Pillar 3 Disclosure

Aegon Bank N.V.

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1. Introduction

This report should be read in conjunction with the financial statements in the 2014 Aegon Bank Annual Report to comply with the disclosure requirements, to the extent that certain disclosures are not included in the financial statements. There are no significant differences between the scope of consolidation for prudential purposes compared to the accounting scope of consolidation as reported in the Annual Report. The information in this section has not been audited by the external auditors of Aegon Bank NV.

1.1. Regulations

Since the introduction of the Basel II Capital Framework, codified in the Dutch Financial Supervision Act [*Wet financieel Toezicht*], requirements have been set to promote transparency of financial institutions. These requirements are contained in Pillar 3 ‘Disclosures and Market Discipline’ of the Basel II Capital Framework.[1] The Basel III Accord was adopted in 2010 and consequently translated into regulation by the EU in the Capital Requirement Regulation (CRR) and a Capital Requirement Directive IV[2]. Specifically, Title II of CRD IV (Technical Criteria on Transparancy and Disclosure) relate to disclosure requirements. Institutions are required to apply the new rules from 1 January 2014, with full implementation on 1 January 2019.[3]

The ICAAP (Internal Capital Adequacy Assessment Process) and the SREP (Supervisory Review and Evaluation Process) are part of the Basel II framework. Basel II is the abbreviation for the second Basel Capital Framework drawn up by the Basel Committee on Banking Supervision.[4] It has been embedded in European[5] and Dutch[6] legislation and regulations. The European Banking Authority (EBA) has drawn up guidelines for the interpretation of ICAAP. At AEGON Bank N.V., the ICAAP is interpreted on the basis of these guidelines.

The ICAAP is a continuous monitoring process that has been put in place by AEGON Bank N.V. to ensure capital adequacy relative to its material risk exposure and risk profile. As part of this ongoing and forward-looking process, AEGON Bank N.V. identifies, assesses and, where possible, quantifies material risks. Stress testing and forward-looking elements play an important role in the process. AEGON Bank N.V.’s management determines the amount of capital to be held to cover material risks relative to its risk profile on the basis of its internal standards.

In the course of the ICAAP process, AEGON Bank N.V. not only assesses its current capital adequacy but also estimates its capital adequacy for the coming years. This analysis therefore projects new activities as well as current activities. At AEGON Bank N.V., capital adequacy is assessed on a Capital Planning sheet. Once the Capital Planning document has been drawn up, the outcomes are

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[1] Specifically, revised Banking Directive (2006/48/EC), Annex XII (Technical Criteria on Disclosure), Part 2 (General requirements) and Part 3 (Qualifying requirements for the use of particular instruments or methodologies).
[2] CRD IV is made up of (i) Capital Requirements Directive (2013/36/EU) (CRD) which must be implemented through national law; and (ii) Capital Requirements Regulation (575/2013) (CRR), which is directly applicable to firms across the EU.
[3] In January 2015, the Bank for International Settlements published its “Revised Pillar 3 disclosure requirements”, specifically focusing on disclosure requirements related to Pillar 1 of the Basel framework (credit risk, operational risk and market risk). The implementation date of these requirements is year-end 2016.
[4] International Convergence of Capital Measurement and Capital Standards, A Revised Framework, November 2005.
[5] Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions (recast). Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions (recast).
[6] Dutch Financial Supervision Act [*Wet op het financiële toezicht*] (Wft) and the related Prudential Rules Decree [*Besluit prudentiële regels*].

continually reviewed against this document, which is fine-tuned where necessary by AEGON Bank N.V. management.
The Basel III requirements result in increased required levels of capital and liquidity with the aim of making the banking sector more stable and the financial system more robust. The present ICAAP 2014 takes the Basel III requirements and indicators into account. As of December 31, 2014 AEGON Bank N.V. already met the new requirements.

Basel II
Basel II is based on three pillars which have the combined aim of increasing the stability of banks.

Pillar 1: Regulatory Capital (minimum capital requirement)
Pillar 1 refers to the minimum capital to be held by banks to cover credit, operational and market risks. No capital buffer needs to be carried for interest rate risks in the non-trading book, i.e. the banking book, under Pillar 1.

Pillar 1 approach chosen at AEGON Bank

- AEGON Bank N.V. Executive Board has chosen to use the Standardised Approach (SA) to credit risk. This approach means that, depending on the asset and rating category, a standardised credit risk weighting is applied to the assets concerned.[7]
- To determine the capital requirement for operational risk, AEGON Bank N.V. Executive Board has adopted the Basic Indicator Approach (BIA). Accordingly, the capital requirement for operational risk is defined as 15% of average net interest and non-interest income for the last three financial years.[8]
- Market risk only applies to trading book. As AEGON Bank N.V. does not undertake trading activities or hold trading positions, and therefore does not have a trading book. As such market risk does not apply.

Pillar 2: Supervisory Review
As explained above, the ICAAP and SREP constitute the Pillar 2 of Basel II. Under Pillar 2, AEGON Bank N.V. Executive Board and process owners must perform an integrated analysis. The risks identified, including Pillar 1 risks, have to be measured and aggregated, after which it is possible to make a link to the capital requirement. The Executive Board will then continuously monitor and, where necessary, escalate these risks.

Pillar 3: Disclosures and market discipline
Finally, Basel II lays down requirements for the disclosure of information to the public. These requirements are set out in Pillar 3 ‘Disclosures and Market Discipline’. AEGON Bank N.V. is implementing the Pillar 3 requirements by publishing this document as a specific schedule to the financial statements.

Basel III
Basel III is a comprehensive set of reform measures, developed by the Basel Committee on Banking Supervision, to strengthen the regulation, supervision and risk management of the banking sector. These measures primary aim to: (i) improve the banking sector's ability to absorb shocks arising from financial and economic stress, (ii) improve risk management and governance, and (iii) strengthen banks' transparency and disclosures.
Basel III rules do not, for the most part, supersede the guidelines known as Basel I and Basel II; rather, they will work alongside them.

[7] The sum of the products of the credit-risk weight multiplied by the carrying value results in the risk-weighted assets (RWA) associated with the credit risk.
[8] The capital requirement multiplied by 12.5 produces the amount of operational risk-weighted assets (RWA).

2. Risk Governance and Risk Appetite

2.1. Risk Governance

This section deals with internal governance at AEGON Bank N.V. in relation to risk management.

Supervisory Board

With respect to risk governance, the supervisory board is involved in the following activities:

- the Executive Board proposes its Aegon Bank N.V. Risk Appetite (see subsection 2.2) for approval at the Supervisory Board. Topics such as the risks related to Aegon Bank N.V. business activities, the assessments, measurements and controls that are in place, as well any significant changes in these systems are discussed. Any changes in Risk Appetite during the year will need to be approved by the Supervisory Board.
- The Supervisory Board discusses the Risk Profile and assesses whether the capital allocation (ICAAP) and liquidity required (ILAAP) are aligned with the Risk Appetite.

Executive Board

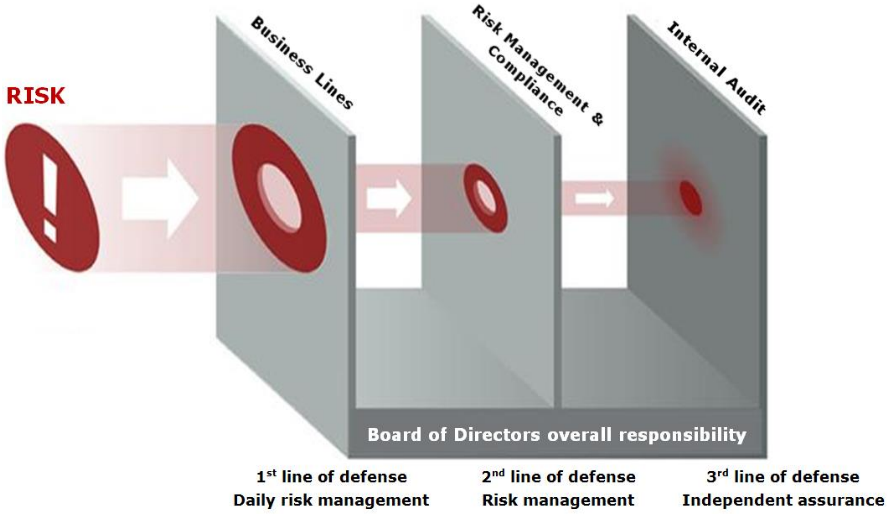
The Executive Board of AEGON Bank N.V. is ultimately responsible and oversees risk management at AEGON Bank N.V. The Executive Board ensures they are informed on the risks associated with AEGON Bank N.V. business activities, the changes in risk profile due to its business strategy and/or changes in market conditions and their consequences on its solvency and liquidity. It ensures risks are identified, allocated within the organisation, managed and monitored. Part of this process involves making sure that effective risk management and control systems are in place. The Executive Board of AEGON Bank N.V. is responsible for establishing its Risk Framework, Risk Governance structure and Risk Appetite (see Section 2.2). Each of these frameworks are discussed, reviewed, updated and approved on an annual basis. Furthermore, the Executive Board presides the Asset and Liability Committees (ALCOs) where decisions are made to actively manage Aegon Bank N.V. financial risks (see subsection 2.1.5).

Three lines of defense

The process owners are responsible that risks associated with its business activities are identified, analysed and active risk management is implemented within Aegon Bank N.V..

The risk governance structure is based on a “3 lines of defense” model, also used at AEGON Nederland and the AEGON Group. In this model, AEGON Bank N.V. has defined three lines of defense within risk management and each function is given a suitable position within the organisational structure. Each line has its own specific responsibilities with regard to risk management.

