

## Sand Grove Capital Management LLP

### PILLAR 3 AND REMUNERATION DISCLOSURE

The Capital Requirements Directive ('CRD') and Alternative Investment Fund Management Directive ('AIFMD') of the European Union establish a revised regulatory capital framework across Europe governing the amount and nature of capital credit institutions and investment firms must maintain.

In the United Kingdom, the CRD and AIFMD have been implemented by the Financial Conduct Authority ('FCA') in its regulations through the General Prudential Sourcebook ('GENPRU'), the Prudential Sourcebook for Banks, Building Societies and Investment Firms ('BIPRU'), The Interim Prudential Sourcebook for Investment Business ("IPRU (INV)").

The CRD consists of three 'Pillars':

- Pillar 1 sets out the minimum capital amount that meets the firm's credit, market and operational risk capital requirement;
- Pillar 2 requires the firm to assess whether its capital reserves, processes, strategies and systems are adequate to meet pillar 1 requirements and further determine whether it should apply additional capital, processes, strategies or systems to cover any other risks that it may be exposed to; and
- Pillar 3 requires disclosure of specified information about the underlying risk management controls and capital position to encourage market discipline.

The AIFMD adds further capital requirements based on the Alternative Investment Fund ('AIF') assets under management and professional liability risks.

The rules in BIPRU 11 set out the provision for Pillar 3 disclosure. This document is designed to meet our Pillar 3 obligations.

The Pillar 3 disclosure document has been prepared by Sand Grove Capital Management LLP ('The Firm') in accordance with the requirements of BIPRU 11 and is verified by the Senior Members. Unless otherwise stated, all figures are as at the March 31<sup>st</sup> 2020 financial year-end.

Pillar 3 disclosures will be issued on an annual basis after the year end and made available as soon as practical after the annual accounts are finalised.

We are permitted to omit required disclosures if we believe that the information is immaterial such that omission would be unlikely to change or influence the decision of a reader relying on that information for the purpose of making economic decisions about the Firm.

In addition, we may omit required disclosures where we believe that the information is regarded as proprietary or confidential. In our view, proprietary information is that which, if it were shared, would undermine our competitive position. Information is considered to be confidential where there are obligations binding us to confidentiality with our customers, suppliers and counterparties.

We have omitted certain data on the grounds of materiality, and confidentiality.

### **Scope and Application of the Requirements**

The Firm is authorised and regulated by the FCA and as such is subject to minimum regulatory capital requirements. The Firm is categorised as a Collective Portfolio Management Investment ('CPMI') Firm by the FCA for capital purposes.

The Firm is not a member of a group and so is not required to prepare consolidated reporting for prudential purposes.

### **Risk Management**

The Firm has established a risk management process in order to ensure that it has effective systems and controls in place to identify, monitor and manage risks arising in the business. The risk management process is overseen by the Chief Operating Officer, with the Senior Management team taking overall responsibility for this process and the fundamental risk appetite of the Firm. The Chief Operating Officer has responsibility for the implementation and enforcement of the Firm's risk principles.

Senior Management meet on a regular basis and discuss current projections for profitability, cash flow, regulatory capital management, business planning and risk management. Senior Management engage in the Firm's risks through a framework of policies and procedures having regard to the relevant laws, standards, principles and rules (including FCA principles and rules) with the aim of operating a defined and transparent risk management framework. These policies and procedures are updated as required.

The Senior Management team has identified that business, operational, market and credit are the main areas of risk to which the Firm is exposed. Annually the Senior Management team formally review their risks, controls and other risk mitigation arrangements and assess their effectiveness.

A formal update on operational matters is provided to the Senior Management team on a monthly basis. Management accounts demonstrate continued adequacy of the Firm's regulatory capital and are reviewed on a regular basis.

Appropriate action is taken where risks are identified which fall outside of the Firm's tolerance levels or where the need for remedial action is required in respect of identified weaknesses in the firm's mitigating controls.

### **Business Risks**

Specific risks applicable to the Firm come under the headings of business, operational, credit and market risks.

### **Business Risk**

The Firm's revenue is reliant on the performance of the existing funds under management and its ability to obtain new mandates. As such, the risk posed to the Firm relates to investment underperformance and adverse market conditions hindering fund-raising and ultimately the risk of redemptions from the funds managed by the Firm resulting in a decline in revenue. This risk is mitigated by:

- the use of lock up periods and redemption gates imposed by the funds;
- the avoidance of excessively long-term contracts with suppliers;
- regular monitoring of expenses (budget and actual), income and regulatory capital;
- sufficient levels of capital held by the Firm which will continue to cover the operating expenses of the business.

### **Operational Risk**

The Firm places strong reliance on the operational procedures and controls that it has in place in order to mitigate risk and seeks to ensure that all personnel are aware of their responsibilities in this respect.

