

## Pillar 3 and remuneration disclosure

### Background

The European Capital Requirements Directive (CRD) created a revised regulatory capital framework based on the provisions of the Basel 2 Capital Accord.

This was implemented in the United Kingdom by the FSA through the creation of the General Prudential Sourcebook ('GENPRU') and the Prudential Sourcebook for Banks, Building Societies and Investment Firms ('BIPRU').

The framework consists of three 'pillars' namely;

- Pillar 1 – which sets out the minimum capital requirements that firms are required to meet for credit, market and operational risk;
- Pillar 2 – which requires firms to take a view on whether additional capital should be held against capital risks not covered by Pillar 1; and
- Pillar 3 - which requires firms to publish certain details of its risks, capital and risk management process.

BIPRU 11.5 (technical criteria on disclosure: general requirements) and 11.6 (qualifying requirements for the use of particular instruments or methodologies) require that a firm subject to the provisions of the CRD must disclose, as appropriate, the relevant information required under Pillar 3. This must be done in accordance with a formal disclosure policy which sets out the firm's policies for assessing the appropriateness of its disclosures, including their verification and frequency.

The rules provide that the firm may omit one or more of the required disclosures if it believes 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. Where the firm considers a disclosure to be immaterial, it should state this in the relevant section.

The firm is also permitted to omit one or more of the required disclosures where it believes that the information is regarded as proprietary or confidential. Proprietary information is that which, if it were shared, would undermine the firm's competitive position. Information is considered to be confidential where there are obligations binding the firm to confidentiality with its clients and counterparties. Where the firm has omitted information for either of these two reasons it should state this in the relevant section and the reasons for this. Where appropriate, the firm has published more general information on the subject matter of the required disclosure.

In this document the firm discloses information in accordance with the following BIPRU 11.5 rules unless it has been determined as immaterial or of a proprietary or confidential nature:

- BIPRU 11.5.1R on our risk management objectives and policies;
- BIPRU 11.5.2R on the scope of application of directive requirements;
- BIPRU 11.5.3R on our capital resources;
- BIPRU 11.5.4R (subsections 1 and 2) on our compliance with the rules in BIPRU and on Pillar 2 requirements;
- BIPRU 11.5.16R on our interest rate risk

BIPRU 11.6 does not apply to SG Wealth Management Ltd

These Pillar 3 Disclosures have been subject to internal review procedures. The information has not been audited by the firm's external auditors.

### **Scope and application of Directive requirements**

The disclosures in this document are made in respect of SG Wealth Management Ltd which provides independent financial advice and / or discretionary investment management services.

The firm is a limited licence firm as defined by the FSA.

### **Risk management objectives and policies**

Our risk management policy reflects the FSA requirement that we must manage a number of different categories of risk. These include: liquidity, credit, market, interest rate, business and operational risks.

#### **i. Liquidity risk**

The firm manages all cash and borrowing requirements to maximise potential interest income whilst ensuring the firm has sufficient liquid resources to meet the continued operating needs of the business. This is supported by a robust budgeting and forecasting process which has the full involvement of the senior management team.

#### **ii. Credit risk**

The main credit risk for the firm relates to advisory fees, being the risk that a client does not pay amounts due for services provided. This risk is mitigated by the high number of clients in respect of which amounts are mainly covered by payments from the investment platform and offset against fees due. The risk of non payment is also reduced due to the nature of the clients as they are typically wealthy individuals.

The firm's revenues also include annual management charges received from clients based on a percentage of client assets under management. These charges are typically made directly to the clients' portfolios, and therefore the credit risk relating to this income is minimal.

The risk relating to amounts due from providers as a result of legacy renewal commission streams is considered to be low. This is because these amounts are due from institutions that are regulated by the FSA.

#### **iii. Market Risk**

The firm is indirectly subject to market risk as a significant element of income is dependent upon the value of client funds under management. This risk is mitigated by the asset allocation strategy adopted, which ensures that clients have highly diversified portfolios with limited exposure to any one asset class. Accordingly exposure to market risk is considered minimal.