Figure 1 Relations Overview: “3 lines of defense”



A fourth line (external auditor) and fifth line (DNB/AFM) could also be added as external lines of defense. The external auditor provides an objective external assessment of the risks that exist and the effectiveness of the measures taken with regard to risk management and internal auditing. External regulatory bodies provide the framework within which AEGON Bank N.V. must act to manage risks. In addition, external regulatory bodies oversee compliance with legislation and regulations.

The responsibilities of the different functions within AEGON Bank N.V. are shown in the RACI-table below. A RACI-model is a matrix where responsibilities of various tasks are assigned to various functions.

Table 1: RACI model Aegon Bank

	Executive Board	BM[9]	FRM & ORM[10]	Internal Audit
Identify risks	A	R	C	
Asses risks	A	R	C	
Determine risk treatment	A/R	R	C	
Risk monitoring	A	R	R	
Risk reporting	A	R	R	I

R = Responsible C = Consulted
A = Accountable I = Informed

2.1.1. First line: process owners

First-line risk management consists of the management measures which have been taken in the course of activities to provide services. This risk management takes place in AEGON Bank N.V. operational processes and is organised by the process owners.

- Process owners are responsible for managing the activities of their process or business unit;
- Process owners are responsible for identifying relevant risk factors, implementing risk control and risk monitoring;
- effective management measures to reduce risks, so that the management is in line with the risk that the department intends to incur;
- management is responsible for ensuring that the design and implementation of management measures comply with AEGON Bank N.V. specified policies and, where applicable, with policies of AEGON Nederland and the AEGON Group.

2.1.2. Second line: supporting functions

Second-line risk management is performed by risk management that are independent of the process owners. The functions are (1) Financial Risk Management; (2) Operational Risk Management and (3) Compliance.

The second line sets risk management policies and standards. Based on the policies and controls it tests whether the first-line daily processes are conform the set policies and standards. It provides training and supervision and is responsible for monitoring processes and issuing regular risk reports. It also has a supporting role in monitoring that policy and standards are implemented.

Financial Risk Management
Financial Risk Management (FRM) is responsible for independently identifying and assessing material financial risks of Aegon Bank N.V.. It develops policies that are in line with external regulators (DNB) and internal stakeholders (Aegon NL and the Aegon Group). Specific tasks are:

- Model validation

[9] BM stands for Business Manager in his/her role as process owner. This is the first line of defense.
[10] FRM stands for Financial Risk Management; ORM stands for operational risk management.These are the second lines of defense.

- Identify material financial risks related to Aegon Bank N.V. business activities, for example by performing stress tests;
- Develop policies to monitor and actively manage risk;
- Assess the impact of financial risks and provide advise how to actively manage those risks;
- Identify Risk Appetite (see subsetion 2.2.)
- Assess whether risks taken are in line with agreed upon Risk Appetite (see subsection 2.2)
- Independent advice on risks of new initiatives;

Operational Risk Management

Operational Risk Management (ORM) is responsible for facilitating, coordinating and communicating risk management strategy within AEGON Bank N.V.. ORM advises the management teams of Aegon Bank and Knab and the executive board with respect to its risk management policies. ORM focuses on helping process owners to identify and manage operational risks. This is done by facilitating Risk & Control Self-Assessments and helping to implement management measures, providing assistance to determine Key Risk Indicators (KRIs) and providing accurate management information on risks that AEGON Bank N.V. faces. One of ORM's objectives is to create and raise risk awareness within AEGON Bank N.V.. Specific ORM tasks are:

- Advise management on risk issues;
- Identify Risk Appetite (see subsection 2.2);
- Draft and maintain Risk Framework;
- Perform Risk & Control Self-Assessments;
- Analyze and report incidents;
- Report to Operational Risk Committee;
- Report to Risk & Audit Committee;
- Raise risk awareness on operational risks throughout the organization.

Functions such as, Security, Fraud and Compliance are seen as subfunctions within ORM.

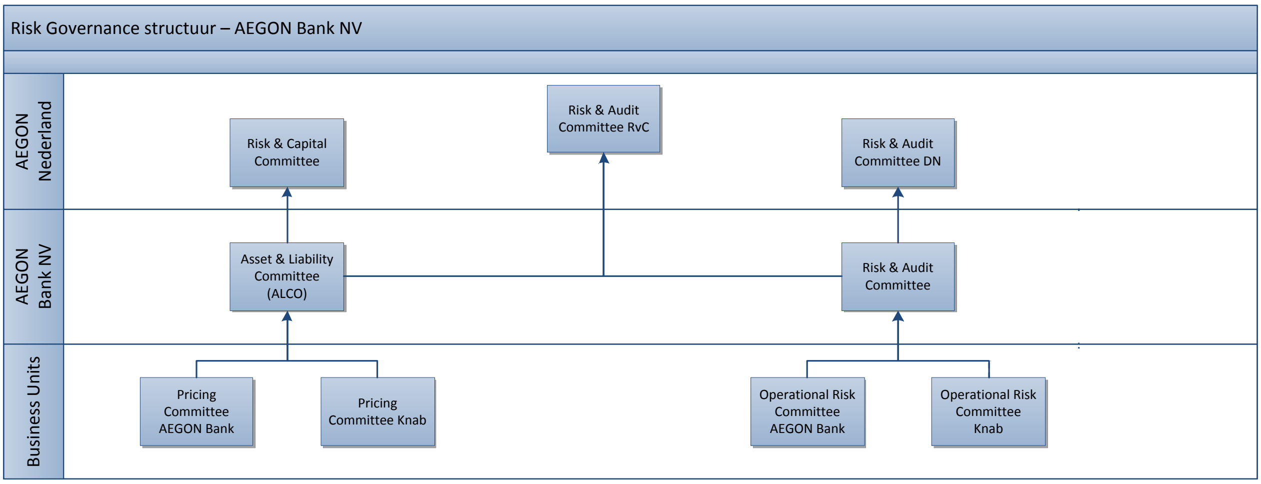
2.1.3. Third line: internal audit

Third-line risk management is provided by Internal Audit Nederland (IAN). IAN investigates the effectiveness and efficiency of business processes, the quality of information supplied and risk management within AEGON Bank N.V. It combines operational, financial and ICT aspects of business processes in order to meet management's requirements in terms of process and risk management. In order to fulfill this responsibility, IAN is authorised to conduct an audit at any time to establish whether ICAAP is in place and operating, even if this is outside the predetermined audit scope. The results of this audit are presented to the chairman of AEGON Nederland N.V., the Risk & Audit Committee, the Executive Board of AEGON Bank N.V. and the Chief Risk Officer of AEGON Bank N.V.

2.1.4. Committee structure

It is AEGON Bank' N.V. policy to manage its operational risks in an integrated manner. In order to do so efficiently, AEGON Bank N.V. has divided risks into financial risks and operational risks and established a separate committee structure for these two categories of risks. The Asset & Liability Committee ("ALCO") at AEGON Bank N.V. plays a key role in the management of financial risks. ALCO's tasks and responsibilities are explained in a subsequent section. As can be seen in the figure below, the pricing committees provide the ALCO with information so that the ALCO can act accordingly.
For operational risks, it has been decided to treat the two business lines, Aegon Bank and Knab, separately, because of different systems, different employees and different processes – the causes of operational risk. In operational terms, these committees report to AEGON Bank NV's Risk & Audit Committee ("RAC"). Both the ALCO and the RAC have an operational link to similar bodies at AEGON Nederland. This structure can be shown as follows:

Figure 2 Relationships between AEGON Bank committees



2.1.5. Financial Risk Committees

As discussed in the previous subsection, the ALCO plays a key role in managing Aegon Bank N.V. financial risks. The Executive Board is ultimately responsible for risk & capital management at AEGON Bank N.V.. The Board determines the Risk Appetite in relation to its capital adequacy. Risk monitoring and decisions made with respect to financial risks are delegated to the ALCO. The operational ALCO contains at least one member of the Executive Board, Head of Capital & Risk Management, capital managers and financial risk manager.

Frameworks

First and foremost, the ALM policy is governed by the legal frameworks such as the Dutch Financial Supervision Act (especially the Basel II framework), Basel III and the internal framework of Enterprise Risk Management of AEGON NV.
Frameworks for the ALM policy were determined in cooperation with the Executive Board of AEGON Nederland N.V. and the Risk and Capital Committee (RCC). Finally, the risk appetite and solvency requirement determined by AEGON Bank N.V. Executive Board are considered as frameworks.

The Strategic ALCO meets on a quarterly basis where senior members of Risk NL, Aegon NL, Treasury and Asset Management are present to ensure methodologies used are consistent across business units. In this setting, strategic subjects such as the risk policies, methodologies, long- and medium term financing are discussed.
The Tactical ALCO meets on a monthly basis. As a standard part of the tactical ALCO, financial analyses based on monthly data are reviewed and discussed as part of the monitoring process. In these monthly meetings, representatives from Aegon NL, Treasury and Asset Management are present.
The Operational ALCO reconvenes on a weekly basis where cash and investment positions are reviewed as part of the weekly monitoring process. Other day-to-day issues are also discussed in this setting.

Responsibilities

AEGON Bank N.V. ALCO is responsible for:

- The implementation of AEGON Bank N.V. Risk & Capital Management within the RCC framework
- The implementation of Asset & Liability Management (ALM) policy, the strategic and operational process of balance sheet control: giving direction to and controlling (1) financial risks (interest rate, credit and liquidity risks), (2) internal capital and (3) solvency, within the specified framework. Among others, stress testing is an important management tool
- The optimisation of the return on AEGON Bank N.V. equity within the specified framework.

