Cape Ann Asset Management Limited
(FRN 735908)
Pillar 3 Disclosure Statement
1st September 2016

Introduction

Cape Ann Asset Management Limited ("**Cape Ann**") is authorised and regulated by the Financial Conduct Authority ("**FCA**"). Cape Ann is a BIPRU firm and is subject to the following capital framework:

- Pillar 1 specifies the minimum capital that Cape Ann is required to carry to cover business risks;
- Pillar 2 sets out the supervisory review process to be used when determining whether additional capital should be maintained against any other risks not covered under Pillar 1;
- Pillar 3 specifies the disclosure requirements which Cape Ann is required to make of its capital, risk exposures and risk assessment processes.

Cape Ann is regulated as an Alternative Investment Fund Manager ("**AIFM**") pursuant to the Alternative Investment Fund Managers Directive ("**AIFMD**") and the FCA's adopting legislation. Cape Ann must satisfy applicable capital requirements and disclosure obligations. As a general rule, Cape Ann's capital requirements are driven by Cape Ann's overall assets under management rather than just underlying expenditure requirements and financial commitments. These capital requirements generally rise and/or fall in line with Cape Ann's assets under management.

This disclosure is prepared on the basis that Cape Ann is a full scope AIFM that is subject to BIPRU subject to the FCA regulations for the disclosures required under Pillar 3 contained in the Prudential Sourcebook for Banks, Building Societies and Investment Firms ("**BIPRU**") and the AIFMD capital requirements contained in the Interim Prudential sourcebook for Investment Businesses ("**IPRUINV**"). Further information on BIPRU and IPRUINV can be found on the FCA website (www.fca.gov.uk). These rules allow each firm to exclude disclosures where the information is regarded as immaterial, proprietary or confidential. Disclosures have been made in this document unless that disclosure has been regarded by Cape Ann as being immaterial, proprietary or confidential. Additional information is available from Pete Lockey, Cape Ann's Chief Compliance Officer (pete.lockey@capeannam.com)

Business Structure

Cape Ann is a limited company. Cape Ann's employees and their families hold 100% of Cape Ann's "B" Shares representing 50.1% of Cape Ann's total equity. Silchester Partners Limited ("**SP Ltd**") holds 100% of Cape Ann's "A" Shares representing 49.9% of Cape Ann's total equity.

Operational Risk Management

Cape Ann's Board 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 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 abiding by applicable regulations, improving procedures, minimising risk and establishing a robust risk, capital and performance structure.

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. These are set out in the following table:

	£'000
Total capital after deductions	750
Capital requirement	257
Excess capital before stress test	493
Additional capital required following stress test	0
Excess capital after stress test	493

Cape Ann's ICAAP analysis highlights that Cape Ann had surplus Tier 1 capital compared to the capital resource requirements computed under Pillar 1 and maintains surplus capital under AIFMD rules. The capital requirement will be recalculated in the event any material changes occur to Cape Ann's business. Under Pillar 2 and as required according to GENPRU 1.2, Cape Ann is required to adopt an internal capital adequacy assessment process ("**ICAAP**"). In its ICAAP analysis, Cape Ann stress tested its business under various scenarios. Under each stress test, the capital required fell below Cape Ann's regulatory capital requirement. As a result, Cape Ann has surplus liquid capital compared to its requirements under Pillar 2.

Operational Risk Assessments and Impact on Capital Computation

As a long only asset manager that primarily invests client assets in publicly traded equity securities, Cape Ann is mainly exposed to operational risk; however there is some small exposure both to business risk and credit risk. All of 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. These include risks at both the client and firm level and take the form of loss of revenue, loss of assets or higher costs. Two specific factors have been considered in defining the risk appetite; the likelihood of occurrence of an event and secondly, the impact level of an event. Further information is set out below.

- ***Credit Risk.*** As an asset management firm, Cape Ann is subject to credit risk. Cape Ann receives investment management fees on a monthly basis. Investment management fees are typically paid within five business days of each month. As Cape Ann only manages money on a "long only" basis and does not use leverage, margin or derivative products, there is little credit risk associated with the fees. Cape Ann does not utilise risk mitigation techniques (i.e., credit default swaps) to minimise financial exposure to its corporate banking counterparties.

