

# Pillar 3 Disclosures 2018



## Aegon Bank N.V.



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## List of abbreviations used in this report

AAM	Aegon Asset Management
AEB	Aegon Bank NV
AENL	Aegon Nederland NV
AFD	Aegon Financiële Diensten (Aegon Financial Services)
ALCO	Asset and Liability Committee
AT1	Additional Tier 1
BE CPR	Best Estimate Constant Prepayment Rate
BIA	Basic Indicator Approach
bIn	Billion
CACF	Crédit Agricole Consumer Finance
CCB	Capital Conservation Buffer
CCF	Credit Conversion Factor
CCyB	Countercyclical Capital Buffer
CDD	Customer Due Diligence
CDS	Credit Default Swap
CEO	Chief Executive Officer
CET1	Common Equity Tier 1
CFO	Chief Financial Officer
CM	Capital Management
COREP	Common Reporting
CRC	Credit Risk Committee
CRD	Capital Requirements Directive
CRO	Chief Risk Officer
CRR	Capital Requirements Regulation
CSA	Credit Support Annex
CVA	Credit Valuation Adjustment
DNB	De Nederlandsche Bank NV (Dutch Central Bank)
DO	Directie Overleg (Board meeting)
DV01	Dollar Value of one basis point
EAD	Exposure at Default
EAR	Earnings at Risk
EBA	European Banking Authority
ECAI	External Credit Assessment Institution
ECB	European Central Bank
ERAC	Enterprise Risk & Audit Committee
ERM	Enterprise Risk Management
EU	European Union
EUR	Euro
FINREP	Financial Reporting
FRM	Financial Risk Management
FTE	Full Time Equivalent
FX	Foreign Exchange
GBP	Great British Pound
GL	Guidelines
G-SII	Global Systemically Important Institution
HQLA	High Quality Liquid Assets
HR	Human Resources
HY	Half Year
IAN	Internal Audit Nederland
IAS	Internal Accounting Standard
ICAAP	Internal Capital Adequacy Assessment Process
IFRS	International Financial Reporting Standards

ILAAP	Internal Liquidity Adequacy Assessment Process
IRB	Internal Rating Based
IRRBB	Interest Rate Risk in the Banking Book
IRS	Interest Rate Swap
ISDA	International Swaps and Derivatives Association
IT	Information Technology
KYC	Know Your Customer
LCR	Liquidity Coverage Ratio
LGD	Loss Given Default
LtV	Loan-to-Value
MB	Management Board
MDA	Maximum Distributable Amount
mIn	Million
MVC	Model Validation Committee
NFRC	Non-Financial Risk Committee
NHG	Nationale Hypotheek Garantie (National Mortgage Guarantee)
NL	The Netherlands
NSFR	Net Stable Funding Ratio
ORM	Operational Risk Management
O-SII	Other Systemically Important Institution
PARC	Product Approval Review Committee
PARP	Product Approval & Review Process
PD	Probability of Default
QCT	Quality Control Team
RAS	Risk Appetite Statement
TRS	Technical Regulatory Standard
RW	Risk Weight
RWEA	Risk Weighted Assets
SB	Supervisory Board
SME	Small and Medium-sized Enterprises
SREP	Supervisory Review & Evaluation Process
T2	Tier 2
TREA	Total Risk Exposure Amount
VaR	Value at Risk
Wft	Wet financieel toezicht (Dutch Financial Supervision Act)

# 1 Introduction

This report should be read in conjunction with the financial statements of Aegon Bank N.V. (AEB), as included in AEB's Annual Report 2018<sup>1</sup>. Through this Pillar 3 Disclosures document, AEB complies with applicable 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 and the basis of consolidation used in the Annual Report. The information in this document has not been audited by AEB's external auditors.

## 1.1 Regulations

Since the introduction of the Basel II Capital Framework, codified in the Dutch Financial Supervision Act (*Wet financieel toezicht*; or *Wft*), requirements have been set to promote the transparency of financial institutions. Those requirements are set out in Pillar 3 'Disclosures and Market Discipline' of the Basel II Capital Framework. The Basel III Accord was adopted in 2010 and converted by the European Union (EU) into the Capital Requirement Regulation (575/2013) (CRR) and Capital Requirement Directive (2013/36/EU) (CRD IV)<sup>2</sup>. Specifically, Title II of CRD IV (Technical Criteria on Transparency and Disclosure) relates to disclosure requirements. Institutions have been required to apply the new rules since 1 January 2014, with full adoption on 1 January 2019<sup>3</sup>.

### 1.1.1 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.

- Credit risk: AEB uses the Standardized Approach (SA) for credit risk. This approach prescribes a standardized credit risk weighting, depending on the exposure class and rating category, to be applied to the exposures concerned in order to determine its contribution to the Total Risk Exposure Amount (TREA)<sup>4</sup>.
- Operational risk: In order to determine the capital requirement for operational risk, AEB uses the Basic Indicator Approach (BIA). Accordingly, the capital requirement for operational risk is defined as 15% of the average 'relevant indicator' for the last three of twelve-monthly observations at the end of AEB's financial year. The elements of the relevant indicator are based on the Finrep template F02.00 and the indicator equals net operating income excluding the elements set out in Article 316-1 (b)<sup>5</sup> CRR<sup>6</sup>.
- Market risk: AEB defines market risk as the risk of incurring losses on on-balance sheet and off-balance sheet items arising from adverse movements in market prices. Market risk is subdivided into the following risks: position risk (for assets in the trading book), foreign currency conversion (FX) risk, and commodities risk. AEB currently holds FX positions in Great British Pounds (GBP), which means that it is exposed to FX risk. Because the net position in GBP remains below the 2% 'de

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<sup>1</sup> The 2018 annual report is available on our website at: <https://www.aegon.nl/overaegon/jaarverslagen>

<sup>2</sup> CRD IV comprises (i) Capital Requirements Directive (2013/36/EU) (CRD), which has been transposed into national law, and (ii) Capital Requirements Regulation (575/2013) (CRR), which is directly applicable to firms across the EU.

<sup>3</sup> 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, operational and market risk). The implementation date for these requirements is year-end 2016.

<sup>4</sup> 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.

<sup>5</sup> Article 316(b): Institutions shall not use the following elements in the calculation of the relevant indicator: (i) realised profits/losses from the sale of non-trading book items, (ii) income from extraordinary or irregular items, (iii) income derived from insurance.

<sup>6</sup> The capital requirement multiplied by 12.5 produces the amount of RWA for operational risk.

*minimis*' threshold, AEB does not calculate own funds requirements for FX risk. As such, AEB is not required to hold capital for market risk under Pillar 1.

### **1.1.2 Pillar 2: Supervisory Review**

Under Pillar 2, AEB's Management Board and process owners annually perform an integrated analysis of the bank's business model, balance sheet and associated risks under base and adverse scenarios. The risks identified, including Pillar 1 risks, are measured and aggregated, after which AEB estimates the appropriate capital requirements for each identified risk factor. The Management Board (MB) continuously monitors and, where necessary, takes action if certain risks materialize in excess of AEB's risk appetite limits.

### **1.1.3 Pillar 3: Disclosures and market discipline**

Finally, the CRR lays down requirements for the disclosure of information to the public. These requirements are set out in Pillar 3 'Disclosures and Market Discipline'. AEB meets the Pillar 3 requirements by publishing this document as a specific schedule to its financial statements. AEB has prepared its Pillar 3 report in accordance with the CRR and CRD IV, as required by the supervisory authority. In addition to the Pillar 3 requirements as described in the CRR, the following guidelines were used:

- European Banking Authority (EBA) Regulatory Technical Standards (RTS) on disclosure of encumbered and unencumbered assets under Article 443 of the CRR;
- Supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for the disclosure of information in relation to the compliance of institutions with the requirement for a countercyclical capital buffer in accordance with Article 440;
- Implementing Technical Standards (ITS) with regard to disclosure of the leverage ratio for institutions, according to Regulation (EU) No 575/2013 of the European Parliament and of the Council;
- EBA guidelines on Liquidity Capital Ratio (LCR) disclosure to complement the disclosure of liquidity risk management under Article 435 of Regulation (EU) No 575/2013;
- EBA Guidelines on sound remuneration policies under Articles 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013; and
- ITS with regard to disclosure of own funds requirements for institutions according to Regulation (EU) No 575/2013 of the European Parliament and of the Council.

The Pillar 3 report is published annually and the 2018 Pillar 3 Disclosures document should be seen as an addition to AEB's Annual Report 2018.

## **2 General Information**

AEB is a public limited liability company organized and existing under Dutch law and recorded in the Trade Register of the Chamber of Commerce in The Hague, under number 30100799. Its registered office is situated at Aegonplein 50, 2591 TV The Hague. AEB is a wholly owned subsidiary of Aegon Nederland N.V. (Aegon Nederland, or AENL), based in The Hague. AEB's ultimate parent company is Aegon N.V., also based in The Hague. Please refer to AEB's Annual Report 2018 for more information on the following topics.

### **2.1 Purpose and mission statement**

Aegon N.V.'s mission is to "help people achieve a lifetime of financial security". This is also reflected in Aegon Nederland's mission to "enable people to make conscious decisions about their financial future".

In 2017, Aegon Nederland started rolling out its Future Fit Strategy and transforming its business into four divisions, with an increased focus on the customer segments Aegon Zakelijk, Aegon Particulier, Knab and Aegon Bank & Beleggen (AEB). Within these divisions, Aegon Nederland seeks to offer comprehensive value propositions that will suit our customers' needs at every stage of their lives.

An AENL subsidiary, AEB occupies a well-defined position in terms of Aegon Nederland's vision and mission and plays a vital part in executing its strategy. AEB does so by delivering banking solutions, products and services that provide customers with the means to:

- compile a personal financial plan;
- invest in a range of products designed to achieve wealth accumulation; and/or
- invest in future income arrangements to secure a healthy financial future.

### **2.2 Main activities, products, services, and geographic areas**

AENL offers a wide range of financial products and services to its clients, including pensions, insurance (life and non-life), mortgage loans, savings and investment solutions. Contributing to the AENL mission, AEB specializes in developing, selling and maintaining payment, savings and investment products. AEB does this through two labels: (1) Aegon Bank and (2) Knab.

1. Aegon Bank is predominantly an online retail bank that develops third-pillar pension products (tax-friendly banking savings) and fourth-pillar pension products (investments and online savings) for future income, in addition to individual second-pillar pensions. These products and services are focused on long-term wealth accumulation.
2. Knab was introduced in 2012 as a disruptive online banking initiative for retail and self-employed clients. Currently it is a full-scope banking concept with payment services, investments, savings, financial planning tools, alerts and experts. Knab seeks to provide high-quality client services and to be a driver of (online) developments. By the end of 2018 Knab had grown to 200,000 clients. It is perceived to be one of the most popular brands within the Dutch retail banking landscape.

### **2.3 Internal organizational structure**

The operations of AEB's two labels are separate, but the supporting functions (in the context of the banking license) for both labels such as Risk & Compliance, Capital Management, Asset & Liability Management, Investments & Funding, HR & Support, Strategic & Regulatory Affairs and Finance, Control & Regulatory Reporting are shared and carried out at aggregate AEB level. AEB employs a holistic risk governance model to

optimize business support and oversight, and has implemented a “three lines of defense” risk management model.

To enjoy benefits of scale, AEB has outsourced part of its activities, such as Marketing & Communications, first-line Customer Service, Facility & IT and Online, to AENL, which has dedicated teams working on AEB’s behalf. AEB remains accountable for the effective implementation and execution of those processes. Knab, on the other hand, either independently performs or sources the full range of its operations including IT, Client Contact Centre and Marketing & Development to support its rapid development and cement its culture.

In the past year, Knab has shown tremendous growth, particularly in banking products. In order to achieve further sustainable growth, enhance its governance and improve its efficiency, Knab launched a strategic review of its activities in 2018. The review findings are expected to be implemented by Knab and AEB in 2019 and 2020.

