Shares and other variable income securities	10,222,396	4,077,480	8,383,419	22,683,295
Securities used for hedging	22,085,696			22,085,696
Loans to customers			2,524,269	2,524,269
Derivatives		2,734,216		2,734,216
Other assets			30,202	30,202
Measured at fair value through other comprehensive income				
Fixed income securities	21,303,362			21,303,362
Total	66,797,675	11,574,225	11,732,428	90,104,329

Financial liabilities	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
Mandatorily measured at fair value through profit and loss				
Short positions held for trading	1,323,631			1,323,631
Short positions used for hedging	1,280,868			1,280,868
Derivatives		3,008,401		3,008,401
Other liabilities			483,486	483,486
Total	2,604,499	3,008,401	483,486	6,096,387

Transfers of fixed income securities and transfer of shares and other variable income securities from Level 1 to level 3 amounted to ISK 247 million and ISK 735 million, respectively, during the year 2021.

31.12.2020

Financial assets	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
Mandatorily measured at fair value through profit and loss				
Fixed income securities	5,637,466		200,799	5,838,266
Shares and other variable income securities	2,406,085	385,570	2,281,174	5,072,830
Securities used for hedging	19,620,240			19,620,240
Loans to customers			2,743,851	2,743,851
Derivatives		389,671		389,671
Other assets			327,210	327,210
Measured at fair value through other comprehensive income				
Fixed income securities	22,946,767			22,946,767
Total	50,610,558	775,241	5,553,035	56,938,834

Financial liabilities	**Level 1**	**Level 2**	**Level 3**	**Carrying amount**
Mandatorily measured at fair value through profit and loss				
Short positions held for trading	1,520,547			1,520,547
Short positions used for hedging	731,987			731,987
Derivatives		1,750,346		1,750,346
Other liabilities			386,001	386,001
Total	2,252,534	1,750,346	386,001	4,388,881

Transfers of fixed income securities from Level 1 to level 3 amounted to ISK 199 million during the year 2020.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

66. Financial assets and financial liabilities measured at fair value (cont.)

b. Reconciliation of changes in Level 3 fair value measurements

31.12.2021	Fixed income securities	Shares and other var. income securities	Loans to customers	Other assets	Other liabilities	Total
Balance as at 1 January 2021	200,799	2,281,174	2,743,851	327,210	(386,001)	5,167,034
Total gains and losses in profit or loss	(361,080)	1,570,435	185,667		(97,548)	1,297,473
Additions through a business combination	290,553	4,357,464				4,648,017
Additions	417,151	698,907	1,889,964			3,006,022
Repayments			(2,295,212)	(297,008)	63	(2,592,157)
Disposals		(1,259,488)				(1,259,488)
Transfers in (out) of Level 3	247,114	734,927				982,041
Balance as at 31 December 2021	794,538	8,383,419	2,524,269	30,202	(483,486)	11,248,942

31.12.2020	Fixed income securities	Shares and other var. income securities	Loans to customers	Other assets	Other liabilities	Total
Balance as at 1 January 2020	1,480	1,766,071	2,346,662		(494,991)	3,619,222
Total gains and losses in profit or loss	(18)	248,743	235,355		(286,058)	198,023
Additions		298,594	1,539,245	327,210		2,165,049
Repayments		0	(1,377,411)		395,048	(982,363)
Disposals		(32,234)				(32,234)
Transfers in (out) Level 3	199,337	0				199,337
Balance as at 31 December 2020	200,799	2,281,174	2,743,851	327,210	(386,001)	5,167,034

c. Fair value measurements for Level 3 financial assets and liabilities

Level 3 assets consist primarily of illiquid, unlisted bonds, shares and share certificates and loans measured at fair value. Each asset is evaluated separately but assets within an asset group share a valuation method. The following valuation methods are in use:

Asset class	Method	Significant unobservable input	Range	Book value 31.12.2021
Unlisted bonds	Expected recovery	Value of assets	0-95%	794,538
Unlisted variable income securities	Market price	Recent trades	-	8,383,419
Loans to customers	Expert model	Value of assets and collateral	-	2,524,269
Receivables at fair value	Expert model	Information on turnover	-	30,202
Total				11,732,428

Asset class	Method	Significant unobservable input	Range	Book value 31.12.2020
Unlisted bonds	Expected recovery	Value of assets	0-95%	200,799
Unlisted variable income securities	Market price	Recent trades	-	2,281,174
Loan to customers	Expert model	Value of assets and collateral	-	2,743,851
Receivables at fair value	Expert model	Information on turnover	-	327,210
Total				5,553,035

Given the methods used, the possible range of the significant unobservable inputs is wide. When determining the values used the Group considers the financial strength of the entity in question, recent trades if any and multipliers for comparable instruments.

d. The effect of unobservable inputs in Level 3 fair value measurements

The Group believes its estimates represent appropriate approximations of fair value and that the use of different valuation methodologies and reasonable changes in assumptions or unobservable inputs would not significantly change the estimates.

A 10% change in the estimates would have the following effect on profit before taxes:

	+10%	-10%
Fixed income securities	79,454	(79,454)
Shares and other variable income securities	838,342	(838,342)
Loans to customers	252,427	(252,427)
Receivables at fair value	3,020	(3,020)
Total	1,173,243	(1,173,243)

Notes to the Consolidated Financial Statements

67. Financial assets and financial liabilities not measured at fair value

The Group holds financial instruments which are not measured at fair value. Except for loans to customers, the Group believes that the best estimate of the fair value of these financial instruments is equal to the carrying amount at the reporting date and does therefore not report a fair value for these financial instruments. Loans to customers measured at amortised cost are classified as level 3, in the fair value hierarchy, and have a book value of ISK 69,063 million at end of December 2021. The estimated fair value of loans to customers measured at amortised cost at end of December 2021 is ISK 69,191 million.

Cash and balances with Central Bank includes several components as detailed in note 19. These assets are either balances available on-demand or on very short notice, or other assets easily converted to cash. Other financial assets consist primarily of short-term receivables. The carrying amount of these assets is therefore a reasonable approximation of their fair value.

Deposits and other borrowings are typically either short-term or have variable interest rates. Other liabilities consist primarily of accounts payables, withholding taxes and other short-term payables. The carrying amount of these liabilities is therefore considered a reasonable approximation of their fair value.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

Other information

68. Pledged assets

31.12.2021	Settlement and committed facilities	Securities borrowing	Asset backed securities	Total
Cash and balances with Central Bank	1	2,126,209	1,409	2,127,620
Fixed income securities	4,088,885	1,454,453	0	5,543,338
Loans to customers	6,498,490	0	9,372,337	15,870,827
Other assets	0	46,704	0	46,704
Total	10,587,377	3,627,366	9,373,746	23,588,489

31.12.2020	Settlement and committed facilities	Securities borrowing	Asset backed securities	Total
Cash and balances with Central Bank	0	1,457,323	0	1,457,323
Fixed income securities	3,984,688	906,073	0	4,890,761
Other assets	0	96,102	0	96,102
Total	3,984,688	2,459,498	0	6,444,186

The Group has pledged assets, in the ordinary course of banking business, to the Central Bank of Iceland to secure general settlement in the Icelandic clearing system and to secured committed facilities. Cash pledged to secure the borrowing of securities from other counterparties than the Central Bank of Iceland is classified as other assets. Furthermore, the Group has pledged loans to customers as collateral against asset backed bonds that it has issued.

69. Related parties

a. Definition of related parties

The Group has a related party relationship with the board members of the Bank, the CEO of the Bank and key employees (together referred to as management), associates as disclosed in note 26, shareholders with significant influence over the Bank, close family members of individuals identified as related parties and entities under the control or joint control of related parties.

b. Arm's length

Transactions with related parties are carried out at arm's length and subject to an annual review by the Bank's internal auditor.

c. Effects on statement of financial position

31.12.2021	Loans & receivables	Deposits & payables
Management	0	128,067
Associates	0	0
Total	0	128,067

31.12.2020	Loans & receivables	Deposits & payables
Management	1,851	83,166
Associates	0	0
Total	1,851	83,166

d. Effects on income statement

2021	Interest income	Interest expense	Fees received	Fees paid
Management	60	281	3,870	3,395
Associates	0	0	0	0
Total	60	281	3,870	3,395

2020	Interest income	Interest expense	Fees received	Fees paid
Management	0	487	1,362	10,560
Associates	10,379	209	26,279	0
Total	10,379	696	27,641	10,560

Further information about salaries and benefits paid to the Board of Directors, the CEO and Managing Directors is provided in note 12.

Notes to the Consolidated Financial Statements

70. Remuneration policy

The Board of Directors has adopted a remuneration policy at the proposal of the Remuneration Committee. The Bank's Annual General Meeting approved the Bank's current remuneration policy in April 2021. The Board of Directors will submit an updated remuneration policy for approval at the Bank's Annual General Meeting in 2022.

The remuneration policy conforms to Article 57 of Act No. 161/2002 on Financial Undertakings, Act No. 2/1995 on Public Limited Companies and the Icelandic FSA's rules No. 388/2016 on Incentive Schemes. A more detailed description of the policy can be found on the Bank's website, www.kvika.is.

71. Incentive scheme

The Board of Directors has approved a performance based incentive scheme at the proposal of the Remuneration Committee. The scheme forms a part of the remuneration policy adopted by the Bank.

a. Description

The incentive scheme conforms to the Icelandic FSA's rules No. 388/2016 on Incentive Schemes. Payments according to the scheme are based on key performance indicators (KPIs) that reflect the goals of the Bank, the division and the employee. The basis for performance based pay reflects sound risk management and does not induce excessive risk taking. Performance based pay to individual employees shall not exceed 25% of their annual salary and 40% of the performance based pay shall be deferred for three years. Performance based pay that does not exceed 10% of annual salary is not subject to deferral. A more detailed description of the scheme can be found in the Bank's remuneration policy on it's website, www.kvika.is.

b. Performance based payments through profit and loss

	2021 Cash	2020 Cash
Non-deferred	189,506	64,818
Deferred	86,324	2,640
Salary related expenses	77,849	18,387
Cancelled deferred performance based payments	0	(33,283)
Total	353,679	52,563

c. On-balance sheet deferred performance based payments

	31.12.2021	31.12.2020
Deferred cash payments	158,540	24,955
Deferred cash payments, acquired via business combinations	87,017	0
Total	245,556	24,955

72. Share-based payments

On 21 April 2021 the general meeting of the Bank authorised the Board of Directors to approve a share option plan in accordance with Article 10 of the Income Tax Act No. 90/2003 for all employees of Kvika and its subsidiaries. On 10 November 2021 the Bank's Board of Directors implemented a share option plan which was approved by Iceland Revenue and Customs on 9 December 2021.

The objective of the Bank's stock option plan is to integrate the interests of employees with the long-term goals of the group. Each eligible employee has been granted a stock option for up to ISK 1,500,000 per year the next three years on the following exercise dates:

a. on 15 December 2022, the stock option holder has earned the right to purchase share capital for up to ISK 1,500,000;
b. on 15 December 2023, the stock option holder has earned the right to purchase share capital for up to ISK 1,500,000;
c. on 15 December 2024, the stock option holder has earned the right to purchase share capital for up to ISK 1,500,000.

The Bank´s previous stock option plan, from 2017, ended in full in September 2020 and thus there are no outstanding obligations based on that plan.

a. Description

The calculation of the purchase price was based on weighted average price in transactions with shares of the Bank for ten whole business days prior to the contract date, cf Article 10(1)(4) of the Income Tax Act No 90/2003, i.e. ISK 26.44 per share.

