Cape Ann Asset Management Limited
(FRN: 735908)
Pillar 3 Disclosure Statement
September 2020

Introduction

The Financial Conduct Authority ("FCA") has set out its regulatory capital requirements in its Handbook of Rules and Guidance for regulated firm

- Pillar 1 sets out the minimum capital requirements for credit, market and operational risk and under AIFMD this extends to include consideration of AUM and professional negligence risks;
- Pillar 2 requires regulated firms, and the FCA, to take a view on whether additional capital should be held against capital risks not covered adequately or at all by Pillar 1; and,
- Pillar 3 requires regulated firms to publish certain information on their risk management objectives and policies and on their capital resources.

These disclosures are made in respect of Cape Ann Asset Management Limited ("**Cape Ann**") in compliance with the rules and guidance set out in the FCA Handbook and Cape Ann's disclosure policy[1]. The information contained herein has been prepared on an unconsolidated basis.

The Firm

Cape Ann is a private limited company providing discretionary investment management services primarily to institutional clients through commingled funds established, operated and managed by the firm. Cape Ann has one subsidiary, Cape Ann Asset Management, Inc. ("**CAAM Inc.**"). There are no current or foreseen material, practical or legal impediments to transfers of capital between Cape Ann and CAAM Inc.

Risk Management

FCA requires that a regulated firm manage a number of different categories of risk.

- ***Credit Risk.*** *The potential risk that arises from clients or counterparties failing to meet their obligations as they fall due.* Cape Ann has adopted a standardised approach to credit risk. Because of the nature of its business, Cape Ann's credit risk is limited to that arising in respect of unpaid investment management fees, fund investments, cash deposits and prepaid expenses. Investment management fees from the commingled funds are calculated on an ad valorem basis in arrears and are normally paid within five business days of each month end, or quarterly with respect to any segregated accounts under mangement. Cape Ann's investments primarily comprise units in The Cape Ann (Ireland) Trust, an Irish UCITS. Cape Ann's cash deposits are primarily held in current accounts offered by major banking institutions. No provisions have to date been required in respect

[1] FCA rules provide that required disclosures may be omitted if the information is believed to be immaterial or where it is regarded as proprietary or confidential. Materiality is based on the criteria that the omission or misstatement could change or influence the assessment or decision of a user relying on that information for the purpose of making economic decisions. Information is regarded as proprietary if sharing that information with the public would undermine a firm's competitive position. Information is regarded as confidential where there are obligations to customers or counterparties binding a firm to confidentiality. Where a disclosure is considered to be immaterial or has been omitted on the grounds that it relates to information that is proprietary or confidential in nature, this has been described.

of asset impairment or non-recovery. Credit risk arising in relation to prepaid expenses is not considered material for the purposes of this disclosure.

- ***Market Risk.*** *The risk that the value of, or income arising from, assets and liabilities varies as a result of changes in interest rates, exchange rates or other market prices.* Cape Ann has no trading book and does not invest in commodities. Market risk under Pillar 1 is therefore limited to foreign exchange fluctuations where Cape Ann's assets and liabilities are denominated in currencies other than GBP. Non-GBP assets primarily comprise investments in the Cape Ann (Ireland) Trust and a proportion of cash deposits. Cape Ann regularly assesses its foreign exchange needs and exposures and does not actively seek foreign exchange exposures via forward currency hedging activities.

- ***Liquidity Risk.*** *The risk that a firm may have insufficient liquid resources to cover cash flow shortfalls or fluctuations in funding and be unable to meet its obligations as they fall due.* Liquidity risk consists of two primary items – funding liquidity risk and market liquidity risk. Funding liquidity risk is the risk that the counterparties who provide Cape Ann with short-term funding will withdraw or not roll over that funding. Market liquidity risk is the risk of a generalised disruption that makes normally liquid assets illiquid. Cape Ann has no borrowing and is not dependent on external financing. Cape Ann has some exposure to market liquidity risk. This could occur if Cape Ann's corporate banks were to suffer from severe financial distress.