## **2.4 Underlying assumptions**

### **2.4.1 Scope and reference date**

AEB’s Pillar 3 document covers the bank’s full consolidated balance sheet at 31 December 2018, including the ‘Aegon Bank’ and ‘Knab’ labels that are part of its business. All amounts in this Pillar 3 report are stated in millions of euros (EUR), unless stated otherwise.

### **2.4.2 Basis of consolidation**

The consolidated financial statements include the financial statements of AEB and its subsidiaries. Subsidiaries (including structured entities) are entities over which AEB exercises control. AEB controls an entity when AEB is exposed to or has rights to variable returns from its involvement with the entity and has the ability to influence those returns through its control over the entity. Please refer to AEB’s Annual Report 2018 for more information.

### **2.4.3 Accounting and risk principles**

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRSs), as adopted by the EU, and Part 9 of Book 2 of the Dutch Civil Code. Please refer to AEB’s Annual Report 2018 for more information.

## **3 Overview of risk management**

### **3.1 Introduction**

AEB manages risks on behalf of its customers and stakeholders. The bank's Enterprise Risk Management (ERM) Framework provides the core structure that allows it to assess, control and manage all the risks to which it is exposed. The ERM Framework is therefore essential to ensuring AEB's financial strength.

The ERM Framework is a comprehensive framework. Not only does it define the principles for the way in which risk management is to be embedded in the bank's daily business activities, but it also sets out the policies and standards on how risk management should be part of AEB's strategic planning process. In addition, the framework ensures the identification, measurement and control of risks at all levels across the organization. It also provides a means to identify any new risks that could potentially arise. The framework covers risk measurement and reporting, and underlines the importance of general risk awareness among and appropriate behavior by our employees, management, and leadership.

The ERM Framework can only be effective if there is a sound and consistent risk culture throughout the organization. AEB's management has therefore defined principles for an excellent risk culture.

A strong risk management function, which has been integrated into day-to-day management of the business and strategic planning, has given the bank a strategic competitive advantage. It has helped the bank protect its reputation, lower the cost of capital, and ultimately reduce costs. It has also helped the bank minimize the risk of investigations, prosecution, and fines. By effectively managing risks, the bank enhances its competitive position by building trust among all stakeholders.

In other words, the role of risk management is:

“to be responsible, on the MB's behalf, for the supervision and oversight of the organization acting in a risk-aware manner, and proactively advising the MB. In this context, AEB expects Risk Management to proactively support management by highlighting risk responsibilities and helping management design and implement appropriate controls.”

### **3.2 Risk Governance**

In 2017 and 2018, the organizational and governance structure was strengthened to reflect the bank's growth ambitions, and to enable a more pro-active risk management approach. The MB comprises the statutory Chief Executive Officer (CEO, Eric Rutten), statutory Chief Financial Officer (CFO, Mike de Boer), statutory Chief Risk Officer (CRO, Ebbe Negenman), Chief Operational Officer (COO, Bianca Joustra), and General Counsel (Axel van Doorn).

Aegon Bank N.V.'s organization chart is as follows:

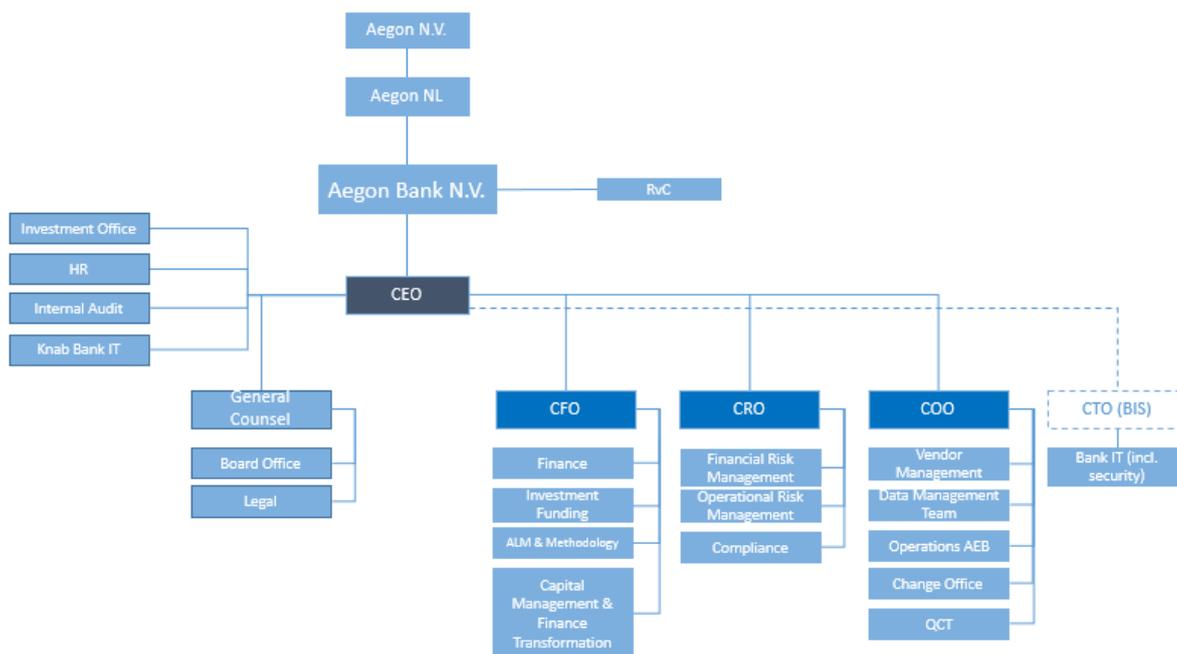


Figure 1: Organizational chart

In the first quarter of 2018, Aegon Bank launched the Horizon project aimed at improving the bank's risk management and achieving a high-quality risk management set-up in line with its business strategy and growth ambitions. The Horizon project identified some 260 deliverables that would contribute to the bank's goal of delivering excellence in risk control. By November 2018, more than 90% of deliverables were achieved according to plan. As a follow-up on the Horizon project, new and smaller projects were initiated to ensure full embedding of all Horizon deliverables in 2019. To ensure further progress on our "risk control excellence journey", we significantly hired more risk management staff in 2018, in terms of both quantity (FTEs) and quality; the average risk management employee now has over thirteen years' experience.

In 2018, in the course of the Horizon project, we also found that compliance risks needed to be addressed through a separate work flow. As regards Know Your Customer (KYC) procedures, the project flagged up a specific deliverable: "Review customer base to assess proper management of KYC risks". Due to the issue's complexity and importance, we decided to start a separate project in November, with the assistance of an external advisor. The review has led to key goals being defined in order to create an environment where client acceptance is a sustainable and ongoing process across our business.

### 3.2.1 Three lines of defense

AEB's risk governance structure is based on the "three lines of defense" model, as elaborated in the EBA Guidelines on Internal Governance (GL 44), 2011. The business is 'the first line of defense', the independent risk management function is the 'second line of defense', and the internal audit function operates as the 'third line of defense'. Each line has been assigned a specific role and responsibilities, in such a way as to ensure that the performance of tasks is segregated from oversight of the same tasks. At the same time, the three lines of defense work closely together to identify, assess and mitigate risks. The following sections describe each line of defense.

#### 3.2.1.1 First line of defense: the Business Lines

The bank's first line of defense is responsible for performance, operations, compliance and effective control of risks affecting the business. The first line of defense consists of the following departments:

- Capital Management and Financial Transformation;

- ALM (Asset & Liability Management) and Methodology;
- Investments and Funding;
- Business Control;
- Regulatory Reporting;
- Financial Control;
- Customer Service;
- Business Information Services (IT);
- Operations;
- Marketing and Sales;
- Investment Office;
- Communications;
- Human Resources;
- Legal, Board office and Regulatory Affairs; and
- Quality Control Team.

The managers of the first-line departments are responsible for managing the risks arising from the activities conducted by their department. They own the business processes in their departments and are responsible for identifying the key risks in their departments and processes by performing Risk Control Self Assessments (RCSAs). They are also responsible for drawing up and maintaining process descriptions and work instructions, designing and executing controls, and monitoring procedures to ensure that any residual risk (after implementation of controls) remains within the risk appetite. They are also responsible for ensuring that the design and implementation of controls comply with the policies of AEB and, to the extent applicable, those of Aegon Nederland and Aegon NV.

### **3.2.1.2 Second line of defense: Risk Management and Compliance**

The second line of defense comprises oversight functions, with a key role being assigned to the risk management organization headed by the CRO. The Risk Department is independent from the business lines and responsible for supervising and monitoring financial and non-financial risks and controls in the first line. Within the Risk Management & Compliance department, Compliance, Operational Risk Management (ORM) and Financial Risk Management (FRM) are segregated functions.

### **3.2.1.3 Third line of defense: Internal Audit**

The internal audit function performed by Internal Audit Nederland (IAN) is the third line of defense. IAN provides an on-going independent (i.e. outside of the businesses and risk organization) and objective assessment of the effectiveness of the internal control framework and risk management by the first two lines of defense, including financial and non-financial risks. IAN is responsible for testing the design and implementation of the risk control framework. IAN issues recommendations to ensure that any gaps are effectively addressed.

AEB's Internal Audit charter and annual audit program based on the outsourcing agreement with IAN provide that IAN must perform systematic audits of the management of risks affecting the Bank's activities. IAN reports directly to the Statutory Board of Aegon Nederland and AEB. IAN's findings are always discussed with AEB's management.

### **3.2.2 Risk committees**

AEB has set up several risk committees composed of members of the management board and senior management. The risk committees are responsible for advising the MB on AEB's overall current and future risk appetite and strategy, and assisting the MB in overseeing the implementation of that strategy by senior management.

The Non-Financial Risk Committee (NFRC) meets monthly and monitors the development of the non-financial risk profile against the defined risk strategy and appetite and decides on any mitigating action as and when required. In addition, the NFRC discusses, promotes

awareness of, and supports the organization on all subjects and issues relevant to managing AEB's non-financial risks. The NFRC also advises and supports the MB in its supervisory role and oversees the implementation of the non-financial risk strategy so as to assess its adequacy against the approved risk appetite and strategy.

The Enterprise Risk & Audit Committee (ERAC-Bank) meets quarterly and monitors, discusses, supports progress, and decides on all subjects and issues relevant to managing AEB's financial and non-financial risks, taking the bank's risk appetite into account.

AEB produces a comprehensive set of risk reports to measure, monitor and manage the risks inherent to its business, including monthly NFRC and NFRC highlights reports for the Statutory Board and quarterly ERAC-Bank reports.

Set up in 2018, the Credit Risk Committee (CRC) reports to the MB. It discusses and reviews the policies, methodologies and procedures related to credit risk and counterparty risk within the bank prior to AEB's Statutory Board's final approval. The CRC also discusses and approves transactions involving credit risk. The committee meets monthly and is chaired by the CRO.

Asset and Liability Committees (ALCOs) discuss and approve AEB's financial risk profile, except for credit risk, which has been delegated to the CRC. ALCOs exist on tactical and strategic levels and they define the capital, interest rate mismatch, funding, liquidity and foreign exchange risk policies for Aegon Bank. The Strategic ALCO meets quarterly and the Tactical ALCO meets monthly. Both are chaired by the CFO.

The bank's Model Validation Committee (MVC) meets at least once every quarter and is chaired by the CRO. The committee is responsible for discussing all model validation findings from a technical perspective.

### **3.3 Risk Appetite Framework**

The risk appetite framework is defined as the overall approach, including policies, processes, controls and systems, through which risk appetite is established, communicated and monitored. It covers the Risk Appetite Statement (RAS) and risk limits and outlines the roles and responsibilities for implementing and monitoring the risk appetite framework.

AEB's risk appetite framework determines the bank's risk profile and forms part of the process of developing and implementing its strategy and identifying the risks taken in relation to its risk capacity. The risk appetite framework does not include the processes for establishing the strategy, developing the business plan, or the risk measurement and aggregation models and systems. However, the risk appetite framework is aligned with AEB's business plan, strategy development and capital planning, and provides a common framework and comparable measures for AEB's MB and senior management to communicate, understand, and assess the types and levels of risk that they are willing to accept. The framework identifies and assesses material risks for AEB and for its shareholders, depositors and customers.