The Firm has identified a number of key operational risks to manage. These relate, amongst other things, to systems failure, failure of a third-party provider, potential for serious regulatory breaches, market abuse, trade and settlement errors. The Firm has a comprehensive Operations Manual that documents risk and mitigating controls throughout the operational cycle. This is supplemented by appropriate policies. Operational risk is reviewed at monthly senior management meetings and is reported on to the Funds' Boards. Procedures and controls are adjusted as required to reflect the changing operational environment.

The Firm has taken out adequate professional indemnity insurance and this is reviewed on at least an annual basis.

### **Credit Risk**

The Firm is exposed to credit risk in respect of its debtors, investment management fees billed and cash held on deposit.

Management fees are drawn monthly in arrears from the funds managed and performance fees are drawn annually where applicable. The Firm considers that there is little risk of default by its clients. All bank accounts are held with reputable credit institutions which are subject to annual credit review.

Given the nature of the Firm's exposures, no specific policy for hedging and mitigating credit risk is in place. The Firm uses the simplified standardised approach detailed in BIPRU 3.5.5 of the FCA Handbook when calculating risk weighted exposures of 1.6% (Cash in Bank) and 8% in respect of its other assets.

**Credit Risk Summary**

Credit risk exposure	Risk weighting	8% of risk weighted exposure
Cash	20%	£41,760
Other Debtors (<1 year)	100%	£79,920

**Market Risk**

The Firm takes no market risk other than foreign exchange risk in respect of its accounts receivable and cash balances held in currencies other than GBP. The Firm maintains minimal foreign currency balances purely for the funding of foreign currency expenses.

The Firm calculates its foreign exchange risk by reference to the rules in BIPRU 7.5.1 of the FCA Handbook and applies an 8% risk factor to its foreign exchange exposure.

**Professional Liability Risk**

The Firm has a legal responsibility for risks in relation to investors, products & business practices including, but not limited to: misrepresentations and misleading statements made to the AIF or its investors; acts, errors or omissions; failure by the senior management to establish, implement and maintain appropriate procedures to prevent dishonest, fraudulent or malicious acts; improper valuation of assets and calculation of unit/share prices; and risks in relation to business disruption, system failures, process management. The Firm is aware of, and monitors, a wide range of risks within its business operations and towards its investors. The Firm has in place appropriate internal operational risk policies and procedures to monitor and detect these risks. These procedures and risks are documented, demonstrating how the Firm aims to mitigate these risks and they are reviewed regularly.

The Firm's holds additional own funds of £159k, equating to 0.01% of the total AIF funds under management.

**Liquidity Risk**

The Firm is required to maintain sufficient liquidity to ensure that there is no significant risk that its liabilities cannot be met as they fall due or to ensure that it can secure additional financial resources in the event of a stress scenario.

The Firm retains an amount it considers suitable for providing sufficient liquidity to meet the working capital requirements under normal business conditions. The Firm has always had sufficient liquidity within the business to meet its obligations and there are no perceived threats to this given the cash deposits it holds. Additionally, it has historically been the case that all management fee debtors are

settled promptly, thus ensuring further liquidity resources are available to the Firm on a timely basis. The cash position of the Firm is monitored by the Chief Operating Officer on a monthly basis and is reported to the Senior Members.

### Regulatory Capital

The Firm is a Limited Liability Partnership and its capital arrangements are established in its Partnership deed. The main features of the Firm's capital resources for regulatory purposes are as follows:

	<b>31/3/20</b>
	<b>£000</b>
Tier 1 capital*	3,229
Tier 2 capital	-
Tier 3 capital	-
Deductions from Tiers 1 and 2	
<b>Total capital resources</b>	<b>3,229</b>
*No hybrid tier one capital is held	

Our Firm is small with a simple operational infrastructure. Its market risk is limited to foreign exchange risk on its accounts receivable in foreign currency, and credit risk from management and performance fees receivable from the funds under its management. The Firm follows the standardised approach to market risk and the simplified standard approach to credit risk.

As discussed above the Firm is a CPMI Firm and as such its capital requirements are the higher of:

- €125,000 (+ 0.02% of excess AIF AUM where AUM exceeds €250m); and
- The fixed overheads requirement ('FOR') which is essentially 25% of the Firm's operating expenses less certain variable costs.

A CPMI Firm must also hold a further amount of own funds to cover risks arising from professional Negligence. These are calculated as 1 basis point of AUM.

The FOR is calculated, in accordance with FCA rules, based on the Firm's previous year's audited expenditure. The Firm is not subject to an operational risk requirement.

It is the Firm's experience that the Fixed Overhead Requirement establishes its capital requirements.

**Capital Requirement**

The Firm's Pillar 1 capital requirement has been determined by reference to the Firm's Fixed Overheads Requirement ('FOR') and calculated in accordance with Article 95 and the EBA Final draft technical standards as referenced in IPRU(INV) 11.3.3A . The requirement is based on the FOR since this exceeds the total of the credit and market risk capital requirements it faces and also exceeds its base capital requirement of €125,000.