In total, 326 employees entered into a stock option agreement with the Bank for up to 18.494.632 shares per year based on 100% exercise of their options. The options do not allow for cash settlement. The options are conditional on the employee remaining employed by the Bank and various other conditions.

b. Movements in the number of stock options outstanding and their related weighted average exercise prices

The grant date fair value of the options granted through the scheme was as follows:

	Average exercise price per share	Stock options (thousands)
At 1 January 2020	6.24	8,544
Exercised in 2020	6.46	(7,303)
Forfeited in 2020	0.00	(1,240)
At 31 December 2020	0.00	0
Granted in 2021	26.44	55,484
At 31 December 2021	26.44	55,484
Exercisable stock options at 31 December 2021	0.00	0

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

73. Shareholders of the Bank

Shareholder	Country	31.12.2021 %	31.12.2020 %	Beneficial owners
Lífeyrissjóður verzlunarmanna	Iceland	8.20%	7.57%	
Lífeyrissjóður starfsmanna ríkisins A-deild	Iceland	6.28%	5.86%	
Stoðir hf.	Iceland	6.11%	8.24%	
Gildi - lífeyrissjóður	Iceland	4.61%	0.29%	
Arion banki hf.	Iceland	4.40%	2.18%	
Birta lífeyrissjóður	Iceland	4.33%	2.30%	
Stapi lífeyrissjóður	Iceland	3.08%	0.28%	
Lífsverk lífeyrissjóður	Iceland	2.47%	2.89%	
Brú Lífeyrissjóður starfsmanna sveitarfélaga	Iceland	2.14%	0.23%	
Bóksal ehf.	Iceland	2.02%	-	Bogi Þór Siguroddsson (50%), Linda Björk Ólafsdóttir (50%)
Almenni lífeyrissjóðurinn	Iceland	1.90%	2.64%	
Íslandsbanki hf.	Iceland	1.77%	1.87%	
Stefnir - Innlend hlutabréf hs.	Iceland	1.68%	1.42%	Investement fund managed by Stefnir hf.
Kvika Banki - Safnreikningur	Iceland	1.61%	0.00%	
Akta Stokkur hs.	Iceland	1.58%	1.06%	Investement fund managed by Akta sjóðir hf.
Lífeyrissjóður starfsmanna ríkis B-deild	Iceland	1.57%	1.60%	
Landsbréf - Úrvalsbréf hs.	Iceland	1.51%	2.07%	Investement fund managed by Landsbréf hf.
SNV holding ehf.	Iceland	1.36%	6.24%	Svanhildur Nanna Vigfúsdóttir (100%)
Attis ehf.	Iceland	1.36%	-	Guðmundur Örn Þórðarson (100%)
Kvika - Innlend hlutabréf	Iceland	1.28%	1.02%	Investement fund managed by Kvika eignastýring hf.
Kvika - IHF hs.	Iceland	1.26%	1.25%	Investement fund managed by Kvika eignastýring hf.
Frjálsi lífeyrissjóðurinn	Iceland	1.22%	0.11%	
Sigla ehf.	Iceland	1.19%	2.45%	Tómas Kristjánsson (100%)
Vátryggingafélag Íslands hf.	Iceland	1.13%	4.32%	
Landsbankinn hf.	Iceland	1.02%	1.11%	
Others, each less than 1%		32.53%	42.99%	2021: 2795, 2020: 964
		97.61%	100.00%	
Treasury shares		2.39%	0.00%	
Total		100.00%	100.00%	

Beneficial owners are defined as owners holding a share of 10% or greater, directly or indirectly. The information presented is, among other things, based on publicly available information.

74. Events after the reporting date

Acquisition of Ortus Secured Finance Completed

On 24 February 2022, Kvika signed a purchase agreement to acquire a majority shareholding in alternative lender Ortus Secured Finance Ltd. (“Ortus”), following the signing of Heads of Terms in late October 2021. Following the transaction, Kvika holds close to 80% of Ortus’ ordinary shares, having first acquired a minority share of 15% in 2018. The acquisition has no impact on 2021 financial results. Details of the transaction can be found in a press release dated 24 February 2022.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

Significant accounting policies

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Notes to the Consolidated Financial Statements

Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these Consolidated Financial Statements, and have been applied consistently by Group entities.

75. Basis of consolidation

a. Subsidiaries

Subsidiaries are entities controlled by the Group. Control exists when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The Group reassesses its relationship with an entity when there is a change in one or more of the elements of control.

b. Business combinations

The Group uses the acquisition method to account for the acquisition of subsidiaries. The cost of an acquisition is measured as the fair value, at the date of exchange, of the assets given, liabilities incurred or assumed and equity instruments issued. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest.

The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recognised as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised immediately in the income statement.

Any contingent consideration is measured at fair value at the date of acquisition. If an obligation to pay contingent consideration that meets the definition of a financial instrument is classified as equity, then it is not remeasured and settlement is account for within equity. Otherwise, other contingent consideration is remeasured at fair value at each reporting date and subsequent changes in the fair value of the contingent consideration are recognised in profit and loss.

c. Non-controlling interest

Non-controlling interest represent the portion of profit or loss and equity not owned, directly or indirectly, by the Bank. Non-controlling interest is presented separately in the income statement and is included in equity in the statement of financial position, separately from equity attributable to owners of the Bank.

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

d. Fiduciary services

The Group provides custody services, fund management and discretionary and advisory investment management services which require the Group to make decisions on the handling, acquisition or disposal of financial instruments on behalf of its clients.

The financial statements of managed funds and investment portfolios managed by the Group on behalf of customers are not included in the financial statements, as they do not constitute assets or liabilities of the Group.

e. Transactions eliminated on consolidation

Intra-bank balances, income and expenses, and unrealised gains and losses arising from intra-bank transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with associates are eliminated against the investment to the extent of the Group's interest in the associate. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

f. Structured entities

Structured entities are entities that have been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, such as when any voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements.

The Group acts as investment manager or investment advisor, for example, to a number of investment funds operated by the fund management companies Kvika eignastýring hf. and Gamma Capital Management hf. The purpose of these fund management companies is to generate fees from managing assets on behalf of third-party investors by providing investment strategies. These investment funds are financed through the issue of units to investors. The Group has no contractual obligation to provide financial support to these structured entities.

From time to time, the Group makes seed capital investments in certain fund products in order to establish track records for new products, to test new investment strategies or to launch new products at a viable minimum size.

The Group has set up a formal procedure to assess whether or not to consolidate investment funds managed and administered by the Group on behalf of its customers and other investors in the consolidated financial statements. As part of this assessment, the Group reviews all facts and circumstances including the purpose and design of the investment fund, to determine whether the Group, as fund manager, is acting as agent or principal. The Group is deemed to be a principal when the Group acts as fund manager and cannot be removed without cause, has variable returns through significant holdings and is able to influence the returns of the funds by exercising its power.

Notes to the Consolidated Financial Statements

76. Foreign currency

a. Foreign currency transactions

Transactions in foreign currencies are translated into the functional currency of the respective Group's entity using the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated to the functional currency using the exchange rate at the reporting date. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated using the exchange rate at the date the fair value was determined.

Foreign currency differences are posted as a separate line item under net financial income as disclosed in notes 8 and 81.

b. Foreign operations

The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into the functional currency at spot exchange rate current at the reporting date. The income and expenses of foreign operations are translated into the functional currency at the spot exchange rates at the dates of the transactions.

Translation differences on foreign operations are presented as a separate category in the statement of changes in equity.

77. Interest income and expense

Effective interest rate

Interest income and expense are recognised in the income statement using the effective interest method. The effective interest rate is the rate that exactly discounts estimated future cash flows through the expected life of the financial instrument to the gross carrying amount of the financial asset or the amortised cost of the financial liability. When calculating the effective interest rate for financial instruments other than purchased or originated credit-impaired assets, the Group estimates future cash flows considering all contractual terms of the financial instrument but not ECL. For purchased or originated credit-impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including ECL.

Amortised cost and gross carrying amount

The amortised cost of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance. The gross carrying amount of a financial asset is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

Presentation

Interest income and expense presented in the income statement includes interest on:
- financial assets and liabilities measured at amortised cost
- financial assets at fair value through other comprehensive income (FVOCI)
- financial assets at fair value through profit and loss
- derivatives

78. Fee and commission income and expense

The Group earns income from providing various services to its customers. This includes fees for managing assets on behalf of customers, commissions received for equity and bond transactions and fees and commissions for various other financial services. Fee and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Fee and commission income and expense are recognised in the income statement when an agreement with a customer meets all of the following criteria:
- the parties to the contract have approved the contract and are committed to perform their respective obligations
- performance obligations have been established for services to be transferred
- the payment terms have been established for the services to be transferred
- the transaction price can be allocated to each individual service in the agreement
- it is probable that a consideration will be collected in exchange for the services that will be transferred to the customer

The following applies to recognition of income for various types of fees and charges:
- Fees that are earned gradually as the services are performed, such as management fees in asset management, are recognised as income at the rate these services are delivered. In practice, these are on a straight line basis
- Fees attributable to a specific service or action are recognised as income when the service has been performed. Examples of such fees are brokerage and payment commissions

Notes to the Consolidated Financial Statements

79. Net premiums and claims

Premiums are recognised proportionally during the period in which insurance covers. Premium liability is the part of the premium that belongs to subsequent financial years. Recognised premiums in the income statement are therefore the premiums that occurs during the operating year plus transferred premiums from previous years, less premiums for subsequent years. Premiums written for the period are presented less depreciated premiums but without commissions or sales cost and the change in premium liability is presented without changes due to foreign exchange differences. Definition of net premiums is in line with the guidelines of the Central Bank‘s Financial Supervisory body, nr. 1/2020.

Claims in the income statement are comprised of claims paid during the period and changes in the claims liability due to insurance operations and risk margin. The changes in the claims liability due to insurance operations include changes of estimates of previous years‘ liability as well as changes in the reporting year liability. Net claims are claims with the reinsurers‘ share deducted both for the paid claims and the changes in claims liability. Changes in prior years‘ liabilty is presented without the unwinding, interest and exchange rate change of the claims liability, which is transferred to the investment segment. Definition of net claims is in line with the guidelines of the Central Bank‘s Financial Supervisory body, nr. 1/2020.

80. Insurance Contracts

As part of its insurance operations the Group's entities issue contracts that transfer insurance risk from the customers to the Group.

Insurance contracts are contracts under which the insurer accepts insurance risk from policyholders by agreeing to compensate the policyholders if a specified uncertain future event would occur.

The Group's insurance contracts are categorised in Non-life insurance and Life insurance contracts.

Non-Life insurance
Insurance contracts that are categorised as in this section are liability insurances, casualty insurance and property insurance.

Liability insurance contracts protect the customers against the risk of causing harm to third parties. Casualty insurance compensates harm that the customer suffers because of an accident. Property insurance contracts mainly compensate the company's customers for damage suffered to their properties. Customers who undertake commercial activities on their premises could also receive compensation of the loss of earnings caused by the inability to use the insured properties in their business activities (business interruption cover).

Life and Health insurance
These contracts insure events associated with human life, for example death or critical illness.

Insurance contracts are contracts under which the insurer accepts insurance risk from policyholders by agreeing to compensate the policyholders if a specified uncertain future event would occur.

The Group's insurance contracts are categorised in Non-life insurance and Life insurance contracts.

Life and Health insurance
These contracts insure events associated with human life, for example death or critical illness.

