



## **Capital Requirements Directive: Pillar 3 Disclosure** (as at 31 December 2013)

**The F&C Group**

## Purpose

The Capital Requirements Directive (“CRD”) introduced a revised capital adequacy framework across Europe seeking to reduce the probability of consumer loss or market disruption as a result of prudential failure. It does so by seeking to ensure that the financial resources held by firms are commensurate with the risks associated with their business profile and their control environment.

## Background

The framework under the CRD consists of three 'pillars' of regulatory capital. Pillar 1 sets out the minimum capital requirements firms are required to meet for credit, market and operational risk. Under Pillar 2, firms and their supervisors are required to form an opinion on whether they should hold additional capital against risks not adequately covered by Pillar 1 and must take action accordingly. The aim of Pillar 3 is to then improve market discipline by requiring firms to publish certain details of their capital, risk exposures and management practices, and to have a formal disclosure policy to assess the appropriateness, verification and frequency of disclosure. This document is F&C's response to the Pillar 3 requirements and, as such, constitutes the F&C Group Pillar 3 disclosure.

F&C's Pillar 3 disclosure covers the applicable requirements as set out in chapter 11 of the BIPRU Handbook.

## Scope and Application Of Disclosure Requirements

The disclosures in this document relate to the F&C Group (“F&C” or “the Group”), the parent of which, F&C Asset Management plc (“FCAM”), is an unregulated holding company, listed on the London Stock Exchange.

The Group obtained a waiver from the UK's financial regulator<sup>1</sup> from meeting any minimum capital requirements under the consolidated supervision rules and consequently under the FCA rules, specifically BIPRU 11.2.1 R (3), disclosures must be made on an individual basis across all in-scope CRD firms. These firms are:

| F&C Group Company                 | Abbreviation | Country of incorporation | Prudential Regulator |
|-----------------------------------|--------------|--------------------------|----------------------|
| F&C Asset Managers Limited        | F&CAM        | England                  | FCA <sup>1</sup>     |
| F&C Management Limited            | FCM          | England                  | FCA                  |
| F&C Managers Limited              | FCMGRS       | England                  | FCA                  |
| F&C REIT Property Asset Mgmt. plc | FCRPAM       | England                  | FCA                  |
| F&C Investment Business Limited   | FCIB         | Scotland                 | FCA                  |
| Thames River Capital LLP          | TRC          | England                  | FCA                  |
| Thames River Multi-Capital LLP    | TRMC         | England                  | FCA                  |
| F&C Netherlands B.V.              | FCNL         | Netherlands              | DNB <sup>2</sup>     |
| F&C Portugal S.A.                 | FCPGL        | Portugal                 | BoP <sup>3</sup>     |

All firms detailed are consolidated into the Group for accounting purposes. There are no known current or foreseen practical or legal impediments (other than those set out by law or in regulation) to the prompt transfer of capital resources or

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<sup>1</sup> Financial Conduct Authority

<sup>2</sup> De Nederlandsche Bank

<sup>3</sup> Banco de Portugal

repayments of liabilities between parent and subsidiary undertakings and there are no subsidiary undertakings where actual capital resources are less than the required minimum, i.e. each regulated company within the Group currently holds a surplus of regulatory capital.

### **Risk Management Objectives and Policies**

The Group is a diversified asset management group focused on two core client segments: strategic partners and consumer and institutional clients. The Group manages investments from multiple investment centres including London, Edinburgh, Amsterdam and Lisbon. Investment teams have clearly differentiated products and processes with no overlap. Each product managed by the Group is rigorously monitored from a risk management perspective.

Our risks are typical to those of investment managers and fall under the categories of financial risk, operational risk and strategic risk. It is important to note that all risks are monitored and managed as part of a governance and risk management framework which is consistently applied across all firms within the Group. This uniformity arises as all Group firms are managed and operated to support the Group's objectives and strategies, and the FCAM Board and Group Management provides oversight of all operations.

The procedures that the Directors have established are designed to provide effective control within the Group and accord with the UK Corporate Governance Code issued by the Financial Reporting Council ("FRC"). The ongoing process of identifying, assessing and managing significant risks is regularly reviewed by the FCAM Board to ensure that it complies with FRC corporate governance standards.

### **Control Environment**

The Group is committed to high standards of business conduct and seeks to maintain these across all areas of its business and all jurisdictions in which it operates. The Group has procedures for reporting and resolving matters that do not meet the required standards of business conduct.

The Group has an appropriate organisational structure for planning, executing, managing and monitoring business operations in order to achieve its objectives. This structure is designed to provide clear responsibilities and a control framework for key areas of the Group's business.

Operational responsibility for the control environment rests with the Chief Executive and is devolved through a documented executive structure with clearly delegated and appropriate levels of authority. Members of Group Management are, therefore, accountable for the operation of the systems of internal controls within the Group's business.