The risk appetite process focuses on determining risk appetite at AEB level and across the different risk categories. It is therefore essentially a top-down process, based on AEB's ambition in terms of its risk profile, and dependent on its capital and liquidity levels and ambitions, the regulatory environment, and economic conditions.



Figure 2 – Aegon Bank NV's risk appetite process

### 3.4 Risk Embedding

AEB's ERM Framework is thoroughly embedded in its key functional areas. This section describes how risk considerations are taken into account in decision-making on business planning, capital planning, liquidity planning, recovery planning, product development, and recruitment/human resources.

#### 3.4.1 Capital Planning

The Internal Capital Adequacy Assessment Process (ICAAP) is a process aimed at ensuring AEB's capital adequacy in relation to the relevant risks and the bank's risk profile. As part of this forward-looking process, AEB identifies, assesses and, where possible, quantifies risks. Stress-testing and a forward-looking element are key parts of this process. The bank's management determines the capital required in relation to the bank's risk profile based on its internal standards for all relevant risks.

The bank reviews its ICAAP for current capital adequacy and expected capital adequacy over the (three-year) medium term. The review projects new activities alongside current activities. Assessing the bank's capital adequacy is done by means of a quarterly ICAAP update presented to AEB's Strategic ALCO. The update provides a comparison between the actual situation and projections so as to allow AEB's management to take any action if necessary.

#### 3.4.2 Liquidity Planning

The Internal Liquidity Adequacy Assessment Process (ILAAP) document describes AEB's liquidity risk management and funding plan. ILAAP aims to ensure liquidity adequacy and to manage liquidity risk in relation to all other risks identified. As part of ILAAP, senior management identifies, assesses and, where possible, quantifies elements of liquidity risk. AEB assesses and identifies potential shortcomings and takes management action when needed. Stress-testing and projections of future liquidity needs are key control components of ILAAP.

AEB's senior management have an important part to play in ILAAP. They are actively involved in all elements of liquidity risk. The CFO and CRO are ultimately responsible and accountable for their specific line activities and tasks.

### **3.4.3 Product development**

Risk considerations form an integral part of AEB's product development and pricing policy. Product development and pricing decisions must take into account economic value creation requirements for shareholders, the fair treatment of customers, and the impact on statutory and regulatory requirements, speed of recouping capital expenditures, impact on financials, and impact on risk appetite statements and risk policies.

During 2018 AEB implemented and used its own Product Approval & Review Process (PARP) and took part in meetings of the Product Approval Review Committee (PARC).

### **3.4.4 Recruitment/Human resources**

To ensure effective risk management, AEB also operates requirements for its employees, organizational culture, and risk awareness. The knowledge and skills that employees need to have are detailed in their job descriptions. The core values of both business lines clearly show the importance of risk awareness. Those values contribute to a culture where employees are involved in the organization and so there is a natural form of social control. AEB's core values are 'working together', 'exceeding expectations', and 'bringing clarity'. These values are in line with those of Aegon NV.

### **3.4.5 Business continuity plan and recovery plan**

The business continuity plan describes the steps that need to be taken in the case of a business interruption due to a disaster, and the advance planning and preparations necessary to minimize losses and to ensure the continuity of key (and time-sensitive) business functions during a major business interruption. AEB defines the resources, actions, tasks and data required in preparing for and recovering from such an emergency.

AEB's Recovery Plan is intended to reduce the likelihood of transitioning into a gone-concern scenario and subsequent resolution, and provides detailed actions that may be taken upon the occurrence of different stress scenarios so as to restore confidence, AEB's liquidity or capital position, or a combination of the above.

## **3.5 Stress Testing**

AEB's stress-testing framework aims to adequately assess the bank's vulnerability to low-probability but plausible events, and to determine the adequacy of the bank's own funds, liquidity position and earnings to withstand financial losses or liquidity outflows.

The stress tests are forward-looking and address the main risks to which the bank may be exposed.

As part of its ICAAP and ILAAP, AEB tests its capital and liquidity adequacy periodically. The impact of extreme scenarios on AEB's earnings due to changes in interest rates is regularly assessed as part of the Interest Rate Risk in the Banking Book (IRRBB) report. The impact of credit risk exposures on AEB's solvency is assessed regularly by means of point-in-time scenarios and sensitivity analyses. The economic and regulatory capital in the stress scenarios needs to be sufficient to absorb the loss of equity and regulatory available capital, and the available liquidity needs to exceed the required liquidity under those stress scenarios.

The stress-test scenarios are designed, and parameter values set, annually. The validity of the assumptions is reviewed in the case of any significant market events, substantial changes to AEB's organization or strategy, or significant regulatory changes.

The results of the capital stress tests performed as part of the bank's ICAAP are presented quarterly to the Strategic ALCO, and the results of the liquidity stress tests are presented monthly to the Tactical ALCO. Additional stress tests may be performed on an ad-hoc basis.

AEB may also use stress tests as an internal communication tool across management levels to raise awareness and encourage discussions about existing and potential risks and possible management actions. Stress tests therefore support a variety of business decisions and processes as well as strategic planning.

AEB has designed an iterative process to review its stress tests. This means that some steps in the stress testing process are repeated. The stress-testing cycle consists of six steps, as shown in the figure below.

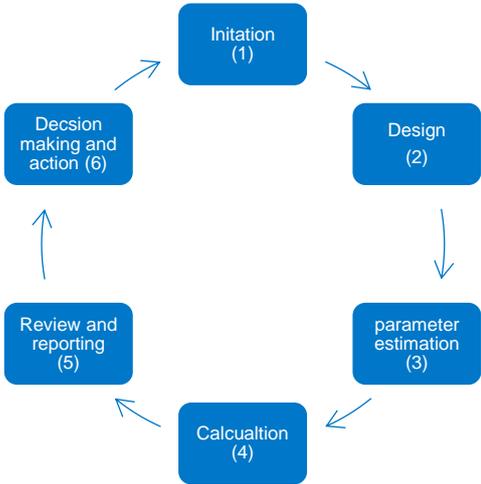


Figure 3: Stress-testing process

## 4 Capital Management

As part of its capital management policy, AEB identifies, assesses and, where possible, quantifies material risks. In accordance with internal requirements, AEB determines the amount of capital it needs to hold to cover those material risks relative to its risk profile now and in the years ahead, consistent with its strategy.

The capital planning process is at the heart of AEB's capital management, linking the company's mission statement, strategy and risk profile to its capital management. The assumptions underpinning the capital plan are reviewed and adjusted periodically throughout the year. The capital plan projections are also updated quarterly based on actual figures, and reported to the MB and ALCO to allow for frequent monitoring. Adjustments may be made on the basis of expected developments relative to actual outcomes, where necessary in accordance with existing contingency plans.

AEB's own funds increased by EUR 83 million to EUR 629 million at 31 December 2018. This increase was mainly driven by a EUR 50 million CET1 capital injection from Aegon Nederland to facilitate further balance sheet growth. As shown in Table 1, AEB's capital ratios improved by ~1%, compared to 31 December 2017. AEB's capital position remains well above the internal and external requirements.

Metrics	2017	2018
CET1 capital	536	619
T1 capital	546	629
<b>Own funds</b>	<b>546</b>	<b>629</b>
Total exposure amount (in accordance with CRR)	13,870	14,198
Total Risk Exposure Amount (TREA)	2,605	2,866
CET1 ratio	20.6%	21.6%
Tier 1 ratio	20.9%	21.9%
Total capital ratio	20.9%	21.9%
Leverage ratio	3.9%	4.4%

Table 1: Key capital metrics

In millions of euros	2017	2018
Paid-up capital instruments	37	37
Share premium	352	402
Retained earnings	137	174
Profit or loss attributable to owners of the parent	45	6
Part of interim or year-end profit not eligible	-45	-6
Accumulated OCI	15	8
Adjustments to CET1 due to prudential filters	-2	-1
Other transitional adjustments to CET1 capital	-3	-
<b>CET1 Capital</b>	<b>536</b>	<b>619</b>
AT1 Capital	10	10
<b>T1 Capital</b>	<b>546</b>	<b>628</b>
T2 Capital	-	-
<b>Own funds</b>	<b>546</b>	<b>628</b>

Table 2: Composition of own funds

## **4.1 Own Funds**

This section describes the definitions of the underlying elements of AEB's own funds in accordance with the CRR.

### **Common Equity Tier 1 Capital**

The CET1 Capital deployed at AEB is wholly owned by Aegon Nederland in accordance with Article 50 of the CRR.

### **Additional Tier 1 Capital**

AEB's AT1 Capital solely consists of 'Knab participations'. Until November 2017 AEB provided customers with the opportunity to buy 'participations' in AEB through the KNAB label. The participations had a fixed notional of EUR 5,000, no fixed maturity date and a coupon of 5% (subject to AEB's Maximum Distributable Amount; or MDA). Since November 2017, no new participations have been issued and participation holders can sell their participations to Aegon Nederland. Knab participations are considered AT1 Capital in accordance with Article 61 of the CRR.

### **Tier 2 Capital**

AEB does not have any Tier 2 Capital instruments as at 31 December 2018.

## **4.2 Capital ratios**

### **Total capital ratio**

During the year, AEB's total capital ratio increased by 1%, driven mainly by the addition of the audited 2017 earnings and a EUR 50 million capital injection from Aegon Nederland to facilitate future growth. AEB aims to maintain a strong capital position, seeking a total capital ratio of 21% by 2019.

### **Leverage ratio**

In accordance with Article 429 of the CRR, AEB is required to have a (non-risk weighted) leverage ratio above 3%. In accordance with Article 87 of the CRD IV, AEB is required to identify, monitor and manage the risk of excessive leverage. Internally AEB aims to have a leverage ratio above 3.6%.

At 31 December 2018, AEB's leverage ratio stood at 4.4%, well above the internal and external requirements.

### **Managing excessive leverage**

The total capital ratio, CET1 ratio and leverage ratio are reported to the ALCO on a monthly basis. In addition, three-to-five-year forecasts and comparisons with AEB's capital plan are reported to and discussed by the ALCO periodically. Internal buffers have been defined, including the actions to be undertaken if certain thresholds are breached.

### **SREP ratio**

DNB annually reviews AEB's ICAAP as part of SREP and assesses whether AEB holds enough capital given its risk profile, its peers, and/or market conditions. Based on this assessment, AEB receives a SREP decision letter, in which DNB stipulates and substantiates AEB's specific SREP capital requirements. AEB's internal monitoring system includes various buffers to ensure that AEB meets SREP capital requirements.

## **4.3 Minimum Required Eligible Liabilities**

In the coming years AEB plans to diversify its funding mix with the introduction of unsecured wholesale funding on its balance sheet. At the same time AEB plans to anticipate on Minimum Required Eligible Liabilities (MREL) requirements for LSI banks – expected in 2020 - with the issuance of an Senior Non-Preferred bond in June 2019. AEB will use the Single Resolution Board default formula as an indication of the forthcoming MREL requirement.

## 5 Credit risk

### 5.1 Credit risk management

During 2018, credit risk was monitored by the Credit Risk Committee (CRC), which reports to the MB. The CRC is responsible for monitoring the performance of the loan book and investment portfolio, focusing in particular on compliance with internal targets and limits as set out in the RAS. Chaired by the CRO, the committee members include management and senior representatives of business and risk departments. The CRC met on a monthly basis.

#### Risk measurement methodology

The capital required under Pillar 1 is calculated in accordance with the Standardized Approach (SA) as prescribed by the CRR. Under the SA, the CRR prescribes a standard classification of the exposures per asset class in order to determine the risk weight. Subsequently, the regulatory capital requirement is calculated by taking 8% of the total RWA.

In addition to monitoring the credit risk regulatory requirements, AEB also monitors the credit risk developments in its portfolio through internal reports and dashboards. Compliance with the Credit Risk Policy is monitored on a monthly basis.

