



## PILLAR III DISCLOSURES

According to Directives DI144-2014-15 and DI144-2014-14 of the Cyprus Securities & Exchange Commission for the prudential supervision of investment firms and Part Eight of Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms

**YEAR ENDED 31 DECEMBER 2018**

**April 2019**

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## 1. INTRODUCTION

### 1.1 CIF Information

H.C.F.S. High Capital Financial Services Ltd (hereinafter, the ‘Company’) was incorporated in the Republic of Cyprus on 26 September 2016 as a private limited liability company with registration number HE 360438 and it is a Cyprus Investment Firm. The Company was licensed by the Cyprus Security Exchange Commission (hereinafter, the ‘CySEC’) with number CIF 368/18 to provide financial services, on 30 July 2018 while its licence was activated on 13 December 2018.

Table 1 below illustrates the current licence information of the Company:

**Table 1: Company Licence Information (based on the First Appendix of the Law 87(I)/2017 as amended)**

		Investment Services and Activities								Ancillary Services						
		1	2	3	4	5	6	7	8	1	2	3	4	5	6	7
Financial Instruments	1	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	2	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	3	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	4	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	5	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	6	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	7	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	8	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	9	✓	✓	-	-	-	-	-	-	✓	✓	-	-	-	-	-
	10	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
	11	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-

The Company is authorised to provide the following **Investment Services**, in accordance with Part I of the First Appendix of the Law 87(I)/2017, as amended:

- Reception and transmission of orders in relation to one or more financial instruments
- Execution of orders on behalf of clients

The Company is authorised to provide the following **Ancillary Services**, in accordance with Part II of the First Appendix of the Law 87(I)/2017, as amended:

- Safekeeping and administration of financial instruments for the account of clients, including custodianship and related services such as cash/collateral management
- Granting credits or loans to one or more financial instruments where the firm granting credit or loan is involved in the transaction.
- Foreign exchange services where these are connected to the provision of investment services

The Company is authorised to provide the aforementioned investment and ancillary services solely for the Financial Instrument, “*Financial contracts for differences*”, in accordance with Part III of the First Appendix of the Law.

Moreover, pursuant to the Regulation (EU) 575/2013 (the “Regulation” or “CRR”) and, the Company is categorised as “**Limited Licenced**” CIF with minimum/initial capital requirement of €125k.

### 1.2. Scope of application

The Company is publishing the disclosures on an individual (solo) basis. The Pillar III disclosures is prepared in accordance with the Pillar 3 disclosure requirements as laid out in Part Eight of the Regulation No. 575/2013 (CRR) and Capital Requirement Directive IV

The report is based on the Annual Reports and Financial Statements which are prepared in accordance with International Financial Reporting Standards (IFRS) and the provisions of the Cyprus Company Law, Cap. 113.

### 1.3. Pillar III Regulatory framework

#### 1.3.1. Overview

This Pillar III report (the ‘Report’) has been prepared in accordance with Section 4 (Paragraph. 32) of the CySEC Directive DI144-2014-14 of 2014 (the “Directive”) for the prudential supervision of investment firms which implements the Regulation 575/2013 (the “Regulation” or “CRR”) and the European Directive 2013/36/EU (the “European Directive” or “CRD IV”), as well as the relevant provisions of new Law 87(I)/2017 (hereinafter, the “Law”), as amended. It is noted that the Law 144(I)/2007 has been replaced by Law 87(I)/2017, for the purpose of harmonization with European Directive 2014/65/EU (“MIFID II”) which applies to Cypriot investment firms (CIFs), market operators, data reporting service providers (DRSP), and third-country firms providing investment services or activities through the establishment of a branch in the Republic.

The CRR establishes the prudential requirements for capital, liquidity and leverage that entities need to abide by. Furthermore, CRR introduces significant changes in the prudential regulatory regime applicable to institutions including amended minimum capital ratios, changes to the definition of capital and the calculation or risk weighted assets and the introduction of new measures relating to leverage, liquidity and funding. Additionally, CRR permits a transition period for certain of the enhanced capital requirements and certain other measures, such as the leverage ratio, which are not expected to be fully implemented until 2018. CRR is immediately binding on all EU member states. CRD IV governs access to internal governance arrangements including remuneration, Board of Directors (the “Board”) composition and transparency.

The Regulatory framework consists of a three “Pillar” approach:

- **Pillar I** - Establishes minimum capital requirements, defines eligible capital instruments, and prescribes rules for calculating RWA for credit risk, market risk and operational risk.
- **Pillar II** – Requires firms and supervisors to take a view on whether a firm should hold additional capital against: risks considered under Pillar I that are not fully captured by the Pillar I process (e.g. credit concentration risk), risks not taken into account by the Pillar I process (e.g. interest rate risk in the banking book, business and strategic risk) and factors external to the firm (e.g. business cycle effects). Pillar II connects the regulatory capital requirements to the Company’s Internal Capital Adequacy Assessment Process (“ICAAP”) and to the reliability of its internal control structures. The function of Pillar II is to provide communication between supervisors and institutions on a continuous basis and to evaluate how well the institutions are assessing their capital needs relative to their risks. If a deficiency arises, prompt and decisive action is taken to restore the appropriate relationship of capital to risk.
- **Pillar III** - Market Discipline requires the disclosure of information regarding the risk management policies of the Company, as well as the results of the calculations of minimum capital requirements, together with concise information as to the composition of original own funds.

### 1.3.2. Disclosure Policy: Basis and Frequency of Disclosure / Location and verification

The Company has a formal policy, approved by the Board, which details its approach in complying fully with the Pillar 3 disclosure requirements as laid out in Part Eight of the CRR.