The FOR is based on annual expenses net of variable costs deducted, which include discretionary bonuses paid to staff. The Firm monitors its expenditure on a monthly basis and takes into account any material fluctuations in order to determine whether the FOR remains appropriate to the size and nature of the business or whether any adjustment needs to be made intra-year.

This is monitored by the Chief Operating Officer and reported to senior management on a monthly basis.

## REMUNERATION DISCLOSURE

The Firm is authorised and regulated by the Financial Conduct Authority as a Collective Portfolio Management Investment ('CPMI') Firm and is therefore subject to FCA Rules on remuneration. These are contained in the FCA's Remuneration Codes located in the SYSC Sourcebook of the FCA's Handbook.

The Remuneration Code covers an individual's total remuneration, fixed and variable. The Firm incentivises staff through a combination of the two.

The Firm's business is a manager of alternative investment funds.

Our policy is designed to ensure that we comply with the Remuneration Code and our compensation arrangements:

1. are consistent with and promote sound and effective risk management;
2. do not encourage excessive risk taking;
3. include measures to avoid conflicts of interest (examples include a fixed allocation policy, gifts & inducement policy, use of commission policy and broker assessment process, and alignment with investors through a common absolute return objective coupled with a high-water mark);
4. are in line with the Firm's business strategy, objectives, values and long-term interests.

### Scope / Application

The general provisions of this policy will apply to all staff and Members of the Firm providing AIFM investment management functions, with certain provisions potentially applying only to those persons whose professional activities have a material impact on the risk profiles of the AIFM or the AIFs it manages, otherwise known as "AIFM code staff".

AIFM code staff are typically:

- senior management (including NEDs), control functions (i.e. staff responsible for compliance, risk and audit), business unit heads, risk takers (including portfolio managers);
- Delegates who provide portfolio management or risk management;
- staff who exert a material influence on the risk profile of the AIFs or AIFM; and
- any employee remunerated in the same bracket as the above.

With regards to performance related remuneration for employees, the total amount of remuneration will take into account performance of the individual, the AIFs and the overall results of the Firm. When assessing individual performance, financial and non-financial criteria are taken into account.

### Proportionality

Enshrined in the European remuneration provisions is the principle of proportionality. The FCA has sought to apply proportionality in the first instance by instituting two tests. Firstly, a firm that is significant in terms of its size must disclose quantitative information referred to in BIPRU 11.5.18R at the level of senior personnel. Secondly, that a firm must make disclosure that is appropriate to the size, internal organisation and the nature, scope and complexity of their activities.

The Firm is not 'significant', that is to say has relevant total assets <£50bn\* and so makes this disclosure in accordance with the second test (BIPRU 11.5.20R(2)).

\* average total assets on the last three accounting dates.

### **Application of the requirements**

We are required to disclose certain information on at least an annual basis regarding our Remuneration policy and practices for those staff whose professional activities have a material impact on the risk profile of the Firm. Our disclosure is made in accordance with our size, internal organisation and the nature, scope and complexity of our activities. The Firm's Remuneration Policy is available at the request of investors.

- The Firm's policy has been agreed by the Senior Management in line with the Remuneration principles laid down by the FCA.
- Remuneration of all members and employees of the Firm is directly overseen by the Remuneration Committee which will make recommendations on remuneration to the Managing Member of the Firm. The Remuneration Committee will independently review this remuneration policy at least annually.
- The Firm's policy will be reviewed as part of an annual review of process and procedures, or following a significant change to the business requiring an update to its internal capital adequacy assessment.
- There is limited involvement of the Firm in deriving asset prices as the majority of assets held are in liquid securities and are independently verified by the Fund Administrator, with oversight by the Funds' Boards.

### **Remuneration Recommendation Determination**

When determining the recommendation for remuneration levels the Remuneration Committee will specifically consider the AIFM remuneration principles but more generally will consider the below factors.

For Members of the LLP:

- The profitability of the Firm as a whole
- The individual's contribution to the profitability of the Firm
- The individual's performance in carrying out their role
- Market levels of compensation for individuals carrying out similar roles
- The individual's efforts to promote the broader values of the Firm
- The long-term contribution of the individual to the success of the Firm

The Remuneration Committee appreciates the necessity for non-investment staff remuneration to be structured appropriately to prevent conflicts of interest and sufficient independence from investment performance. Therefore, the Remuneration Committee will recommend to the Managing Member that should the Firm be sufficiently profitable, non-investment members are allocated sufficient profits so as to cover their monthly draw.

For employees of the Firm and related entities:

- The individual's performance in carrying out their role
- Market levels of compensation for individuals carrying out similar roles
- The individual's efforts to promote the broader values of the Firm
- The long-term contribution of the individual to the success of the Firm

We may omit required disclosures where we believe that the information could be regarded as prejudicial to the UK or other national transposition of Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regards to the processing of personal data and on the free movement of such data. Due to the small number of Remuneration Code Staff the Firm has determined not to disclose remuneration data here. Partnership profits allocated to members of the LLP are disclosed in aggregate in the LLP's report and accounts, and further remuneration information is available to fund investors within the relevant Annual Report Disclosures.