- ***Business Risk.*** *The risk that a firm may not be able to carry out its business plan and/or desired strategy.* The principal business risks facing Cape Ann are:

    - ***Operational Risk.*** *The risk of loss, or breach of contractual requirements, resulting from inadequate or failed internal processes, people or systems; human error; or, external events.* This includes the risk of loss or breach arising from the inadequate supervision of third party service providers. Cape Ann seeks to mitigate these risks by (i) keeping its business simple; (ii) taking advantage of technology solutions; (iii) identifying and managing sources of risk, stress testing those risks and maintaining insurance to offset financial losses; (iv) documenting procedures; and (v) reviewing the operations of material business operations on a periodic basis. Cape Ann is not required to calculate an operational risk requirement.

    - ***Concentration Risk.*** *The risk that exposures to specific sectors or asset concentration could result in losses.* Cape Ann invests client assets principally in publicly traded developing market equity securities. Cape Ann's business could suffer (i) from a decline in its investment performance (ii) a change of sentiment on the part of institutional investors away from publicly traded developing market equity securities and/or a shift of their asset allocations to private equity, hedge funds, commodities or other types of investments, or (iii) a sharp appreciation of US dollar.

    - ***Insurance Risk***. *The risk of a failure of insurance cover.* Cape Ann maintains fiduciary liability (e.g. professional indemnity), crime (e.g. errors and omissions) and ERISA insurance at a level and with a deductible which Cape Ann considers appropriate for the business. Cape Ann seeks to obtain insurance only from well capitalised insurance firm(s) to minimise the risk of loss arising from insurance risk.

    - ***Interest Rate Risk***. *The risk that significant changes in interest rates may have an adverse impact on the business.* Cape Ann does not engage in or run a trading book and has no significant borrowings that might give rise to material interest rate risks.

Cape Ann's Board of Directors is responsible for determining Cape Ann's risk strategy, setting its risk appetite and ensuring that risk is monitored and controlled effectively. Cape Ann's Board consults the Compliance and Operational Risk Management Group before deciding to make (i) material investments, loans or capital expenditures; (ii) significant investments; (iii) material changes in its cost structure, base salaries or the level of discretionary bonus payments; or (iv) material repayments or distributions of shareholder capital. Cape Ann's operational risk management framework is updated when needed to reflect material changes in Cape Ann's business, capital obligations or resource requirements. Cape Ann's operational risk appetite is regularly reviewed. Cape Ann aims to ensure that staff remain focused on compliance with applicable regulations, improving procedures, minimising risk and establishing a robust risk, capital and performance structure.

Capital Resources and Regulatory Obligations

Cape Ann is a BIPRU firm subject to a base own funds requirement of €50,000. That is because Cape Ann is not authorised to take proprietary trading positions or hold client money. Cape Ann is exempt from the operational risk requirement at Pillar 1 and is not required to calculate an operational risk capital charge. Cape Ann must calculate the sum of its core regulatory capital and its professional liability risks capital requirement. Cape Ann's most recent capital requirement calculations are set out below:

Cape Ann	**£'000**
Core Capital	750
Total capital after deductions	2,328
Capital requirement	956
Surplus Capital Resources	**1,372**

Cape Ann has prepared an assessment of capital adequacy (Internal Capital Adequacy Assessment Process document or "**ICAAP**") in accordance with CRD Pillar 2 requirements set out in BIPRU 2.2 of the FCA Handbook. The ICAAP takes account of the principal risks and uncertainties set out above. As a long only asset manager that invests client assets primarily in publicly traded developing market equity securities, Cape Ann is mainly exposed to operational risk; however there is some small exposure both to business risk and credit risk. These exposures are regarded as typical for a business engaged in the activity of asset management. Cape Ann's Chief Compliance Officer, who is independent of Cape Ann's investment function, acts as the firm's operational risk manager and monitors and manages these risk exposures with input from Cape Ann's business groups. In assessing operational risk appetite, consideration has been given to identifying the material risks facing Cape Ann's business. The ICAAP process involves separate consideration of risks to firm capital combined with stress testing using scenario analysis and consideration of the financial resources required in a wind down situation. The ICAAP is updated formally on an annual basis and in the interim should a material change occur in the risk or business profile of the firm.