2.1.6. Operational Risk Committees

Operational Risk Committee (ORC)

Both Aegon Bank and Knab have an ORC. The ORC assesses, values the impact and monitors the operational risks of all business lines. In addition, the ORC monitors and ensures that incidents and audit findings are followed up. ORC's tasks are described in subsection 2.1.2 above. ORC focuses on operational risks.

The frequency of Risk Committee meetings is initially once per month. This frequency can vary:

- If a meeting of the Risk & Audit Committee is held in the relevant month
- On the instructions of the Executive Board.

Each process owner is invited to the ORC meetings, as well as the Executive Board. This way, each representative has the opportunity to report to the ORC the risks currently affecting the processes. The scope, tasks and responsibilities of the ORC are stated in a charter.

Risk & Audit Committee (RAC) of Aegon Bank

The RAC focuses on all individual operations of Aegon Bank and Knab as well as on key operational risks of Aegon Bank N.V. It monitors and evaluates the management of key operational risks, taking the risk appetite into account. Representatives of Aegon NL and Internal Audit are invited. Aegon Bank N.V. RAC meets on a quarterly basis.

The RAC of Aegon Bank N.V. has a functional reporting line to the RAC of Aegon Nederland.

2.2. Risk Appetite

The appetite for risk is an inherent part of entrepreneurship. As a result of its general business operations, AEGON Bank N.V. endorses and accepts a certain degree of risk. AEGON Bank N.V. has developed clear frameworks for financial risks.

Risk Appetite is *"The aggregate level and types of risk our organization is willing to assume within its risk capacity to achieve its strategic objectives and business plan."*

Aegon Bank N.V. thinks it is important to be transparent with regards to the risks it is willing to take when pursuing its strategic goals. The Risk Appetite, elaborated with measurable tolerances and limits, enables making risk-based decisions at every level of the organisation. Moreover, the Risk Appetite is an important starting point for the Internal Capital Adequacy Assessment Process (ICAAP), to be discussed later in section 3.1.

2.2.1. Risk Appetite Process

Risk Appetite is determined by mission, vision and strategic targets of Aegon Bank N.V.. Explicitly expressing risk appetite has the following purposes:

- Supports strategic decision-making and accountability;
- Enable Executive Board to control and manage risk effectively;
- To streamline existing risk management processes (risk based);
- To raise risk awareness in the entire organisation;
- To comply with internal and external regulation and to meet the increasing information needs from internal and external stakeholders.

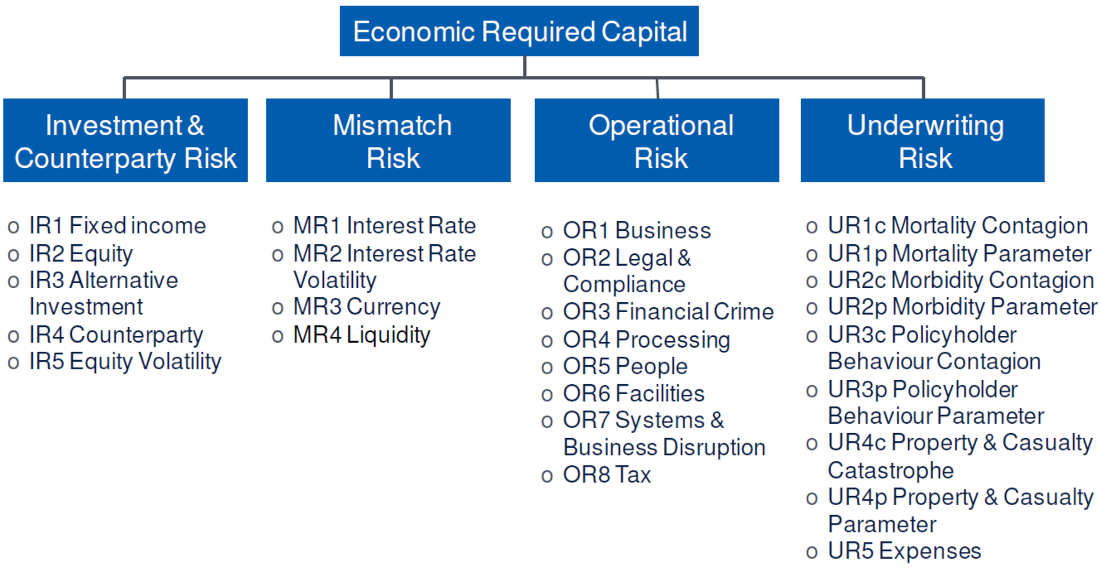
The Risk Appetite process is a continuous and iterative process, as shows in figure 3 below. The first step in the Risk Appetite process is to determine the strategic goals and the thereby associated risks. Aegon Bank N.V. Risk Appetite is reviewed and approved by the board of supervisors on an annual basis.

Figure 3 Risk Appetite Process

The second step is to determine the risk categories. For every risk category a risk tolerance is determined.

AEGON adopts a holistic approach to its risk management. The risks encountered by AEGON can be divided into four main categories, as shown in the diagram below.

Figure 4 Summary of risks defined within AEGON Group



This risk classification is also used in the Risk & Control Self Assessments by process owners. Therefore, there is a direct link between the various processes and their associated risks. Therefore, the agreed upon risk appetite by the Executive Board can be linked to the daily processes. Where possible, key risk indicators are linked to these processes.
By including the losses as a result of operational risk to processes and risks, total realized losses can be determined and discussed at the next evaluation of the risk appetite.

Although underwriting risk is generally not material for Aegon Bank NV, as AEGON Bank does not sell insurance under its own name, Aegon Bank N.V. is sensitive for client behaviour (e.g. prepayment of mortgages and in-and outflow of savings products) and rising expenses.

The third step involves translating the risk appetite from strategic level to operational level by defining risk limits and key controls.

The fourth step relates to implementing a governance structure to monitor, manage and perform management action with respect to risks, risk limits and key risk indicators.

The second line of defense performs the risk monitoring function and reports the results in accordance to the risk governance structure. Reporting occurs according to the risk commission structure as depicted in figure 2 above.

As the last step of the cyclus, should the risk taken fall outside the beforehand set risk limits, the Executive Board can decide to take corrective actions. The Executive Board can take advice from the ALCO (financial risks) and RAC (operational risks).

2.2.2. Risk Appetite Areas

With the set risk appetite and strategy in mind, it is possible to set out tolerances for each of the risk categories identified. The tolerances were chosen so that it can be reasonably stated that AEGON Bank N.V. can fulfill its obligations and promises to its stakeholders (customers, shareholder, regulatory bodies, staff and business partners). Tolerances and the associated limits and standards are established by the Executive Board as described in the articles of association, but are also partly dependent on standards and bandwidths imposed by the regulatory body and the internal shareholder AEGON.

The strategic plan of AEGON Bank NV, builds on the mission of AEGON to enable our customers to make decisions for a healthy financial future and results in risk appetite statements in the areas of:

- **Financial strength** - plays a major role in enabling AEGON Bank to compete in key markets.
- **Continuity** – of safeguarding our clients assets under plausible extreme events.
- **Risk culture** - for operational excellence and to treat our stakeholders fairly.
- **Risk Balance** – to manage concentrations of risk and to encourage risk diversification.

With the set risk appetite and strategy in mind, it is possible to set out risk tolerances for each of the risk categories identified. The tolerances were chosen so that it can be reasonably stated that AEGON Bank N.V. can fulfill its obligations and promises to its stakeholders (customers, shareholder, regulatory bodies, staff and business partners).

Risk tolerance and the associated limits and standards are established by AEGON Bank N.V. Executive Board as described in the articles of association, but are also partly dependent on standards and bandwidths imposed by the regulatory body and the shareholder AEGON NL/Group.

Financial strength
As described above, AEGON Bank N.V. is aiming to create a risk profile in which it is possible to have sufficient liquidity and solvency available at all times for all of its stakeholders. AEGON Bank N.V. focuses on a number of measures by means of which to guarantee its financial condition:

- S&P: A rating objective of an Ax long-term issuer rating from Standard & Poor's[11]
- BIS ratio: An internal BIS ratio standard of 15.2%
- Core Tier 1 ratio: An internal standard of 10.5%
- Economic Capital Model: Market value of equity is higher than Economic Required Capital
- Leverage ratio: A leverage ratio[12] greater than or equal to 3.6%.

[11] An Ax rating means an A+, A or A- rating.
[12] This ratio (regulatory capital/total assets) does not become mandatory until 2018. In advance of the final implementation, regular monitoring has been taking place since the second half of 2011.

- Net Stable Funding Ratio: A ratio greater than 110%
- Liquidity Coverage Ratio: A ratio greater than 130%

Continuity
AEGON Bank N.V. has defined a number of extreme scenarios to establish whether AEGON Bank N.V. can continue to keep its promises to its stakeholders in these circumstances . These scenarios are (among others) “Reverse Stress Test scenario” and a “Nightmare scenario” for liquidity risk. These scenarios are based on the stress scenarios used by AEGON Group. Where necessary, the scenarios are adjusted slightly so that they also comply with the guidelines that the regulatory body imposes on stress scenarios for banks. Furthermore a recovery plan has been defined with trigger points for several scenarios that can vary in unfolding speed and in impact. For every scenario, mitigating measures have been developed to prevent resolution. These mitigating measures have an effects on the following aspects:

- Liquidity
- Solvency
- Operational
- Reputation

Risk Culture
A strong risk culture is an essential element in achieving a situation in which risks are in proportion to benefits. Specific risk appetite statements concerning operational risk have been included to support AEGON’s ERM framework. A positive risk and control culture does not restrict the development of new business, even where it involves an increased initial risk. However, the organization must be aware of the risk and treat it in a controlled way, in view of the risk appetite as established by the Executive Board and Supervisory Board. A key method of raising risk awareness is to carry out Risk and Control Self-Assessments (RCSAs). The purpose of an RCSA is to identify and assess risks at strategic level or within individual processes, to identify the controls put in place to mitigate these risks and to assess the effectiveness of the controls. The input for the RCSAs is supplied by staff and management. An RCSA consists of four steps: desk research, interviews, workshops and reporting.

