insparo
asset management

CAPITAL REQUIREMENTS DIRECTIVE PILLAR 3 DISCLOSURE

Overview

The European Capital Requirements Directive ("CRD") and the Alternative Investment Fund Managers Directive ("AIFMD") (together, the "Directives") establish a revised regulatory capital framework across Europe governing the amount and nature of capital which credit institutions and investment firms must maintain. In the United Kingdom, the Directive has been implemented by the Financial Conduct Authority ("FCA") in its Handbook of rules and guidance, including in particular in the General Prudential Sourcebook ("GENPRU"), the Prudential Sourcebook for Banks, Building Societies and Investment Firms ("BIPRU") and the Investment Funds Sourcebook ("FUND").

The FCA's framework consists of three 'Pillars':

- **Pillar 1**
  This sets out the minimum capital amount that meets the Company's credit, market and operational risk.
- **Pillar 2**
  Requires the Company to assess whether its Pillar 1 capital is adequate to meet its risks.
- **Pillar 3**
  Requires public disclosure of qualitative and quantitative information about the Company's underlying risk management controls, capital position and remuneration arrangements.

The AIFMD adds further capital requirements which relate to the assets under management and professional liability risks of the Alternative Investment Funds ("AIFs") operated by a manager.

The rules in BIPRU 11 set out the provision for Pillar 3 disclosure. This document is designed to meet the Pillar 3 obligations of Insparo by setting out the Insparo's risk management objectives and policies.

Frequency and location of disclosure

Future disclosures will be issued on an annual basis, at a minimum, and will be made available on Insparo's website.

Scope and application of the requirements

Insparo is authorised and regulated by the FCA and has permission to provide discretionary investment management and investment advisory services on behalf of professional clients and eligible counterparties. Insparo is a full scope alternative investment fund manager ("AIFM") and is classed as a Collective Portfolio Management Investment firm ("CPMI") *that is an external AIFM* by the FCA for capital purposes.

Risk Management

The Directors determine the Company's business strategy and risk appetite along with designing and implementing a risk management framework that recognises the various risks that the business faces. They also determine how those risks may be mitigated and assess on an ongoing basis the arrangements to manage those risks. The Directors generally meet on a quarterly basis (or more frequently should the need arise) and discuss all key business issues, including the current budget, forecast profitability, regulatory capital management, business planning and risk management. The Directors manage the Company's risks though a framework of policies and procedures, having regard to relevant laws, standards, principles and rules (including FCA principles and rules), with the aim to operate a defined and transparent risk management framework. These policies and procedures are updated as required. The Board have identified that the main risks to which the Company is exposed are as follows:

- **Operational Risk**

  This is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk.

  Insparo seeks to mitigate all operational risks to acceptable levels, in accordance with its risk appetite, by maintaining a strong control environment, ensuring that staff have appropriate skills and training and establishing an efficient and effective management structure.

- **Business Risk**

  The most significant business risk faced by the Company is that of a substantial and sustained reduction in funds under management, caused by adverse market conditions or investor redemptions, resulting in a loss of management fee income.

- **Market Risk**

  Insparo has limited exposure to market risk. It does not have a trading book and as such, market risk is limited to exposure to net foreign exchange risk on the net amounts receivable and payable in foreign currency.

  Management has assessed the available capital resources required for market risk under Pillar 1 as adequate.

- **Credit Risk**

  This is the risk that a third party will default on a financial obligation. Insparo is exposed to credit risk from fund management and performance fees due from the investment funds which Insparo manages.

  Credit risk is typically defined as the risk that a party will default on a financial arrangement. Insparo deems this risk to be minimal as the company does not provide loans or credit facilities to its clients. In addition, Insparo does not maintain positions or deal in money market or fixed income instruments.

  As part of assessing credit risk, management has assessed the exposure that the company has to concentration risk. No calculation for concentration risk is calculated under Pillar 1 as the company does not have a trading book. The company has an exposure to one bank through holdings of its cash deposits. This bank is one of the largest banks in the UK and is regulated by FCA and PRA. The exposure is monitored by the Chief Operating Officer and could easily be transferred to an alternative account in the event of any concerns re. its solvency.

Regulatory capital

Insparo is small with an operational infrastructure appropriate to its size and regulatory activities. The Company follows the simplified standard approach to credit risk and is subject to the Fixed Overhead Requirement and is not required to calculate an operational risk capital charge.

Insparo is a BIPRU limited licence firm and as such its Pillar 1 capital requirements are the greater of:

- Base capital requirement of €50,000; or

- The sum of its market and credit risk requirements; or
- Its Fixed Overhead Requirement ("FOR").

In addition, the Company, on account of its classification as a full-scope AIFM, is subject to an "own funds" requirement as follows:

The higher of:

1) The funds under management requirement, which is the Base Capital Requirement of €125k + 0.021% of AIF AUM in excess of €250m (but subject to a maximum of €10m);
2) The sum of its market and credit risk requirements; or
3) Variable Capital Requirement, which is the Fixed Overhead Requirement Plus whichever is applicable of:
   a) The professional negligence capital requirement; or
   b) The PII capital requirement.

It is the Company's belief and experience that its Pillar 1 capital requirement normally consists of FOR calculated as £270k and market and credit risks are considered not to be material.

Internal Capital Adequacy Assessment Process (ICAAP) Pillar 2 requirements

Pillar 2 requires the Company to take a view on whether the Company needs to hold additional capital against firm-specific risks not adequately covered by Pillar 1.

The Company has carried out a full business risk assessment and scenario analysis and concluded that the Company considers it appropriate to hold additional capital. The FCA has not issued internal capital guidance on the Company.

The main features of the Company's capital resources for regulatory purposes as at 31 December 2017 are as follows:

Capital item	**£'000**
• Tier 1 capital less innovative tier 1 capital:	975
• Total tier 2, innovative tier 1 and tier 3 capital:	-
• Deductions from tier 1 and tier 2 capital:	-
• Total capital resources, net of deductions:	975
Pillar 2 Capital Assessment	**402**

Remuneration

Insparo has adopted a remuneration policy that complies with the requirements of chapter 19B of the FCA's Senior Management Arrangements, Systems and Controls Sourcebook ("SYSC"), as interpreted in accordance with ESMA's published Guidelines on sound remuneration policies under AIFMD as well as the FCA's published guidance ("Guidance").

The Executive Board at the Company oversees compliance with the Company's remuneration policy including reviewing the terms of the policy at least annually.

Insparo currently sets the variable remuneration of its staff in a manner which takes into account staff and firm performance, by reference to individual employee performance; performance of the individual's business unit or department; performance of the relevant

AIF; and the Company’s overall results. In line with the Guidance, the Executive Board have assessed the AIFM remuneration proportionality criteria and have determined that many of the more onerous provisions, such as the Payout Process Rules, may be disapplied.

The Company only has one "business area", namely its investment management business. All of the Company’s Identified Staff fall into the “senior management” category of Identified Staff or the “risk taker” category for the purposes of the Remuneration Code. The aggregate "remuneration" (as defined in the FCA Rules) awarded to the Insparo’s Identified Staff during the financial year ending on 31 December 2017 was £550k.