### 5.2 Credit portfolio

This section deals with AEB's loans and advances to banks, the public sector and retail customers, interest-bearing securities in the banking book, and derivatives.

The credit risk exposure, expressed as Exposure at Default (EAD), increased by EUR 328 million compared to 31 December 2017. The overall risk weight percentage (RW%) has remained fairly stable, indicating that the credit portfolio grew without credit risk increasing in relative terms. Growth was driven mainly by growth in the retail loan book in line with AEB's strategy.

Asset category	Asset class	2017			2018		
		Leverage Exposure	RWA	RW%	Leverage Exposure	RWA	RW%
<b>Non-retail</b>	Bank	709	109	15%	579	91	16%
	Sovereign	1,608	-	0%	1,506	-	0%
	Public Sector Entities	458	12	3%	334	12	4%
	Securitization	738	179	24%	495	114	23%
	Corporate	188	129	70%	146	109	75%
	<b>Subtotal non-retail</b>	<b>3,701</b>	<b>429</b>	<b>12%</b>	<b>3,060</b>	<b>326</b>	<b>10%</b>
<b>Retail</b>	Mortgages	9,300	1,313	14%	9,794	1,338	14%
	Consumer loans	772	580	75%	1,076	810	75%
	SME loans	81	46	57%	260	149	58%
	<b>Subtotal retail</b>	<b>10,152</b>	<b>1,940</b>	<b>19%</b>	<b>11,130</b>	<b>2,297</b>	<b>21%</b>
<b>Other</b>	<b>Other</b>	<b>17</b>	<b>10</b>	<b>58%</b>	<b>8</b>	<b>3</b>	<b>42%</b>
<b>Total credit risk exposure</b>		<b>13,870</b>	<b>2,379</b>	<b>17%</b>	<b>14,198</b>	<b>2,626</b>	<b>18%</b>

Table 3: Credit risk exposures by asset class

## Retail portfolio

The Retail portfolio mainly consists of loans secured by mortgages on residential property and unsecured loans to consumers and small and medium-sized enterprises (SMEs). AEB has agreements in place with a number of lending platforms to be able to invest in consumer loans and SME loans. In order to ensure the availability of eligible loans, for some of the platforms AEB, under certain conditions, guarantees the purchase of loans for a fixed period of time and for a certain maximum amount.

Detailed information on AEB's exposure at 31 December 2018 is provided in the Annual Report, Section 4.4.11.

The impairment percentage increased for both consumer loans and SME loans, which reflects the maturing of these portfolios compared to their limited seasoning as of 31-12-2017. AEB's management recognizes that the bank's consumer and SME loan portfolios are relatively new and rapidly growing (except for the CACF portfolio). However, these portfolios also have a much shorter duration (generally between 3-5 years) and lower loan balances.

Asset class	2017				2018			
	Exposure (gross of impair.)	Impairments	Exposure (net of impair.)	% impaired	Exposure (gross of impair.)	Impairments	Exposure (net of impair.)	% impaired
Mortgages	9,304	4	9,300	0%	9,794	0.3	9,794	0%
Consumer loans	807	35	773	4%	1,194	75	1,120	6%
SME loans	82	1	81	1%	268	8	260	3%

Table 4: Impairments in the retail loans portfolios

## Secured by mortgages on residential property

AEB's mortgages are originated and serviced by Aegon Hypotheken B.V., a subsidiary of Aegon Nederland. Aegon Hypotheken B.V. has strict underwriting processes, which are aligned with AEB's credit risk appetite in terms of its mortgage portfolio.

Table 5: Exposure to mortgages by LtV bucket at 31 December 2017 and 31 December 2018

shows that most of the mortgages are backed by an NHG guarantee (73% of the total mortgage portfolio). The largest portion (15.1%) of non-NHG backed mortgages is in the 40%-80% bucket. AEB's strategy going forward is to maintain a high portion of NHGs in its mortgage portfolio.

Mortgages	2017		2018	
	Exposure (net of impairments)	% of Total	Exposure (net of impairments)	% of Total
NHG guaranteed Amount	5,517	59%	5,551	57%
LTV less than 80%	2,779	30%	3,691	38%
LTV more than 80%	1,004	11%	552	6%
<b>Total</b>	<b>9,300</b>	<b>100%</b>	<b>9,794</b>	<b>100%</b>

Table 5: Exposure to mortgages by LtV bucket at 31 December 2017 and 31 December 2018

## Consumer loans and SME loans

AEB invests in consumer loans and SME loans through several third-party lending platforms. The lending platforms provide a variety of services related to origination, client management, and collection and receivables processes. AEB has specific mandate agreements in place with each servicer detailing, amongst other things, AEB's credit risk appetite.

Table 6 shows the geographical distribution of consumer loans by country. The Dutch portfolio has significantly decreased in line with expectations, as the Dutch consumer loans portfolio is a closed book and in run-off. The UK and German portfolios have increased rapidly through our strategic lending partners in these countries. The French portfolio decreased slightly as it became a closed book in the third quarter of 2018.

	2017			2018		
	Leverage Exposure	RWA	RW%	Leverage Exposure	RWA	RW%
the Netherlands	293	220	75%	215	162	75%
Germany	199	150	75%	431	324	75%
the UK	213	159	75%	377	283	75%
France	68	51	75%	54	40	75%
<b>Total Consumer Loans</b>	<b>772</b>	<b>580</b>	<b>75%</b>	<b>1,076</b>	<b>810</b>	<b>75%</b>

Table 6: Geographical distribution of consumer loans EAD by country

AEB's exposure to SME loans in the UK has grown in line with its strategic plans in 2018. The Dutch SME loans portfolio remains of limited size as it supports separate account crowdfunding investments available for Knab clients.

Servicer	2017			2018		
	Leverage Exposure	RWA	RW%	Leverage Exposure	RWA	RW%
the UK	79	45	57%	258	148	57%
the Netherlands	1	1	76%	2	1	76%
<b>Total SME loans</b>	<b>81</b>	<b>46</b>	<b>58%</b>	<b>260</b>	<b>149</b>	<b>58%</b>

Table 7: Geographical distribution of SME loans EAD by country

Table 8 shows the industry distribution of the UK loans portfolio. The portfolio is considered well-diversified across several industries. AEB monitors the distribution based on the Hirschmann Herfindahl Index using the RWA by industry.

SIC category	2017		2018	
	RWA	HHI	RWA	HHI
Agriculture, Forestry and Fishing	-	0%	0.9	0%
Mining and Quarrying	0.3	0%	0.2	0%
Manufacturing	4.3	1%	13.5	1%
Electricity, gas, steam and air conditioning supply	0.1	0%	0.3	0%
Water supply, sewerage, waste management and remediation	0.2	0%	1.0	0%
Construction	5.8	2%	20.9	2%
Wholesale and retail trade; repair of motor vehicles and motorcycles	6.3	2%	24.2	3%
Transportation and storage	1.6	0%	5.1	0%
Accommodation and food service	2.0	0%	7.2	0%
Information and communication	4.1	1%	11.0	1%
Financial and insurance	1.0	0%	2.3	0%
Real estate	0.8	0%	3.3	0%
Professional, scientific and technical	4.9	1%	16.7	1%
Administrative and support service	4.7	1%	15.5	1%
Public administration and defense; compulsory social security	0.1	0%	0.1	0%
Education	0.8	0%	1.8	0%
Human health and social work	1.6	0%	5.7	0%
Arts, entertainment and recreation	1.3	0%	3.8	0%
Other service activities	2.2	0%	4.8	0%
Activities of households as employers; undifferentiated goods- and services-producing activities of households for own use	0.2	0%	0.3	0%
Extraterritorial organizations and bodies	0.1	0%	0.1	0%
Not classified	2.9	0%	9.4	0%
<b>Total</b>	<b>45</b>	<b>9%</b>	<b>148</b>	<b>10%</b>

Table 8: Industry distribution of UK loans EAD by industry (based on SIC classification)

### Non-retail portfolio

The non-retail portfolio currently consists of an investment portfolio and a treasury portfolio (cash management). The portfolios are managed by Aegon Asset Management (AAM) and Aegon Group Treasury (Aegon NV's treasury department) respectively, under terms and agreements mandated by AEB.

For the exposure classes covered by the investment portfolio and treasury portfolio, credit quality steps are used to assign risk weights. For exposures to counterparties for which a credit assessment is available from an External Credit Assessment Institution (ECAI), AEB applies credit quality steps in accordance with the CRR. If no credit assessment or surrogate is available, the bank assigns a risk weight of 100%. For credit assessments of exposures to obligors, AEB uses the rating scales of and ratings assigned by S&P, Moody's, and Fitch.

Movements in the investment portfolio are monitored through periodic reporting. The reports detail fair market value changes for various exposure types<sup>7</sup> and rating grades and price and yield developments at ISIN-level. Separate reports specific to asset-backed exposures monitor, amongst other things, the level of credit enhancement and collateral performance. These reports are presented to the Credit Risk Committee on a monthly basis.

<sup>7</sup> Such as Asset Backed Securities (other than CDO's and CLO's), CDO's or CLO's, Sovereign Debt, Corporate Credits and Covered Bonds

At 31 December 2018, AEB's own securitization activity was limited to its outstanding 2013 Kigoi B.V. transaction, with regard to which AEB has continued to hold all notes issued by the SPV. The underlying assets of that transaction are Dutch consumer loan exposures. Because all notes are held by AEB, the structure is consolidated on AEB's balance sheet, and risk weights for loans sold to the SPV are determined on a look-through basis. In 2018 the residential mortgage backed transaction SAECURE 13 NHG B.V. was wound down on its First Optional Redemption Date following the repurchase of the mortgage loans by AEB. At 31 December 2018, AEB had no specific assets earmarked for securitization. Nor did AEB undertake any securitization activities in 2018.

	2018		2017	
	Notional	RWA	Notional	RWA
<b>The total amount of outstanding exposures securitised by the institution</b>	227	157	304	212
<b>The aggregate amount of on- balance sheet securitisation positions retained or purchased</b>	212	184	283	220
<b>off-balance sheet securitisation exposures</b>	54	8	77	11

Table 9: Outstanding exposures securitized per 31 December 2017 and 31 December 2018

### Counterparty credit risk

Part of the non-retail bank portfolio is exposed to the counterparty credit risk (CCR). AEB is applying the Standardized Approach to measure EAD for CCR. Table 10 lists entities where AEB has a direct exposure to. The EAD increased from EUR 52 million in 2017 to EUR 69 million in 2018. This increase relates primarily to CCR originating from derivatives exposures entered into for the purpose of interest rate risk management.

Counterparty	2017		2018	
	EAD	RWA	EAD	RWA
ABN AMRO	0.8	0.4	0.7	0.4
Aegon NV	1.4	0.3	2.7	0.5
Banco Santander, S.A.	0.7	0.4	0.9	0.4
Barclays PLC	0.4	0.2	0.4	0.2
BNP Paribas	0.6	0.3	0.6	0.3
Citigroup Inc.	2.7	1.3	2.5	1.3
Rabobank	8.6	1.7	-	-
Credit Suisse Group AG	0.7	0.4	0.5	0.2
Deutsche Bank AG	0.9	0.5	-	-
Deutsche Bank Aktiengesellschaft	0.3	0.1	0.9	0.5
HSBC Bank PLC	3.5	0.7	3.1	0.6
HSBC Holdings PLC	0.3	0.1	-	-
ING	0.3	0.1	0.3	0.1
JP Morgan Securities PLC	23.8	11.9	50.3	10.1
Merrill Lynch International	1.3	0.7	1.2	0.6
Morgan Stanley	0.6	0.3	0.6	0.3
Nomura Holdings, Inc.	0.9	0.4	0.9	0.4
Other	0.3	0.1	0.0	0.0
RBS	1.3	0.6	1.0	0.5
Societe Generale	1.2	0.6	1.1	0.6
UBS AG	1.4	0.7	1.4	0.7

Counterparty	2017		2018	
	EAD	RWA	EAD	RWA
<b>Total CCR</b>	<b>51.9</b>	<b>21.9</b>	<b>69.2</b>	<b>17.7</b>

Table 10: Overview of counterparties of AEB's derivatives

### Past due and impaired (defaulted) loans

A financial asset is past due when the counterparty fails to make payment when due under the contract. A financial asset is impaired and an impairment loss is incurred if, and only if, there is objective evidence of impairment as a result of one or more events occurring after initial recognition of the asset and that event has an impact on the financial asset's estimated future cash flows that can be reliably estimated.