Risk culture is a component of organizational culture. In a strong risk culture, people at every level manage risk as an intrinsic part of their jobs. Rather than being risk averse, they understand the risks of any activity they undertake and manage them accordingly. Such a culture supports open discussion about uncertainties, encourages employees to express concerns, and maintains processes to elevate concerns to appropriate levels. The first line of defense at AEGON Bank N.V. are the process owners. A process owner is responsible for organizing a process, identifying the inherent risks and developing (jointly with FRM & ORM) controls and reports. It is important that this responsibility does not stop at the boundaries of a department but continues through the rest of the organization. Because it is specified who is responsible for what, it is immediately clear who can be contacted if there are any questions. Working together with FRM & ORM, the process owners have an important task in improving the risk culture and in translating risk appetite into everyday policy: they must get the message across to everyone within a process that they are the first line of defense against undesirable risks. Everyone is encouraged to suggest improvements to the process and ban undesirable risks. The Executive Board also plays an important part. Staff meetings are held to provide an insight into the risks that AEGON Bank N.V. faces and the risk treatment formulated to control the risk.

Risk Balance
The fourth and final area, risk balance, contains details of the standards and bandwidths used by AEGON Bank in its risk management system. The risk balance is aimed at ensuring concentration of risk is well managed in the organization while at the same time promoting risk diversification. This serves as the primary driver for specific risk limits that apply to all major risk types at group level. The risk category limits provide direction towards the development of the risk type limits. The sum of risk types limits within one risk category should stay within defined percentage of aggregated limits. In the risk strategy, it is assessed, per risk type, whether the risk serves a customer need and Aegon Bank has the competence to manage the risk, what AEGON Bank’s risk preferences are and whether the risk fits within AEGON Bank’s risk bearing capacity.

Aspects assessed to define the risk preferences are

- Level of return expected to earn when running a risk
  - Presence of a risk premium for taking the risk
  - Liquidity and level of competition in the underlying market
- AEGON Bank's and AEGON Bank's customers interest are aligned
- The amount of the risk AEGON Bank has already on the balance sheet
- The characteristics of the risk
  - Pro-cyclicality
  - Horizon
  - Tail risk
  - Speed of risk
  - Liquidity/hedge-ability
  - Diversification benefits with other risks and within risk type

3. Capital Management Organization

3.1. Capital Planning

The capital planning process lies at the heart of the ICAAP. It links the company's mission statement, strategy and risk profile to operational capital management. AEGON Bank N.V. mission statement and strategy are key factors in defining its risk profile (Section 3.2). The mission statement, strategy and risk profile together are the input for operational capital management (Section 3.3), which sets the requirements, risk limits and risk bandwidths.

As part of its operational capital management, AEGON Bank N.V. identifies, assesses and, where possible, quantifies material risks. Stress testing plays an important role in the process (Section 3.3.8). In accordance with internal requirements, AEGON Bank N.V. determines the amount of capital to be held to cover material risks relative to its risk profile, both for the current situation and for the years ahead, again by reference to its mission statement and strategy. Taking the company's mission statement, strategy and risk profile as a basis, the capital planning process annually produces a target-linked capital planning document (Section 3.3.4) for the medium term (five years).

The assumptions underlying capital planning are regularly reviewed and adjusted throughout the year. Capital planning is also updated monthly on the basis of actual outcomes, and reported to the Executive Board and ALCO to allow continuous monitoring (Section 3.3.5). Adjustments may be made on the basis of expected developments relative to actual outcomes (Section 3.3.6), where necessary in accordance with existing contingency plans (Section 3.3.7).

3.2. Prudent Risk Management

The exceptionally turbulent developments on the financial markets in the past few years have shown that 'trust', or rather the 'erosion of trust' due to cash shortages or poor solvency, can play a dominant role. This has strengthened the belief of AEGON Bank N.V. Executive Board that it is of vital importance that we must regain, retain and bolster the trust of our customers and other stakeholders at all times. This belief is reflected in the company's mission statement, core values, strategy, risk profile and targets. In terms of our risk profile, this means that we seek to maintain our rating target, which is an Ax long-term issuer rating from Standard & Poor's.[13]

Aside from the rating target, this is also reflected in the company's investment policy, more specifically the mandate that imposes limitations on the asset categories that can be invested in. Given its Ax rating from Standard and Poor's, AEGON Bank N.V. uses a confidence interval of 99.9% and one-year horizon in determining its internal capital for specific risks. This means that only in the event of a shock of the type occurring once every 1000 years there is likely to be an insufficient capital cushion to absorb a specified risk. AEGON Bank N.V. also applies add-ons (also known as prudential filters) to its internal capital requirements for unquantified risks in its Economic Capital Model.

[13] An Ax rating means an A+, A or A- rating.

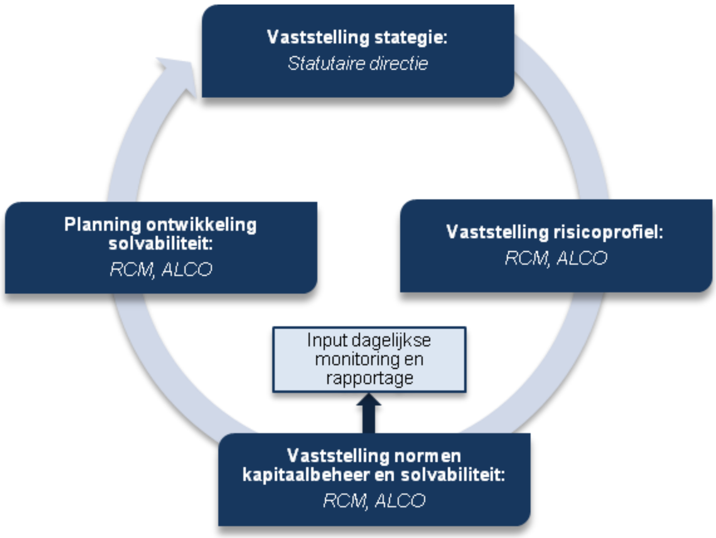
3.3. Operational capital management

This section explains how we have organised the operational side of the capital planning process and how the various roles have been assigned. It also sets out the targets and bandwidths in terms of our solvency objective and provides details of our contingency policy. Finally, we take a closer look at stress testing, which is fundamental to proper operational capital management.

3.3.1. Capital planning process

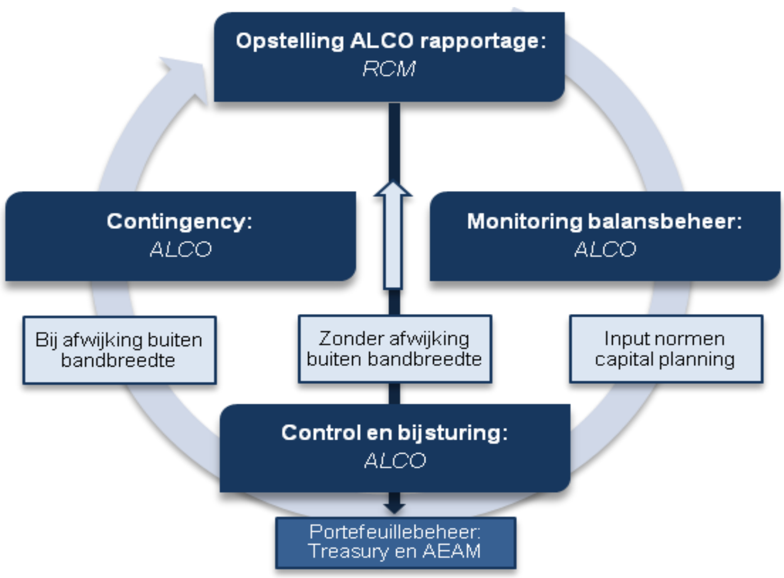
The figure below shows the annual capital planning process.

Figure 5 Annual capital planning process



The figure below shows the capital planning process on a monthly basis.

Figure 6 Monthly capital planning process



In addition to monthly monitoring, solvency fluctuations are also monitored on a weekly basis. If any deviations are identified, ALCO will meet, urgently if necessary, to discuss appropriate measures. The guiding principles and assumptions are assessed and adjusted on a quarterly basis after consulting Bank's Executive Board.

3.3.2. Role division

The table below shows the responsibilities for the capital planning process by the various company bodies.