According to the Directive, the risk management disclosures should be included in either the financial statements of the CIFs if these are published, or on their websites. The Pillar III disclosure requirements are contained in Articles 431 to 455 of the Regulation. In addition, these disclosures must be verified by the external auditors of the CIF. The CIF will be responsible to submit its external auditors' verification report to CySEC. The Company has included its risk management disclosures as per the Directive on its website as it does not publish its financial statements. Verification of these disclosures has been made by the external auditors and sent to CySEC.

The Regulation provides that institutions may omit one or more disclosures, if such disclosures are not regarded as material, except for the following disclosures:

- Regarding the policy on diversity with regard to selection of members of the management body, its objectives and any relevant targets set out in that policy, and the extent to which these objectives and targets have been achieved (*Article 435 (2) (c)* of CRR).
- Own funds (*Article 437* of CRR).
- Remuneration policy (*Article 450* of CRR).

Materiality is based on the criterion that the omission or misstatement of information would be likely to change or influence the decision of a reader relying on that information for the purpose of making economic decisions. Where the Company has considered a disclosure to be immaterial, this was not included in the document.

#### Disclosures and Confidential Information

The Regulation also provides that institutions may omit one or more disclosures, if such disclosures are regarded as confidential or proprietary. The CRR defines proprietary as if sharing that information with the public would undermine its competitive position. It may include information on products or systems which, if shared with competitors, would render an institution's investments therein less valuable.

Information is regarded as confidential if there are obligations to customers or other counterparty relationships binding an institution to confidentiality. Under the light of the above, the Company avoided to disclose such confidential information in this report.

#### Frequency

The Company's policy is to publish the disclosures required on an annual basis. The frequency of disclosure will be reviewed should there be a material change in approach used for the calculation of capital, business structure or regulatory requirements.

#### Medium and location of publication

Institutions may determine the appropriate medium, location and means of verification to comply effectively with the disclosure requirements. In this respect, the Company's Pillar III disclosures are published on the Company's website which is <http://highcapital.trade/>.

#### Verification

The Company's Pillar III disclosures are subject to internal review and validation prior to being submitted to the Board for approval. The Company's Pillar III disclosures have been reviewed and approved by the Board. In addition, the Remuneration disclosures have been reviewed by the Risk Manager.

#### 1.4. Risk management objectives and policies

To ensure effective risk management, the Company has adopted the Three Lines of Defence model, with clearly defined roles and responsibilities.

First Line of Defence: Managers are responsible for establishing an effective control framework within their area of operation and identifying and controlling all risks so that they are operating within the organisational risk appetite and are fully compliant with Company's policies and where appropriate defined thresholds. First Line of Defence acts as an early warning mechanism for identifying (or remedying) risks or failures.

Second Line of Defence – The Risk Management Function is responsible for proposing to the Board appropriate objectives and measures to define the Company's risk appetite and for devising the suite of policies necessary to control the business including the overarching framework and for independently monitoring the risk profile, providing additional assurance where required. The Risk Management Function will leverage their expertise by providing frameworks, tools and techniques to assist management in meeting their responsibilities, as well as acting as a central coordinator to identify enterprise wide risks and make recommendations to address them. Integral to the mission of Second Line of Defence is identifying risk areas, detecting situations/activities, in need of monitoring and developing policies to formalise risk assessment, mitigation and monitoring.

Third Line of Defence - Comprises by the Internal Audit Function which is responsible for providing assurance to the Board on the adequacy of design and operational effectiveness of the systems of internal controls. Internal Audit undertakes on-site inspections/visits to ensure that the responsibilities of each Function are discharged properly (i.e. soundly, honestly and professionally) as well as reviews the Company's relevant policies and procedures. Internal Audit works closely with both the First and Second Lines of Defence to ensure that its findings and recommendations are taken into consideration and followed, as applicable.

##### 1.4.1. Risk Management Framework

Managing risk effectively in a Company operating in a continuously changing risk environment requires a strong risk management culture. As a result, the Company has established an effective risk oversight structure and the necessary internal organisational controls to ensure that the Company undertakes the following:

- The adequate risk identification and management
- The establishment of the necessary policies and procedures
- The setting and monitoring of the relevant limits and
- Compliance with the applicable legislation

The Board meets on a regular basis, and receives updates on risk and regulatory capital matters from management. The Board reviews regularly (at least annually) written reports concerning compliance, risk management and internal audit policies, procedures and work as well as the Company's risk management policies and procedures as implemented by Management.

As part of its business activities, the Company faces a variety of risks, the most significant of which are described further below. The Company holds regulatory capital against three all-encompassing main types of risk: credit risk, market risk and operational risk.

### **Risk Policy Statement (PS-01-2019)**

The Policy Statement (PS-01-2019), provides public guidance on CySEC's approach on the risk management arrangements of those Cypriot Investment Firms ("CIFs") providing investment services and/or performing investment activities in financial contract for differences ("CFDs").

The European Securities and Markets Authority (ESMA) has adopted new intervention measures on the provision of CFDs including the Negative Balance Protection (NBP) Requirement for protecting retail clients exposed to the consequences of trading in CFD. The purpose of this arrangement is to ensure that the maximum loss for the clients from trading CFDs never exceeds the client's available funds in the specific amount when the "margin close-out protection" cannot be effectively applied. Following the implementation of the ESMA decision and following a market-wide review of CFD CIFs, the Cyprus Securities and Exchange Commission (CySEC) has imposed Risk Management Transferring Arrangements in order to enhance the market structure for CFD CIFs and monitor the compliance with the new requirements.

Further to the above and according to the Policy Statement, all Limited Licence CIFs are required to maintain an additional of CET 1 Capital of either a) €2.000.000, or b) 2% of their total risk exposure, whichever is higher unless they collaborate and have in place Liquidity and Contractual Arrangements with entities (Credit Institutions or Investment Firms) domiciled in a third country listed in Annex I of the Commission Implementing Decisions (EU) 2016/230 and/or EEA regulated entities and/or entities domiciled in a member of G20.