AEB takes the following factors into account when deciding whether to impair a financial asset:

- the issuer or obligor being in significant financial difficulty;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- the lender granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;
- it becoming probable that the borrower will enter bankruptcy or other financial reorganization;
- the disappearance of an active market for that financial asset because of financial difficulties; or
- observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group.

Once the impairment loss is reversed in a subsequent period, the asset is no longer considered to be impaired. If the terms and conditions of the financial asset are renegotiated, the new agreement applies in determining whether the financial asset is past due.

Detailed information on AEB's exposure at 31 December 2018 is provided in the Annual Report, Section 4.4.11.

## Required capital

Table 11 shows that the capital required for credit risk increased by EUR 22 million compared to 31 December 2017, driven by growth in the retail portfolio and offset slightly by the decrease in securitization positions.

Asset category	Asset class	2017	2018
<b>Non-retail</b>	Bank	9	7
	Sovereign	-	-
	Public Sector Entities	1	1
	Securitization	14	9
	Corporate	11	9
	<b>Subtotal non-retail</b>		<b>38</b>
<b>Retail</b>	Mortgages	105	107
	Consumer loans	46	65
	SME loans	5	12
	<b>Subtotal retail</b>	<b>156</b>	<b>184</b>
<b>Other</b>	Other	1	-
<b>Total credit risk capital estimate</b>		<b>192</b>	<b>210</b>

Table 11: Capital required for credit risk

## 5.3 Credit valuation adjustment (CVA)

AEB enters into derivatives contracts for hedging purposes only. Derivatives are used to hedge interest rate risk and FX risk. By entering into these derivatives, AEB becomes exposed to credit value risk on the derivatives contract. Credit value risk is defined as the risk that the value of derivative positions taken by AEB will fluctuate driven by changes in the financial position of the counterparty to the derivatives contract.

The process of entering into contracts and managing collateral on derivatives contracts has been outsourced to Aegon Global Derivatives and Hedging.

From May 2016 onwards, all new IRSs are cleared centrally, which reduces credit value risk for AEB. All IRSs entered into before May 2016 are bilateral derivatives which are cash collateralized on a daily basis through International Swaps and Derivatives Association (ISDA) contracts and Credit Support Annexes (CSAs) with all counterparties.

### Risk measurement methodology

The risk limit for counterparty risk is expressed in terms of the capital requirements for AEB's derivatives contracts under the CRR. Those capital requirements consist of a charge for the Credit Valuation Adjustment (CVA) and a charge for counterparty credit risk. Within the CRR framework, the CVA charge is only applicable to bilateral derivatives. Counterparty credit risk applies to both centrally cleared and bilateral derivatives.

AEB uses the Standardized Approach to determine its capital requirements for CVA risk, as prescribed in Title VI of the CRR and Article 384 in particular. AEB considers the Standardized Approach to be appropriate to estimate the capital it needs to cover CVA risk, given AEB's size and relatively small and simple derivative positions.

### Required capital

AEB's required capital for CVA risk remained stable at EUR 2 million during the year. The number of bilateral derivatives did not increase, with the credit quality of existing counterparties to OTC derivative transactions remaining stable in 2018.

## **6 Operational Risk**

The operational or non-financial risks within AEB's ERM framework are classified according to Aegon N.V.'s operational risk taxonomy and are defined as losses resulting from inadequate or failing internal processes, controls, people or systems, or external events. The lower level risk categories are grouped into the following eight higher level risk categories:

1. Business risk;
2. Legal, regulatory, conduct & compliance risk;
3. Financial crime risk;
4. Processing risk;
5. Systems and business disruption risk;
6. Tax risk;
7. People risk; and
8. Facility risk.

Tax risk, people risk and facility risk are deemed immaterial to Aegon Bank. The first five sub-risk types are described in greater detail in the following sections.

### **6.1 Operational risk types**

#### **6.1.1 Business risk**

Aegon defines business risk as the risk of loss resulting from failing or inadequate strategy execution, governance, project risk or pricing. In terms of business risk, the most significant underlying risks for AEB are:

1. Strategy execution risk;
2. Unbundling risk; and
3. Project risk.

To support the bank's growth and improve strategy development and implementation, AEB introduced new roles and departments in 2017 and 2018. In order to adapt to the rapidly changing environment, Knab has adopted an agile way of working. Knab has a high NPS, which is one of the key drivers of growth in its customer base and not easy for new competitors to replicate. The Aegon Bank label has a solid position in the bank savings market ("Box 1"), with a broad network of intermediaries. AEB has a market share of 6.5% of Box 1 savings deposits.

Unbundling risk covers the largest part of the capital required for business risk. Unbundling risk is the risk of potential future losses due to a forced separation of AEB from its parent company Aegon Nederland or Aegon NV. Being part of a financial conglomerate has disadvantages as well as benefits. Benefits include the well-known brand, synergies from shared services, and potential (capital) support from the parent companies. Potential disadvantages are that the parent companies, or Aegon affiliates, may run into financial difficulties or face reputational problems, which could affect AEB's business model and/or financials. In such circumstances, AEB might need to separate some of its business and/or operational relationships from its parent company, or cut the ties with its parent company altogether, in order to ensure its own financial stability.

### **6.1.2 Legal, regulatory, conduct & compliance risk**

AEB defines legal, regulatory, conduct & compliance risk as the risk of loss resulting from non-voluntary legal obligations, inadequate legal documentation, inadequate patenting of brands or intellectual property, and the risk of impairment to the organization's business model, reputation, integrity or financial condition resulting from failure to comply with laws, regulations or internal company rules and policies, or the late identification of significant legal and regulatory developments, possibly resulting in the inability to influence the final outcome. In terms of legal, regulatory, conduct & compliance risk, significant underlying risks for AEB are:

1. Legal and regulatory;
2. Company-related; and
3. Customer-related.

During 2018, AEB experienced a number of risk events arising from customers going bankrupt. In the case of bankruptcy, the customer's accounts have to be blocked immediately to prevent any further transactions being made by that customer. Significant scenarios that have been taken into account involving legal and regulatory risk are:

- Failure to comply with duty of care regulations;
- Failure to identify and adopt legal developments and requirements;
- NHG claim risk.

As regards non-compliance with its duty of care, AEB considers this to be a remote risk because the company has embedded its duty of care into the way in which it communicates with its customers and into its product approval and review processes. Moreover, there have been no significant incidents in the recent past.

Legal developments and newly introduced requirements are monitored by specialists from the Board Office and AEB's legal team. The implementation of large-scale new requirements is governed by portfolio management, which provides for the monitoring of significant projects undertaken by AEB.

NHG claim risk is the risk that AEB may not be able to recover all claims covered by NHG guarantees, for example because of operational errors in the origination of the mortgages and/or incomplete files leading to non-compliance with the NHG terms and conditions.

Notwithstanding an NHG guarantee, AEB may still incur losses on NHG-backed mortgages, for example if the defaulted individual loan was provided without full compliance with the NHG terms and conditions and is therefore ineligible for payment under the NHG guarantee. Also, under an industry-wide arrangement that came into force in 2013, AEB incurs 10% of the realized loss on a mortgage loan with the NHG guarantee.

Aegon defines customer-related risk as the risk of loss arising from failure to comply with regulations with regard to politically and reputationally exposed persons and export control transactions via countries against which sanctions have been imposed.

### **6.1.3 Financial crime risk**

Aegon defines financial crime risk as a wrongful act, omission or breach of duty or trust intentionally committed by an Aegon employee, intermediary or external party and which could harm Aegon or any other party. This sub-risk type comprises the following underlying risks:

1. Internal fraud;

2. External fraud; and
3. Money laundering.

All underlying sub-risk types are covered by a scenario analysis. For financial crime risk, AEB takes into account scenarios for all underlying risks and fraud-related incidents. These include, but are not limited to, phishing, skimming and identity fraud.

#### **6.1.4 Processing risk**

Processing risk is defined as the risk of loss resulting from inadequate or failing administrative processes or related internal controls, inadequate capturing of source data, reporting errors, modelling errors or failing outsourcing and supplier arrangements. In terms of processing risk, significant underlying risks for AEB are:

1. Reporting;
2. Modelling; and
3. Outsourcing & supplier.

AEB has put in place policies and procedures to ensure accurate and timely reporting. The models used by AEB support both the decision-making processes and reporting processes. To manage its modelling activities, AEB operates (1) a Model Governance Framework, (2) a standardized Model Development Process, (3) an internal Model Development Team, and (4) a risk-based timetable for the development of key models (approved by the Management Board).

The main outsourcing and supplier risks are considered to be (1) discontinuity of services by outsourcing partners, and (2) the high number of outsourcing agreements. AEB has introduced monitoring and controls to mitigate these potential risks.

#### **6.1.5 Systems and business disruption risk**

This is the risk of loss resulting from inadequate or failing business continuity plans, back-up and recovery or fall-back arrangements, IT security, IT maintenance or change management, identification of relevant technological developments, and other technical causes of systems-related failures or errors. In terms of systems risk, significant underlying risks for AEB are:

1. IT security (mainly related to cybercrime); and
2. Business continuity.

AEB continuously monitors, updates and maintains its IT systems and processes. The bank also has in place business contingency plans (Aegon Nederland Business Continuity Plan for the Aegon Bank label, and Knab Business Continuity Plan for the Knab label) in order to effectively respond to events that could lead to disruptions to its systems and processes.

## 6.2 Risk measurement methodology

In order to determine the capital requirement for operational risk under Pillar 1, AEB uses the Basic Indicator Approach (BIA). Accordingly, the capital requirement for operational risk is defined as 15% of the average 'relevant indicator' for the last three of twelve-monthly observations<sup>8</sup> at the end of AEB's financial year. AEB also calculates a Pillar 2 capital estimate for operational risk. The total capital (Pillars 1 and 2) required for operational risk is shown in the following table:

	2017	2018
Operational Risk Pillar 1	11	16
Operational Risk Pillar 2	69	73
<b>Total capital estimate</b>	<b>80</b>	<b>89</b>

Table 12: Total capital estimate for operational risk

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<sup>8</sup> The relevant indicator for AEB is the sum of net interest income and net non-interest income and consists of the following elements (positive or negative): Interest receivables and similar income, Interest payable and similar charges, Income from shares and other variable/fixed-yield securities, Commissions/fees receivable, Commissions/fees payable, Net profit or loss on financial operations and Other operating income.

## **7 Market Risk (FX Risk)**

AEB's functional currency is the euro, which means that FX risk arises if a currency other than the euro is used in transactions, creating exposure to potential adverse movements in exchange rates. AEB is exposed to FX risk through its UK loan portfolio. AEB's objective is to fully hedge its GBP-denominated lending activities on an IFRS equity neutral basis. FX risk in the loan portfolio could materialize if actual cash flows differ from expectations or there is any adverse movement in exchange rates and the hedge needs to be rolled over.

### **Risk measurement methodology**

In order to determine its capital requirement for FX risk, AEB currently uses the Standardized Approach described in Articles 351-354 of the CRR. Article 351 provides that an institution must allocate capital for FX risk if the sum of its overall net FX position exceeds 2% of its total own funds. The net FX position for each currency is calculated by reference to the difference between the short FX position and long FX position, with the amounts being denominated in the reporting currency. The capital requirement for FX risk under the Standardized Approach is determined by taking the total net FX position denominated in the reporting currency (EUR) and multiplying it by 8%.