Table 2 Responsibilities for capital planning process, by company body

Body	Responsibilities
Executive Board of AEGON Bank N.V	▪ Ultimately responsible for ICAAP and ILAAP ▪ Defines strategic goals ▪ Defines risk profile in partnership with ALCO ▪ AEGON Bank's Executive Board has delegated Asset & Liability Management to ALCO
ALCO (Asset & Liability Committee)	▪ Responsible for ALM policy within the limits of its mandate ▪ Responsible for strategic and operational processes involved in balance sheet control ▪ Responsible for maximising return on equity ▪ ALCO monitors solvency fluctuations on a monthly basis and carries out balance sheet management on the basis of reports drawn up by RCM ▪ Reviews risks against tactical and strategic bandwidths ▪ If set bandwidths are exceeded, ALCO instructs AAM to sell or purchase securities to bring solvency to required level ▪ Defines strategic portfolio ▪ Adopts strategic risk budget ▪ Establishes investment mandate for AAM ▪ Defines strategic bandwidths for all types of risk
RCC (Risk & Capital Committee)	▪ RCC is responsible for giving direction to and controlling AEGON Nederland NV's risk exposure, capital and returns. In that capacity, RCC defines frameworks for AEGON Bank N.V. in a Policy Directive
AAM (AEGON Asset Management)	▪ AAM manages AEGON Bank N.V. investment portfolios by pursuing an active investment policy based on a clear vision of markets. In doing so, AAM operates within the limits of the investment mandates set out in the asset management agreement between AEGON Bank N.V. and AAM[14].
Risk & Capital Management	• Risk & Capital Management draws up reports for use by ALCO. RCM also monitors on a daily basis movements in solvency, economic capital and risk exposure. If the minimum requirement is exceeded, this is reported and ALCO will convene urgently.

3.3.3. Requirements

AEGON Bank N.V. Executive Board and ALCO annually define the medium-term requirements for liquidity, solvency and the composition of capital. AEGON Bank N.V. also sets requirements in terms of its dividend policy, investment policy, interest rate risk exposure and the potential impact of hypothetical stress scenarios.

Liquidity

The internal liquidity requirement is based on stress testing. The current internal requirement stipulates that there must be sufficient cash available, or that sufficient assets can be liquidated in the

[14] The arrangements made between AEGON Bank NV and AAM are set out in an SLA.

short term to withstand a nightmare scenario (please see section 3.3.8 for more details). Moreover, on a monthly basis, Aegon Bank N.V. monitors whether its liquidity coverage ratio (LCR) fulfills its internally set target.

Solvency

The regulator reviews the ICAAP, including the capital planning process, and sets the amount of Pillar 2 capital, also known as SREP capital. Although the SREP capital may equal the economic capital (internal capital) that is based on the entity's ICAAP, the regulator may find this to be inadequate and require additional capital (prudential filter). The Dutch Financial Supervision Act imposes solvency requirements that are based on the ratio between the SREP capital on the one hand, and risk-weighted assets on the other. The regulatory available capital comprises Tier 1 and Tier 2 capital and must be at least 8% of Pillar 1 risk-weighted assets. AEGON Bank N.V. applies an internally set signalling limit of 15.2%. Below this limit, measures must be taken in accordance with the contingency policy (Section 3.3.7). The Financial Supervision Act also sets requirements for the capital cushion to be carried under Pillar 2 (Section 0**Error! Reference source not found.**).

Composition of capital

CRR article 92 sets requirements for the composition of regulatory capital, which comprises core capital (Tier 1) and supplementary capital (Tier 2). Supplementary capital is only included in the regulatory capital to the extent that it does not exceed core capital. Basel III prescribes (i) a minimum of 4.5% Common Equity Tier 1 capital ratio; (ii) a minimum of 6% of Tier 1 capital ratio; and (iii) a minimum total capital ratio of 8%. AEGON Bank N.V. internal requirement for its capital is to consist of 100% Tier 1 capital, barring special circumstances. Within Tier 1 Capital, Aegon Bank N.V. mainly has core Tier 1 capital, and a marginal amount of Additional Tier 1 Capital: the Knab client participations. Combined with its BIS ratio requirement, this means that AEGON Bank N.V. intends to hold at least 15.2% Tier 1 capital. Based on the current stricter internal Tier 1 requirement, AEGON Bank N.V. already conforms to the stricter composition of capital requirements under Basel III.

Dividend policy

AEGON Bank N.V. and its operating companies are subject to statutory restrictions on dividend payouts. The amount available for the payment of dividends comprises shareholders' equity less the issued capital and less the statutory reserves as reported in AEGON Bank N.V. financial statements.

Moreover, as advised by the Dutch authorities, Aegon Bank N.V. can only issue dividends if it can still fulfill its minimal capital requirements, even when economic and financial conditions deteriorate.

Each year, in consultation with its shareholder, AEGON Bank N.V. determines whether there is space for a dividend payment, taking into account future growth expectations. As growth expectations are high, there are no dividend payouts in 2014 and 2015.

Investment policy

AEGON Bank N.V. strategic ALCO annually determines the target balance sheet composition. Aegon Nederland provides a Policy Directive, a framework in which Aegon Bank N.V. investment portfolio has to fulfill. A high-quality rating class distribution and a desired amount of liquid assets is encouraged at the same time. The management of the bond portfolio is outsourced to AAM. Aegon Bank N.V. provides a medium-term strategic bond portfolio to AAM, including targets and risk limits for authorised asset categories. In 2013, it was decided to add consumer loans to the asset mix, next to mortgages, a treasury portfolio and a bond portfolio to provide further diversification.
With respect to 'responsible investment', Aegon Bank N.V. follows the policy from the Aegon NL.

Risk control

As part of its integrated risk control, AEGON Bank N.V. sets requirements for a variety of risks, including interest rate, credit and concentration risks. See Section 2.1 (Risk Governance), Section 3.3.8 (stress testing) and Section 0 (internal capital).

3.3.4. Capital planning

Capital planning at AEGON Bank N.V. is the consolidated aggregate of the capital planning of all banking activities under the AEGON Bank and Knab labels. AEGON Bank N.V. capital planning document provides details of performances and five-year projections for:

- movements in profit and equity under IFRS;
- capital requirements under Pillar 1 and the BIS ratio;
- internal capital requirements under Pillar 2 for the various risks and total internal capital after diversification;
- movements in own funds at market value;
- the capital surplus;
- a variety of ratios, such as return on equity (ROE).

Capital planning allows an assessment to be made of historic, current and future capital adequacy levels. Capital planning is underpinned by the company's mission statement, strategy and risk profile. These are the driving forces behind the revenue model. In practical terms, this is reflected in the adoption of guiding principles, assumptions and projections for:

- Expected volumes of savings deposits, investments and service fees;
- Asset mix and expected premium for credit risk;
- Expected shifts in the yield curve and premium for interest rate risk;
- Expected movements in margins and cost base;
- Expected movements in specific risk exposures.

The assumptions underlying capital planning are regularly reviewed and adjusted throughout the year, partly on the basis of actual outcomes (Section 3.3.5 Monitoring).

3.3.5. Monitoring

Capital planning is also updated monthly on the basis of actual outcomes, and reported to the Executive Board and ALCO. Other reports prepared for operational capital management purposes and which contribute to the ongoing monitoring of liquidity, capital base, risks and capital adequacy include:

- daily interest rate risk reports
- weekly reports on ratios and market value movements
- monthly reports on consumer loans and mortgages
- monthly stress testing reports
- monthly concentration risk reports
- COREP, FINREP, and other DNB filings

Adjustments may be made on the basis of expected developments relative to actual outcomes (Section 3.3.6), where necessary in accordance with existing contingency plans (Section 3.3.7).

3.3.6. Control

Control involves taking action when the cash position, risk exposure or capital adequacy threatens to exceed signaling levels. This may range from - alert – limits being exceeded to statutory requirements threatening to be breached. Possible actions include:

- Intensifying the monitoring process through more wide-ranging, in-depth or more frequent reporting;
- Improving the cash position by selling securities, obtaining cash under repurchase agreements, etc.;
- Selling assets to reduce (credit risk) exposures and capital requirements;
- Buying or selling derivatives to reduce interest rate or currency risk.

3.3.7. Contingency procedure

Actions of the kind referred to in the previous section generally require a decision by ALCO. However, certain shortfalls may potentially be so serious that ALCO needs to convene urgently and the method for making adjustments and escalating the matter needs to be known beforehand. All of this is described in the AEGON Bank Recovery Plan, which shows the contingency procedure in place at AEGON Bank N.V. and lists a set of potential management actions and their expected impact on various ratios.

3.3.8. Stress testing

AEGON Bank N.V. has a comprehensive stress testing framework in place. The framework gives a description of AEGON Bank N.V. policy on stress testing, provides details of the stress scenarios applied and defines stress limits. The impact of the stress scenario's are described in terms of decrease in market value equity and decrease in BIS-ratio. The stress limits are set with regards to the recovery capacity of Aegon Bank N.V.. In the Recovery Plan, Aegon Bank N.V. laid out several scenario's and for each scenario its recovery capacity. The recovery capacity in the worst of these scenario's determines the stress limits: The stress limit is set as the minimum required BIS ratio minus the recovery capacity. As such, for each stress scenario falling within the stress limit, Aegon Bank N.V. believes that it can still recover to at least the minimum required BIS ratio within a year. The recovery capacity, and hence the stress limit, is set by the Strategic ALCO every quarter. Once every month, ALCO reviews the outcomes of the stress tests against the limits. The framework provides guidance for stress testing and reporting on the following risks:

Interest rate risk
Several stress scenarios are used, in particular:
1) Earnings at risk
2) Parallel (upward and downward) shift of 200 bps
3) Non-parallel shifts of the curve (via principal component analysis)

As explained in the previous paragraph, recovery capacity and the BIS ratio are analysed within this stress test framework.

Credit risk
Several stress scenario's are used, in particular:
- Extreme credit spreads widening; for each asset class, depending on the quality (rating) of the investment a stress spread add-on is added.
- Mortgages scenario; this stress scenario only applies to the mortgages. This scenario contains a spread widening combined with an extra loss on mortgages (both PD and LGD are stressed).
- Consumer loans scenario; this stress scenario only applies to the mortgages. This scenario contains a spread widening combined with an extra loss on mortgages (both PD and LGD are stressed).
- Rating migration scenario: in this scenario all positions in the investment portfolio of AegonBank N.V. are downgraded 1 quality step (1 full letter), which has a direct impact on the risk weight of the assets.