### **Monitoring and Corrective Action**

The Group has a formal compliance function and separate risk and internal audit functions. Compliance conduct regular monitoring of various business areas and control procedures in line with a plan agreed quarterly with the Group Audit and Compliance Committee ("ACC"), a sub-committee of the FCAM Board. Any issues of significance are brought to the attention of the ACC by compliance through the regular reporting process. Planned corrective actions are independently monitored for timely completion and reviewed by the ACC.

The ACC reviews the effectiveness of the operation of the control framework at least twice each year.

A formal annual internal control report is produced for F&C's clients providing assurance on both the design and the operating effectiveness of F&C's control procedures. The report follows the Audit & Assurance Faculty ("AAF") guidelines established by the ICAEW.

### **Approach to Operational and Strategic Risk**

Operational risk is defined as the risk of loss resulting from unexpected changes in elements related to operations such as human resources, technology, processes and other events. Strategic risk is defined as the risk of loss resulting from unexpected changes in key elements of strategy formulation or execution.

The identification of major operational and strategic risks is carried out by the FCAM Board in conjunction with management, and procedures to manage these risks, where possible, are reviewed and agreed.

Quarterly risk reports are prepared by each of the business units, across all locations including the Group's overseas operations. The quarterly reports include issues of material risk. These reports are discussed in detail by Group Management, which includes the Executive Directors of FCAM. All significant items are identified and reported to the Board on a regular basis.

The risk function facilitates the identification and documentation of risk in the business and helps the business identify mitigating actions. In addition, any business incidents, including mandate breaches, are reported by the business to the risk team where they are recorded and progress actively monitored until resolved.

### **Approach to Financial Risk**

The Group's risk management objectives and policies applicable to this disclosure and with specific regard to counterparty credit risk, liquidity risk, market risk and pension obligation risk are summarised below.

- Counterparty credit risk is defined as risk associated with unexpected changes in the credit-worthiness of counterparties.
- Liquidity risk is defined as the risk of the Group failing to maintain adequate levels of financial resources to enable it to meet its financial obligations as they fall due.
- Market risk is defined as the risk that the fair value or future cash flows of financial instruments will fluctuate because of changes in market prices.
- Pension obligation risk is defined as risk to a firm caused by its contractual or other liabilities to or with respect to a pension scheme.

F&C adopts a low risk approach to treasury management and seeks to ensure that its capital is preserved and financial risks are managed appropriately.

The Group's corporate treasury activities are managed by the Finance function within parameters defined by the Board. The regulatory capital and treasury positions of the Group are reported to the Board on a regular basis.

The Group is exposed to a number of financial risks in the normal course of its business. The risk management policies adopted are designed to manage risk and recognise that treasury management operations are specifically not treated as a profit centre. The key aspects of this policy and its implementation are detailed below:

- The Board Reserved List prohibits the establishment of borrowing facilities without the prior approval of the Board.
- Placing of funds on deposit is short term only (maximum term 90 days) – unless approved by Group Management.
- Deposits may only be placed with counterparties approved by the F&C Credit & Counterparty Approval Committee, and the Board sets the appropriate limit of exposure to any one counterparty.
- Foreign currency exposure is managed to reduce the risk and impact of movements in exchange rates by the repatriation of surplus foreign currency to Sterling and the hedging of non-Sterling balances when exchange rates are considered by the Board to present an opportunity to fix the Sterling value of future Euro-denominated income streams at an acceptable level. Surplus currency balances are defined as being the level of cash which exceeds the regulatory, legal and working capital requirements of the relevant firms.

The Directors give careful consideration to the appropriate funding structure for financing all acquisitions including the capacity to fund anticipated restructuring activity.

The Group is exposed to the effects of fluctuations in the prevailing levels of market interest rates on its financial assets, but benefits from the certainty of fixed interest rates on its issued debt.

## **Remuneration**

The Group is subject to the FCA's Remuneration Code (the Code). A key objective of the Code is to ensure remuneration policies promote effective risk management and in line with this, the FCA has issued guidance as to how firms may apply the Code in a proportionate manner based on their risk profile. The Group is required to comply with the Code and considers itself a Tier Three entity in terms of the FCA's guidance on proportionate application. The following represents F&C's remuneration disclosure under Pillar 3 for the year ended 31 December 2013.

Decision-making process for remuneration policy - F&C has formed a Remuneration Committee (REMCom) which meets regularly to consider human resources matters relating to terms and conditions of employment, remuneration and retirement benefits. Within the authority delegated by the Board, REMCom is responsible for the approval, review and implementation of F&C's Remuneration Policy and in doing so takes into account the pay and conditions across the Group. This includes the terms of bonus plans, share plans, other long-term incentive plans and the individual remuneration packages of executive Directors and other senior management including those employees deemed to have an impact on F&C's risk profile (Code Staff).