Furthermore, according to the Policy Statement Limited Licence CFD CIFs which are engaging in Aggregation of Client Orders (irrespective of the client categorisation) were requested to either cease this trading model or extend their licence to also include the investment activity of Dealing on Own Account, within the meaning of the Law. Furthermore, Limited Licence CIFs were requested to restructure their contractual agreements with their LPs in order to ensure that they do not assume any responsibility to cover any negative balances that may appear in the trading accounts of their retail clients. Otherwise, these CIFs are required to apply for licence extension to include the Dealing on Own Account investment service.

The Company has amended the Contractual Agreements which are in place with its LPs in order to assume that any negative balances that may appear in the trading accounts if the retail clients will be covered by the LPs. Moreover and in light of the above, the Company maintains contractual agreements with solely EU entities and as such it is not required to hold additional capital as per the provisions of the Policy Statement.

### **1.4.2. Risk Appetite Statement**

Risk appetite is the level and type of risk a firm is able and willing to assume in its exposures and business activities, given its business objectives and obligations to stakeholders. Risk appetite is generally expressed through both quantitative and qualitative means and should consider extreme conditions, events and outcomes. In addition, risk appetite should reflect potential impact on earnings, capital and funding/liquidity.



The Company has a low risk appetite in respect to investing and to managing business and operational activities

According to Financial Stability Board (FSB) an appropriate risk appetite framework (RAF) should enable risk capacity, risk appetite, risk limits, and risk profile to be considered for business lines and legal entities as relevant, and within the group context. The Risk appetite framework is defined as the overall approach, including policies, processes, controls, and systems through which risk appetite is established, communicated, and monitored. It includes a risk appetite statement, risk limits, and an outline of the roles and responsibilities of those overseeing the implementation and monitoring of the RAF. The RAF should consider material risks to the financial institution, as well as to the institution's reputation vis-à-vis policyholders, depositors, investors and customers. The RAF aligns with the institution's strategy.

The company is assessing its risk appetite in respect to investing and to managing business and operational activities while the Company's Risk Appetite Statement is prepared by the Risk Manager and approved by the Board of Directors.

**Table 2: Risk Appetite areas**

Risk Area	Risk Types
Financial	Credit Risk Market Risk Liquidity Risk
Reputational	Conduct Risk Customer Risk Regulatory Risk External reputational Risk
Operational & People	The risk associated with the failure of key processes or systems and the risks of not having the right quality and quantity of people to operate those processes

The Risk Appetite framework has been designed to create links to the strategic long term plan, capital planning and the Company's risk management framework.

The Board approves the Company's corporate strategy, business plans, budget, long term plan and ICAAP. The Company employs mitigation techniques defined within the Company's policies, to ensure risks are managed within Risk Appetite.

#### 1.4.3. Risk Culture

Risk culture is a critical element in the Company's risk management framework and procedures. Management considers risk awareness and risk culture within the Company as an important part of the effective risk management process. Ethical behaviour is a key component of the strong risk culture and its importance is also continuously emphasised by the management.

The Company is committed to embedding a strong risk culture throughout the business where everyone understands the risks they personally manage and are empowered and qualified to take accountability for them. The Company embraces a culture where each of the business areas is encouraged to take risk-based decisions, while knowing when to escalate or seek advice.

**1.5. Declaration of the Management Body**

The Board is responsible for reviewing the effectiveness of the Company's risk management arrangements and systems of financial and internal control. These are designed to manage rather than eliminate the risks of not achieving business objectives, and – as such – offer reasonable but not absolute assurance against fraud, material misstatement and loss. The Board considers that it has in place adequate systems and controls with regard to the Company's profile and strategy and an appropriate array of assurance mechanisms, properly resourced and skilled, to avoid or minimise loss.