AEB applies the VaR methodology to monitor currency risk internally. The VaR represents the sum of potential financial losses on foreign currencies in one year with a confidence level of 99.5%. The VaR is also reported to the ALCO.

### **Required capital**

AEB's required capital for FX risk was EUR nil million at 31 December 2018 due to the bank's limited exposure to FX risk, with the net position remaining below the 2% threshold.

## 8 Interest rate risk in the banking book

### 8.1 Risk description

IRRBB is an important risk type inherent to banking activities. It arises from the transformation function performed by banks: funding long-term loans from short-term deposits. Maturity and interest rate mismatches between a bank's assets and liabilities will expose the bank to interest rate risk, which may adversely affect the economic value of its equity and earnings. Interest rate risk is amplified by the use of embedded options in many common banking products (e.g. prepayment options on loans or early withdrawal options for term deposits).

In line with EBA guidelines, AEB identifies three material categories of IRRBB: gap risk, option risk, and basis risk.

- Gap risk – risk resulting from the term structure of interest rate-sensitive instruments and arising from differences in the timing of rate changes, including changes to the term structure of interest rates occurring consistently across the yield curve (parallel risk) or differentially by period (non-parallel risk).
- Option risk - risk arising from options (embedded and explicit), where the institution or its customer can alter the level and timing of their cash flows, more specifically the risk arising from interest rate-sensitive instruments where the holder will almost certainly exercise the option if it is in their financial interest to do so (embedded or explicit automatic options) and the risk arising from flexibility embedded implicitly or within the terms of interest rate-sensitive instruments, such that changes in interest rates may affect a change in the client's behaviour (embedded behavioural option risk).
- Basis risk – risk arising from the impact of relative changes in interest rates on interest rate-sensitive instruments that have similar tenors but are priced using different interest rate indices. It arises from the imperfect correlation in the adjustment of the rates earned and paid on different interest rate sensitive instruments with otherwise similar rate change characteristics.

Furthermore, credit spread risk in the banking book and pipeline risk are also part of AEB's risk identification and internal capitalization for IRRBB.

- Credit spread risk from non-trading book activities (CSRBB) – any kind of spread risk of interest rate-sensitive instruments that is not IRRBB or credit risk.
- Pipeline risk – the risk that interest rates (and hence mortgage rates) rise in the period between the application for mortgage and mortgage issue dates, i.e. mortgage loans at application date have a lower coupon compared to the mortgage rates in the (current) market.

In line with EBA Guidelines on IRRBB<sup>9</sup>, Articles 12 and 26, CSRBB is not included in AEB's Pillar 2 capital estimate. However, spread risk and pipeline risk are included in the Alert Zone as described in AEB's Capital Management Policy.

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<sup>9</sup> Reference: EBA/CP/2017/19. 31/10/2017

## 8.2 Risk measurement methodology

AEB calculates an IRRBB internal capital estimate for the following sub-risk types:

- Gap risk (Pillar 2);
- Option risk (Pillar 2);
- Basis risk (internal management buffer);
- Credit spread risk (internal management buffer); and
- Pipeline risk (internal management buffer).

The capitalization measurement approach for gap risk and option risk is determined as the worst outcome of a number of economic value-at-risk (EVaR) and earnings-at-risk (EaR) scenarios. The table below gives a general description of the capitalization measurement approach for both gap risk and option risk.

Consideration	Description
<b>Combine EVE and EaR</b>	To include the risks to both earnings and economic value is a requirement under the EBA 2017 Guidelines on IRRBB. Article 26.e specifically requires that account must be taken of the impact on economic value and earnings. Article 23 requires that the amount of capital be commensurate with the level of IRRBB and "institutions are not expected to double count capital for economic value and earnings measures". Using the maximum potential loss of an earnings metric and value metric is an effective way of taking both metrics into account for capitalization purposes.
<b>Use of scenarios</b>	<p>EBA requires banks 'to not only rely on the supervisory outlier test' for their capitalization (Article 25, 2017 guideline). AEB interprets this as follows: institutions should take both the supervisory outlier test and internal scenarios into account.</p> <p>AEB believes that the most appropriate approach is to capitalize based on a set of scenarios. This involves taking both the supervisory outlier test and internal scenarios into account. AEB has chosen a set-up where it capitalizes for a number of internal and external scenarios. The seven AEB-specific scenarios are interest rate and CPR shock scenarios that have been developed internally in accordance with the nature, scale and complexity of AEB's portfolio. The scenarios make the capitalization formula more transparent and allow for the explicit inclusion of the supervisory outlier test and internal scenarios.</p>
<b>Choice of scenarios</b>	<p>AEB uses the following scenarios for capitalization purposes:</p> <p><b>6 EBA scenarios:</b></p> <ul style="list-style-type: none"> <li>• Parallel +200 bps</li> <li>• Parallel -200 bps</li> <li>• Short rates up</li> <li>• Short rates down</li> <li>• Steepener</li> <li>• Flattener</li> </ul> <p><b>7 Internal scenarios:</b></p> <ul style="list-style-type: none"> <li>• Low rates scenario</li> <li>• Inflation scenario</li> <li>• EBA stress scenario</li> <li>• Rates up</li> <li>• Rates down</li> <li>• Long rates up</li> <li>• Long rates down</li> </ul>

Table 13: General description of capitalization measurement approach for gap risk and option risk

### 8.3 Internal capital estimate

Table 14 shows the internal capital estimate for IRRBB at 31 December 2018. In AEB's Capital Management zones, AEB will adjust its capital allocation to IRRBB dynamically if its IRRBB profile changes. More granular results are shown in the subsections below.

<b>Risk type</b>	<b>2017</b>	<b>2018</b>
Gap risk	38	48
Option risk	38	25
<b>IRRBB Pillar 2 capital estimate</b>	<b>77</b>	<b>73</b>

Table 14: Internal capital estimate for IRRBB at 31 December 2018 and 2017

#### 8.3.1 Gap risk and option risk

AEB's internal capital estimate for IRRBB is based on the combined maximum loss of gap risk and option risk under 13 interest rate risk scenarios. AEB incurs the highest loss of Economic Value of Equity (EVE) under the EBA -2% parallel shock scenario. Hence, this scenario determines the total capitalization (EUR 72.7 million) for gap risk and option risk combined.

The maximum loss due to gap risk is EUR 48.0 million worth of earnings under the EBA - 2% parallel scenario, which is therefore the internal capital estimate for gap risk.

The capitalization for option risk is calculated as the difference between the total IRRBB internal capitalization estimate and the capitalization for gap risk. As a result, the internal capital estimate for option risk was EUR 24.7 million under ICAAP 2018.

#### 8.3.2 Basis risk

Movements in the reference curve for the mortgage portfolio (from 3M EURIBOR to 6M EURIBOR curve) resulted in the elimination of the mismatch between the mortgage and interest rate swaps reference curves (also valued using 6M EURIBOR). This led to the elimination of basis risk at 31 December 2018.

#### 8.3.3 Pipeline risk

At 31 December 2018, AEB was not vulnerable to any pipeline risk. AEB holds capital for pipeline risk in the internal capital management zones in case this risk arises as a result of large orders.

## **9 Liquidity Management**

### **9.1 Liquidity Risk Management Framework**

The primary goal of AEB's liquidity risk management is to ensure compliance with internal targets and external requirements at all times and to have sufficient liquidity available to support AEB's strategy. AEB's liquidity need is based on its risk appetite and business plans and the expectations and requirements of external stakeholders, such as its customers, regulators and investors.

The current framework of limits and target levels is described in the Risk Appetite document. AEB evaluates its risk appetite at least annually to ensure that the Risk Appetite Statement (RAS) and corresponding risk tolerances are still adequate. In addition, AEB assesses whether advanced or new insights should lead to adjustments being made to its business strategy and/or risk appetite.

Moreover, ALM & Methodology and FRM, in their first and second line of defense functions, assess AEB's liquidity adequacy on a monthly basis, providing actuals and forecasts for all RAS-liquidity metrics. AEB also has in place a liquidity trigger framework, consisting of different leading and supporting triggers related to the appropriate management urgency level. Both the current level of and outlook for these triggers are assessed. The trigger framework is laid down in the Recovery Plan and fully aligned with the RAS.

As described in AEB's Liquidity Risk Policy, ALM & Methodology is the first line of defense with regard to liquidity risk management. Aegon Group Treasury is responsible for managing the cash position while at the same optimizing risk-return ratios. As such, the daily cash liquidity positions are reported by Aegon Group Treasury on a daily basis. ALM & Methodology actively monitors AEB's liquidity position, and reports its findings to the ALCO.

The second line control is FRM. FRM validates the models and assumptions used by ALM & Methodology and performs Risk Compliance checks, which among other things involves checking the Key Risk Indicators (e.g. LCR, NSFR, level of overnight cash), Key Performance Indicators and Recovery Plan Indicators against their predefined limits. Aegon NL Internal Audit provides the third line of defense.

### **9.2 Funding Strategy**

AEB's funding strategy consists of a mix of savings deposits, mainly variable rate savings at Knab and tax-friendly ("Box 1") bank savings deposits at Aegon Bank, and wholesale funding currently in the form of covered bonds. In the coming years AEB plans to diversify its funding mix and to add unsecured wholesale funding to the funding mix, acting ahead of MREL requirements for LSI banks.

The exact timing and type of funding transactions depend on market conditions at the time and the actual funding need. If the funding need is higher than anticipated, there is room for additional unsecured funding or covered bonds. In addition, AEB can use its liquidity buffer through European Central Bank refinancing operations or repos with other parties. In case of liquidity stress, AEB has a Liquidity Contingency Plan in place, as part of its Recovery Plan.

### 9.3 Current liquidity buffer

At 31 December 2018, the liquidity buffer (HQLA<sup>10</sup>) amounted to EUR 1,965 million (adjusted for haircuts). A substantial part of the liquidity buffer consists of cash held in the DNB account (EUR 1,196 million), excluding the cash reserve requirement because this cannot be freely withdrawn. It should be noted that the underlying assets making up the liquidity buffer are all denominated in euros. The concentration risk of the liquidity buffer is limited.

### 9.4 Liquidity Coverage Ratio

AEB uses the LCR to monitor the short-term resilience of its liquidity risk profile. The aim is to ensure that AEB has an adequate stock of unencumbered HQLA that can be easily and immediately converted into cash in private markets to meet the bank's liquidity needs under a 30-calendar day liquidity stress scenario<sup>11</sup>. The LCR is calculated by dividing the 'stock of HQLA' by the 'net outflow', for which a 100% regulatory minimum applies from 1 October 2015.

AEB's current strong short-term liquidity position reflects the high amount in cash deposits held with the ECB and the quality of AEB's investment portfolio, a large part of which consists of Level 1 or Level 2 assets. The Statutory Board highly values prudent liquidity management and having access to sufficient liquidity because that is important for institutional confidence and stakeholder management. The LCR ratio target level is based on that approach.

At 31 December 2018, the LCR ratio was 209%, which is above internal and external limits and requirements. If the LCR is forecasted to fall below the required internal limit, AEB will prepare a plan to increase the LCR. One option will be to sell non-qualifying positions and to convert assets into Level 1 or Level 2 assets. Other possibilities are to attract long-term funding (wholesale or retail). Please refer to the Appendix for details of the Liquidity Coverage Ratio.

### 9.5 Net Stable Funding Ratio

The NSFR requires AEB to maintain a stable funding profile in relation to the composition of its assets and off-balance sheet activities. A sustainable funding structure is intended to reduce the likelihood that disruptions to AEB's regular sources of funding will erode its liquidity position in a way that would increase the risk of failure and potentially lead to broader systemic stress. The NSFR penalizes high reliance on short-term wholesale funding, encourages improved assessment of funding risk across all on- and off-balance sheet items, and promotes funding stability.<sup>12</sup>

The NSFR is calculated by dividing the 'Available Stable Funding' by the 'Required Stable Funding', both of which are defined for a 12-month horizon. The NSFR is reported to the Dutch Central Bank on a quarterly basis. In December 2018, the NSFR ratio was 141%, which is above internal and external limits and requirements. If the NSFR is forecasted to fall below the internal limit, AEB will prepare a plan to increase the NSFR. One option will be to convert positions with a high RSF weight into assets with a low RSF weight. In addition, actions may be initiated to attract long-term funding (wholesale or retail).