There were 4 meetings of REMCom during 2013. Following each meeting, REMCom reports to F&C's Board on its activities. The members of REMCom are independent non Executive Directors of the Board.

External Consultants - REMCom received independent advice on various remuneration issues from Kepler Associates, McLagan & Partners, Deloitte and PricewaterhouseCoopers.

No individual is involved in decisions relating to his or her own remuneration.

Role of the relevant stakeholders - REMCom takes account of F&C's strategic objectives in setting remuneration policy and is mindful of its duties to shareholders and other stakeholders. The Terms of Reference of REMCom ensures that the long-term interests of shareholders, investors and other stakeholders are taken into account. REMCom seeks to preserve shareholder value by ensuring the successful retention, recruitment and motivation of employees.

Code Staff criteria - F&C recognises that Code Staff includes Directors and employees who are carrying out Significant Influence Functions, senior management, risk takers, heads of control functions and any employee (in the same remuneration bracket) whose professional activities have a material impact on F&C's risk profile. (Code Staff are defined with reference to managerial responsibility to influence F&C's overall risk profile). REMCom will determine those Directors and employees whose role and responsibilities have a material impact on F&C's risk profile. Sixteen Directors and employees have been identified as Code Staff and whose roles include Directors, Group Management, risk and other senior managers and heads of control functions as deemed appropriate. A record of Code Staff is maintained by Human Resources and is reviewed at least annually by the REMCom.

The link between pay and performance for Code Staff - Remuneration is made up of fixed pay (i.e. salary and benefits) and variable performance-related pay. Performance related pay is designed to reflect success or failure against a range of

targets. F&C is committed to awarding an appropriate mix of salary, cash bonus and long-term awards as warranted by company and individual performance and market practice.

Aggregate remuneration cost for Code Staff by business area - The aggregate annual remuneration of the Code Staff (excluding Non-Executive Directors) in respect of 2013 was £8.8m. This is made up of fixed pay, variable pay, non-contributory pension/ and benefits in kind and share plan related remuneration. F&C's business is defined as one business unit covering Asset Management.

Further details on remuneration are set out in the Report on Directors' Remuneration section of the 2013 Annual Report & Accounts.

## Capital Resources

The core tier 1 capital resources of each firm consist of share capital (or members capital for, Thames River Capital LLP and Thames River Multi-Capital LLP), share premium and profit & loss account and other reserves. Share capital relates to

ordinary shares in each firm that are allotted, called up and fully paid. F&C Management Limited holds tier 3 capital of £10m relating to a subordinated loan with a fellow subsidiary undertaking, which was settled in January 2014.

| <b>Capital Resources<br/>31 December 2013</b> | <b>F&amp;CAM</b><br>£'000 | <b>FCM</b><br>£'000 | <b>FCMGRS</b><br>£'000 | <b>FCRPAM</b><br>£'000 | <b>FCIB</b><br>£'000 | <b>TRC</b><br>£'000 | <b>TRMC</b><br>£'000 | <b>FCNL</b><br>€'000 | <b>FCPGL</b><br>€'000 |
|---|---------------------------|---------------------|------------------------|------------------------|----------------------|---------------------|----------------------|----------------------|-----------------------|
| Core Tier 1:                                  |                           |                     |                        |                        |                      |                     |                      |                      |                       |
| Share Capital                                 | 16,000                    | 32,332              | 500                    | 1,000                  | 13,000               | 7,000               | 3,260                | 209                  | 9,000                 |
| Share Premium                                 | -                         | 42,197              | -                      | -                      | -                    | -                   | -                    | 112,927              | -                     |
| Profit & loss and other reserves <sup>4</sup> | (327)                     | 11,479              | 21,394                 | 1,748                  | (847)                | 0                   | 0                    | (94,306)             | 12,370                |
| <b>Total Core Tier 1 Capital</b>              | <b>15,673</b>             | <b>86,008</b>       | <b>21,894</b>          | <b>2,748</b>           | <b>12,153</b>        | <b>7,000</b>        | <b>3,260</b>         | <b>18,830</b>        | <b>21,370</b>         |
| Deductions from Tier 1:                       |                           |                     |                        |                        |                      |                     |                      |                      |                       |
| Intangible Assets                             | -                         | -                   | -                      | -                      | 708                  | -                   | -                    | -                    | -                     |
| Material holdings in financial inst.          | -                         | 50                  | -                      | -                      | -                    | -                   | -                    | -                    | -                     |
| <b>Tier 1 capital after deductions</b>        | <b>15,673</b>             | <b>85,958</b>       | <b>21,894</b>          | <b>2,748</b>           | <b>11,445</b>        | <b>7,000</b>        | <b>3,260</b>         | <b>18,830</b>        | <b>21,370</b>         |
| Tier 2 and Tier 3 capital                     | -                         | 10,000              | -                      | -                      | -                    | -                   | -                    | -                    | <b>13</b>             |
| Deductions from total capital                 | 0                         | 59,142              | 13,872                 | 238                    | 5                    | 540                 | <b>3</b>             | 644                  | 0                     |
| <b>Total resources after deductions</b>       | <b>15,673</b>             | <b>36,816</b>       | <b>8,022</b>           | <b>2,510</b>           | <b>11,440</b>        | <b>6,460</b>        | <b>3,257</b>         | <b>18,186</b>        | <b>21,383</b>         |