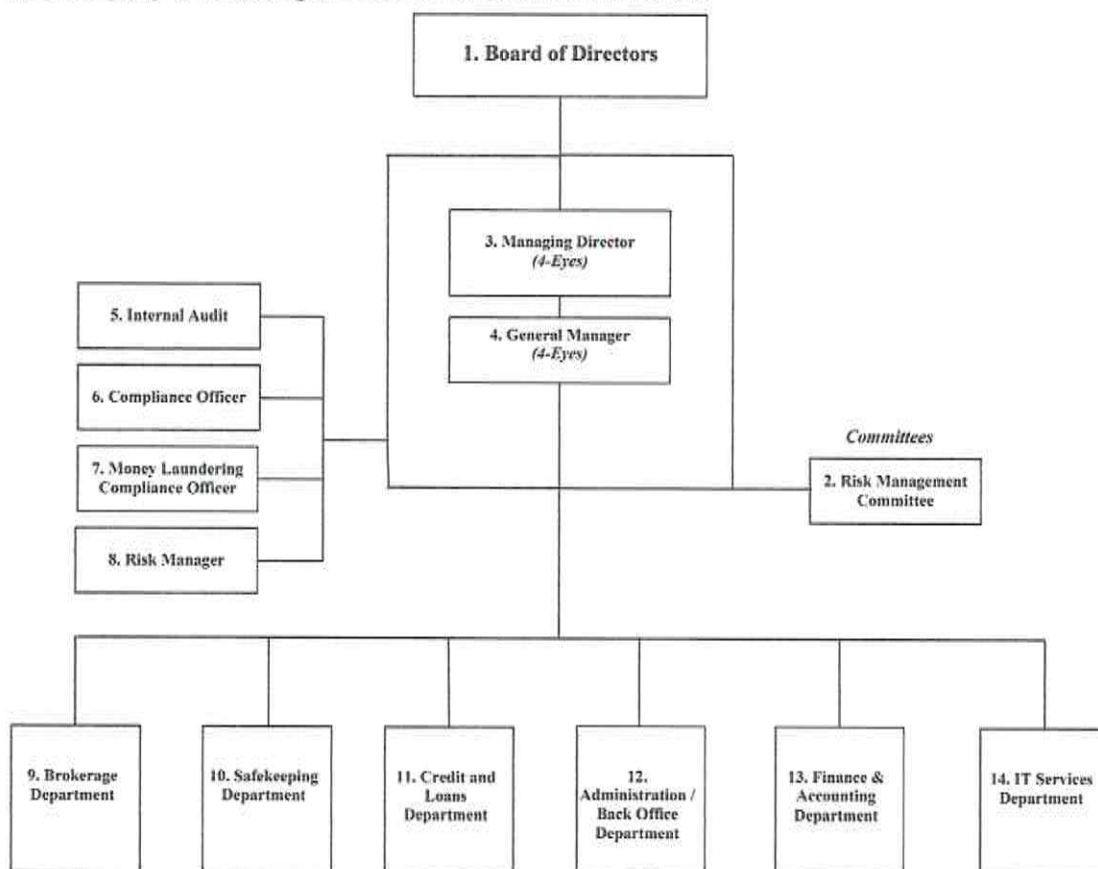
## 2. CORPORATE GOVERNANCE

The Company's systems of risk management and internal control include risk assessment, management or mitigation of risks, including the use of control processes, information and communication systems and processes for monitoring and reviewing their continuing effectiveness.

The risk management and internal control systems are embedded in the operations of the Company and are capable of responding quickly to evolving business risks, whether they arise from factors within the Company or from changes in the business environment.

### 2.1. Organisational Structure

The company's latest organizational structure is as follow:



### 2.2. The Board of Directors

The Board has the overall responsibility for the establishment and oversight of the Company's Risk Management Framework. The Board satisfies itself that financial controls and systems of risk management are robust. The Board comprises of two executive and two non-executive directors.

The Company has in place the Internal Operations Manual which lays down the activities, processes, duties and responsibilities of the Board, Committees, Senior Management and staff constituting the Company.



The Company implements and maintains adequate risk management policies and procedures which identify the risks relating to the Company's activities, processes and systems, and where appropriate, set the level of risk tolerated by the Company. The Company adopts effective arrangements, processes and systems, in light of that level of risk tolerance, where applicable.

### 2.3. Number of Directorships held by members of the Board

All members of the Board commit sufficient time to perform their functions in the Company. The number of directorships which may be held by a member of the Board at the same time shall take into account individual circumstances and the nature, scale and complexity of the Company's activities. Unless representing the Republic, members of the Board of a CIF that is significant in terms of its size, internal organisation and the nature, the scope and the complexity of its activities shall not hold more than one of the following combinations of directorships at the same time:

- One executive directorship with two non-executive directorships;
- Four non-executive directorships.

For the purposes of the above, Executive or non-executive directorships held within the same group shall count as a single directorship. Furthermore, directorships in organisations which do not pursue predominantly commercial objectives such as non-profit or charitable organisations shall not count for the purposes of the above guidelines.

During the year 2018, the four Directors of the Company held the following directorships:

- 2 directors held 1 executive directorship
- 1 director held 3 non-executive directorships
- 1 director held 5 non-executive directorships

### 2.4. Policy on Recruitment

The Company follows a predetermined procedure for the appointment of the members of the Senior Management and the Board of Directors. Recruitment into the Board combines an assessment of both technical capability and competency skills referenced against the Company's leadership framework.

Members of the Board shall possess sufficient knowledge, skills and experience to perform their duties. The overall composition of the Board shall reflect an adequately broad range of experiences to be able to understand the CIF's activities, including the principal risks faced by the Company as well as sufficient knowledge, of the legal framework governing the operations a CIF.

Specifically, when considering the appointment of the members of the Board and Senior Management, special attention shall be given to the following:

- Essential qualifications, business administration skills, education and experience so as to ensure the sound and prudent management of the Company, and diversity in order to conduct effectively and efficiently all their duties and responsibilities;
- Very strong interpersonal skills as well as managerial skills including time management and leadership skills;
- Profound and solid corporate governance;



- Financial markets and financial advisory sector market knowledge, experience and knowledge in the financial services industry, risk management knowledge and experience with local and international financial matters;
- Sufficient knowledge of the legal framework governing the operations of a Cyprus investment firm, including the investment services and activities which are regulated by the Cyprus Investment Firms Law;
- High sense of responsibility and work ethics portraying the professional traits of initiative;
- Criminal record certificate from the competent authorities of the country of residence of the person for the last five years, attesting that the person has no criminal records;
- Good knowledge of the Greek or/and English languages. Particularly, when considering the appointment of a member of the Board, special attention shall be given to the potential member's skills review which aims to assess the specific experience and skills needed to ensure the optimum blend of the potential individual and the aggregate capability having regard to the Company's long term strategic plan. Members of the Board and Senior Management appointment are subject to the approval of the Chief Executive Officer and the Board. Regulatory approval is co-ordinated through the Compliance Officer. The majority of the members of the Board shall be residents of Cyprus.

## 2.5. Policy on Diversity

The Company is committed to promoting a diverse and inclusive workplace at all levels, reflective of the communities in which it does business. It approaches diversity in the broadest sense, recognizing that successful businesses flourish through embracing diversity into their business strategy, and developing talent at every level in the organization.

The Company recognises and embraces the benefits of having a diverse Board, and sees increasing diversity at Board level as a necessary element in maintaining a competitive advantage.