<u>Non-trading book exposures in equities</u>: Disclosures of non-trading book exposures in equities are considered immaterial as any investment in equities is limited to investments in the Cape Ann (Ireland) Trust. Full disclosure of these investments and of the accounting techniques and valuation methodologies employed are disclosed in Cape Ann's audited annual report and accounts.

Remuneration Code Provisions

For the purposes of these disclosures, Cape Ann Asset Management Limited and Cape Ann Asset Management, Inc are referred to as "Cape Ann".

Applicability of the Remuneration Code

Under the Remuneration Code, Cape Ann must establish, implement and maintain remuneration policies, procedures and practices that are consistent with and promote effective risk management. The policies, procedures and practices must not encourage risk-taking inconsistent with the risk profiles of its investment guidelines and the structure of its collective investment schemes and, where possible, avoid conflicts of interest. Cape Ann may apply regulations in a proportionate manner based on the nature, size and complexity of its business. Cape Ann must assess its own characteristics and develop and implement policies and practices that appropriately align it with the risks faced by its business. In designing its approach towards remuneration and alignment, Cape Ann has taken into account its structure and the nature, size and complexity of its business.

Identification of Remuneration Code Staff

Cape Ann is required to identify those members of staff who are covered by the Remuneration Code ("**Remuneration Code Staff**"). Because of its small size and the responsibilities assumed, Cape Ann considers all staff to be Remuneration Code Staff. All Remuneration Code Staff are provided with a copy of this document on an annual basis.

Investment Approach

Cape Ann is a private limited company providing discretionary investment management services primarily to institutional clients through commingled funds established, operated and managed by the firm and segregated account clients. Cape Ann principally invests client assets in publicly traded, global developing market equity securities. Cape Ann does not short stocks, utilise derivatives or margin, underwrite securities, issue or write options, futures, warrants or over-the-counter instruments. Cape Ann does not participate in securities lending programmes. Cape Ann does not invest in fixed income instruments, physical real estate, commodities or contracts for difference. Cape Ann may invest in spot and forward foreign exchange contracts. Assets included in client portfolios are normally priced by independent fund administrators using closing market prices and exchange rates. Cape Ann does not charge performance fees. It is therefore reasonable to state that Cape Ann does not trade in unusual or high risk products and has designed its systems and controls with this in mind.

Cape Ann's Remuneration Policy

The split between each employee is determined by the Remuneration Group. The Remuneration Group seeks to obtain feedback on the performance and contribution of individual employees. Remuneration is not based on the profitability of any specific investment recommendation, the implementation of given trade(s) or the growth/retention of any particular investor. The Remuneration Group considers the following factors when determining the levels of remuneration and/or discretionary drawings paid to each member of staff:

- *Skill and expertise*. These can be tangible such as the ability to build a spreadsheet or organize a series of tasks (generally easier to measure) or they can be more intangible (although data may improve) such as exercising judgement, acting sensibly under pressure, or problem solving.
- *Reliability*. Measures the ability of an individual to get the assigned tasks done on time with the requisite amount of care and accuracy. Our clients, prospects and colleagues should be able to rely on us to do what we promise and deliver it as planned. Part of the assessment in this area also needs to address how the individual manages the process when deadlines are not met and deliverables are behind schedule.