#### **iv. Interest rate risk**

The firm has no borrowings and no exposure to interest rate risk.

#### **v. Business Risk**

The firm's Pillar 2 business risk assessment principally takes the form of a fall in assets under management following a market downturn that leads to lower management fees, although other risks such as loss of advisers and systems failures are also considered. To mitigate our business risk, we regularly analyse various different economic scenarios to model the impact of economic downturns on our financial position.

## **vi. Operational Risk**

Operational risk is defined as the potential risk of financial loss or impairment to reputation resulting from inadequate or failed internal processes and systems, from the actions of people or from external events.

Major sources of operation risk include: outsourcing of operations, IT security, internal and external fraud, implementation of strategic change and regulatory non-compliance.

The firm operates a robust risk management process which is regularly reviewed and updated with details being provided to all staff. The firm's Compliance Oversight is responsible for the periodic reviews and recommending any changes to the Board

All senior management will bear responsibility for internal controls and the management of business risk as part of their accountability to the board.

Individuals are responsible for identifying the risks surrounding their work, implementing controls over those risks and reporting areas of concern to their line manager.

The Compliance Oversight will provide the board with a half-yearly summary report on all significant risk issues using a traffic light system – red (unacceptable), amber (watch list) and green (acceptable).

## **vii. Capital resources**

### **Pillar 1 requirement**

In accordance with GENPRU 2.1.45R (calculation of variable capital requirement for a BIPRU firm), our capital requirement has been determined as being our fixed overhead requirement and not the sum of our credit risk capital requirement and our market risk capital requirement.

The Pillar 1 capital requirement for SG Wealth Management Ltd was £102,000 as at 21<sup>st</sup> January 2011.

### **Pillar 2**

Our overall approach to assessing the adequacy of our internal capital is set out in our Internal Capital Adequacy Assessment Process (ICAAP). The ICAAP process involves separate consideration of risks to our capital combined with stress testing using scenario analysis. The level of capital required to cover risks is a function of impact and probability. We assess impact by modelling the changes in our income and expenses caused by various potential risks over a 1-year time horizon. Probability is assessed subjectively.

In addition, we have reviewed the outputs of our risk reviews to quantify any risks identified. This has identified a number of key business risks which we have classified against the risk categories contained in GENPRU 1.2.30R and reviewed the guidance in BIPRU 2.2.61-65.

Our Pillar 2 capital requirement, which is our own assessment of the minimum amount of capital that we believe is adequate against the risks identified, has been assessed as greater than our Pillar 1 requirement. There is a considerable surplus of reserves above the capital resource requirement deemed necessary to cover the risks identified.

### **Other risks**

The firm operates a simple business model. Accordingly, many of the specific risks identified by the FSA do not apply.

## Regulatory capital

The main features of SG Wealth Management Ltd's capital resources for regulatory purposes, as at 31/12/10 are as follows:

Capital item:	£000s
Tier 1 capital (called up share capital, share premium account, profit and loss account, externally verified interim net profits)	401
Total of tier 2 and tier 3 capital (broadly long and short term subordinated loans)	0
Deductions from tier 1 and tier 2 capital	0
<b>Total capital resources, net of deductions</b>	<b>401</b>

The firm holds regulatory capital in accordance with the Capital Requirements Directive. All such capital is classified as Tier 1 capital and is therefore of the highest quality.

## Remuneration Disclosure

- The executive directors are responsible for remuneration policy. No individual receives remuneration above the current de minimus figure published under Principle 12c.
- There is no guaranteed variable remuneration linked to sales performance for any member of staff.

Breakdown of remuneration of staff in respect of whom disclosure is required by business area (BIPRU 11.5.18(6))	
	Total Remuneration
Wealth Management	£ below de minimus
	£

*Date of publication 20<sup>th</sup> July 2011*