The Company believes that the diversity of the board enhances decision-making capability and that a diverse board is more effective in dealing with organisational changes. A truly diverse Board will include and make good use of differences in the skills, regional and industry experience, background, gender, race and other distinctions between members of the Board. These differences will be considered in determining the optimum composition of the Board and when possible should be balanced appropriately. The Company believes that the Board should be characterized by a broad range of views arising from different experiences.

For the purpose of this policy, the Company considers that the concept of diversity incorporates a number of different aspects, therefore all Board appointments are made on merit, in the context of the skills, experience, knowledge, business perspectives, industry or related experience, independence, gender, age, cultural, educational background and more general experience which the Board as a whole requires in order to be effective.

### Skills and Experience

The Board should possess a balance of skills appropriate for the requirements of the business of the Company, in order for the Company to benefit from its directors' experience in a range of activities including varied industries, education, government, investment and the professions. Further reference is made to Company's Recruitment Policy, which aims to assess the specific experience and skills

needed to ensure the optimum blend of the potential individual and the aggregate capability having regard to the Company's long term strategic plan.

### Independence

The Board includes a composition of Executive and Non-executive Directors so that there is a strong element of independence in the Board. The Independent Non-executive Directors shall be of sufficient calibre and stature for their views to carry weight. Each member of the board must act with independence of mind to properly assess and challenge the decisions of the senior management where necessary and to effectively oversee and monitor management decision-making.

### Gender

The Company is committed to maintaining an environment of respect for people regardless of their gender in all business dealings and achieving a workplace environment free of harassment and discrimination on the basis of gender, physical or mental state, race, nationality, religion, age or family status. The same principle is applied to the selection of potential candidates for appointment to the Board.

## **2.6. Governance Committees**

### **Risk Management Committee**

In order to support effective governance and management of the wide range of responsibilities the Board has established the *Risk Management Committee*. The role of the Risk Management Committee is to provide oversight, review and challenge of the material risks both current and future affecting the business whilst ensuring that there is effective management and control of all key risks and issues facing the Company.

The Risk Management Committee, inter alia, scrutinizes, and decides on various risks inherent with the operation of the Company with the view to formulate internal policies and measure the performance of the said policies in dealing with the risks associated with the operation of the Company. Moreover, the Risk Management Committee reviews the risk management procedures in place (monitors and controls the Risk Manager in the performance of his duties and the effectiveness of the Risk Management Department).

The Risk Management function operates independently and monitors the adequacy and effectiveness of policies and procedures, the level of compliance to those policies and procedures, in order to identify deficiencies and rectify. The Investment Committee is responsible for monitoring and controlling the Risk Manager in the performance of his/her duties.

The Risk Management Committee meets at least annually, unless the circumstances require extraordinary meetings. Extraordinary meetings can be called by any member of the Risk Management Committee, as well as by the Risk Manager.

## **2.7. Other Governance Functions**

### **Internal Audit**

The Company, taking into account the nature, scale and complexity of its business activities, as well as the nature and the range of its investment services and activities, establishes and maintains an

internal audit function through the appointment of a qualified and experienced Internal Auditor. The Internal Auditor is appointed and reports to the Senior Management and the Board of the Company.

The Internal Auditor is separated and independent of the other functions and activities of the Company. The Internal Auditor bears the responsibility to:

- a) establish, implement and maintain an audit plan to examine and evaluate the adequacy and effectiveness of the Company's systems, internal control mechanisms and arrangements
- b) issue recommendations based on the result carried out in accordance with point (a)
- c) verify compliance with the recommendations of point (b)
- d) provides timely, accurate and relevant reporting in relation to internal audit matters to the Board of Directors and the Senior Management of the Company, at least annually.

The Internal Auditor is responsible for applying the Internal Control System (hereinafter, the "ICS"), which confirms the accuracy of the reported data and information. Furthermore, the role of the Internal Auditor is the programming, on an at least annual basis (as applicable), of checks on the degree of application of the required ICS.

The Internal Auditor has clear access to the Company's personnel and books. Likewise, the Company's employees have access to the Internal Auditor for the reporting of any significant deviations from the guidelines provided.

The Board ensures that internal audit issues are considered when presented to it by the Internal Auditor and appropriate actions shall be taken. The Board ensures all issues are dealt with and prioritized according to the Board's assessment.

### **Compliance Officer**

Pursuant to the regulatory obligations of the Company and with the view to complement the Internal Governance framework of the Company, the Board has appointed a Compliance Officer, to head the Compliance Function of the Company in order to establish, implement and maintain adequate policies and procedures designed to detect any risk of failure by the Company to comply with its obligations, to put in place adequate measures and procedures designed to minimize such risks and to enable the competent authorities to exercise their powers effectively. The Compliance Officer is independent and reports directly to the Senior Management of the Company, having at the same time the necessary authority, resources, expertise and access to all relevant information.

The Compliance Officer is responsible, *inter alia*, to:

- a) liaising with all relevant business and support areas within the Company
- b) to monitor on a permanent basis and to assess, on a regular basis, the adequacy and effectiveness of the measures, policies and procedures put in place, and the actions taken to address any deficiencies in the firm's compliance with its obligations;
- c) monitoring and assessing the level of compliance risk that the Company faces, taking into account the investment and ancillary services provided, as well as the scope of financial instruments traded and distributed
- d) monitoring the adequacy and effectiveness of the measures and procedures of the Company
- e) advising and assisting the relevant persons responsible for carrying out the investment services to be in compliance with the Law

### **Anti-Money Laundering Compliance Officer**

The Board retains a person to the position of the Company's Anti-Money Laundering Compliance Officer (hereinafter the "AMLCO") to whom the Company's employees report their knowledge or suspicion of transactions involving money laundering and terrorist financing. The AMLCO belongs to the higher hierarchical levels/layers of the Company so as to command the necessary authority. The AMLCO leads the Company's Anti-Money Laundering Compliance procedures and processes and report to the Senior Management and the Board of the Company.