- ***Market Risk.*** As an asset management firm, Cape Ann's portfolios are subject to market risk. Cape Ann's fees are asset based fees and Cape Ann's revenue increases as AUM increase and will fall if AUM falls. Cape Ann has structured its business so that many costs are variable and will fall as its AUM fall. More importantly, Cape Ann keeps base salaries low and remunerates employees through discretionary bonuses. Surplus liquid capital is not at risk until a loss fully offsets Cape Ann's profit before remuneration and taxes ("**PBRT**") less committed salaries and benefits.

- ***Liquidity Risk.*** 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 benefits from an operational subsidy payable by SP Ltd in the early years of its business operations. SP Ltd is a private company with significant financial resources. Given this, Cape Ann is not exposed to funding liquidity risk. 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.

- ***Operational Risk.*** Operational risk refers to the risk of a direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events. Cape Ann attempts to mitigate these risks by (i) maintaining substantial financial resources, (ii) ensuring that Cape Ann is able to meet its regulatory capital obligations on an on-going basis as required under Pillar 1, (iii) identifying and managing sources of risk, stress test those risks and maintain insurance or other capital to offset financial losses that may be created by various risks under Pillar 2, (iv) aligning the interests of all staff with supervision of the operations of the business through its remuneration policies, (v) reviewing the operations of material business groups on a periodic basis, (vi) providing training where required, (vii) taking advantage of technology solutions, and (viii) keeping the business simple.

- ***Concentration Risk.*** Concentration risk is the risk that exposures to specific sectors or asset concentration could result in losses to Cape Ann or its business. Cape Ann principally invests client assets in publicly traded equity securities. Cape Ann's business could suffer (i) from a decline in its investment performance relative to benchmark indices, (ii) if institutional investors choose not to invest in publicly traded global developing market equity securities and/or shift their asset allocations to private equity, hedge funds, commodities or other types of investments, or (iii) the US dollar sharply appreciates, negatively impacting relative returns.

- ***Business Risk.*** Business risk arises from changes in the business that prevents Cape Ann from carrying out its business plan and desired strategy. Cape Ann is a limited company. All material structural changes to Cape Ann's business are subject to discussion at Board meetings. The Board consults the Compliance Group before (i) an investment, loan or capital subscription is made; (ii) before a significant investment is made; or (iii) before any material change in Cape Ann's cost structure or base salaries;

- ***Interest Rate Risk***. Cape Ann does not engage in any principal trades or run any trading book exposures that could be subject to interest rate risk. From a business perspective (given its cash balances) and assuming no impact on investment performance, Cape Ann would expect to benefit from increases in interest rates as its interest income would rise.

- ***Insurance Risk.*** Cape Ann maintains fiduciary liability (also referred to as professional indemnity), crime (also referred to as errors and omissions). Professional indemnity, crime cover is set at a limit which Cape Ann considers appropriate for the business of Cape Ann and subject to a deductible which Cape Ann can reasonably afford to meet if called upon. Cape Ann would be exposed to potential losses in the event that an error occurred and its insurers did not pay the anticipated insurance settlement proceeds. Cape Ann attempts to obtain insurance only from well capitalised insurance firms to minimise the risk of loss arising from insurance risk.

Summary - Capital Resources and Regulatory Obligations

Cape Ann has calculated its capital needs in accordance with relevant FCA regulations and has determined that it has surplus regulatory capital.

Remuneration Code Provisions

Cape Ann has completed this section of the Pillar 3 disclosure document on the basis that it is a full scope AIFM BIPRU firm that is subject to the remuneration rules set out in SYSC 19B and SYSC 19C and is eligible to apply principles of proportionality pursuant to BIPRU rules. Market regulators impose a variety of requirements on asset management firms with respect to remuneration. The general thrust of these remuneration codes (in aggregate, the "**Remuneration Code**") is to ensure that regulated firms have (i) robust governance arrangements in place, (ii) established remuneration controls for staff whose professional activities could have a material impact on the risk profile of their firms, and (iii) qualitative and quantitative disclosures of their remuneration policies.