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<sup>10</sup> The definition of High Quality Liquid Assets (HQLA) is based on the LCR.

<sup>11</sup> <http://www.bis.org/publ/bcbs238.pdf>

<sup>12</sup> <http://www.bis.org/bcbs/publ/d295.pdf>

## 9.6 Liquidity Stress Testing

AEB uses three standard scenarios for internal Liquidity Stress Testing (LST) purposes:

- Group Scenario;
- Entity Specific Scenario; and
- Reverse Scenario

Pursuant to Aegon N.V.'s liquidity risk policy, AEB runs a stressed liquidity scenario that is also used by all other Aegon entities (the [Aegon] Group scenario). The Group scenario is defined as a "run on the bank" scenario where policy and contract-holders demand cash at a highly accelerated rate, applied over a duration of two full years. Demands for cash are driven by an immediate and permanent parallel increase in interest rates and outflows from savings deposits, among other things.

In addition, each Aegon entity is required to perform a stress test based on a locally defined liquidity stress scenario that is appropriate to the entity's individual business model (the Entity Specific Scenario). The Entity Specific Scenario for AEB has been designed in close cooperation with FRM, as detailed in the AEB LST Model Documentation.

For the Reverse Scenario, the savings deposits outflow is used as a risk parameter to which additional stress is applied until an excess liquidity of zero is reached.

Responsibility for the model and annual reviews lies with ALM & Methodology, with FRM being responsible for risk monitoring, reporting, and validation in accordance with the Model Validation Policy.

## 9.7 Liquidity Stress Management and AEB's Recovery Plan

In times of liquidity stress, it is important to take decisive and effective action. AEB's approach to liquidity stress is set out in its Recovery Plan. This plan defines liquidity triggers that activate the Crisis Management Team.

As part of AEB's Recovery Plan, a Contingency Funding Plan is in place that sets out the strategies for addressing liquidity shortfalls in emergency situations. Controls have been defined, all of which are intended to materially improve AEB's liquidity position in the event of a near-default. The plan describes for each control its potential impact and implementation, including responsibilities and expected hurdles.

## 9.8 Encumbered Assets

The Asset Encumbrance Ratio (AER) is related to liquidity risk, because elevated encumbrance means that there are fewer assets available for liquidation or capable of being pledged when needed.

Monitoring the AER has become more important with the issuance of four Covered Bonds on 31 December 2017. In 2018 AEB also repurchased securitized notes (SAECURE 13 Program) backed by mortgages, which has been called on the First Optional Redemption Date in February 2018. AEB issued the EUR 750 million (1 tranche) RMBS program (SAECURE 13) on 27 March 2013. In addition, collateral provided to other parties (Aegon Derivatives, KAS Bank) in order to conduct business activities has also been encumbered.

AEB launched a covered bond programme to meet its funding needs as part of its funding strategy in November 2015. Covered bonds are regarded by investors as a safe investment, given their high ratings and double recourse mechanism. In 2018, S&P and Fitch confirmed their AAA/AAA rating of AEB's covered bond programme.

In normal market conditions, the covered bond programme gives AEB access to additional investors alongside investors in the RMBS market.

AEB currently has EUR 2,250 million in covered bonds (EUR 750 million in November 2015, EUR 500 million in May 2016, EUR 500 million in June 2017, and EUR 500 million in November 2017) outstanding under its covered bond programme.

## 10 Remuneration

### *Remuneration policy*

The remuneration for Aegon Bank Board members is in line with Aegon Bank's remuneration policy, as approved by the Supervisory Board in May 2018.

Aegon Bank pursues a careful, sound and sustainable remuneration policy. In line with Aegon Nederland, Aegon Bank has adopted the Regulation on Sound Remuneration Policies (*Regeling beheerst beloningsbeleid*). Aegon Bank's remuneration policy complies with the requirements stipulated in that regulation.

Aegon Bank's remuneration policy covers the Management Board, management teams, senior management and other Aegon Bank employees, and complies with applicable national and international regulations as well as the Governance Principles. Based on criteria laid down in the European Banking Authority Regulatory Technical Standards (EBA RTS), Aegon Bank designated a number of employees as Identified Staff in 2018.

The bank's remuneration policy also complies with Aegon Group's Global Remuneration Framework 2018 (AGGRF 2018), drawn up by Aegon N.V., and has due regard to developments in society. AEB's remuneration policy is in line with Aegon Nederland's strategy, vision, core values and risk appetite.

### *Governance*

In accordance with Aegon Banks' remuneration policy, the Supervisory Board's duties and responsibilities are to: (i) approve the general principles of the remuneration policy, (ii) review those principles regularly, (iii) determine the remuneration policy for the Management Board, (iv) review the remuneration of Identified Staff, (v) instruct the Management Board to implement the remuneration policy, and (vi) instruct the Remuneration Steering Group and/or Internal Audit to assess the application of the policy and procedures covered.

Under the governance provisions of Aegon Bank's remuneration policy, the Supervisory Board is authorized, based on the results of an ex-post assessment, to suspend or cancel all or any part of the variable remuneration granted conditionally to Identified Staff ('malus clause').

The governance provisions also confer on the Supervisory Board the power to recover any variable remuneration paid to management team members or senior management if granted on the basis of inaccurate financial or other information ('claw-back clause').

The remuneration policy and its implementation were discussed at a Supervisory Board meeting on 31 January 2018. The Supervisory Board also discussed the level of variable remuneration, and approved the variable remuneration targets for Identified Staff for 2018 within the framework set out in the AGGRF. The variable remuneration paid was found to be in line with Aegon Bank's remuneration policy.

### *Policy application*

In 2018, the actual payout of fixed and variable remuneration was in line with the remuneration policy. Variable remuneration for the Statutory Board and other Identified Staff was paid 50% in cash and 50% in Aegon N.V. shares. In 2018, in accordance with Aegon Nederland's remuneration policy, 40% of the 2017 variable remuneration was paid directly to board members appointed according to the articles of association, with the remaining 60% being conditional. The 60% will be paid in three equal instalments over a period of three years, unless an ex-post risk assessment reveals a reason for reducing the amounts or for not making any payment at all. In 2018, Aegon Bank had no reason to rely on the malus clause or claw-back clause in terms of recovering any variable remuneration paid.

# 11 Appendix

All amounts in this Section are in euros.

## 11.1 Disclosure of Own Funds

Common Equity Tier 1 capital: instruments and reserves		31-dec-18	(B) REGULATION (EU) No 575/2013 ARTICLE REFERENCE
1	Capital instruments and the related share premium accounts	439,187,868	26 (1), 27, 28, 29, EBA list 26 (3)
2	Retained earnings	174,002,217	26 (1) (c)
3	Accumulated other comprehensive income (and any other reserves)	7,709,511	26 (1)
3a	Funds for general banking risk	0	26 (1) (f)
4	Amount of qualifying items referred to in Article 484 (3) and the related share premium accounts subject to phase out from CET1	0	486 (2)
	Public sector capital injections grandfathered until 1 January 2018	0	483 (2)
5	Minority interests (amount allowed in consolidated CET1)	0	84, 479, 480
5a	Independently reviewed interim profits net of any foreseeable charge or dividend	-474,924	26 (2)
6	<b>Common Equity Tier 1 (CET1) capital before regulatory adjustments</b>	<b>620,424,672</b>	
<b>Common Equity Tier 1 (CET1) capital: regulatory adjustments</b>			
28	<b>Total regulatory adjustments to Common Equity Tier 1 (CET1)</b>	<b>-1,434,589</b>	
29	<b>Common Equity Tier 1 (CET1) capital</b>	<b>618,990,083</b>	
<b>Additional Tier 1 (AT1) capital: instruments</b>			
30	Capital instruments and the related share premium accounts	9,500,000	51, 52
31	of which: classified as equity under applicable accounting standards	0	
32	of which: classified as liabilities under applicable accounting standards	0	
33	Amount of qualifying items referred to in Article 484 (4) and the related share premium accounts subject to phase out from AT1	0	486 (3)
	Public sector capital injections grandfathered until 1 January 2018	0	483 (3)
34	Qualifying Tier 1 capital included in consolidated AT1 capital (including minority interest not included in row 5) issued by subsidiaries and held by third parties	0	85, 86, 480
35	of which: instruments issued by subsidiaries subject to phase-out	0	486 (3)
36	<b>Additional Tier 1 (AT1) capital before regulatory adjustments</b>	<b>9,500,000</b>	
<b>Additional Tier 1 (AT1) capital: regulatory adjustments</b>			
43	<b>Total regulatory adjustments to Additional Tier 1 (AT1) capital</b>	<b>0</b>	
44	<b>Additional Tier 1 (AT1) capital</b>	<b>9,500,000</b>	
45	<b>Tier 1 capital (T1 = CET1 + AT1)</b>	<b>628,490,083</b>	
<b>Tier 2 (T2) capital: instruments and provisions</b>			
51	<b>Tier 2 (T2) capital before regulatory adjustment</b>	<b>0</b>	
<b>Tier 2 (T2) capital: regulatory adjustments</b>			
57	<b>Total regulatory adjustments to Tier 2 (T2) capital</b>	<b>0</b>	
58	<b>Tier 2 (T2) capital</b>	<b>0</b>	
59	<b>Total capital (TC = T1 + T2)</b>	<b>628,490,083</b>	
60	<b>Total risk-weighted assets</b>	<b>2,865,767,921</b>	
<b>Capital ratios and buffers</b>			
61	<b>Common Equity Tier 1 (as a percentage of total risk exposure amount)</b>	<b>21.60%</b>	92 (2) (a), 465
62	<b>Tier 1 (as a percentage of total risk exposure amount)</b>	<b>21.93%</b>	92 (2) (b), 465
63	<b>Total capital (as a percentage of total risk exposure amount)</b>	<b>21.93%</b>	92 (2) (c)
64	<b>Institution specific buffer requirement (CET1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements plus a systemic risk buffer, plus systemically important institution buffer expressed as a percentage of total risk exposure amount)</b>	<b>59,535,256</b>	CRD 128, 129, 140
65	of which: capital conservation buffer requirement	53,733,149	
66	of which: countercyclical buffer requirement	5,802,107	
67	of which: systemic risk buffer requirement	0	
67a	of which: Global Systemically Important Institution (G-SII) or Other Systemically Important Institution (O-SII) buffer	0	CRD 131
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	6.15%	CRD 128
<b>Amounts below the thresholds for deduction (before risk-weighting)</b>			
72	Direct and indirect holdings of the capital of financial sector entities where the institution does not have a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	0	36 (1) (h), 45, 46, 472 (10) 56 (c), 59, 60, 475 (4), 66 (c), 69, 70, 477 (4)
73	Direct and indirect holdings of the CET1 instruments of financial sector entities where the institution has a significant investment in those entities (amount below 10% threshold and net of eligible short positions)	0	36 (1) (i), 45, 48, 470, 472 (11)
75	Deferred tax assets arising from temporary difference (amount below 10% threshold, net of related tax liability where the conditions in Article 38 (3) are met)	0	36 (1) (c), 38, 48, 470, 472 (5)
<b>Applicable caps on the inclusion of provisions in Tier 2</b>			
76	Credit risk adjustments included in T2 in respect of exposures subject to standardised approach (prior to the application of the cap)	0	62
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	0	62
78	Credit risk adjustments included in T2 in respect of exposures subject to internal rating-based approach (prior to the application of the cap)	0	62
79	Cap for inclusion of credit risk adjustments in T2 under internal ratings-based approach	0	62
<b>Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2014 and 1 Jan 2022)</b>			
80	- Current cap on CET1 instruments subject to phase-out arrangements	0	484 (3), 486 (2) & (5)
81	- Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)	0	484 (3), 486 (2) & (5)
82	- Current cap on AT1 instruments subject to phase-out arrangements	0	484 (4), 486 (3) & (5)
83	- Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	0	484 (4), 486 (3) & (5)
84	- Current cap on T2 instruments subject to phase-out arrangements	0	484 (5), 486 (4) & (5)
85	- Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)	0	484 (5), 486 (4) & (5)