81. Net financial income

Net financial income comprises the following:
- Realised and unrealised gains or losses from price changes of fixed income securities measured at fair value
- Realised and unrealised gains or losses from price changes of variable income securities
- Interest income from fixed income securities carried at fair value through profit or loss
- Dividends
- Fair value changes of loans to customers held at fair value
- Fair value changes in derivatives
- Unwinding, interest and exchange rate change of technical provision
- Foreign exchange difference

82. Dividend income

Dividend income is recognised when the right to receive income is established. Usually this is the ex-dividend date for equity securities. Dividends are presented as a component of net financial income.

83. Administrative expenses

Administrative expenses comprise expenses other than interest expenses, fee and commission expenses and expenses related to fair value changes. A breakdown of administrative expenses is provided in note 10.

Notes to the Consolidated Financial Statements

84. Employee benefits

a. Short-term employee benefits

Short-term employee benefits obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

b. Defined contribution plans

Obligations for contributions to defined contribution plans are expensed in profit or loss as the related service is provided. The Group has no further obligations once those contributions have been paid.

c. Share-based payments

Equity-settled share-based payments to employees are measured at the fair value of the equity instruments at grant date. The grant date fair value of equity-settled share-based payment awards granted to employees is recognised as an employee expense, with a corresponding increase in equity, over the period that the employees become unconditionally entitled to the awards. The amount recognised as an expense is adjusted to reflect the number of awards for which the related service and non-market performance conditions are expected to be met, such that the amount ultimately recognised as an expense is based on the number of awards that meet the related service and non-market performance conditions at the vesting date.

85. Income tax

Income tax comprises current and deferred tax. Income tax is recognised in the income statement, except to the extent that it relates to items recognised directly in other comprehensive income or equity, in which case it is recognised there.

Current tax liabilities include the estimated tax payable next year on current year's profit according to the tax rates prevailing at reporting date, in addition to corrections on tax from previous years.

The deferred income tax asset and/or liability has been calculated and recognised in the statement of financial position. The calculation is based on the difference between assets and liabilities as presented in the tax return on the one hand, and in the consolidated financial statements on the other, taking into consideration tax losses carried forward. This difference is due to the fact that the tax assessment is based on premises that differ from those governing the financial statements, mostly due to temporary differences arising from the recognition of revenue and expense in the tax returns and in the financial statements.

Deferred tax assets and tax liabilities are offset in the statement of financial position when there is a legal right to settle on a net basis and they are levied by the same taxing authority on the same entity or on different entities subject to joint taxation.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and reduced to the extent that it is no longer probable that the related tax benefit will be realised.

86. Financial assets and financial liabilities

a. Recognition

The Group initially recognises loans and advances, deposits, debt securities issued and subordinated liabilities on the date on which they are originated. All other financial assets and liabilities are initially recognised on the trade date, which is the date when the Group becomes a party to the contractual provisions of the instrument.

b. Classification

Financial assets

The Group's financial assets are classified into one of three measurement categories, i.e. i) at amortised cost, ii) at fair value through other comprehensive income or iii) at fair value through profit or loss. The measurement basis of individual financial assets is determined based on an assessment of the cash flow characteristics of the assets and the business models under which they are managed.

Financial assets at amortised cost

A financial asset is measured at amortised cost if the contractual terms of the financial asset give rise to cash flows that are solely payment of principal and interest and the asset is held within a business model whose objective is to collect contractual cash flows, i.e. Held to collect. After initial measurement, financial assets in this category are carried at amortised cost using the effective interest rate method. Amortisation is included in interest income in the Consolidated Income Statement. The majority of the Group's loans to customers are carried at amortised cost using the effective interest rate method. Interest on loans to customers is recognised as interest income.

Impairment on financial assets measured at amortised cost is calculated using the expected credit loss approach. Loans and debt securities measured at amortised cost are presented net of allowance for credit losses in the Consolidated Statement of Financial Position.

Notes to the Consolidated Financial Statements

86. Financial assets and financial liabilities (cont.)

Financial assets at fair value through other comprehensive income (FVOCI)

Fixed income securities may be classified as financial instruments measured at fair value through other comprehensive income ("FVOCI") when they meet the classification criteria. Interest income is calculated using the effective interest rate. Interest income and foreign exchange gains or losses are recognised in the Consolidated Statement of Comprehensive Income. Fixed income securities classified as FVOCI are subject to impairment measurement using the expected credit loss approach. Fair value measurements are recognised in Other Comprehensive Income while on derecognition, cumulative gains (losses) recognised in Other Comprehensive Income are reclassified to the Consolidated Statement of Income.

Financial assets at fair value through profit or loss (FVTPL)

Financial assets classified at fair value through profit or loss are all other financial assets which are not classified at amortised cost or at fair value through other comprehensive income. This includes financial assets classified mandatorily at fair value through profit or loss and financial assets which are irrevocably designated by the Group at initial recognition as at fair value through profit or loss that would otherwise meet the requirements to be measured at amortised cost or at fair value through other comprehensive income. The Group may designate financial assets as at fair value through profit or loss if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Financial assets at fair value through profit or loss are measured in the Consolidated Statement of Financial Position at fair value. Loans to customers which are measured at fair value through profit or loss are assets whose cash flows do no represent payments that are solely payments of principal and interest but are non-trading assets. Interest on loans to customers measured at fair value through profit or loss is recognised as interest income. Changes in fair value, as well as any gains or losses realised on disposal, are recognised in the line item Net financial income (expense) in the Consolidated Income Statement.

Business model assessment

The Group makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Group's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated - e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Group's stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at fair value through profit or loss because they are neither held to collect contractual cash flows nor held to both collect contractual cash flows and to sell financial assets.

Cash flow characteristics assessment

Financial assets held within the business models Held to collect and Held to collect and sell are assessed to evaluate if their contractual cash flows are comprised of solely payments of principal and interest (SPPI). SPPI payments are those which are consistent with a basic lending arrangement. Principal is the fair value of the financial asset at initial recognition and may change over the life of the instruments, e.g. due to repayments. Interest relates to basic lending returns, including compensation for the time value of money and credit risk associated with the principal amount outstanding and for other basic lending risks (expected losses, liquidity risks and administrative costs), as well as a profit margin.

Where the contractual terms introduce exposure to other risk or variability of cash flows that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

Reclassifications

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Group changes its business model and if the change is significant to the Group's operations.

Financial liabilities

The Group's financial liabilities are classified into one of two measurement categories, i.e. at amortised cost or at fair value through profit or loss. Financial liabilities held for trading are measured at fair value through profit or loss, all other financial liabilities are measured at amortised cost. Financial liabilities measured at amortised cost are initially recognised at fair value, which is typically equal to cost, i.e. cash advanced less any transaction costs. They are subsequently measured at amortised cost using the effective interest method. Accrued interest, in the case of interest bearing liabilities is included in the carrying amount. Interest expense is recognised in net interest income.

Notes to the Consolidated Financial Statements

86. Financial assets and financial liabilities (cont.)

Derecognition

Financial assets

A financial asset is derecognised when the contractual rights to the cash flows from the asset expire, or when the Group enters into a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Group is recognised as a separate asset or liability.

The Group enters into transactions whereby it transfers assets recognised on its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. In such cases, the transferred assets are not derecognised. Examples of such transactions are securities lending and sale and repurchase agreements.

Financial liabilities

Financial liabilities are derecognised when the obligation of the Group is discharged, cancelled or expires.

87. Offsetting

Financial assets and liabilities are offset, and the net amount reported in the statement of financial position, when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis for gains and losses arising from a group of similar transactions, such as in the Group's trading activity, or other circumstances permitted by International Financial Reporting Standards.

88. Determination of fair value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk. When available, the Group measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Group uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction. For further information on valuation techniques, refer to notes 65 - 67.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Group determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

89. Impairment

Expected Credit Loss

The Group recognises loss allowances for ECL on the following financial instruments that are not measured at FVTPL:

- debt instruments measured at amortised cost;
- debt instruments measured at fair value through other comprehensive income;
- finance lease receivables measured at amortised cost;
- contract assets;
- loan commitments issued; and
- financial guarantee contracts issued.

The Group estimates an ECL for each of these types of assets or exposures. However, IFRS 9 specifies three different approaches depending on the type of asset or exposure:

1. For trade receivables and contract assets without a significant financing component a simplified (lifetime expected loss) approach can be applied.
2. For assets that are credit-impaired at purchase or origination lifetime expected loss approach shall be applied.
3. For other assets/exposures a general (or three-stage) approach shall be applied.

The general approach

The Group measures the ECL on each balance sheet date according to a three-stage expected credit loss impairment model.

Stage 1 covers financial assets that have not deteriorated significantly in credit quality since initial recognition or (where the optional low credit risk simplification is applied) have low credit risk.

Stage 2 covers financial assets that have deteriorated significantly in credit quality since initial recognition (unless the low credit risk simplification has been applied and is relevant) but that do not have objective evidence of a credit loss event.

Stage 3 covers financial assets that have objective evidence of a credit loss event at the reporting date.

Notes to the Consolidated Financial Statements

89. Impairment (cont.)

12-month expected credit losses are recognised in stage 1, while lifetime expected credit losses are recognised in stages 2 and 3. IFRS 9 draws a distinction between financial instruments that have not deteriorated significantly in credit quality since initial recognition and those that have. Measurement of the expected credit losses is determined by a probability-weighted estimate of credit losses over the expected life of the financial instrument.

An asset moves from 12-month expected credit losses to lifetime expected credit losses when there has been a significant deterioration in credit quality since initial recognition. Hence the ‘boundary’ between 12-month and lifetime losses is based on the change in credit risk not the absolute level of risk at the reporting date.

There is also an important operational simplification that permits companies to stay in ‘12-month expected credit losses’ if the absolute level of credit risk is ‘low’. This applies even if the level of credit risk has increased significantly.

There is also a third stage. This applies to assets for which there is objective evidence of impairment. In Stage 3 the credit loss allowance is still based on lifetime expected losses but the calculation of interest income is different.

In the periods subsequent to initial recognition, interest is calculated based on the amortised cost net of the loss provision, whereas the calculation is based on the gross carrying value in Stages 1 and 2.

Finally, it is possible for an instrument for which lifetime expected credit losses have been recognised to revert to 12-month expected credit losses should the credit risk of the instrument subsequently improve so that the requirement for recognising lifetime expected credit losses is no longer met.

Expected credit losses
Expected credit losses are defined as the difference between all the contractual cash flows that are due to an entity and the cash flows that it actually expects to receive (‘cash shortfalls’). This difference is discounted at the original effective interest rate (or credit-adjusted effective interest rate for purchased or originated credit-impaired financial assets).

12 month expected credit losses
12-month expected credit losses are a portion of the lifetime expected credit losses. They are calculated by multiplying the probability of a default occurring on the instrument in the next 12 months by the total (lifetime) expected credit losses that would result from that default. They are not the expected cash shortfalls over the next 12 months. They are also not the credit losses on financial instruments that are forecast to actually default in the next 12 months.

Lifetime expected credit losses
Lifetime expected credit losses are the expected shortfalls in contractual cash flows, taking into account the potential for default at any point during the life of the financial instrument.

Definition of default
The Group considers a financial asset to be in default if one of the following applies:
- the borrower is 90 days past due of one of his exposures with the Bank;
- the borrower is registered as in delinquency by Creditinfo (Icelandic: vanskilaskrá);
- the borrower is registered in public records as filed for bankruptcy, has terminated his business or is no longer a going concern;
- the borrower is considered to be unlikely to pay as determined by the Bank's Risk Management department. Events that are likely to lead to default as determined by the Risk Management department include the following:
  - breach of covenants of loan commitments;
  - loan concessions or stressed restructuring; or
  - Risk Management's internal risk assessment is 4 or 5.
- the borrower has been in default in accordance with above at any point for the previous three months.