Applicability of 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 excessive risk-taking. Cape Ann may apply regulations in a proportionate manner based on the size, nature 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. Cape Ann must ensure that adequate and effective incentives are given to all members of staff. In designing its approach towards remuneration and alignment, Cape Ann has taken into account its structure and the size, nature 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. Certain burdensome provisions of the Remuneration Code (i.e., the requirements to restrict the ratio of discretionary payments to base salary, to defer remuneration over a period of time or to pay a portion of remuneration in shares) are not deemed to be applicable to Cape Ann's operations.

Investment Approach

Cape Ann principally invests client assets in publicly traded equity securities. Cape Ann does not short stocks, utilise derivatives or margin, underwrite securities, issue or write options, futures, warrants or over-the-counter ("**OTC**") instruments, with the exception of the potential investment in a very limited number of Market Access Products ("**MAPs**") designed to provide access to local markets Cape Ann cannot access directly. 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. 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

Cape Ann does not charge performance fees and receives asset based fees on a monthly basis. The articles of association that govern Cape Ann's business specifies the ratio of profits less direct costs before any remuneration (internally referred to as profits before remuneration and tax or "**PBRT**") is shared between Cape Ann employees and shareholders. The ratios set out are as follows:

		Shareholders & Corporate Tax	
Year	Working Staff	"A"	"B"
1	100%	0.00%	0.00%
2	100%	0.00%	0.00%
3	90%	4.99%	5.01%
4	80%	9.98%	10.02%
5	70%	14.97%	15.03%
Thereafter	60%	19.96%	20.04%

The first financial year is 1st April 2016 – 31st March 2017.

Establishing these ratios ensures that both employees and shareholders are focused on growing Cape Ann's business in a profitable and efficient manner. While a minimum of 60% of PBRT will be distributed to working staff as remuneration, the split between each working employee is determined by the Remuneration Group. The current members of the Remuneration Group are Jonathan Bell, Pete Lockey and Tim Linehan. Cape Ann does not believe that the appointment of external staff to the Remuneration Group would benefit the firm or its clients. The Remuneration Group obtains feedback on the performance and contribution of each individual employee or member. Remuneration is not based on the profitability of any specific investment recommendation, the implementation of a given trade(s) or the growth/retention of any particular investor. The Remuneration Group considers the following factors when determining the levels of remuneration paid to each member of staff:

- *Contribution and Ownership of Responsibility*. Cape Ann looks at contribution to the success of the firm over a multi-year period, ownership of various responsibilities, whether related to investment, marketing and client service, investment administration or firm management.
- *Market Levels*. Cape Ann believes that whilst base salaries should be competitive in the longer term, they will be below market rates during the early years of the business.
- *Reliability*. It is a great benefit to a lean organisation when Cape Ann can rely on someone over a period of years to get a task done. Good work which has needed a great deal of supervision is less valuable although, of course, normal in the early stages of a responsibility.
- *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 also 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 employees.

Notifications of discretionary payments are typically provided bi-annually. Actual allocations can be amended at any time by the Remuneration Group. Bonuses are only paid after Cape Ann ensures that FCA capital and liquidity requirements are satisfied and fees are collected. The year ending 31st March 2017 will the first in which Remuneration Code Staff are remunerated by Cape Ann. Cape Ann has not broken out details by business area or between various senior staff.

Over time, Cape Ann will look to ensure that fixed elements of expenditure are less than 50% of Cape Ann's total revenues. Cape Ann takes this approach to minimise risk to its underlying clients and to the firm itself from financial losses that may result from errors, market and foreign exchange rate volatility, investor redemptions, increased costs, etc. Cape Ann believes this approach reduces risks to the firm and to the marketplace as a whole and is consistent with Remuneration Code objectives. Cape Ann does not offer guaranteed bonuses. Cape Ann is aware of Remuneration Code provisions governing the deferral of variable remuneration and the retention of part of this variable remuneration in Cape Ann's commingled funds. Cape Ann has applied principles of proportionality when implementing the Remuneration Code in this regard and has implemented policies that meet core regulatory objectives without creating undue administrative overheads or complexities.

Disapplication of Remuneration Code Provisions

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 dis-applied provisions or proportionately applied provisions related to (i) leverage for fixed and variable components of remuneration, (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.