- *Hard work and initiative.* An assessment of the effort expended, is also a useful measure not just as a proxy for commitment but also to ensure the effort being expended is commensurate with the value of the work being produced. If two people make a similar contribution but one does so with half the effort it raises issues of the suitability of the work assigned to individuals and whether the skill set is appropriate for the job.
- *Team play.* Takes into account factors such as an individual's professionalism, helpfulness, and flexibility. For example, does the person make a positive or negative contribution to the team and its working atmosphere (it could be that someone produces good work but leaves havoc in their wake)?
- *Success of Cape Ann.* If Cape Ann is successful there should be a benefit to all. Cape Ann recognises a system of this sort cannot deliver when the business is not doing well. In other words, if PBRT drops, remuneration must fall.
- *Split Between Fixed and Discretionary Components.* Fixed remuneration should be more oriented to those with a reliable proven record of adding value and discharging responsibility. Where such a record has not been established the flexibility of discretionary payments is more appropriate. Fixed aspects of expenditure should be kept low as this provides the greatest level of flexibility and allows Cape Ann to withstand various stresses – performance volatility, loss of client assets, exchange rate volatility and changes in interest rates – without needing to terminate staff.

Risk Management
Cape Ann's Board is responsible for Cape Ann's risk strategy, setting its risk appetite and ensuring that risk is monitored and controlled effectively. Cape Ann's Board consults the Compliance Group before deciding to make (i) material investments, loans or capital expenditures; (ii) significant investments; (iii) material changes in its cost structure, base salaries or the level of member drawings; or (iv) material repayments or distributions of member capital. Cape Ann's operational risk management framework is updated when needed to reflect material changes in Cape Ann's business, capital obligations or resource requirements. Cape Ann's operational risk appetite is regularly reviewed. Cape Ann aims to ensure that staff remain focused on compliance with applicable regulations, improving procedures, minimising risk and establishing a robust risk, capital and performance structure. The Compliance Group prepare, and the Board reviews and approves, an assessment of capital adequacy (Internal Capital Adequacy Assessment Process document or "ICAAP") in accordance with Pillar 2 requirements set out in BIPRU 2.2 of the FCA Handbook on an annual basis. The ICAAP process involves separate consideration of the principal risks and uncertainties faced by the firm and the impact that various item could have.

Alignment of Risk Management and Remuneration
Cape Ann believes that it has achieved a close alignment between its risk management objectives and remuneration policy. The firm's risk management objectives have been established in order to promote consistent, sound and effective risk management and so as not to encourage risk-taking which is inconsistent with the risk profile of the instruments constituting the commingled funds and separate accounts for which it has been appointed as investment manager.

Alignment and Co-Investment
From 1 April 2019, all employees must invest 10% of their gross total remuneration arising with respect to a given financial year into either shares (if available) or the programme. In both cases, choice is available as to timing but if insufficient investment has been made by the time final bonuses are paid, then the required amount will be deducted from any final variable payment.
All investments in shares or the programme in the name of the professional, their spouse or civil partner, children, grandchildren or pension funds, and including any reinvestment of dividend income, count towards these thresholds. The Board may at any time, in its sole discretion, waive or amend the applicability of the remuneration rules. This discretion could

be exercised, as an example, if a medical emergency or other significant event occurs. The Board would not ordinarily anticipate providing a waiver for house purchases, school fees or to meet income tax liabilities.

Other Issues

Guaranteed bonus or variable remuneration arrangements are not used other than in the first year of employment for any individual. Guaranteed bonus or variable remuneration arrangements will only be agreed on an exceptional basis. No contractual arrangements are in place to provide early termination payments to any member of staff. Any such payments would be agreed at the time of termination in accordance with then applicable law and regulation.

Code staff may not undertake personal hedging strategies or enter into remuneration or liability contracts of insurance intended to undermine these objectives.

Given the limited size, scope and nature of Cape Ann's activities and consistent with the explicit guidance given by the FCA, Cape Ann has disapplied provisions or proportionately applied provisions related to (i) requirement to establish a remuneration committee; (ii) retained shares and other financial instruments, (iii) deferral and (iv) performance adjustments. Cape Ann has considered the impact of remuneration policies on its capital requirements, ICAAP and monitoring programme.