The Risk Management department can manually override automatic default triggers if the following applies:
- the reason for reported default triggers is known to the Bank and not considered to be lack of willingness or ability to pay.
- re-financing of borrower’s exposures is expected and has been confirmed.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

89. Impairment (cont.)

Probability of default and credit risk rating

The Group utilises an external Probability of Default model (PD model) developed and maintained by Creditinfo Iceland, an Icelandic credit bureau, for the Group. The PD model is based on information compiled by Creditinfo on the creditworthiness of corporates and individuals in Iceland based both on personal and demographic factors. It predicts the probability of default in the next 12 months. The model has been calibrated to using historical default rate information representative of the Group's portfolio. The model is designed as a point in time model and correlation between forecasted and actual default rates and macroeconomic forecasts has been identified. This enables the Group to calculate different forward looking probabilities of default given different forecasts for changes in inflation rate and unemployment rate. Lifetime PD for loans in stage 3 is 100% as by definition they are already in default.

The Group utilises an economic forecast and the current 12 month PD for the purpose of estimating lifetime PD for loans in stage 2. The 12 month PD is adjusted with a survival rate for each year until maturity with the following formula: $PD_t = PD_{12} * SR_t$ where PD_{12} is the 12 month PD from the credit rating model and SR_t is the survival rate at time t, which is calculated recursively as $SR_t = SR_{t-1} * (1-PD_t)$. The Group monitors the appropriateness of the assumption as a part of it’s yearly validation and monitoring process.

Significant increase in credit risk

When considering whether a significant increase in credit risk (SICR) has occurred the Group considers both quantitative and qualitative factors. In general the Group will rely on a quantitative analysis based on the PD model but will additionally consider qualitative factors based on the information available to the Group.

Quantitative SICR assessment

The Group has defined the following criteria’s for SICR:

1. 30 days past due of any of the client's exposures
2. Grading migrations – SICR has occurred if the current grade has increased compared to the origination grade more or equal to the following thresholds:

Origination grade	Threshold grade
1	7
2	7
3	7
4	7
5	7
6	8
7	8
8	9
9	10

Migration of one or two risk grading in the PD model is considered to be a significant increase in risk and therefore warrant a transfer to stage 2, depending on the origination grade. However, the Group considers risk grades less than 5 for corporations to be low risk and therefore excludes any movement between categories that does not result in a rating above that level. Ratings above 10 are considered to indicative of default and therefore warrant elevation to stage 3 unless overridden based on other available information or expert judgement.

Qualitative SICR assessment

Risk Management is responsible for managing the credit risk of the Group which includes a qualitative SICR assessment. Risk Management reviews on a monthly basis large exposures, unsecured loans and loans that are past due on a loan by loan basis.

Notes to the Consolidated Financial Statements

89. Impairment (cont.)

Exposure at default

Lifetime definition

The Group considers the lifetime of each exposure to be the contractual maturity of each loan. The Group considers this to be the case as any lending subsequent to that period would be based on an independent lending decision at that time based on the prevailing market terms. The Group only considers contractual cash flows when estimating exposure at default. The average lifetime of the Group's exposures is relatively short and it does therefore not consider the likelihood of prepayment when concluding on the lifetime of the assets.

Committed facilities

The Group considers the off-balance portion of exposure at default to be 50% (credit conversion factor) of any facilities not drawn upon that are considered committed. Such facilities include overdrafts, credit cards and guarantees. The credit conversion factor is subject to expert review on a case by case basis. The Bank does not consider credit line facilities to be committed facilities as disbursements are subject to predetermined conditions and constitute a separate credit review. These predetermined conditions will in most cases lead directly to an increase in posted collateral and disbursements therefore stay within acceptable collateral coverage.

Expected credit loss measurement

IFRS 9 requires the Group to determine an expected credit loss (ECL) amount on a probability-weighted basis as the difference between the cash flows that are due to the Group in accordance with the contractual terms of a financial instrument and the cash flows that the Group expects to receive. The Group has implemented an ECL model which is consistent with regulatory and best practices. The model is based on four components.

Probability of Default (PD). This is an estimate of the likelihood of default over a given time horizon. The Bank uses an external PD model developed by CreditInfo for the Group.

Exposure at Default (EAD). This is an estimate of the exposure at a future date, taking into account expected changes in the exposure after the reporting date, including repayments of principal and interest, and expected drawdowns on committed facilities.

Loss Given Default (LGD). This is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from any collateral. It is expressed as a percentage of EAD and derived from value of underlying collaterals.

Discount rate. This is used to discount an expected loss to present value at the reporting date using the effective interest rate (EIR) at initial recognition.

Forward looking probability weighted scenarios

The Group's management has identified and probability weighted two macro-economic scenarios for the purpose of calculating expected credit loss. Forecasts of macro-economic variables and scenario weights are based on the Group‘s management judgement. The Group incorporates the following forward-looking macro- economic variables into its probability weighted expected credit loss calculations: (i) unemployment rate and (ii) inflation rate.

90. Cash and balances with Central Bank

Cash and balances with Central Bank include notes and coins on hand, balances held with the Central Bank and other financial institutions, and highly liquid financial assets with original maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Group in the management of its short-term commitments.

Cash and balances with Central Bank are carried at amortised cost in the statement of financial position.

91. Fixed income securities

Fixed income securities are initially measured at fair value and subsequently accounted for depending on their classification as discussed in note 86.

92. Shares and other variable income securities

Shares and other variable income securities consist of equity investments and unit shares in mutual funds. Shares and other variable income securities are initially measured at fair value and subsequently accounted for depending on their classification as discussed in note 86.

93. Securities used for hedging

Securities used for hedging consist of non-derivative financial assets that are used to hedge the Group's exposure arising from derivative contracts with customers. Securities used for hedging are measured at fair value as discussed in note 86.

Notes to the Consolidated Financial Statements

94. Loans to customers

Loans are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and include loans provided by the Group to its customers, participation in loans from other lenders and purchased loans that are not quoted in an active market and which the Group has no intention of selling immediately or in the near future. Finance lease receivables are a part of the line item Loans to Customers.

Loans are initially recognised at fair value, which is the cash advanced, plus any transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. Accrued interest is included in the carrying amount of the loans and advances. The carrying amount of impaired loans is reduced through the use of an allowance account.

When the Group purchases a financial asset and simultaneously enters into an agreement to resell the asset, or a substantially similar asset, at a fixed price at a future date ("reverse repo" or "stock borrowing"), the arrangement is accounted for as a loan and the underlying asset is not recognised in the Group's statement of financial position.

95. Derivatives

A derivative is a financial instrument or another contract that falls under the scope of IFRS 9 and generally has the following three characteristics:

- Its value changes due to changes in an underlying variable, such as bond price, share price, security or price index (including CPI), foreign currency exchange rate or interest rate
- The contract requires no initial investment or an initial investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors
- Settlement takes place at a future date

The Group uses derivatives for trading purposes and to hedge its exposure to market price risk, foreign exchange risk and inflation and interest risk arising from operating, financing and investing activities. The Group does not apply hedge accounting.

Derivative assets and liabilities are initially recognised and subsequently measured at fair value in the statement of financial position. Derivatives with positive fair values are classified as financial assets and derivatives with negative fair values as financial liabilities. Revenue from derivatives is split into interest income and net income from financial instruments at fair value and presented in the corresponding line items in the income statement.

96. Investments in associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence generally exists when the Group holds between 20% and 50% of the voting power, including potential voting rights, if any. Investments in associates are initially recognised at cost.

The Group's share of the total recognised gains and losses of associates is included in the financial statements of the Group on an equity accounted basis, from the date the significant influence commences until the date it ceases.

If the Group's share of loss exceeds its interest in an associate, the Group's carrying amount is reduced to zero and recognition of further losses is discontinued except to the extent that the Group has incurred legal or constructive obligations or made payments on behalf of the associate. If the associate subsequently reports profits, the Group resumes recognising its share of those profits only after its share of the profits equals the share of losses not recognised.

97. Investment properties

An investment property is an asset which is specified for leasing to third parties, for returns or for both purposes. Investment properties are initially recognised at cost and subsequently measured at fair value. Changes in fair value are recognised as gains or loss in the income statement.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

98. Intangible assets

a. Asset categories

The Group groups intangible assets into four categories:

- Goodwill

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

  Customer relationships have been acquired as part of recent acquistions and are capitalised and amortised using the straight line method over their useful life of maximum 16 years.
- Brands

  Brands have been acquired as part of recent acquistions and are capitalised and amortised using the straight line method over their useful life, but not exceeding 20 years.
- Software and other

  Software comprise acquired software licences and external costs associated with the development of bespoke applications.

The Group has not defined any internally generated intangible assets.

b. Initial recognition

Intangible assets are initially recognised at cost.

c. Subsequent measurement

The Group uses the cost model for measurement after recognition and intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Intangible assets are reviewed for indications of impairment or changes in estimated future economic benefits at each reporting date. If such indications exist, then the asset's recoverable amount is estimated. Goodwill is tested annually for impairment.

For impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that is largely independent of the cash inflows of other assets or cash generating units (CGUs). Goodwill arising from a business combination is allocated to CGUs or groups of CGUs that are expected to benefit from the synergies of the combination.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. Value in use is based on the estimated future cash flows, discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or CGU.

An impairment loss is recognised if the carrying amount of an asset or CGU exceeds its recoverable amount.

Impairment losses are recognised in profit or loss. They are allocated first to reduce the carrying amount of any goodwill allocated to the CGU, and then to reduce the carrying amounts of the other assets in the CGU on a pro rata basis.

An impairment loss in respect of goodwill is not reversed. For other assets, an impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

d. Amortisation

Intangible assets with finite useful life are amortised using the straight-line method over their estimated useful economic life, with the amortisation recognised in the income statement. The estimated useful life of intangible assets is as follows:

Customer relationships	13-16 years
Brands	10-20 years
Software and other	3-10 years

Depreciation of property and equipment and amortisation of intangible assets are presented together as a separate line item in administrative expenses as disclosed in note 10. Further breakdown on depreciation of intangible assets is provided in note 28.

99. Operating lease assets

Operating lease assets are recognised at cost less depreciation and impairment. Depreciation are calculated and recognised in the income statement on a straight-line basis based on estimated useful life, taking into account the residual value.

Kvika banki hf. Amounts are in ISK thousands

Notes to the Consolidated Financial Statements

100. Property and equipment

a. Asset categories

The Group groups tangible assets into two categories:

- Real estate, which includes office and residential buildings, land and building rights
- Other property and equipment, which includes automobiles for own use, furniture and fixtures, computers and other office equipment

b. Initial recognition

Property and equipment is initially recognised at cost, which includes direct expenses related to the purchase.

c. Subsequent measurement

The Group uses the cost model for the measurement after recognition and property and equipment is carried at cost less any accumulated depreciation and any accumulated impairment losses. Property and equipment is reviewed for indications of impairment or changes in estimated future economic benefits at each reporting date. If such indications exist, the assets are analysed to assess whether their carrying amount is fully recoverable.

d. Subsequent cost

The Group recognises in the carrying amount of an item of property and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. The decision, if subsequent costs are added to the acquisition cost of property and equipment, is based on whether an identified component, or part of such component, has been replaced or not, or if the nature of the subsequent cost means a contribution of a new component. All other costs are expensed in the income statement when incurred.

e. Depreciation

Depreciation is recognised in the income statement on a straight-line basis over the estimated useful lives of each component of an item of property and equipment. The estimated useful lives are as follows:

Real estate	15-50 years
Other property and equipment	3-5 years

Where parts of an item of property and equipment have different useful lives, those components are accounted for separately.