Concentration Risk
The following stress tests are applied concerning concentration risk:
- Name concentration: in this scenario it is assumed the 10 largest counterparties go into default.
- Geographic concentration: this scenario contains an economic downturn in Portugal, Italy, Ireland, Greece, Spain, Belgium and France.
- Sector concentration: in this scenario a new banking crisis rises. This leads to spread widening combined with a rating downgrade.

Macro-economic downturn
In addition to applying defined stress test scenarios to individual risk categories, AEGON Bank N.V. also conducts simultaneous macroeconomic shocks on a variety of risk components.The following stress scenario's are used:
- Downward shift of yieldcurve combined with credit spread widening and a stressed loss on mortgages and consumer loans

- Upward shift of yieldcurve combined with credit spread widening and a stressed loss on mortgages and consumer loans
- Downward shift of yieldcurve combined with credit spread widening and a stressed loss on mortgages and consumer loans and a rating downgrade of the investment portfolio
- Upward shift of yieldcurve combined with credit spread widening and a stressed loss on mortgages and consumer loans and a rating downgrade of the investment portfolio

Besides these macro-economic scenario's also some history based scenarios are in place:

- Euro stress scenario: in this scenario Greece is stepping out of the Euro and returns to the Drachme.
- Crisis of fall 2008; in this scenario the parameters are based on the period of 9 September 2008 - 1 December 2008.
- Black week 2008: This scenario is also based on the period of fall 2008, but only contains the 5 worst days (for the financial markets) of this period, i.e. 6-10 October 2008.

Liquidity risk

Key liquidity risk components for AEGON Bank N.V. are the liquidity of its investments and the fact that a very large portion of savings deposits are on-demand deposits. The imagined stress scenarios may be described as follows: (1) Aegon Bank N.V. is not able to refinance maturing capital market transactions (2) an unexpected and sudden loss of trust in AEGON Bank N.V. among customers leading to unexpected and very rapid withdrawals; and (3) an unexpected and extreme decline in the liquidity of assets, combined with a uniform default rate of 10% applied to all assets, meaning that the investment portfolio can be liquidated less quickly and at considerably lower market values. AEGON Bank N.V. holds sufficient liquid assets and securities to withstand this hypothetical 'nightmare' scenario at all times. AEGON Bank N.V. specified stress scenarios and associated parameters are currently in line with Basel III. This means that the stress scenarios are partly based on the Liquidity Coverage Ratio (LCR), as specified in the Basel III framework, within a horizon of one month. Where the horizon is three months or more, the Net Stable Funding Ratio (NSFR) approach is adopted for the stress scenarios. Historical bank runs are also being taken into account in the recalibration of the liquidity stress scenarios.

In addition to analysing the Nightmare scenario, Aegon Bank N.V. also performs reverse stress testing where in combination with an interest rate decrease the maximimum outflow percentage of savings is calculated so that there is still sufficient liquidity within the first year. Three interest rate scenarios are analysed:

- no interest rate decrease,
- 1% interest rate decrease
- 2% interest rate decrease.

Interest rate decrease scenarios are chosen for reverse stress tests because interest rate decreases hurt Aegon Bank N.V. liquidity position the most. In order to hedge interest rate risk Aegon Bank N.V. holds a portfolio of payer swaps, as the duration of liabilities (primarily savings products) is lower than its assets. When interest rate decreases, payer swaps will decline in value and collateral needs be placed immediately. While interest rate decreases cause asset values to increase, not all assets are liquid assets (e.g. mortgages).

The above mentioned stress scenario's are last reviewed as of December 2014. Reviews take place on an annual basis. When market conditions change, the ALCO can request additional stress scenario's to be run.

4. Internal capital

4.1. Methodology chosen

AEGON Bank N.V. calculates its Pillar 2 internal capital in accordance with the 'Pillar 1 Plus' method. This method involves calculating the internal capital required for each type of material risk, with the amount of capital required to cover credit risk and operational risk being based, in principle, on the Pillar 1 requirements (regulatory capital), as supplemented by additional internal capital to reflect circumstances and risks that are specific to AEGON Bank N.V.. Accordingly, no internal models have been developed for credit risk or operational risk.
AEGON Bank N.V. has chosen the 'Pillar 1 Plus' method, based on the following criteria:

- Small size and complexity of the institution
- Compliance with regulatory requirements
- Consistency and possibility of reconciling regulatory and economic capital
- Common practice within the banking industry.

The types of risk for which capital must be maintained according to internal requirements are identified on the basis of an ongoing process of risk identification, assessment and quantification. ALCO takes centre stage throughout this process. Risk identification and risk assessment cover at least the following material types of risk:

1. Credit risk
2. Concentration risk
3. Incomplete NHG-payout risk
4. Country risk
5. Operational risk
6. Modelling risk
7. Conglomerate risk
8. Special litigation risk
9. Strategic enterprise risk
10. Interest rate risk in the banking book
11. Hedging risk

Table 4 below shows the captial buffer set for each type of identified risk. These types of risk are discussed in the following sections. Other residual risks are deemed to be insignificant for AEGON Bank N.V.

Table 4 Capital Buffer by Risk Type as of December 31, 2014

	Capital Req.	
in millions of euro's	**Dec-2014**	**Dec-2013**
Credit Risk (including CVA)	175	140
Concentration Risk	9	7
Incomplete coverage mortgage guarantee	14	14
Country Risk	5	8
Operational Risk	7	8
Model Risk	26	3
Conglomerate Risk	20	28
Litigation Risk	2	6
Strategic Enterprise Risk	13	5
Interest Rate Risk	20	12
Hedging Risk	3	3
Total capital requirement	294	234

4.1.1. Credit risk

Nature of risk
Credit risk is the risk that a counterparty is unable to meet its obligations on time. As far as AEGON Bank N.V. is concerned, credit risk mainly affects the investment portfolio.

Method to determine internal capital
AEGON Bank N.V. calculates credit risk under Pillar 2 in accordance with the 'Pillar 1 Plus' method. The Pillar 2 capital requirement for credit risk is calculated, in principle, according to what is known as the standard approach adopted by AEGON Bank N.V. under Pillar 1, as supplemented by additional internal capital to reflect circumstances and risks that are specific to AEGON Bank N.V.. The standard approach uses a standard classification of the investment portfolio by asset category and rating grades. For each combination, standard add-on capital is required. Consideration is given to credit risk mitigating circumstances, such as collateral or guarantees. Credit risk mainly consists of the risk resulting from the consumer loans, mortgages and the investment portfolio (banking book).

Credit risk mitigation under Pillar 1
AEGON Bank N.V. used credit risk mitigation for its mortgage portfolio. A large portion (>75%) of the mortgage portfolio is backed by a National Mortgage Guarantee Scheme [*Nationale Hypotheek Garantie*] (NHG). Because of the guarantee, a net credit risk weighting of 0% is applied to the guaranteed part of these mortgage loans under Pillar 1.

Moreover, Aegon Bank N.V. strives to invest in a well-diversified investment portfolio.

Furthermore, credit risk mitigation was used for bonds which carry an explicit guarantee from a sovereign. In those instances, the credit quality of the sovereign was used to determine the risk weighting.

Counterparty Risk
Included in the Credit Risk is the Credit Value Adjustment (CVA), which is a capital charge for counterparty credit risk. The CVA calculation is performed conforming standardized approach.

Securisation
Also included in Credit Risk are securitized issues. As of December 31, 2014, Aegon Bank N.V. has two securitizations. The first one are the Saecure 13 notes with Dutch mortgages as underlying and the second one is Kigoi with consumer loans as underlying. The credit risk of both issues are included by taking a look-through of all underlying loans and assess the credit risk thereof. No specific risk reduction is taken into account.

Aegon Bank N.V. takes full ownership of the Kigoi notes. The senior notes of Saecure 13 are placed at investors. The purpose for emitting notes is for financing purposes.

In addition, Aegon Bank N.V. has securitized bonds in its investment portfolio. These are securities such as residential mortgage backed securities (RMBS), commercial mortgage backed securities (CMBS), collateralized debt/loan obligation (CDO/CLO) and covered bonds. The risk weight of those securities are determined using the credit rating combined with the remaining maturity. In mid-2014, Aegon Bank N.V. has an investment policy in place with respect to securitised positions to ensure a well-diversified portfolio of high quality. Subjects such as analyses to be performed prior to selection, monitoring and stress testing are stated in this policy. This is in response to CRR article 449 concerning exposure to securitisation positions.

Capital buffer
The capital buffer for credit risk increased to EUR 175 mln (2014) from EUR 140 mln (2013), mainly as a result of an expansion of the balance sheet.

4.1.2. Concentration risk

Nature of risk
The call for awareness of concentration risk stems from the fact that, being designed to meet the portfolio variance principle, the Basel II model is calibrated for large international and well-diversified banks. If AEGON Bank N.V. credit portfolios are less diversified or include concentrations of exposures to countries, sectors or types of assets or portfolios, the standard risk weighting under Pillar 1 will lead to an underestimation of credit risk.