<sup>4</sup> Excludes 2013 unaudited profits where applicable

### Capital Resource Requirements

All firms captured by the CRD are “limited licence” as specified by Article 20(2) of the CRD, and this dictates that each firm’s Pillar 1 capital requirement must follow the higher of: (a) the sum of the credit risk capital requirement and the market risk capital requirement; and (b) the fixed overheads requirement.

The exception to this is F&C Netherlands B.V. where the capital resource requirement is the sum of the credit risk capital requirement and the market risk capital requirement, per De Nederlandsche Bank prudential regulations. No operational risk requirement is calculated or included under Pillar 1.

| Capital Resource Requirements<br>31 December 2013 | F&CAM<br>£'000 | FCM<br>£'000  | FCMGRS<br>£'000 | FCRPAM<br>£'000 | FCIB<br>£'000 | TRC<br>£'000 | TRMC<br>£'000 | FCNL<br>€'000 | FCPGL<br>€'000 |
|---|----------------|---------------|-----------------|-----------------|---------------|--------------|---------------|---------------|----------------|
| <b>Base Capital Requirement</b>                   | <b>104</b>     | <b>104</b>    | <b>42</b>       | <b>104</b>      | <b>104</b>    | <b>42</b>    | <b>104</b>    | <b>50</b>     | <b>50</b>      |
| Credit risk capital requirement                   | 525            | 2,649         | 667             | 200             | 916           | 261          | 181           | 814           | 687            |
| Market risk capital requirement                   | 5              | 1,972         | -               | 73              | 94            | 23           | 1             | 90            | -              |
| Fixed overheads requirement                       | 6,338          | 15,455        | 1,054           | 305             | 1,977         | 2,048        | 349           | 9,409         | 1,678          |
| <b>Total variable capital requirement</b>         | <b>6,338</b>   | <b>15,455</b> | <b>1,054</b>    | <b>305</b>      | <b>1,977</b>  | <b>2,048</b> | <b>349</b>    | <b>904</b>    | <b>1,678</b>   |

The Group calculates the Pillar 1 credit risk capital requirement in accordance with the standardised approach. Further disclosures relating to the credit risk capital component have in most cases been considered immaterial under BIPRU 11.3.5R as the capital requirement for most firms is the fixed overhead requirement. The following table shows the credit risk exposure class for F&C Netherlands B.V. where the capital resource requirement is not the fixed overhead requirement. The market risk for F&C Netherlands B.V. relates to foreign exchange.

| Credit risk exposure class            | FCNL<br>€'000 |
|---------------------------------------|---------------|
| Institutions                          | 703           |
| Other items                           | 111           |
| Total credit risk capital requirement | 814           |

#### **Compliance With Rules In BIPRU and Pillar 2 Rule Requirements**

The adequacy of capital to support current and future activities is monitored in the F&C Internal Capital Adequacy Assessment Process (“ICAAP”). The level of capital required has been assessed through reviewing a number of scenarios and comparing them with the base case scenario of our budgeted business plan. This approach identifies the timescale and extent of possible capital deficiencies should an adverse scenario arise. The additional level of capital required to cover the Group against such a scenario can then be assessed and / or the mitigating actions identified which are required to ensure a continued capital surplus.

The latest base case scenario has been prepared as at the end of 2012, with actual results to this date and forecasts for a three-year time span to the end of

2015. This time span is deemed appropriate as it shows both a short-term view of any adverse scenarios and also an impact over the medium-term during which actions would be taken if continued deterioration were to occur.

#### **Verification, Frequency and Ongoing Review of the Disclosures**

The disclosures detailed in this document are updated in conjunction with the F&C Group ICAAP, and generally on an annual basis, unless there is a significant event which would detrimentally impact the capital and risk position of the Group.

The disclosures detailed in the ICAAP are reviewed and formally adopted by Group Management and the Board of FCAM, and the Board of each requisite firm.

The Pillar 3 disclosure document is reviewed and approved by the F&C Group Chief Financial Officer.

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