101. Reinsurance assets

Reinsurance contracts are made in order to reduce the Group's risks. Reinsurance contracts can be either proportional or carry risk exceeding a fixed amount.

102. Other assets

Other assets are measured at amortised cost, except for certain receivables which are measured at fair value.

Part of other assets are life-insurance policies offered by TM líftryggingar hf. which consist of life-insurance and contribution to investments funds. Life-insurance policyholder bears the investment risk.

103. Deposits

Deposits consist of time deposits and demand deposits. Money market deposits are included in borrowings. Deposits are recognised at amortised cost, including accrued interest.

104. Technical provision

The technical provision in the Consolidated Financial Statements represents the Group's liability as a result of insurance contracts made and consists of the best estimate of the claims provision, the premium provision and the risk margin.

The core of the claims provisions is an actuarial estimate of payments of incurred claims until they will be settled less what has already been paid. According to Act on Insurance No. 100/2016 and related legislation, margins are added to the core of the claim’s provision. The margins are:

- Expected settlement expenses not allocated to specific claims. This cost is recognized among operating expenses when it is due.
- The effect of future inflation from the date of accounts to payment.
- The effect of discounting the future payments using a risk-free interest rate curve.

The premium provision is the part of the premiums already written that cover insurance protection against events happening after the date of the financial statements, taking into account expected cancellation of premiums. The premium provision is therefore the value of the insurance protection that the Group is obligated to fulfil after the date of the financial statements.

The risk margin represents the cost of capital that an insurance company would require to take on the obligations of the company. The risk margin will not be paid unless the Group or part of it will be sold.

The insurance companies of the Group have used the same method to estimate claims provision since 2014. The method is in accordance with IFRS 4 and Act on Insurance No. 100/2016. The claims provision is the same as used in the Solvency calculations, but the estimates of the premium provision and risk margin are not.

Notes to the Consolidated Financial Statements

105. Borrowings

Borrowings are mostly comprised of money market deposits. They are initially recognised at fair value less attributable transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. Accrued interest is included in their carrying amount.

When the Group sells a financial asset and simultaneously enters into an agreement to repurchase the asset, or a substantially similar asset, at a fixed price at a future date ("repo" or "stock lending"), the arrangement is accounted for as a borrowing and the underlying asset continues to be recognised in the Group’s statement of financial position.

106. Issued bills

Issued bills are initially recognised at fair value less attributable transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. Accrued interest is included in their carrying amount.

107. Issued bonds

Issued bonds are initially recognised at fair value less attributable transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. Accrued interest is included in their carrying amount.

108. Subordinated liabilities

Subordinated liabilities are initially recognised at fair value less attributable transaction costs. Subsequently, they are measured at amortised cost using the effective interest method. Accrued interest is included in their carrying amount.

109. Short positions held for trading

Short positions are obligations of the Group to deliver financial assets borrowed by the Group and sold to third parties. Short positions are carried at fair value through profit or loss with all fair value changes recognised in the income statement under net financial income.

110. Short positions used for hedging

Short positions used for hedging are obligations of the Group to deliver financial assets borrowed by the Group and sold to third parties. Short positions used for hedging consist of non-derivative financial liabilities that are used to hedge the Group's risk exposure arising from derivative contracts with customers. Short positions used for hedging are carried at fair value through profit or loss with all fair value changes recognised in the income statement under net financial income.

111. Other liabilities

Other liabilities are measured at amortised cost, except for the contingent consideration which is measured at fair value.

112. Right of use asset and lease liability

The Group assesses whether a contract is or contains a lease, at inception of the contract. The Group recognises a right-of-use asset and a corresponding lease liability with respect to all lease arrangements in which it is the lessee, except for short-term leases and leases of low value assets. For these leases, the Group recognises the lease payments as an operating expense on a straight-line basis over the term of the lease. The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted by using the Group's incremental borrowing rate. The right-of-use assets comprise the initial measurement of the corresponding lease liability. They are subsequently measured at cost less accumulated depreciation.

113. Financial guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Financial guarantee liabilities are initially recognised at their fair value. The guarantee liability is subsequently measured at the higher of the loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15. Liabilities arising from financial guarantees are included with provisions.

114. Share capital

a. Treasury shares

Acquired own shares and other equity instruments (treasury shares) are deducted from equity. No gain or loss is recognised in income statement on the purchase, sale, issue or cancellation of treasury shares. Consideration paid or received is recognised directly in equity. Incremental transaction costs of treasury share transactions are accounted for as a deduction from equity, net of any related income tax benefit.

b. Share premium

Share premium represents excess of payment above nominal value (ISK 1 per share) that shareholders have paid for shares sold by the Group.

c. Dividends on share capital

Dividends on share capital are deducted from equity in the period in which they are approved by the Group's shareholders meetings.

Notes to the Consolidated Financial Statements

115. Nature and purpose of equity reserves

a. Option reserve
The option reserve represents the cumulative charge to the income statement for options to purchase shares in the Bank granted under the Bank's Remuneration policy, which is discussed in notes 70-72.

b. Warrants reserve
The warrants reserve represents the consideration received for outstanding warrants, as disclosed in note 42.

c. Deficit reduction reserve
The deficit reduction reserve was created as a part of a share capital reduction approved by the Bank's Annual General Meeting in April 2014. The reserve has no specified purpose and can only be used with the approval of a shareholders' meeting.

d. Translation reserve
The translation reserve comprises all foreign currency differences arising from the translation of the financial statements of foreign operations, until the operations are sold, dissolved or abandoned.

e. Restricted retained earnings
According to the Financial Statements Act No. 3/2006 the difference between share of profit of subsidiary or associate in excess of dividend payment or dividend payment pending, shall be transferred to a restricted retained earnings reserve, net of tax, which is not subject to dividend payments. When shareholding in subsidiary or associate is sold or written off the restricted retained earnings reserve shall be released and the amount transferred to retained earnings.

f. Retained earnings - accumulated deficit
Retained earnings (accumulated deficit if negative) consists of undistributed profits and losses accumulated, less transfers to other reserves.

116. Earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss that is attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares, which comprise share options granted to employees and issued warrants.

117. New standards and interpretations

A number of new standards, amendments to standards and interpretations were not yet effective for the year ended 31 December 2021 and have not been applied in the preparation of these financial statements. Early adoption of new standards and amendments is not planned.

IFRS 17 Insurance Contracts has been issued but will not take effect until 1 January 2023. The Group has not assessed the impact of IFRS 17.

Notes to the Consolidated Financial Statements

118. Use of estimates and judgements

In the process of applying the Group's accounting policies, management makes use of judgements and estimates which are based on various assumptions. These judgements and estimates can affect the reported amounts of assets and liabilities, income and expense.

Assumptions and estimates are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances, and are reviewed on an on-going basis. The estimates form the basis for judgements about the carrying value of assets and liabilities that are not readily available from other sources and actual results may differ. Judgement may also be required in circumstances not involving estimates, e.g. when determining the substance of a particular transaction, contract or relationship.

The areas where the use of judgements and estimates has the most significant effect on the amounts recognised in the statement of financial position or the income statement are disclosed in this note.

a. Final liabilities from claims
The estimation of the expected final liability arising from claims made under insurance contracts is one of the Group's most critical accounting estimate. There are several sources of uncertainty that need to be considered in the estimation of the ultimate liability. The main uncertainty is in the assessment of damages of reported claims as well as assessment of unreported claims. The Group uses standard actuarial claims projection techniques to estimate the ultimate claim cost. Risk related to life insurance, especially accident insurance, depends on many factors that can make the sensitivity analysis difficult. Reference is made to note 33 and note 104 for further information.

b. Fair value of financial instruments
The fair value of financial instruments that are not quoted in active markets is determined using valuation techniques which are reviewed regularly as discussed in note 65.

c. Impairment of financial assets
As outlined in note 89, the use of estimates and judgement is an important component of the calculation of impairment losses. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience. Unforeseen events could, however, result in further impairment losses which would have a material effect on the income statement and statement of financial position.

d. Impairment of intangible assets
The carrying amount of intangible assets are reviewed annually to determine whether there is indication of impairment as disclosed in note 98. If any such indication exists the asset's recoverable amount is estimated. An impairment loss is recognised if the carrying amount of an asset exceeds its recoverable amount.

e. Deferred tax assets
Judgement is required to determine the extent to which deferred tax assets are recognised in the statement of financial position, based on the likely timing and level of future taxable profits.

Appendixes:

1. Statement on the Corporate Governance of Kvika banki hf. 2021
2. Non-Financial Information regarding Kvika banki hf.

Unaudited

Statement on the Corporate Governance of Kvika banki hf. 2021

Business strategy and values

Kvika banki hf. (hereinafter referred to as "Kvika" or the "Company") is a financial conglomerate based on four main pillars in the fields of insurance, asset management, commercial banking and investment banking. Kvika's purpose is to increase competition and simplify customers' finances by utilizing infrastructure and financial strength. Kvika's vision is to transform financial services in Iceland with mutual benefits in mind. On that journey, Kvika is guided by three values that contribute to the development of robust business relationships, long-term results, and active innovation. Kvika's values are long-term thinking, simplicity, and courage. In accordance with those values the Company places emphasis on thinking of the future and contributing to a sustainable community through active participation. Emphasis is placed on putting ourselves in the customers' shoes, rethinking things and selecting projects that provide the most long term value for customers and the Company.

Furthermore, Kvika is categorized by the Financial Supervisory Authority as a financial conglomerate and offers a wide range of financial and insurance services through key subsidiaries such as Kvika eignastýring hf. (hereinafter referred to as "KES") and TM tryggingar hf. (hereinafter referred to as "TM Insurance"). Based on robust infrastructure and exceptional talent, Kvika as a financial conglomerate, generates income through four main business segments.

Commercial Banking, which can be divided into three main areas of operation. The Banking division finances enterprises and the investments of Kvika's clients. Banking also utilises the Company's infrastructure and network to broker loans to other institutional investors. Deposit and fintech operations are mainly through the online deposit platform Auður, which offers competitive deposit rates by automating processes and offering limited services. Finally, the Banking division, offers lease contracts and loans to individuals and companies to finance cars, heavy machinery and other equipment through its brand Lykill.

Asset Management emphasises offering clients a broad range of services for investing in Iceland as well as on foreign markets. Its aim is to provide the best asset and fund management services, guided by clients' long-term interests. Asset and fund management operations are handled by Kvika's subsidiaries, mainly KES.

The investment banking segment consists of Capital Markets, Corporate Finance and the subsidiary Kvika Securities ltd. (hereinafter referred to as "KSL"). Capital Markets offers clients comprehensive securities brokerage and FX market services. The Corporate Finance division provides various types of advisory services in connection with investments and financing. Emphasis is placed on corporate acquisitions and divestments, as well as initial public offerings. KSL is a subsidiary regulated in the United Kingdom by the Financial Supervisory Authority, established in 2017. KSL's focus is on capital raising and M&A Advisory, as well as fund and asset management services. Further, KSL holds Kvika's minority stake in property lender, Ortus Secured Finance, which Kvika recently signed heads of terms to acquire a majority stake in.

Insurance operations are operated through its subsidiary, TM Insurance, which has a rich history and over 60 years of experience. TM Insurance offers a universal and highly diversified product offering to commercial and private customers and its main insurance categories include Motor, Property, Marine, Liability, Accident and Life insurance. TM Insurance operates in accordance with Act no. 100/2016 on Insurance activities and is licensed in the European Economic Area and in the Faroe Islands.

