

Pillar 3 Disclosure - Cazenove Capital

1. Introduction

The Basel II Accord, implemented in the European Union through the Capital Requirements Directive ('the Directive') establishes a revised regulatory capital framework across Europe governing the amount and nature of capital that must be maintained by credit institutions and investment firms. In the United Kingdom, the Directive has been implemented by the Financial Services Authority ('FSA') in its regulations through the General Prudential Sourcebook ('GENPRU') and the Prudential Sourcebook for Banks, Building Societies and Investment Firms ('BIPRU').

The FSA framework consists of three 'Pillars':

- Pillar 1 sets out the minimum capital amount that meets the firm's credit, market and operational risk
- Pillar 2 requires the firm to assess whether its Pillar 1 capital is adequate to meet its risks and is subject to annual review by the FSA
- Pillar 3 requires disclosure of specified information about the underlying risk management controls and capital position

The rules in BIPRU 11 set out the provisions for Pillar 3 disclosure. This document is designed to meet Cazenove Capital's Pillar 3 obligations.

1.1 Disclosure Policy

In accordance with BIPRU 11.3.3R, Cazenove Capital has adopted a formal disclosure policy in that it will comply with the requirement to publicly disclose the relevant information.

The rules provide that one or more of the required disclosures may be omitted if it is believed that the information is immaterial. Materiality is based on the criteria that the omission or misstatement of material information would be likely to change or influence the assessment or decision of a user relying on that information for the purposes of making economic decisions. If disclosure is considered to be immaterial, it will state this in the relevant section.

One or more of the required disclosures may be omitted where it is believed that the information is regarded as proprietary or confidential. Proprietary information is that which, if it were shared, would undermine a competitive position.

Information is considered to be confidential where there are obligations binding Cazenove Capital to confidentiality with customers and counterparties. If information is omitted for either of these two reasons it will state this in the relevant section and the reasons for this. Where appropriate, more general information on the subject matter of the required disclosure will be published.

1.2 Frequency of Publication

The disclosures will be reviewed on an annual basis at a minimum and, if appropriate, more frequently. Disclosures will be published as soon as is practicable following any revisions.

1.3 Verification

The disclosures have been put together to explain the basis of preparation and disclosure of certain capital requirements and provide information about the management of certain risks and for no other purposes. They do not constitute any form of audited financial statement and have been produced solely for the purposes of Pillar 3. They should not be relied upon in making judgements about Cazenove Capital. The disclosures will only be subject to external verification to the extent that they are equivalent to those made under accounting requirements.

The disclosures are reviewed and approved by the Board of Cazenove Capital Holdings Limited.

1.4 Media & Location of Publication

The disclosures will be published on the Cazenove Capital website and will also be available on request by writing to the Chief Financial Officer, 12 Moorgate, London EC2R 6DA.

2. Scope and application of the Directive requirements

Cazenove Capital is a leading, distinctive and innovative provider of financial planning and asset management services to private clients. It is also a manager of investment funds including absolute return, long and institutional in our defined areas of expertise, and it is a market leader in the management of charity assets in the United Kingdom.

The parent company of the group is Cazenove Capital Holdings Limited, an unregulated company incorporated in Jersey. Cazenove Capital Holdings Limited's sole investment is in Cazenove Capital Management Limited ('CCM'), a FSA regulated company incorporated in the United Kingdom. The disclosures are made on a consolidated basis for CCM and its subsidiaries ('the Group'), which includes Cazenove Investment Fund Management Limited ('CIFM'), also FSA regulated.

- CCM is a BIPRU 125k Limited Licence Firm because it does not deal for its own account or underwrite issues on a firm commitment basis, it manages individual portfolios and it holds client money. A BIPRU firm must maintain at all times capital resources equal to or in excess of the base requirement (€125,000). The variable requirement for a BIPRU Limited Licence Firm is the higher of the credit risk capital requirement and the market risk capital requirement, or the fixed overheads requirement (i.e. one quarter of the firm's relevant fixed expenditure). For CCM, the variable requirement is the fixed overheads requirement. A BIPRU firm must maintain at all times capital resources equal to or in excess of the variable requirement
- CIFM, too, is a BIPRU 125k Limited Licence Firm but it is also a UCITS firm. The requirements are therefore similar to CCM's, other than the following:
 - The base requirement for a BIPRU 125k UCITS firm is €125,000 plus, if the funds under management exceed €250million, 0.02% of the excess, subject to a maximum of €10million; and
 - When calculating the credit risk requirement and the market risk requirement for the purposes of calculating the variable requirement, a UCITS firm must do so only in respect of designated investment business. For this purpose, scheme management activity is excluded from designated investment business

3. Governance

The Board of Cazenove Capital Holdings Limited is the governing body ultimately responsible for the risk management regime. The Board has authorised the Cazenove Capital Holdings Limited Audit & Risk Committee (comprised of Non-Executive Directors) to investigate any activity as to the risks which are deemed appropriate to accept and those which are unacceptable and should be eliminated or mitigated; and report to the Board on any significant internal control failures that have occurred and on the quality of internal policies, disciplines, controls, processes and monitoring procedures in place to deal with risk, making recommendations for improvements where applicable.

The Boards of CCM and CIFM are the governing bodies responsible for the day-to-day risk management regime. The Boards have delegated responsibility for CCM's and CIFM's risk management process to the Risk Governance Committee ('the RGC'). The RGC is responsible for ensuring that all key business and reputational, regulatory and legal, operational, people, change and financial risks arising from the business of Cazenove Capital have been identified and that the risk management framework remains appropriate.

