

MEMORANDUM

The Danish Financial Supervisory Authority
12 May 2020

Statement on inspection at Realkredit Danmark A/S

In December 2019, the Danish Financial Supervisory Authority (the FSA) conducted an inspection at Realkredit Danmark A/S.

The inspection comprised a review of the monitoring of LTV ratios (the amount of a loan in relation to the value of the underlying property), arrears and impairment charges, large loans and operational risks as well as governance, including the group structure and the use of outsourcing.

Summary and risk assessment

Realkredit Danmark A/S has outsourced a substantial part of its areas of activity to Danske Bank A/S. The FSA assesses that the setup has built-in organisational weaknesses that, in general, can compromise the independence of the established lines of defence. To a certain degree, Realkredit Danmark A/S has tried to compensate for this, but the FSA is generally of the opinion that a reassessment of the organisation and handling of risks is needed as a result of the extensive outsourcing. Furthermore, the FSA finds that the contractual basis of the outsourcing is inadequate and that certain outsourcing arrangements must be considered to be the outsourcing of significant areas of activity subject to increased outsourcing requirements in the form of monitoring, controls, etc.

This being the case, the FSA issued an order to Realkredit Danmark A/S to the effect that certain outsourcing contracts must be considered to be the outsourcing of significant areas of activity and must be managed in accordance with the relevant rules and that the outsourcing contracts concluded must generally be extended to include the requirements for the tasks, obligations, controls and reporting to be undertaken by Danske Bank A/S. Realkredit Danmark A/S was also ordered to specify the performance of tasks in relation to outsourcing in the form of descriptions of duties and business procedures.

Realkredit Danmark A/S has outsourced the compliance function in its entirety. The FSA observed that compliance activities were not undertaken in all areas at Realkredit Danmark A/S and that the compliance function performed control tasks in the form of access right controls. The FSA assesses that the compliance function, in relation to that task, cannot be an independent function in the second line of defence. The FSA therefore issued an order to Realkredit Danmark A/S to the effect that a chief compliance officer be appointed under the auspices of Realkredit Danmark A/S with responsibility for ensuring that compliance activities are undertaken in all areas and that the compliance function may not perform tasks compromising the independence of the compliance function.

The FSA observed that, in its LTV ratio monitoring, Realkredit Danmark A/S did not update the fair value of a loan in its calculation of the requirement for supplementary collateral until an up-to-date valuation of the underlying property was available. The method applied by Realkredit Danmark A/S to determine the size of the requirement for supplementary collateral thus did not capture ongoing increases in the LTV ratio of a loan on the basis of increases in the fair value of the loan. Realkredit Danmark A/S therefore received an order to correctly calculate the collateral provided for the outstanding mortgage-covered bonds on an ongoing basis.

At 31 December 2019, Realkredit Danmark A/S calculated its solvency need ratio at 10.4%. The total capital ratio was 31.1%, which, in addition to the solvency need ratio, was to cover a buffer requirement totalling 6.5%.