Return on equity is determined by decisions made in accordance with the Company's risk appetite, which reflects its profitability targets. Emphasis is placed on utilising equity as efficiently as possible with regard to risk. Consequently, decisions regarding the optimal composition of the balance sheet to generate income are restricted by risk appetite and funding at any given time. Kvika's target is a return on tangible equity of at least 20%.

Kvika's objective is to deliver to shareholders an annual compensation equivalent to a minimum of 25% of profit, whether in the form of dividend payments or share repurchases, under a formal buy-back programme, as authorised by applicable laws and decisions made at shareholders' meetings. When deciding on the amount of dividends or, as the case may be, the funds allocated for share buy-backs, care is taken to maintain Kvika's strong financial position, bearing in mind risks in the internal and external environment and growth prospects, to ensure that the Company maintains a solid capital ratio and liquidity for the future. Dividend payments are always subject to assessments of the opportunities offered by reinvesting profits in Kvika's operations and growth.

Sustainability and social responsibility

Kvika's values are long-term thinking, simplicity, and courage. Kvika's mergers with TM hf. and Lykill fjármögnun hf. in 2021, as well as the bank's acquisition of Netgiro hf. and Aur app ehf., have brought increased strength to the company and the operations bind minimal equity. Kvika's strategy was reviewed and updated at the end of 2021. The revised strategy stresses the bank's intension to be a transformative force in financial services guided by mutual gain. One of the guiding principles of the strategy is sustainability and social responsibility. In addition, one of the seven key goals of Kvika, as outlined in the strategy, is to have a real and measurable impact on Iceland's carbon footprint and climate issues in general.

Kvika places emphasis on sustainability in its governance structure and has, among other things, established a committee on social responsibility and sustainability, which follows up on the implementation of sustainability on a consolidated basis. Also, Kvika has established variety of policies, rules, and procedures that aim to implement sustainability thoroughly into Kvika's operations. These include an environmental and transportation policy, which emphasizes that Kvika knows the environmental impact of its operations and seeks to reduce negative impacts its operations may have. The bank has also established a Green Financing Framework and policies aimed at supporting and developing responsible product and service offering, in accordance with the bank's values and overall policies.

Kvika has been a member of the United Nations principles for Responsible Investment (UN PRI) since the autumn of 2020, and participates in various collaborations in the field of sustainability, such as being a founding member of IcelandSIF, an organization for responsible investment, a member of Festa Center of Social Responsibility, since 2017, and a sponsor of Grænvangur, a co-operational forum between the business community and the government, regarding climate issues and green solutions, since 2021.

Kvika also provides a variety of grants that have a positive social impact. In recent years, Kvika has focused on supporting UNICEF in Iceland, innovations of women with FrumkvöðlaAuður, and industrial and teacher education with Kvika's Incentive Fund. It's the bank's opinion, that education is one of the best long-term investments for communities and individuals. Environmental issues are considered in internal operations and Kvika's measured total carbon emissions have been offset.

Statement on the Corporate Governance of Kvika banki hf. 2021

The Board of Directors of Kvika has adopted code of conduct and rules on conflicts of interest to support good working and business practices. Kvika also offers its employees a healthy, sound, and positive working environment, characterised by equal opportunities. The focus is on professionalism and ensuring that decisions consider the bank´s value of long-term thinking.

Sustainability is covered thoroughly in a summary with the Board of Director's report and in the sustainability report of the bank for the year of 2021, which is published alongside this financial statement. The sustainability report is based on Nasdaq's UFS guidelines (ESG Reporting Guide 2.0), and in addition the GRI Standards are considered, and relevant indicators are answered. This is the first sustainability report that Kvika publishes in this form.

Compliance with corporate governance guidelines

Kvika is obliged to observe recognised corporate governance guidelines, pursuant to Par. 7 of Article 54 of Act No. 161/2002, on Financial Undertakings. The Company complies with the Guidelines on Corporate Governance issued jointly in February 2021 by the Chamber of Commerce, NASDAQ Iceland and the Confederation of Icelandic Employers in most respects. The Guidelines are available on the website of the Chamber of Commerce www.vi.is. Kvika's only deviation from the guidelines is that it has not appointed a nomination committee nor decided how one should be appointed.

At Kvika's AGM in 2019, shareholders agreed to entrust the Board of Directors at the time with analysing the advantages and disadvantages of appointing a nomination committee for the Company, inviting shareholders to express their views on the question and draft a proposal if this was considered advisable. The Board subsequently examined the matter and announced the results of its assessment to shareholders at the Company's 2020 AGM. Part of the analysis involved a review of actions taken by other companies and discussing the matter with shareholders and representatives of companies where nomination committees operate. In this connection, it should be mentioned that special rules apply to financial undertakings regarding assessment of the composition of their boards. Each year, the Board of Directors carries out a self-assessment with regard to its composition, assisted by external consultants. Bearing this in mind, the Board was of the opinion that the need for a nomination committee was not as great as might exist in other companies.

Furthermore, Kvika's activities comply with the recognised standards and rules of the European Banking Authority (EBA) regarding the internal governance of financial undertakings.

Regulatory framework

Kvika is a financial undertaking subject to provisions of Act No. 161/2002, on Financial Undertakings, Act No. 115/2021, on The Market for Financial Instruments, Act No 100/2016 on Insurance Activity, Act No. 2/1995 on Limited Liability Companies, the Competition Act, No. 44/2005, Act No. 114/2021, on Payment Services, Act No. 3/2006, on Annual Financial Statements, Act No.140/2018, on Measures against Money Laundering and Terrorist Financing and others. Moreover, Kvika is obliged to guarantee the safety of the personal data it processes in its activities, in accordance with Act No. 90/2018, on the Protection of Privacy as regards the Processing of Personal Data. Kvika has an operating licence from the Financial Supervisory Authority of the Central Bank of Iceland ("FME"), which supervises the activities of the Company. Kvika's activities are therefore governed by the rules and instructions of the FME and Central Bank of Iceland as well as other legal provisions regarding the financial market. More details about FME and an overview of the principal legislation and rules that apply to the Company at any given time can be found on the website of FME www.en.fme.is.

The main elements of internal control, risk management and accounting

The Board of Directors is responsible for ensuring that an active system of internal controls is in place within the Company, based on three lines of defence: The first line of defence consists of the management and the employees of business and principal units in charge of the Company's daily management and organization. Their main responsibility is to ensure the functionality and implementation of internal control measures in daily operations. The second line of defence is comprised of the internal control units of the Company, principally the Compliance Officer, who is in charge of ensuring that laws and regulations are observed, and Risk Management, which, among other things, measures and assesses risk according to the Company's criteria. Other units may also be given control functions. The third line of defence are the internal auditor and sub-committees, which ensure internal auditing is in place and functioning. Among other things, they prepare independent surveys and reports for the Board of Directors and Audit Committee.

The implementation and functioning of internal controls is the responsibility of the management of the Company and its control units. Internal control is founded on risk assessment and control measures intended to reduce risk factors in the operations of the Company. Internal control includes documented and formal procedures which Kvika's employees follow in their daily work and which are examined by the control units.

The Board of Directors determines the risk policy and risk appetite of the consolidation with rules on risk management of the financial conglomerate of Kvika, which define risk factors in Kvika's operations, including their nature and acceptable volume. The Board hires an Internal Auditor, signs his/her formal statement of duties and annually approves the audit plan. The CEO appoints the Compliance Officer with the approval of the Board and signs his/her formal statement of duties. The reports and findings of the Internal Auditor and Compliance Officer are presented directly to the Board.

The Board has established rules on risk management of the financial conglomerate of Kvika which are rules on risk and apply to Kvika as a financial conglomerate in whole. The purpose of the rules is to harmonize risk management within the consolidation to ensure it is systematic and effective and geared to enhance transparency within the consolidation's risk taking at all levels of management, from the Board of Directors of Kvika to Boards of subsidiaries, the operating units and individuals who directly participate in daily management and decision-making regarding risk. The rules on risk of the financial conglomerate of Kvika stipulate that the Company and its subsidiaries shall establish a risk policy. The risk policy of the Company and each subsidiary shall implement what is stated in the rules on risk and further define risk-taking within Kvika and each subsidiary. The Board of Directors has established a risk policy for the Company.

Kvika's Finance division prepares annual financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU, and additional requirements, as applicable, in the Act. on Annual Accounts no. 3/2006, the Act on Financial Undertakings no. 161/2002 and rules on accounting for credit institutions no. 834/2003. The annual financial statements are audited by Kvika's external auditors, Deloitte.

The CEO reports to the Board and verifies the effectiveness of internal controls and risk management in the Consolidated Financial Statements. Internal controls and risk management applied in the preparation of the Consolidated Financial Statements are organised with a view to preventing any significant deficiencies in the accounting process.

Kvika's Board of Directors and control units regularly verify the effectiveness of internal controls and risk management.

Statement on the Corporate Governance of Kvika banki hf. 2021

Composition and activities of the Board of Directors, Executive Committee and sub-committees

Each year Kvika's AGM elects a Board of Directors consisting of five board members and two alternates for a one-year term.

Directors come from varied backgrounds and all possess extensive experience and expertise. In accordance with the Company's gender equality policy and the Act on Limited Liability Companies, care is taken to ensure at least 40% representation of each gender on the Board, which is currently comprised of three men and two women. The CEO is appointed by the Board of Directors. Board meetings are generally held once a month. In 2021, 24 board meetings were held and all board members attended all board meetings.

The Board of Directors is the supreme authority in the affairs of the Company between shareholders' meetings. Its main duties are to supervise all Kvika's operations and ensure that they are in good order at all times. The Board is responsible for Kvika's policy making and shall ensure that the accounting and handling of the Company's assets are properly supervised. The Board prepares plans for Kvika in line with its objectives and in accordance with its Articles of Association and determines the strategies to be followed to achieve the objectives set. The Board appoints the CEO and supervises his work, e.g., by receiving regular reports from him at board meetings. The Board annually evaluates the CEO's work in a documented manner. The Board also represents the Company before courts and government authorities and allocates authority to sign and to commit the Company.

Kvika's Board of Directors has three sub-committees, the Audit Committee, Risk Committee and Remuneration Committee.

The members of the Audit Committee are Ingunn Svala Leifsdóttir, as chairperson, Helga Kristín Auðunsdóttir, Hrönn Sveinsdóttir and Inga Björg Hjaltadóttir. The committee operates on a consolidated basis and is intended to play an advisory and supervisory role for Kvika's Board of Directors by, among other things, ensuring the quality of financial statements and other financial information from the Company and the independence of its auditors. The committee supervises accounting procedures and the effectiveness of internal controls as well as internal and external auditing. The committee met 14 times in 2021.

The members of the Risk Committee are Guðmundur Þórðarson, who is chairperson, Sigurður Hannesson and Sigríður Mogensen. The committee's role has an advisory and supervisory role for the Company's Board of Directors, among other things, in determining its risk policy and risk appetite. The committee also monitors the organisation and effectiveness of risk management, management of credit risk, market risk, liquidity risk, operating risk, reputational risk and other risks, as the case may be. The committee met 11 times in 2021.

The members of the Remuneration Committee are Guðjón Reynisson, who is chairperson, Sigurður Hannesson and Helga Kristín Auðunsdóttir. The committee has an advisory and supervisory role for the Company's Board of Directors regarding salaries and other remuneration, ensuring that this supports its objectives and interests. The committee met six times in 2021.

All the Board's sub-committees have established rules of procedure prescribing the implementation of their tasks in detail and endorsed by the Board. The Board appoints sub-committee members by majority vote from its own ranks and nominates the chairpersons. Because of the nature of the committees, neither the CEO nor other employees can serve on them. The rules of procedure of the committees and the Board are accessible on Kvika's website www.kvika.is.