Scope and objectives of the AMLCO:

- a) The improvement of mechanisms used by the Company for counteraction of legalization (laundering) of criminally earned income
- b) To decrease the probability of appearance among the Customers of the Company of any persons/organizations engaged in illegal activity and/or related with such persons/organizations
- c) To minimize the risk of involvement of the Company in any unintended holding and realization of operations with any funds received from any illegal activity or used for its financing
- d) To ensure compliance with anti-money laundering laws and directives issued by CySec as well as the identification and proper reporting of any money laundering activity to the relevant authorities

## 2.8. Information flow on risk to the management body

Risk information flows up to the Board directly from the business departments and control functions. The Board ensures that it receives on a frequent basis, at least annually written reports regarding Internal Audit, Compliance, Money Laundering and Terrorist Financing and Risk Management issues and approves the Company's ICAAP report as shown in the table below:

**Table 3: Information flow on risk to management body**

	Report Name	Owner of Report	Recipient	Frequency
1	Risk Management Report	Risk Manager	Senior Management, Board	Annually
2	Pillar I –CRDIV CoRep Forms	Risk Manager	Senior Management, Board	Quarterly
3	ICAAP (Pillar 2) Report	Risk Manager	Senior Management, Board	Annually
4	Pillar 3 Disclosures	Risk Manager	Senior Management, Board	Annually
5	Risk Register	Risk Manager	Senior Management, Board	Annually
6	Compliance Report	Compliance Officer	Senior Management, Board	Annually
7	Internal Audit Report	Internal Auditor	Senior Management, Board	Annually
8	Anti-money laundering (AMLCO) Report	Anti-money laundering Compliance Officer	Senior Management, Board	Annually

Furthermore, the Company believes that the risk governance processes and policies are of utmost importance for its effective and efficient operation. The processes are reviewed and updated on an annual basis or when deemed necessary.





### 3. OWN FUNDS

Own Funds (also referred to as capital resources) is the type and level of regulatory capital that must be held to enable the Company to absorb losses. The Company is required to hold own funds in sufficient quantity and quality in accordance with CRD IV which sets out the characteristics and conditions for own funds. The Company throughout the year under review managed its capital structure and made adjustments to it in light of the changes in the economic and business conditions and the risk characteristics of its activities. During the 12 month accounting period to 31 December 2018 the Company complied fully with all capital and liquidity requirements and operated well within the regulatory requirements. The Total Capital Ratio of the Company as at 31 December 2018 was 35.98% which is above the minimum regulatory limit of 8%.

#### 3.1. Tier 1 & Tier 2 Regulatory Capital

Institutions shall disclose information relating to their own funds. Furthermore, institutions shall disclose a description of the main features of the Common Equity Tier 1 and Additional Tier 1 instruments and Tier 2 instruments issued by the institution. In this respect, the Company's Tier 1 capital is wholly comprised of Common Equity Tier 1 Capital. Moreover, the composition of the capital base and capital ratios of the company are shown in the following table:

**Table 4: Composition of the capital base and capital ratios**

Capital Instruments	€000
<b>Common Equity Tier 1 (CET1) capital: instruments and reserves</b>	
Capital instruments and the related share premium accounts	213
Advances from Shareholders	121
Retained earnings	(69)
<b>Common Equity Tier 1 (CET1) capital: regulatory adjustments</b>	
Additional deductions of CET1 Capital due to Article 3 of the CRR (*)	(43)
<b>Common Equity Tier 1 (CET1) capital</b>	<b>223</b>
<b>Additional Tier 1 (AT1) capital</b>	<b>-</b>
<b>Tier 1 capital (T1 = CET1 + AT1)</b>	<b>223</b>
<b>Tier 2 (T2) capital</b>	<b>-</b>
<b>Total capital (TC = T1 + T2)</b>	<b>223</b>
<b>Risk weighted assets</b>	
Credit risk	55
Market risk	-
Additional Risk Exposure Amount due to Fixed Overheads	564
<b>Total risk weighted assets</b>	<b>619</b>
<b>Common Equity Tier 1</b>	<b>35.98%</b>
<b>Tier 1</b>	<b>35.98%</b>
<b>Total Capital</b>	<b>35.98%</b>

*\*Treatment pursuant to Circular C162 (Capital adequacy requirements - Change in the treatment of the Investors Compensation Fund ("ICF") Contribution) on 10 October 2016, according to which the contribution to ICF will no longer be risk weighted as an "exposure to public sector entities" pursuant to paragraph 13(3) of Directive DII44-2014-15. The said ICF exposure will be deducted from CET1 Capital pursuant to Article 3 (Application of stricter requirements by institutions) of the*

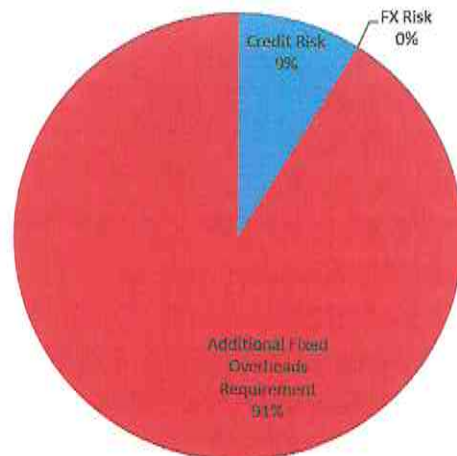
CRR. The aforementioned Article gives the member states the power to request from the institutions to hold own funds in excess of those required by the CRR.