Method to determine internal capital
AEGON Bank N.V. concentration risk policy is designed to encourage diversified investment portfolios and mitigate concentration risk using concentration risk limits. AEGON Bank N.V. also holds internal capital to cover concentration risk.
In its policy, AEGON Bank N.V. distinguishes between three types of concentration risk:
1. Exposure to single names
2. Exposure to sectors and regions
3. Exposure to consumers without collateral

Re 1: Exposure to single names
AEGON Bank N.V. seeks to maintain a diversified portfolio to limit its exposure to a single counterparty or a group of related counterparties so as to prevent excessive potential losses. To manage its exposure to single names, AEGON Bank N.V. sets limits. It also holds capital to absorb potential losses on single names.

Excessive exposure to single names is prevented by internal limits and by external limits introduced under the Financial Supervision Act and detailed in the Prudential Rules Decree [*Besluit prudentiële regels*] and the Regulation on Solvency Requirements for Credit Risk [*Regeling solvabiliteitseisen voor het kredietrisico*], Chapter 7: Large exposures.

Internal limits
The table below shows the internal limits at market value:

Table 5 Internal limits on single names by rating class
(AEGON Nederland N.V. Policy Directive on investment guidelines for AEGON Bank N.V.)

CNLP Rating	Limit
AAA	108.0 mln.
Aax	108.0 mln.
Ax	76.0 mln.
BBBx	50.0 mln.
BBx	30.0 mln.
Bx	15.0 mln.
CCC-Cx / Unrated	6.0 mln.

An additional internal limit of 20% of regulatory capital is set for single names at market value to prevent the external limit on large exposures from being exceeded.

Internal limits applied
The policy covers all credit exposures, with the exception of Dutch government bonds and euro sovereign debt securities with an AAA rating. The limits apply per single counterparty or group and depend on the Credit Name Limit Policy (CNLP) rating to be used. The CNLP rating is modelled on external ratings available from S&P, Moody's and/or Fitch using rather conservative decision rules. This is done as follows:
1. If three different external ratings are available, the middle one is used.
2. If two different external ratings are available, the lowest of the two is used.
3. If only one external rating is available, that one is used.

If an internal rating happens to be available, the lower of the internal rating and the rating calculated according to the above rules is used. If no rating is available, the CCC-C limit applies.

External limits on large exposures
The Financial Supervision Act sets limits on large exposures (formerly the Credit System Supervision Act 4081: large holdings):

- Limit on the balance sheet value (market value) of a large exposure equal to 25% of regulatory capital
- Limit on the total sum of large exposures equal to 800% of regulatory capital

Supplementary capital to cover exposure to single names
In addition to the limits set to prevent potential losses, AEGON Bank N.V. holds supplementary capital to absorb all or part of any losses arising from the concentration of exposures to single names. This involves add-on capital on top of the capital to be held to cover credit risk under Pillar 1.
In light of its activities and investments, AEGON Bank N.V. has set the capital to be held for concentration risk arising from single names at 2%.

Re 2: Exposure to sectors and regions
AEGON Bank N.V. has set limits to mitigate exposures to sectors. These limits ensure a certain diversification in the activities of AEGON Bank N.V., as a result it is not considered necessary to maintain additional capital. AEGON Bank N.V. has set limits for the following sectors mortgage financing, other exposures to investments with real estate as collateral (covered bonds, RMBS, CMBS), and the financial sector. Also the exposure to PIIGS is limited (country risk). As a result of the review of the strategic investment portfolio in 2010, the exposure to real estate continued to increase. This was sufficient reason for AEGON Bank to set a limit for 2014 of 70.00% of the total capital requirement for credit risk under Pillar 2. AEGON Bank N.V. has set a limit for investments in its bond investment portfolio with real estate as collateral. It is important to note that the exposure to real estate largely consists of most senior European RMBS notes that, also according to internal models, carry only very limited risk of credit losses occurring as a result of large numbers of defaults coinciding with an extreme reduction in the value of the collateral.

The capital requirements under Pillar 1 are therefore considered to be adequate. On that basis, the decision was taken not to maintain internal capital to cover excessive exposures to real estate.
In addition to mortgages and other ‘real estate’ investments a limit has been set for 'financials'.

Re 3: Exposure to consumers without collateral
By adding consumer loans to the asset mix, AEGON Bank N.V. introduced exposure to consumers without receiving some collateral. To mitigate credit risk, a large portfolio of relatively small consumer loans is selected. In addition, an allocation limit for consumer loans applies.
A comparative study of peer banks conducted by KPMG UK has shown that AEGON Bank N.V. investment portfolio has a moderately concentrated exposure to sectors and regions. The table below shows indicative add-on percentages by type of bank to cover excessive exposure to sectors and regions.

Table 6 Indicative risk premiums by type of bank (sectors and regions)

Type of bank	Indicative premium
1. Well-diversified national portfolio	2-3%
2. Reasonably diversified regional portfolio	3-4%
3. Moderately diversified local portfolio	5-6%

In light of its activities and the market in which it operates, AEGON Bank N.V. has set the capital to be held for concentration risk arising from sectors and regions at 3%.

Capital buffer
The capital buffer for concentration risk increased to EUR 9 mln from EUR 7 mln (2013), mainly as a result of an expansion of the investment portfolio.

4.1.3. Incomplete NHG-payout risk

Nature of risk
This is the risk that not all claims under the Nationale Hypotheek Garantie (NHG) are paid in full. This might be related to incomplete files or a difference of opinion on the process of mortgage origination.

Method to determine internal capital
The capital requirement for AEGON Bank N.V. exposure to this risk is calculated based on the characteristics of the mortgages. Of each NHG-mortgage the amount of the NHG-guarantee is determined (declining over time). Based on historic analysis, AEGON Bank N.V. assumes that 6% of these claims are expected to be declined by NHG. Based on the LTFV of the mortgage, a risk weight of 35% or 75% is used to calculate the required capital.

Capital buffer
The capital buffer for incomplete NHG-payout risk is EUR 14 mln, there is no increase compared to 2013. This is due to two effects that offset each other. On the one hand there is a slight decline in the level of guarantee, as guarantee level develops as a decreasing annuity. On the other hand, the mortgage portfolio increased in size.

4.1.4. Country risk

Nature of risk
Basel II requires an additional risk premium for amounts owed by – issuers or companies in – countries that carry elevated country risk. In light of the credit and sovereign crisis in Europe, AEGON Bank N.V. decided to hold additional capital against exposures to the European Periphery and put in place limits to the overall exposure.

Method to determine internal capital
The capital requirement for AEGON Bank' N.V. exposure to this risk is calculated based on the exposures to corporates and governments in the PIIGS countries. The total amount of additional capital is determined at 4% of these exposures at market value.

An important point to note is that AEGON Bank N.V. shows its investments at market value in its accounts (available for sale under IFRS), which means that the fall in the market value of investments in the periphery is immediately apparent in the carrying amount and equity of AEGON Bank N.V.. AEGON Bank N.V. reduced its exposure to peripheral countries since 2010, but this has stabilized in 2013.

Capital buffer
The capital buffer for country risk as of December 2014 is EUR 5 mln, a decrease compared to December 2013 (EUR 8 mln). This is mainly due to less exposure to PIIGS countries.

4.1.5. Operational risk

Nature of risk
AEGON Bank N.V. defines operational risk as follows: "Operational risk is defined as the risk of losses arising from inadequate or failing internal processes and controls, people and systems, or external events". As part of this definition, AEGON Bank N.V. identifies eight categories:

- Tax risk
- Legal & compliance risk
- Systemic risk
- Fraud risk
- Processing and administrative risk
- Enterprise risk
- Personnel risk
- Facilities risk

These categories are divided into subcategories. Details of these subcategories are given in the ERM framework of AEGON NV. Reputational risk is not regarded as a separate risk category, but rather as an impact dimension of an operational risk.

Method to determine internal capital
The capital requirement for AEGON Bank N.V. exposure to operational risk under Pillar 1 is calculated according to the basis indicator approach. On the basis of, amongst other things, the assessment of information contained in the operational loss database by AEGON Bank's Risk & Audit Committee.The conclusion is that the current internal capital buffer for regular operational risk under Pillar 2, which is based on the outcomes of Pillar 1, is more than adequate.

Supplementary capital for special operational risks
Details of 'special operational' risks, such as special litigation risk (regarding the Sprintplan product) and 'strategic enterprise risk' are given in the sections 4.1.8 and 4.1.9 below.

Capital buffer
The capital buffer for operational risk as of December 2014 is EUR 7 mln, a small decrease compared to December 2013 (EUR 8 mln).

4.1.6. Modelling risk

Nature of risk
This is the risk that the parameters in the model calculations and the assumptions are incorrect and would lead to inadequate investment decisions. An example would be that the duration of our internet savings account is much longer than modelled or that the prepayment rate in mortgages deviate significantly from those modelled. As a consequence, AEGON Bank N.V. would run an unintended interest rate risk, potentially impacting the capital base of the Bank.

Method to determine internal capital
The capital requirement for AEGON Bank N.V. exposure to this risk is calculated by looking at the potential impact on the interest rate risk exposure of significant changes in the duration of our assets and liabilities. This unintended exposure is than transformed into a monthly VaR figure, assuming that we can re-adjust the interest rate exposure back to desired levels on a monthly basis.

Modelling customer behaviour
The market value and market risk exposure of the mortgage portfolio are measured allowing for early redemption (prepayment). The nominal cash flows of AEGON Bank N.V. mortgage portfolio are adjusted for prepayment using:

1. a constant percentage of the annual nominal cash flow
2. a mark-up on the rate applied to discount the cash flows

These percentages are determined on the basis of expert judgement after careful analysis of historic behaviour in the AEGON Bank N.V. portfolio. The assumptions are validated periodically.