The members of Kvika's Executive Committee, in addition to the CEO are the following employees: Ármann Þorvaldsson, Deputy CEO; Ragnar Páll Dyer, Managing Director of Finance and Operations; Magnús Ingi Einarsson, Managing Director of Banking; Bjarni Eyvinds, Managing Director of Capital Markets; Lilja Jensen, General Counsel; and Baldur Stefánsson, Managing Director of Corporate Finance. More details about the Executive Committee are accessible on Kvika's website www.kvika.is.

Kvika has not established a specific policy on the diversity of its Board of Directors, Executive Committee and senior management with regard to age, gender or educational and professional background. However, the Company has adopted a policy for assessing the eligibility of its directors and CEO as provided for in EBA guidelines and pursuant to Art. 52 of Act No. 161/2002, on Financial Undertakings, provisions of Rules No. 150/2017, on assessment of eligibility of managing directors and directors of financial undertakings and the guidelines. The composition of the Board is also dealt with in Kvika's Articles of Association, which state, among other things, that its Board shall be so comprised that its members jointly possess adequate expertise, skills and experience to understand the activities of the Company, including key risk factors. The Articles also state that the proportion of each gender on the Board and among alternates shall not be lower than 40%. Kvika has also adopted a Human Resources and Equality Policy. According to the Company's equality policy, non-discrimination and diversity shall characterise all its operations. All employees should have the opportunity to make good use of their abilities at work and be valued on their own merit, have equal opportunities and enjoy the same rights in their work and for career advancement, regardless of gender, age and origin.

The CEO can provide more detailed information on the rules of procedure and the operations of the board and sub-committees.

Information on Board members

Sigurður Hannesson is the chairman of the Board. He was appointed to Kvika's Board of Directors in March 2020. He was born in 1980 and is currently the Director General of the Federation of Icelandic Industries. From 2013-2017, Sigurdur worked as a managing director of Kvika asset management (previously MP Bank). In 2015, Sigurdur was the Vice-Chairman of the Government Task Force on lifting of capital controls and in 2013 the Chairman of the Expert Group on household debt relief. From 2010-2013, Sigurdur worked as CEO of Jupiter fund management company, now Kvika Asset Management, and in Capital Markets at Straumur Investment Bank from 2007-2010. Sigurdur holds a DPhil degree in mathematics from the University of Oxford, a BS degree in mathematics from the University of Iceland and is a certified securities broker. Sigurður also sits on the boards of NSA Ventures, Grænvangur (Green by Iceland), Reykjavík University, Auðna-Tæknitorg ehf., Akkur SI, SI 1 ehf., Sundaboginn slhf., Íslenski byggingarvettvangurinn, Seapool ehf., BBL 39 ehf. and the Icelandic Cancer Society. Sigurður owns 8,550,107 shares in the Company through shareholding in the private limited company BBL 39 ehf., but does not have interest links with major clients, competitors or big shareholders in the sense of the Corporate Governance Guidelines.

Statement on the Corporate Governance of Kvika banki hf. 2021

Guðmundur Þórðarson is the deputy chairperson of the Board. He was appointed to Kvika's Board of Directors in March 2017. Guðmundur was born in 1972. He graduated from the University of Iceland with a Cand. oecon business degree in 1997. He has also completed a securities brokerage and asset management exam in the UK. Guðmundur's main focus is on managing his own investments. From 1997 to 2000 he worked in Asset Management at Landsbréf hf. From 2000 to 2003, he worked as a specialist in the development and corporate advisory division of Íslandsbanki hf. From 2003 to 2007 he worked as Managing Director of Corporate Finance at Straumur fjárfestingarbanki hf. Guðmundur also sits on the boards of Hedda eignarhaldsfélag ehf., Skel Investments ehf. and Attis ehf., as well as serving as an alternate in the board of Bílaleiga BTF ehf. Guðmundur holds 66,750,000 shares in the Company through the private limited company Attis ehf. Guðmundur does not have interest links with major clients, competitors or big shareholders in the sense of the Corporate Governance Guidelines.

Guðjón Reynisson was appointed to Kvika's Board of Directors in March 2018. He was born in 1963 and works as an independent investor and board member. Between 2008 and 2017 he served as CEO of Hamleys of London. From 2003 to 2008, he served as managing director of the 10-11 stores. From 1998 to 2003 he was the managing director of the sales division of Tal, an Icelandic phone company. He graduated with an MBA degree from the University of Iceland in 2002. He graduated with an Operations and Business degree from the Continuing Education Study of the University of Iceland in 1999 and also graduated with a degree as a licensed physical education teacher from the University of Iceland in 1986. Guðjón has been on the board of directors of Festi hf. since 2014, of Securitas hf. since 2018 and of Dropp ehf. since 2020. Guðjón controls 10,410,789 shares in Kvika through his private limited company, Hakk ehf., but does not have interest links with major clients, competitors or big shareholders in the sense of the Corporate Governance Guidelines.

Helga Kristín Auðunsdóttir was born in 1980. Helga Kristín holds a doctor's degree in Law from Fordham University in New York. Helga Kristín graduated with a BS degree in Business Law from Bifröst University in 2004 and with a Master's degree in Law from the same university in 2006. She graduated with an LL.M degree in Law from the University of Miami, with a focus on international business law and contracts. Helga Kristín also studied law at University of Thessaloniki, in Greece. In her doctoral studies at Fordham University she researched hedge fund investments and what factors influence how they act as shareholders in listed companies. Helga Kristín has worked as a director and lecturer at Bifröst University for the past nine years. Prior to that, she worked as a lawyer at FGM/Auðkenni, now part of the Central Bank of Iceland, as a lawyer at Stoðir hf., prior FL Group, and as a lecturer at the faculty of law at University of Miami in 2010-2011. Helga Kristín was a board member of TM hf. from 2020 and was an appointed alternate on the Board of Directors of Tryggingamiðstöðin hf. in 2012-2015. Helga Kristín does not own shares in the Company and does not have interest links with major clients, competitors or big shareholders in in the sense of the Corporate Governance guidelines.

Ingunn Svala Leifsdóttir was appointed to Kvika's Board of Directors in September 2021. Ingunn was born in 1976. She graduated with a BS degree in Business from the University of Iceland in 1999, with a focus on accounting and finance, and with a Cand. Oecon business degree from the same University in 2001, with a focus on accounting and management. Ingunn Svala completed the Advanced Management program (AMP) from the IESE Business School in New York in 2018. Ingunn Svala currently works as the executive director of operations at Reykjavík University and sits on the university´s executive board. Ingunn Svala has extensive experience of serving as a board member. She has served as a board member of Slippurinn Akureyri ehf. since 2015, as a board member of the logistics company Parlogis ehf. since 2014 and as a board member of Ósar – lifeline of health hf. since 2021. Ingunn Svala sat on the Audit Committee of VÍS in 2019 to 2021 and was a board member of Líftryggingafélags Íslands (Lífís) from 2017 to 2021. Ingunn Svala has also established and operated her own business, including in accounting and real estate. Ingunn Svala also has extensive experience from the financial sector. She worked for the Kaupthing´s Resolution Committee as Chief Financial Officer from 2009 to 2011 as well as working as a Global Business Controller in Investment Banking at Kaupþing bank in 2007 to 2009. Ingunn Svala also worked within the Actavis Group PTC consolidation in 2006 to 2007 as a CFO for four subsidiaries, namely Actavis hf., Medís ehf., Actavis Group hf. and Actavis Group PTC ehf. Ingunn Svala does not own shares in the Company and does not have interest links with major clients, competitors or big shareholders in in the sense of the Corporate Governance guidelines.

The Board of Directors considers all board members to be independent directors as defined by the Corporate Governance Guidelines.

Sigurgeir Guðlaugsson and Helga Jóhanna Oddsdóttir are alternate members of Kvika's Board of Directors. In the opinion of the Board, they are also independent members of the Board of Directors within the meaning of the Corporate Governance Guidelines.

Main factors in the Board's performance evaluation

The Board of Kvika annually evaluates its performance. It evaluates the performance of tasks and work of the Board for the previous year. The focus of the assessment is on strategic planning, disclosure and future vision, the size and composition of the Board, performance of Board members, the work of sub-committees and performance of the CEO. The development of the Company is examined with a view to assessing whether it is line with objectives. Following the annual performance assessment, the Board defines tasks in areas where improvements are needed. The last performance assessment was conducted in January 2022. The Board also regularly conducts special self-assessments on its composition in accordance with the guidelines of the European Banking Authority (EBA), and last did so in January 2022.

Information on the CEO of Kvika and his main duties

Marinó Örn Tryggvason became CEO of Kvika in May 2019. Marinó was born in 1978 and from August 2017 acted as Kvika's Deputy CEO. Prior to this, Marinó worked in asset management at Arion banki and the bank's forerunner from 2002. Between 2014-2017, Marinó was the Deputy Managing Director of Asset Management at Arion banki and between 2007 and 2014 was the head of institutional asset management. Marinó sat on the board of the Vörður insurance company between 2016-2017. Marinó holds a BSc in business studies from the University of Iceland and possesses a diploma in securities trading. Marinó controls 3,426,559 shares in Kvika, and he also has subscription rights for shares in the Company. Marinó has also entered into a call option agreement with Kvika in accordance with the employees' general stock option plan. He does not have interest links with major clients, competitors or major shareholders as defined by the Corporate Governance Guidelines.

The CEO oversees the daily operations of Kvika and in so doing follows the policies and instructions which have been laid down by the Company's Board of Directors. Daily operations do not include unusual or major arrangements. The CEO shall ensure that Kvika's accounts are kept in accordance with laws and customs and that the Company's assets are handled in a secure manner. The CEO appoints and dismisses employees of the Company. Furthermore, he is obliged to follow all of the Board's instructions. The CEO shall provide Kvika's external auditors with all requested information.

Statement on the Corporate Governance of Kvika banki hf. 2021

Information on violations of laws and regulations, determined by the relevant supervisory body or adjudicating entity

Kvika has not been subject to withdrawal, revocation or dismissal of registration, authorization, membership or permissions to perform certain trades, operations or work. No legal or arbitration proceedings which may have significant effects on the Company or the Group were ongoing or pending at the end of the year.

In 2021 Kvika made an agreement on settlement with the Financial Supervisory Authority regarding violations of paragraph 2 of Art. 8, paragraph 1 of Art. 14, paragraph 1 of Art. 15 and paragraph 1 of Art. 21. of the then applicable Act No. 108/2007 on Securities Transactions regarding marketing and sale of a certain financial instrument in the years 2018 and 2019. In the settlement, Kvika agreed to pay a fine of the amount of ISK 18,000,000.

Communications between shareholders and the Board

Information is provided to shareholders on a non-discriminatory basis and is mainly limited to shareholders' meetings or the communication of harmonised information to all shareholders simultaneously. News of the Company's operations are posted on Kvika's website and press releases are issued when newsworthy events in the Company's operations take place. A detailed presentation of the Company's operations over the past year is also provided at its AGM and information on the Company's operations is published in Kvika's annual report and financial statements.

This statement on the corporate governance practices of Kvika banki hf. was reviewed and approved by the Board of Directors on 24 February 2022.

Non-Financial Information regarding Kvika banki hf.