The figures below illustrate the Capital Ratios and the breakdown of the exposures for the year ended 31 December 2018:

### Capital Ratios



### Overall Exposure Breakdown



### 3.2. Main features of Common Equity Tier 1, Additional Tier 1 and Tier 2 instruments

In order to meet the requirements for disclosure of the main features of these instruments, the company discloses the capital instruments' main features as outlined below:

**Table 5: Main features of capital instruments**

Capital Instruments Main Feature	CET1	
Issuer	H.FS High Capital Financial Services Ltd	
<b>Regulatory Treatment</b>		
Eligible at Solo/(sub-)consolidated/solo	Solo	
Instrument type	Common Equity	
Amount recognized in regulatory capital	€213k	
Nominal amount of instrument	€213k	
Issue Price	€1.00	
Accounting classification	Shareholders' Equity	
Original date of issuance	<i>Share Capital Increase</i>	<i>Effective Date</i>
	€1k	Incorporation Date
	€212k	17/07/2018
Perpetual or dated	Perpetual	
Original maturity date	No maturity	
Issuer call subject to prior supervisory approval	No	
<b>Coupons / Dividends</b>		
Fixed or floating dividend/coupon	Floating	
Coupon rate and any related index	N/A	

The Company's capital resources consist of CET1 Capital. No additional Tier 1 or Tier 2 capital available.

### 3.3. Balance Sheet Reconciliation

Institutions shall disclose a full reconciliation of Common Equity Tier 1 items, Additional Tier 1 items, Tier 2 items, filters, deductions and the balance sheet in the audited financial statements of the institution as follows:

**Table 6: Balance Sheet Reconciliation**

	<b>2018</b>
	<b>€000</b>
<b>Equity</b>	
Share capital	2
Share premium	211
Audited Reserves	(17)
Eligible Loss for the year	(52)
Other reserves	121
<b>Total Equity as per the Audited Financial Statements</b>	<b>266</b>
<b>Regulatory Deductions</b>	
Additional deductions of CET1 Capital due to Article 3 of the CRR	(43)
<b>Total Own funds as per the CoRep Forms</b>	<b>223</b>

## 4. COMPLIANCE WITH REGULATORY CAPITAL AND THE OVERALL PILLAR II RULE

### 4.1. Internal Capital

The purpose of capital is to provide sufficient resources to absorb unexpected losses over and above the ones that are expected in the normal course of business. The Company aims to maintain a minimum risk asset ratio which will ensure there is sufficient capital to support the Company during stressed conditions.

### 4.2. Approach to assessing adequacy of Internal Capital

The Company shall establish an ICAAP, document it in a Manual and produce in this regard the ICAAP Report, as per the Circular C026 and Circular C027. Upon CySEC's request the ICAAP Report shall be submitted to CySEC.

The Company has adopted the Pillar I plus approach whereby it determines the minimum capital required under Pillar I methodology and subsequently incorporates in that methodology the risks that are either not covered or are partially covered by Pillar I. Initially an assessment is made on the general financial position of the Company both from its financial statements and its Capital Adequacy Returns.

The Pillar I variable capital requirement is the sum of the credit risk and market risk requirements and the operational risk. In order to validate the adequacy of the above requirements under the Pillar I calculations, the ICAAP proceeds with the following individual tests:

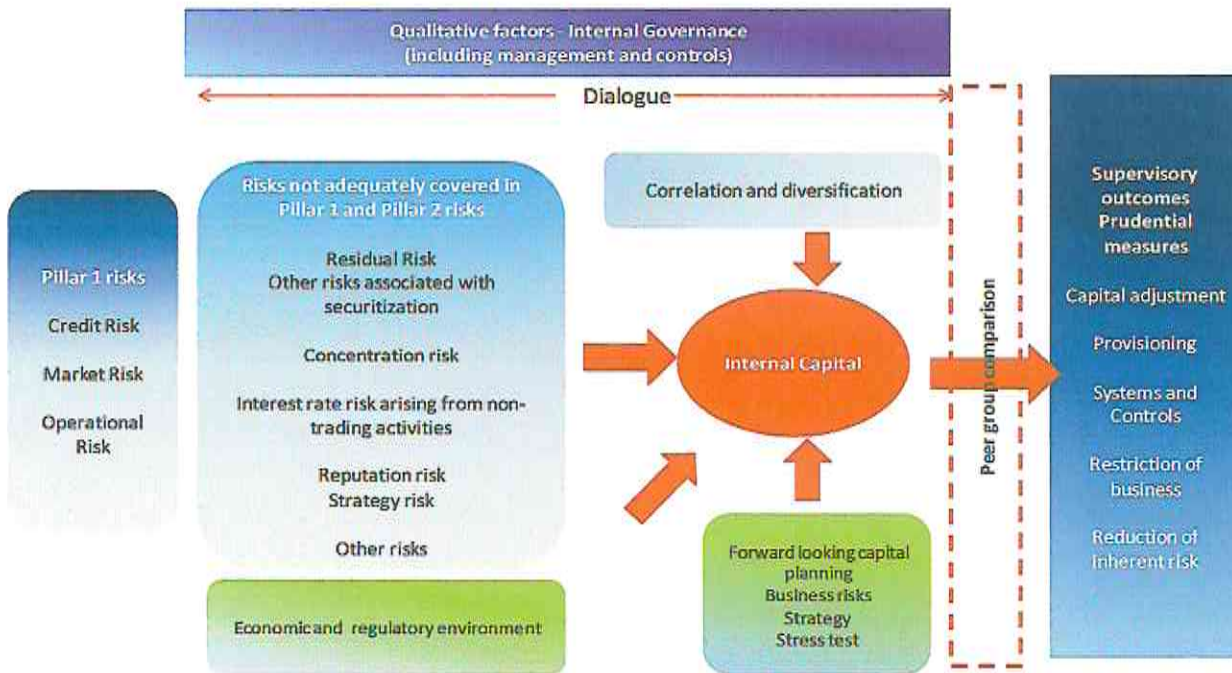
- The adequacy of the credit and market risk requirements is assessed with reference to all relevant balance sheet items in order to ascertain if there are additional risks that are not covered by Pillar I
- Other risks connected with the balance sheet, such as liquidity risk and concentration risk, are reviewed in order to establish whether there should be an additional requirement that might not be covered under Pillar I
- The overall capital adequacy is tested by adding together the resulting requirement of the identified risks.
- The absolute impact of combinations of scenarios, including a severe market downturn, is considered in relation to the financial forecasts of the business to assess the potential impact on the capital base over a three year period (forward-looking).
- A comprehensive risk assessment is carried out for all risks, categorizing them under a risk profile by attributing the anticipated impact and likelihood of occurrence.
- Finally, additional measures are set for the mitigation of the identified risks as well as capital allocation.