## 11.2 Leverage Ratio

Summary reconciliation of accounting assets and leverage ratio exposures		Applicable Amount
1	Total assets as per published financial statements	14,140,046,000
2	Adjustment for entities which are consolidated for accounting purposes but are outside the scope of regulatory consolidation	0
3	(Adjustment for fiduciary assets recognised on the balance sheet pursuant to the applicable accounting framework but excluded from the leverage ratio total exposure measure in accordance with Article 429(13) of Regulation (EU) No 575/2013)	0
4	Adjustments for derivative financial instruments	-169,727,145
5	Adjustment for securities financing transactions (SFTs)	0
6	Adjustment for off-balance sheet items (ie conversion to credit equivalent amounts of off-balance sheet exposures)	227,290,054
7	Other adjustments	0
8	<b>Leverage ratio total exposure measure</b>	<b>14,197,608,909</b>

Leverage ratio common disclosure		CRR leverage ratio exposures
<b>On-balance sheet exposures (excluding derivatives and SFTs)</b>		
1	On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	13,901,164,391
2	Asset amounts deducted in determining Tier 1 capital	0
3	<b>Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets) (sum of lines 1 and 2)</b>	<b>13,901,164,391</b>

Derivative exposures		CRR leverage ratio exposures
4	Replacement cost associated with <i>all</i> derivatives transactions (ie net of eligible cash variation margin)	3,750,000
5	Add-on amounts for PFE associated with <i>all</i> derivatives transactions (mark-to-market method)	65,404,464
11	<b>Total derivatives exposures (sum of lines 4 to 10)</b>	<b>69,154,464</b>

Securities financing transaction exposures		
16	Total securities financing transaction exposures (sum of lines 12 to 15a)	0

Other off-balance sheet exposures		
17	Off-balance sheet exposures at gross notional amount	306,802,398
18	(Adjustments for conversion to credit equivalent amounts)	79,512,344
19	<b>Other off-balance sheet exposures (sum of lines 17 and 18)</b>	<b>227,290,054</b>

Capital and total exposure measure		
20	Tier 1 capital	628,490,083
21	<b>Leverage ratio total exposure measure (sum of lines 3, 11, 16, 19, EU-19a and EU-19b)</b>	<b>14,197,608,909</b>

Leverage ratio		
22	Leverage ratio	4.43%

Choice on transitional arrangements and amount of derecognised fiduciary items		
EU-23	Choice on transitional arrangements for the definition of the capital measure	Transitional
EU-24	Amount of derecognised fiduciary items in accordance with Article 429(11) of Regulation (EU) No 575/2013	0

Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)		
EU-1	<b>Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:</b>	<b>13,901,164,390</b>
EU-2	Trading book exposures	0
EU-3	Banking book exposures, of which:	13,901,164,390
EU-4	Covered bonds	61,096,245
EU-5	Exposures treated as sovereigns	1,813,557,900
EU-6	Exposures to regional governments, MDB, international organisations and PSE <b>not</b> treated as sovereigns	132,077,408
EU-7	Institutions	283,329,335
EU-8	Secured by mortgages of immovable properties	9,008,403,585
EU-9	Retail exposures	1,937,394,342
EU-10	Corporate	136,543,265
EU-11	Exposures in default	25,965,014
EU-12	Other exposures (eg equity, securitisations, and other non-credit obligation assets)	502,797,296

## 11.3 Countercyclical buffer

The total institution-specific countercyclical buffer rate is calculated according to the following formula:

$$ISCCB\ rate = \frac{\sum(CCyB_i * OFR_i)}{Total\ OFRCR} \quad ISCCB\ rate = \frac{\sum(CCyB_i * OFR_i)}{Total\ OFRCR}$$

Where:

*ISCCB rate*

The institution-specific countercyclical buffer rate.

*CCyBi*

Countercyclical buffer rate applicable to AEB's exposures to counterparty i.

*OFRI*

Own funds requirements for the relevant credit exposure to counterparty i.

*Total OFRCR*

AEB's own funds requirements for credit risk that relate to all of AEB's relevant credit exposures.

The countercyclical buffer rate for a particular country (CCyB) must be between 0% and 2.5% and may be calibrated by a public authority or body (a 'designated authority') that is responsible for setting the countercyclical buffer rate for that country in steps of 0.25% or multiples of 0.25%. Each designated authority must assess and set the appropriate countercyclical buffer rate for its Member State on a quarterly basis.

DNB has announced that the countercyclical buffer rate for the Netherlands is 0%. This means that a 0% CCyB rate applies to all exposures to obligors resident in the Netherlands. AEB checks quarterly whether DNB may have updated that decision. For other countries, AEB monitors possible changes to the CCyB rate and prepares an overview of all CCyB rates for countries to which it has exposures. This overview is updated on a quarterly basis.

	General credit exposures		Trading book exposure		Securitisation exposure		Own funds requirements				Own funds requirement weights	Countercyclical capital buffer rate
	Exposure value for SA	Exposure value IRB	Sum of long and short position of trading book	Value of trading book exposure for internal models	Exposure value for SA	Exposure value for IRB	Of which: General credit exposures	Of which: Trading book exposures	Of which: Securitisation exposures	Total		
<b>Breakdown by country</b>	10	20	30	40	50	60	70	80	90	100	110	120
Netherlands	11,572,193,575				120,109,571		124,425,189		2,313,508	126,738,697	62.65%	0.00%
Germany	636,788,638				1,038,807		25,958,863		16,618	25,975,482	12.84%	0.00%
France	166,968,743				89,699,028		3,233,900		1,434,782	4,668,682	2.31%	0.00%
United Kingdom	792,038,466				61,388,616		35,669,128		1,035,249	36,704,377	18.14%	1.00%
Spain	863,120				43,577,805		-		696,328	696,328	0.34%	0.00%
Ireland	-				146,126,304		-		2,450,769	2,450,769	1.21%	0.00%
New Zealand	-				-		-		-	-	0.00%	0.00%
Sweden	30,405,014				-		431,045		-	431,045	0.21%	2.00%
Belgium	31,808,967				-		-		-	-	0.00%	0.00%
Italy	-				21,701,997		-		346,711	346,711	0.17%	0.00%
Luxembourg	-				-		-		-	-	0.00%	0.00%
Other Countries	105,593,383				-		-		-	-	0.00%	0.00%
Austria	112,240,672				-		-		-	-	0.00%	0.00%
Czech Republic	50,105,006				-		2,004,200		-	2,004,200	0.99%	1.00%
Norway	8,451,778				1,120,532		676,142		17,923	694,065	0.34%	2.00%
Portugal	19,450,532				1,319,360		-		61,838	61,838	0.03%	0.00%
Denmark	30,016,698				-		-		-	-	0.00%	0.00%
United States	10,006,690				9,192,618		800,535		730,339	1,530,874	0.76%	0.00%
Finland	135,865,904				-		-		-	-	0.00%	0.00%
<b>Total</b>	<b>13,702,797,186</b>				<b>495,274,838</b>		<b>193,199,003</b>		<b>9,104,065</b>	<b>202,303,069</b>	<b>100%</b>	

Amount of institution-specific countercyclical capital buffer		
10	Total risk exposure amount	2,865,767,921
20	Institution specific countercyclical buffer rate	0.2025%
30	Institution specific countercyclical buffer requirement	5,802,034

## 11.4 Disclosure of Asset Encumbrance

Template A - Encumbered and unencumbered assets									
		Carrying amount of encumbered assets		Fair value of encumbered assets		Carrying amount of unencumbered assets		Fair value of unencumbered assets	
		010	of which notionally eligible EHQLA and HQLA	040	of which notionally eligible EHQLA and HQLA	060	of which EHQLA and HQLA	090	of which EHQLA and HQLA
			030		050		080		100
010	Assets of the reporting institution	2,735,639,410				11,397,788,291	980,184,570		
030	Equity instruments					0	0		
040	Debt securities	87,627,682		87,627,682	87,627,682	1,229,248,572	923,819,907	1,229,248,572	923,819,907
050	of which: covered bonds					61,096,245	61,096,245	61,096,245	61,096,245
060	of which: asset-backed securities					494,811,728	189,383,064	494,811,728	189,383,064
070	of which: issued by general governments	87,627,682		87,627,682	87,627,682	259,988,142	259,988,142	259,988,142	259,988,142
080	of which: issued by financial corporations			0	0	814,454,296	509,025,631	814,454,296	509,025,631
090	of which: issued by non-financial corporations					154,806,135	154,806,135	154,806,135	154,806,135
120	Other assets	2,648,011,728				10,168,539,719	56,364,663		
121	of which: mortgage loans	2,475,000,000				6,923,782,336			

Template B - Collateral received					
		Fair value of encumbered collateral received or own debt securities issued		Unencumbered	
		010	of which notionally eligible EHQLA and HQLA	040	of which EHQLA and HQLA
			030		060
250	TOTAL ASSETS, COLLATERAL RECEIVED AND OWN DEBT SECURITIES ISSUED	2,735,639,410	87,627,682		

Template C - Sources of encumbrance			
		Matching liabilities, contingent liabilities or securities lent	Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered
		010	020
010	Carrying amount of selected financial liabilities	2,628,704,855	2,733,433,313

## 11.5 Disclosure of LCR

Scope of consolidation (Consolidated)		Total unweighted value	Total weighted value
Currency and units (EUR)			
Quarter ending on (31/12/2017)			
<b>HIGH-QUALITY LIQUID ASSETS</b>			
1	Total high-quality liquid assets (HQLA)		1,965,269,676
<b>CASH-OUTFLOWS</b>			
2	Retail deposits and deposits from small business customers, of which:	8,692,441,249	679,763,665
3	<i>Stable deposits</i>	4,379,957,926	218,997,896
4	<i>Less stable deposits</i>	4,279,686,172	427,968,617
5	Unsecured w wholesale funding	193,513,067	74,705,227
6	<i>Operational deposits (all counterparties) and deposits in networks of cooperative banks</i>	0	0
7	<i>Non-operational deposits (all counterparties)</i>	193,513,067	74,705,227
8	<i>Unsecured debt</i>	0	0
9	Secured w wholesale funding		0
10	Additional requirements	156,667,570	120,020,763
11	<i>Outflows related to derivative exposures and other collateral requirements</i>	106,527,515	106,527,515
12	<i>Outflows related to loss of funding on debt products</i>	0	0
13	<i>Credit and liquidity facilities</i>	50,140,055	13,493,248
14	Other contractual funding obligations	168,183,332	158,183,332
15	Other contingent funding obligations	222,345,559	54,245,551
16	<b>TOTAL CASH OUTFLOWS</b>		1,086,918,537
<b>CASH-INFLOWS</b>			
17	Secured lending (eg reverse repos)	0	0
18	Inflow s from fully performing exposures	166,008,378	144,758,841
19	Other cash inflow s	3,797,061	3,797,061
EU-19a	(Difference between total w eighted inflow s and total w eighted outflow s arising from transactions in third countries w here there are transfer restrictions or w hich are denominated in non-convertible currencies)		0
EU-19b	(Excess inflow s from a related specialised credit institution)		0
20	<b>TOTAL CASH INFLOWS</b>	169,805,439	148,555,902
EU-20a	Fully exempt inflow s	0	0
EU-20b	Inflow s Subject to 90% Cap	0	0
EU-20c	Inflow s Subject to 75% Cap	169,805,439	148,555,902
21	<b>LIQUIDITY BUFFER</b>		1,965,269,676
22	<b>TOTAL NET CASH OUTFLOWS</b>		938,362,635
23	<b>LIQUIDITY COVERAGE RATIO (%)</b>		209%