Capital buffer
The capital buffer for model risk as of December 2014 is EUR 26 mln, a large increase compared to December 2013 (EUR 3 mln). The primary reason is an additional amount was reserved for modelling assumptions for client behaviour. As the mortgage portfolio increased in size there is increased attention on modelling assumptions concerning the prepayment rate of mortgages and its impact on interest rate risk.

4.1.7. Conglomerate risk

Nature of risk
Being part of a financial conglomerate has advantages as well as disadvantages. The disadvantage is that the parent company (AEGON NL or AEGON Group) could get into financial difficulties. In such circumstances, AEGON Bank N.V. might need to break the ties with the parent company in order to safeguard the financial stability of the Bank.

Method to determine internal capital
The capital requirement for AEGON Bank N.V. exposure to this risk is calculated based on an internal assessment of all activities which AEGON Bank N.V. has outsourced to the parent company. For each activity, an estimate has been made on the amount of time it might take to either insource the activity or outsource it to a third party. The results of this assessment have been discussed with the regulator. After these discussions, the total amount of internal capital was determined.

Capital buffer
The capital buffer for conglomerate risk as of December 2014 is EUR 20 mln, a decrease compared to December 2013 (EUR 28 mln). The decrease is mainly due to the preparation of the Recovery Plan, where responsibilities and obligations of various stakeholders are laid out.

4.1.8. Special litigation risk

Nature of risk
AEGON Bank N.V. is involved in litigation over its former 'SprintPlan' product. This product – the portfolio of which has since expired – is a type of securities lease, with the loan principal guaranteed on maturity by means of a built-in guarantee. This litigation has progressed to the Dutch Supreme Court, which is expecting additional information from both parties before issuing a ruling.

Method to determine internal capital
After consulting with Legal Affairs Netherlands, AEGON Bank N.V. performed a scenario analysis to determine the capital requirement for litigation risk. The scenario analysis is reviewed periodically. Litigation risk is expected to decline gradually over the next few years, as individual claims are settled regularly. If and when a final ruling by the Dutch Supreme Court is issued, the total liability to AEGON Bank N.V. will be known. The remaining special litigation risk in this case is likely to be minimal.

Capital buffer
The capital buffer for special litigation risk has decreased to EUR 2 mln (as of December 2014 is), a decrease compared to December 2013 (EUR 6 mln).

4.1.9. Strategic enterprise risk

Nature of risk
In recent years, there have been major changes within AEGON Bank N.V., most visible by the launch of Knab as a new online bank in the Netherlands.

Method to determine internal capital
The Executive Board made a qualitative estimate of the internal capital requirement based on temporary less-than-expected operating results over a period of one to two years attributable to the strategic transformation. When the results of the strategic overhaul become more clear, the quantitative estimate will be adjusted downwards. This is a reflection of the fact that the revised strategy should position AEGON Bank N.V. in a good position going forward.

Capital buffer
The capital buffer for strategic enterprise risk has increased to EUR 13 mln (as of December 2014 is) from EUR 5 mln in 2013. The Executive Board decided to temporarily increase the capital buffer for strategic enterprise risk due to start-up costs and uncertainty with respected to the introduction of

Knab. After successful introduction of Knab it is expected that this capital buffer will decrease to EUR 5 mln. The amount of EUR 5 mln is reserved as competition in the retail market remains competitive, with possibly new players entering the market.

4.1.10. Interest rate risk in the banking book

Nature of risk
AEGON Bank N.V. invests deposits from customers, such as on-demand savings accounts and deposits, in both floating and fixed-rated assets like mortgages, consumer loans and bonds. AEGON Bank N.V. incurs interest rate risk due to the mismatch between the interest rate-based maturities of fixed-rate securities on the one hand, and the maturities of deposits from customers on the other.

Frequency of measurements and reporting
AEGON Bank N.V. uses two methods to measure interest rate risk:

- The Value at Risk (historical VaR) and Price Value of a Basis Point measures are reported on a daily basis.
- Monthly stress testing according to (1) the market value approach (six stress scenarios) and (2) Earnings at Risk

Interest rate risk measurements are based on the following main assumptions:

- A core of on-demand savings accounts are assumed to have a limited interest rate-based maturity depending on the interest reset frequency.
- The non-core part is modelled based on historical outflow patterns.
- All cash flows are assumed to take place in accordance with contractual obligations, allowing for early prepayment of mortgage loans and consumer loans.

Controlling interest rate risk in the banking book
The interest rate risk in the banking book is currently controlled on the basis of the historical VaR method and the Price Value of a Basis Point (PV01) measure. The reasons for choosing the historical VaR method and the PV01 measure are explained briefly below.

Historical VaR method:

- Limited complexity;
- The possibility of measuring risks in non-linear portfolios;
- The fact that no assumptions have to be made in terms of the stability of the Variance-Covariance matrix and the normality of interest rate fluctuations.

Validation of the VaR model is done by means of back-testing.

Price Value of a Basis Point measure:

- Sets out in a simple way the economic value impact of a specific interest rate change on assets and liabilities and, ultimately, the effect on equity;
- Forward-looking and based on a change in the current interest rate.

Interest rate risk management
The ALCO monthly sets the target interest rate VaR adhering to the limits agreed upon in the Risk Appetite. Using interest rate derivatives such as interest rate swaps (IRS) and futures, the interest rate VaR is then brought back to the required level. This process is monitored on a daily basis.
Stress test limits are also set (Section 3.3.8). Operating within these stress test limits ensures that even major shifts in the yield curve will have a limited impact on own funds at market value and interest margin.

Method to determine internal capital
AEGON Bank N.V. holds internal capital equivalent to the internal upper limit of interest rate VaR.

Capital buffer
The capital buffer for interest rate risk in the Banking book has increased to EUR 20 mln (as of December 2014 is), from EUR 12 mln (December 2013). The increase is because EUR 20 mln is set as the VaR limit for interest rate risk. By the end of 2013, the VaR applied at that moment was used.

4.1.11. Hedging risk

Nature of risk
In the past AEGON Bank N.V. granted guarantees to customers and issued depositary receipts that are hedged by AAM by means of derivatives in accordance with the mandate. Furthermore, the hedge-accounting inefficiency of the floating leg in an interest rate swap introduces hedging risk as not all market value movements can be offset in the hedged items. As this part of the market value movement is part of the P&L of AEGON Bank N.V., it is potentially impacting the capital base.

Method to determine internal capital
A small amount of add-on Economic Capital is maintained to cover limited basis risk (imperfections of a hedge caused by, for example, timing differences).
Based on the interest rate sensitivity of the floating leg of all interest swaps, and the volatility in the money market rates, the potential impact of the hedge accounting inefficiency is determined.

Aegon Bank N.V. maintains an interest rate swap portfolio to mitigate its interest rate risk. As of December 31, 2014, interest rate swaps are evaluated using the OIS curve, previously the 6M euribor curve is used. The base curve to evaluate the mortgage portfolio is the 1M euribor curve, which is consistent across the Aegon conglomerate. The impact of the change to OIS curve, also in relation to hedge accounting, is currently under review.

Capital buffer
The capital buffer for hedging risk in 2014 is EUR 3 mln (no change compared to 2013).

4.2. Internal capital allocation

AEGON Bank N.V. is not an international bank with different legal entities undertaking a variety of business activities in different countries. This means that allocating internal capital to legal entities other than AEGON Bank N.V. or to specific business lines is not necessary.

5. Risk Weighted Assets

For the investment bond portfolio (including treasury positions, but excluding mortgages and consumer loans), below please find the distribution of exposure, risk weighted assets ("RWA") and capital requirement by geographic region. As shown in table 7 below, 53% of total RWA (of the investment portfolio) is in "Mixed", a country code assigned to CLOs and CDOs, whereas this category only account for 18% of total exposure. As can be seen in table 9 below, the portfolio of securitised products is of relatively high rating (most RWA in 20% risk weight category).

Table 7 Geographic distribution of bond investment portfolio as of December 31, 2014, sorted by RWA

in millions of euro's	Exposure	RWA	Capital Req.
Mixed	470.1	499.0	39.9
Italy	119.0	70.7	5.7
France	244.0	60.5	4.8
Netherlands	371.2	59.7	4.8
Germany	496.2	53.8	4.3
Spain	143.4	51.3	4.1
UK	153.7	30.7	2.5
Ireland	30.4	30.4	2.4
Czech Republic	51.5	25.8	2.1
Norway	60.2	19.0	1.5
Austria	52.3	10.5	0.8
USA	26.8	9.0	0.7
Greece	2.3	7.9	0.6
Portugal	26.3	5.6	0.4
New Zealand	19.9	4.0	0.3
Luxembourg	6.2	1.2	0.1
Supranational	128.4	-	-
Finland	125.1	-	-
Belgium	81.6	-	-
Denmark	30.2	-	-
Sweden	25.1	-	-
Total	2,663.8	939.0	75.1

Table 8 Bond investment portfolio by sector as of December 31, 2014

in millions of euro's	Exposure	RWA	Capital Req.
Securitisation	1,178.7	704.5	56.4
Sovereign, MDB, PSE	728.5	7.0	0.6
Bank	468.4	82.6	6.6
Corporate	288.2	144.9	11.6
Total	2,663.8	939.0	75.1

Table 9 Bond investment portfolio by risk weight category

Exposure in millions of euro's	0%	20%	50%	100%	>100%	Grand Total
Securitisation	0	883.4	167.6	67.7	60.0	1,178.7
Sovereign, MDB, PSE	693.4	35.1	0	0	0	728.5
Bank	170.2	221.6	76.6	0.0	0	468.4
Corporate	0	112.3	107.1	68.9	0	288.2
Total	863.6	1,252.4	351.2	136.6	60.0	2,663.8