4. Risk Management Framework

It is Cazenove Capital's objective to structure a business environment in which threats to the organisation's ability to maximise stakeholder value and achieve strategic objectives are identified, measured, controlled to an acceptable level and reported. Cazenove Capital has identified seven core principles that define risk behaviour and characterise Cazenove Capital's risk management culture:

- Cazenove Capital aims to recruit, keep and reward staff with a strong risk and control awareness
- Cazenove Capital will put in place and maintain a framework which allows staff to manage their risks effectively
- Staff are accountable for managing their risks
- Consistent standards will be established and maintained for identifying, measuring, controlling and reporting risk
- All business areas will put in place and maintain comprehensive standard operating procedures which include processes to identify, measure, control and report risk
- Risk management activity will be prioritised towards the areas of greatest risk
- Key information on the management of risks will be reported to the Risk Governance Committee and the Board

Cazenove Capital has developed a risk management cycle in order to identify and manage its risks. The cycle incorporates regulatory requirements and is designed to be appropriate to the simple nature and scale of Cazenove Capital's business. The key steps in the risk management cycle are as follows:

- Articulation and agreement of risk appetite
- Risk identification and quantification
- Stress and scenario testing
- Management actions
- Documenting an ICAAP
- Reporting and approval

5. Capital Resources

The Group's consolidated regulatory capital resources comprise the following:

	30/09/11 £'000
Tier one capital	
Share capital	21,000
Retained earnings and other reserves	53,960
	74,960
Deductions from tier one	
Intangible assets	-7,740
	67,220
Tier two	
Revaluation reserve	121
	67,341
Tier one and two before deductions	
Material holdings	-2,501
	64,840

Share capital is the permanent, allotted, called up and fully paid ordinary share capital of CCM, the parent company of the regulated UK consolidation group.

Retained earnings are the audited profit and loss reserves retained by the business. Other reserves include a capital contribution from Cazenove Capital Holdings Limited (the Group's ultimate parent company) and a non-distributable capital reserve.

The Material Holdings deduction consists of shares in Cazenove Capital Holdings Limited held in an Employee Benefit Trust to meet liabilities under equity remuneration schemes for the Group's employees.

Upper Tier Two Capital comprises the revaluation reserve representing gains arising on other interests held in the Group's Employee Benefit Trust.

6. Capital Resources Requirement

6.1 Pillar 1

In accordance with GENPRU 2.1.45R (calculation of variable capital requirement for a BIPRU firm), the Group's Pillar 1 capital requirement is determined as the higher of the fixed overheads requirement or the sum of credit risk and market risk capital requirements.

The current Pillar 1 capital requirement is the fixed overheads requirement of £14.4m, which has been calculated based on 2010 expenditure.

6.2 Pillar 2

The Pillar 2 capital requirement has been determined as £6.8m as at 30 September 2011. The Pillar 2 capital requirement is assessed as part of the ICAAP process and results from exposure to the following risks:

6.2.1 Credit Risk

Credit risk is the risk of financial loss arising from a client or other counterparty failing to meet its obligations to repay outstanding amounts as they fall due.

The Group is not exposed to high levels of credit risk, as it does not undertake any principal trading in relation to its own balance sheet, other than placing cash on deposit. The Group only places cash out on deposit with a select list of highly rated counterparties. For sales debtors in our retail funds, the risk of not receiving sums due to us is mitigated as we have the ability to cancel units that have been allocated but have not been paid for. For segregated fund clients, provision for the non-payment of fees is governed by our agreements with these clients.

The Group applies the rules within BIPRU 3 Standardised Credit Risk to calculate an appropriate capital requirement for its credit risk exposure. These rules include additional categories of asset to which credit risk may apply. As a result, the Group calculates a credit risk requirement on the following asset classes:

- Cash
- Fee and other debtors
- Investments held in the Employee Benefit Trust
- Fixed assets

6.2.2 Market Risk

Market risk arises from adverse changes to the values of positions or portfolios arising from changes in market prices, interest rates or exchange rates.

As noted above, the Group does not undertake any principal trading for its own account. As a result, it is not exposed to any significant market risk which would arise from such. Investment objectives and restrictions are agreed with clients and, save breaches from those guidelines, the market movement risk affecting portfolios lies with clients.

The Group does not guarantee returns on portfolios. However, the Group's revenue is affected by the value of assets under management.

The Group earns interest from its cash balances, and is therefore exposed to fluctuations in interest rates.

The Group aims to minimise exposure to this risk through active management of cash deposits with a range of depositories.

The Group's operating policy is for foreign currency exposures to be kept to a minimum but, from time to time, foreign currency bank balances may be held. Such exposures are short-term but, where they do arise, a market risk requirement (foreign currency position risk requirement) will be calculated.

At any time, there will also be a small exposure to market risk in CIFM on positions held in the manager's box. Again, such positions are kept to a minimum but, where they exist, an equity position risk requirement will be calculated.

6.3.3 Business and Operational Risk

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

The majority of the risks affecting the Group can be classified as operational risks and therefore most of the risk management effort is focused on operational risk. The Group seeks to mitigate operational risk to acceptable residual levels, in accordance with its risk appetite policy, by maintaining a strong control environment, which is managed through the Group's operational risk management framework, as set out in section 4. The Group also has insurance arrangements in place to mitigate operational risks.

7. Solvency

At the present time, based on our analysis of risks faced by the business and the capital required to be set aside for those risks, the Group is adequately capitalised with excess capital resources of £44m and a regulatory capital ratio of 307%.

	30/09/11 £'000
Pillar 1	
Fixed Overhead Requirement	14,377
Pillar 2	6,757
	21,134
Surplus Capital	43,706
Regulatory Capital Ratio	307%