About Kvika

Kvika banki hf. (hereafter “Kvika” or the “Bank”) is a public company listed on the main list of Nasdaq OMX Iceland. Kvika’s subsidiaries are TM Insurances hf. (“TM”), Kvika Asset Management hf. (“Kvika Asset Management”), GAMMA Capital Management hf. (“GAMMA”), Aur app ehf. (“Aur”), Netgíró hf. (“Netgíró”) and Kvika Securities Ltd. (“KSL”) in the UK (together the “Group”). The Group´s non-financial disclosure is limited to the Group´s operations in Iceland, not in the United Kingdom. Policies have to some extent been co-ordinated between countries, however, not measured indicators so far.

The Group operates four business segments, Asset Management, Commercial Banking, Insurance Services, and Investment Banking. Kvika‘s operations aim at increasing competition of Icelandic financial services and simplifying the finances of its clients by using infrastructure, financial strength and offering diversified services. The Group provides businesses, investors and individuals with comprehensive investment banking, insurance, and asset management services, as well as selected retail banking services.

The Group´s values are long-term thinking, simplicity, and courage. Kvika’s mergers with TM hf. (“TM”) and Lykill fjármögnun (“Lykill”) in 2021, as well as the Bank’s acquisition of Netgiro and Aur, have brought increased strength to the Group and the operations bind minimal equity. The Group´s strategy was reviewed and updated at the end of 2021. The revised strategy stresses Kvika´s intension to be a transformative force in financial services guided by mutual gain. One of the guiding principles of the strategy is sustainability and social responsibility. In addition, one of the seven key goals of Kvika, as outlined in the strategy, is to have a real and measurable impact on Iceland’s carbon footprint and climate issues in general.

In meeting the challenges of the Covid-19 pandemic, recommendations of national authorities have been followed to ensure protective hygiene measures and the safety of employees. A special working group has monitored and managed reactions to the pandemic within the Group. Most employees worked remotely part of the year, using online meeting services and communication software. This development has brought increased flexibility, and at the same time reduced environmental impacts as the frequency of employee travels by air and road has diminished.

The monitoring of the health and safety of employees, and the associated communication, has been increased, e.g., through online employee meetings. Operations have continued successfully despite the Covid-19 pandemic. Providing clients with the option of signing contracts and other documents electronically, whenever possible, was one of the proposed solutions to meet the challenges of the pandemic.

From the beginning of the Covid-19 pandemic, Kvika has provided societal support through offering temporary deadline extensions to loan payments for companies and individuals, offering approval as second mortgagee following changes in conditions due to the pandemic. The Bank has also participated in supportive actions of the Icelandic government to soften the blow on borrowers due the pandemic.

Policies

Kvika has published a social responsibility policy that was approved by the bank ‘s executive management in October 2020 and shall be revised at least every four years. The policy is intended to offer a common vision of the Bank ‘s priorities concerning investments and business practices, society, human resources and the environment.

Other relevant policies that have been adopted and related to sustainability, are a policy on human resources and equality, environmental and transport policy, policy on responsible lending and investment, policy on responsible product and services offering, code of conduct for suppliers, and code of conduct for employees.

As the Group operates in large part in Iceland, which has clear laws and a legal framework for human rights issues, a specific policy for human rights has not been deemed necessary. Kvika‘s committee for social responsibility and sustainability is responsible for ensuring that policies related to the Group´s journey towards increased sustainability and social responsibility are followed, while the project manager of sustainability follows up on the committee´s work. The composition of the committee is across the units of the Group and includes the deputy CEO of Kvika.

As outlined in Kvika‘s ownership policies, the Bank, as the mother company, defines the general principles for its subsidiaries on governance and matters concerning sustainability and social responsibility. These include, amongst others, human rights, and environmental issues. Kvika encourages its subsidiaries to be open to innovation that enhances sustainability, notably in investments and business practices.

In October 2021 Kvika issued its first Green Financing Framework, which outlines the Bank’s policy for environmentally responsible financing and lending. The framework has received a positive second-party opinion from the global ratings firm Sustainalytics. Kvika has offered green car loans through its brand Lykill, and these loans fall under the terms of the Green Financing Framework as eligible assets. Following the issuing of the framework Kvika started offering green deposit accounts through its brand Audur. In addition, Kvika issued its first green bond in December 2021, also under the terms of the framework.

The Group supports Icelandic and international strategies to combat climate change as well as the goal of the Icelandic governments to be climate neutral by 2040. In September 2020 Kvika signed a declaration of intent - Investment for a Sustainable Recovery - along with the government and other key parties on the Icelandic financial market.

Kvika is a member of the UN PRI, on behalf of the Group, and a founding member of IcelandSIF, the Icelandic association for responsible investments.

Additional information on the scope, status, and impact of the Group on environmental, societal, and human resource matters can be found in Kvika’s sustainability report, which is issued alongside this annual account. The report follows Nasdaq’s ESG Reporting Guide 2.0 and, to a limited extent, the GRI Standards.

Non-Financial Information regarding Kvika banki hf.

Due Diligence

Kvika operates in accordance with laws and regulations that apply to the operations. Kvika has established rules on the prevention of conflicts of interest that aim to increase credibility and protect the Bank's reputation and prevent or deal with conflicts of interest that may occur, among other things, in connection with the offering of investment or additional services. Prevention of conflicts of interest has also been strengthened through the issuance of rules on gifts, rewards, and on incentives, as well as through policies on reputation risk and conduct risk, rules on division of fields of work, and rules on employees' own business. These rules and policies are implemented on a consolidated basis, and in addition to the code of ethics, lay the foundation for Kvika's protection against corruption and bribery.

The Bank has as well-established rules and appropriate procedures and surveillance for measures against money laundry and terrorist financing, in accordance with applicable Law. Kvika performs risk assessments on all of its operations and all clients of the bank must complete an appropriate due diligence form before establishing a contractual relationship. For regular transaction surveillance, Kvika uses the Lucinity software, which uses modern technology and artificial intelligence to detect suspicious behavior.

During 2021 Kvika underwent an audit and received a certification from the audit company BSI that the company's management system for information security is in line with the international information management standard ISO 27001. Kvika is also certified against the equal payment standard IST 085:2012, since 2020.

One of the three sub-committees of Kvika´s Board of Directors is the audit committee, which serves an advisory and monitoring role for the Board, amongst its responsibilities is ensuring the quality of annual accounts and other financial information of Kvika, as well as the independence of the Bank's auditors. The committee supervises the process for the issuing of financial accounts, the effectiveness of internal control and the internal and external auditing process. In June 2021 the Board of Directors approved the updated rules of procedure for Kvika's audit committee.

The external auditors are elected at the annual meeting, and these are auditors of Deloitte in Iceland, which has been the company's auditing firm since 2016. In addition to financial auditing, Deloitte will also provide a limited assurance of the non-financial information included in Kvika's sustainability report for 2021. This entails providing an opinion of selected information and indicators (ESG/GRI) that are included in the report and outlining the development of the key ESG topics that have been selected through Kvika's materiality assessment by Kvika´s committee on social responsibility and sustainability.

Key risks and risk management associated with non-financial information

Operational risk and sustainability risk

Operational risk is the risk associated with the potential financial loss due to insufficient internal processes, systems, and human mistakes or due to external events. Such risk includes social or governance factors, such as inadequate protection against cyber-attacks and data protection or inappropriate payments to managers.

Kvika has adopted a risk policy and rules on risk management, as well as procedures for managing operational risk. The Operations Committee regularly submits proposals to the Bank's Executive Committee for adjustments and/or improvement projects to reduce Kvika's operational risk and follows up on improvement projects. Risk Management, in collaboration with the Operations Committee, sees to the collection, classification and documentation of operating incidents, together with an evaluation of their severity and possible financial loss. The Bank emphasizes that key processes in connection with operational risk are documented and reviewed regularly.

Sustainability risk, which is now included under operational risk, concerns the risk of being negatively affected by factors related to environmental and climate issues, social or governance factors. Following the recommendations of the Task Force on Climate-related Financial Disclosures (TCFD) sustainability risk is evaluated in the context of governance, strategy, risk management, metrics, and targets.

Climate risk, along with social and governance factors, form the framework for the risk management of this area. Climate risk can be divided into two key categories, on the one hand physical risk directly linked to climate change and, on the other hand, transition risk which concerns measures taken to meet this risk.

Work is underway on further enhancing Kvika's response to sustainability risk and integrating the relevant factors into risk management and related risk processes in line with the recommendations of the TCFD. Risk management informs Kvika´s Board of Directors of climate related risks in the bank's annual ICAAP report and climate related matters are also part of the general agenda of the Bank´s Board.

The risk committee is one of three sub-committees of the Board of Directors. The risk committee's role is to provide advice and monitoring on behalf of the Board. Its updated rules and procedures were approved in May 2021. The committee monitors the organization and effectiveness of risk management, manages credit risk, market risk, solvency risk, operational risk, reputation risk and other risks that may be relevant.

Key non-financial indicators and performance

Environmental issues

Kvika is a commercial bank that focuses on and is leading in fintech solutions, with sustainability as one of its guiding principles. As an example of the result of automation of processes and services, Kvika, through its brand Lykill, was the first company in Iceland to register mortgage bonds electronically. The service has several societal and environmental benefits including reduction of the use of paper, transportation, and time.

Other technical solutions of Kvika, such as solutions of the brand Audur and the subsidiaries Netgiro and Aur, have been developed from the start using digital technology and without operating branches with the associated carbon footprint. In addition, the insurance company TM is also very advanced in digital solutions and offers, amongst others, fully electronic claims handling.

Non-Financial Information regarding Kvika banki hf.

The table below shows greenhouse gas emissions in 2021 and employees' emission demand.

Greenhouse Gas Emission	
Scope 1 and 2 (volume in tonnes of CO2 equivalent)	**52.2 tCO2í**
Scope 3 (volume in tonnes of CO2 equivalent)	**160.1 tCO2í**
Employee emission capacity	**671.5 kgCO2/per full time position**

Further information on the relevant ESG and GRI indicators related to environmental matters can be found on page 19 and pages 22-23 in Kvika's sustainability report for 2021.

Social issues

With the merger of Kvika with TM and Lykill, and with the acquisition of Netgiro and Aur, the Group has further enhanced its societal support and increased the amount of grants for various projects. The total amount of grants in 2021 was ISK 87,168,268. Kvika also renewed its collaboration with UNICEF in Iceland during the year. The organization consider the partnerships with Kvika to be one of their most fruitful collaborations.

Every year a workplace survey is sent to employees of the Group with questions about employee engagement, work satisfaction, stress, equality, work-life balance, bullying and harassment among other topics. Following such surveys, the results are analyzed, and an action plan is developed. A workplace survey was sent to employees at the end of 2021. Among results was an average level of employee satisfaction of 4.38 out of 5, and average employee engagement was 4.05.

Turnover of full-time employees at the Group in 2021 was 11.5%, which is in some part due to a re-organization within the Group following Kvika's merger with TM and Lykill. The proportion of women in the company is 47% and the proportion of women in the position of directors and managers is 36%.

In December 2021 all employees were offered to participate in a stock option program which was approved by Kvika's Board of Directors on 10 November 2021, and by tax authorities on 9 December 2021.

Further information about social aspects and the relevant ESG and GRI indictors can be found on pages 11-13 and on page 23 of Kvika's sustainability report for 2021.

Governance

Kvika follows approved guidelines on corporate governance in accordance with the Act on Financial Undertakings no. 161/2002. The company conducts its corporate governance in accordance with the Corporate Governance Guidelines issued in 2004 by the Iceland Chamber of Commerce, Nasdaq Iceland and the Confederation of Icelandic Employers, and updated in July 2021.

Further information about aspects related to governance and the relevant ESG and GRI indictors can be found on pages 20-21 and on page 24 of Kvika's sustainability report for 2021. Also in the annual governance statement published in the annual accounts and on Kvika's website.