The Company operates a fully integrated ICAAP throughout the year that rolls into the final ICAAP assessment. The Company also performs monthly key risk assessments supported by periodic stress testing. The ICAAP considers all of the risks faced by the Company, the likely impact of them if they were to occur, how these risks can be mitigated and the amount of capital that it is prudent to hold against them both currently and in the future.

The ICAAP Report describes how the Company implemented and embedded its ICAAP within its business. The ICAAP also describes the Company's Risk Management framework e.g. the Company's risk profile and the extent of risk appetite, the risk management limits if any, as well as

the adequate capital to be held against all the risks (including risks other than the Pillar I risks) faced by the Company.

The graph below illustrates the process between ICAAP and SREP:



The Supervisory Review and Evaluation Process (SREP) is the supervisory tool for establishing the appropriate level of capital resources that a CIF should hold in order to meet its present and future capital requirements over a period of up to five years. Circular C027 outlines how CySEC applies the supervisory review and evaluation process (SREP) when reviewing the CIFs' internal capital adequacy assessment processes (ICAAP) under the framework of the paragraph 33 of the Directive DI144-2014-14.



## 5. PILLAR I CAPITAL REQUIREMENTS

The following tables show the overall Pillar I minimum capital requirement and risk weighted assets for the Company under the Standardised Approach to Credit Risk, Market Risk and the Basic Indicator Approach for the Operational Risk.

### 5.1. Credit Risk

In the ordinary course of business, the Company is exposed to credit risk, which is monitored through various control mechanisms. Credit risk arises when a failure by counterparties to discharge their obligations could reduce the amount of future cash inflows from financial assets on hand at the balance sheet date.

The Company has policies to diversify risks and to limit the amount of credit exposure to any particular counterparty in compliance with the requirements of the Directive. The Company continuously monitors the fair value calculations, forecast and actual cash flows, and cost budgets so that to ensure that the carrying level of Company's own funds and consequently the Capital Adequacy ratio meet the regulatory requirements at all times.

Trade receivables are shown net of any provision made for impairment. The management believes that no additional credit risk, beyond amounts provided for collection losses, is inherent in the trade receivables. Cash balances are held with high credit quality financial institutions and the Company has policies to limit the amount of credit exposure to any financial institution.

#### 5.1.1. Credit risk adjustments

The Company assesses at the balance sheet date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a "loss event") and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Trade receivables are recognized initially at fair value and are subsequently measured at amortized cost using the effective interest method, less provision for impairment. For those trading receivables that are 90 days or more past due, in non-accrual status, the Company classifies them as "in default", thus an impairment test will emerge. A financial asset is past due if a counterparty has failed to make a payment when contractually due.

Other receivables are recognized initially at fair value and subsequently measured at amortized cost, using the effective interest method, less provision for impairment. A provision for impairment of other receivables is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of receivables. Significant financial difficulties of the debtor, probability that the debtor will enter bankruptcy or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. When a receivable is uncollectible, it is written off against the allowance account for other receivables. Subsequent recoveries of amounts previously written off are credited in the statement of comprehensive income. None of the derivative financial instruments is either past due or impaired.

### 5.1.2. Credit Risk – Risk Weighted Assets

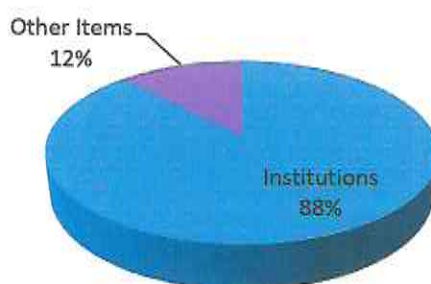
The Company’s Credit Risk Weighted Assets and Capital Requirements broken down by exposure class were as follows:

**Table 7: Exposure classes as at 31 December 2018**

Exposure class	Risk Weighted Assets	Capital Requirements
	€000	€000
Institutions	48	4
Other Items	7	1
<b>Total</b>	<b>55</b>	<b>4</b>

The Regulation requires disclosure for additional asset classes. These have not been shown in the table above as these are nil as at the reporting period.

#### Risk Weighted Assets



### 5.1.3. Credit Risk – Analysis of Average exposures and total amount of exposures

The Company shall disclose the total amount of exposures after accounting offsets and without taking into account the effects of credit risk mitigation and the average amount of the exposures over the period broken down by different types of exposures as follows:

**Table 8: Analysis of Average Exposures**

Exposure class	Original exposure amount, net of specific provisions	Average Exposure
	€000	€000
Institutions	242	216
Other Items	7	5
<b>Total</b>	<b>249</b>	<b>221</b>

### 5.1.4. Credit Risk – Risk Weighted Assets by Geographical distribution

The Company shall disclose the geographical distribution of the exposures, broken down in significant areas by material exposures classes. The geographical distribution of the Company’s exposures is mainly in Cyprus.

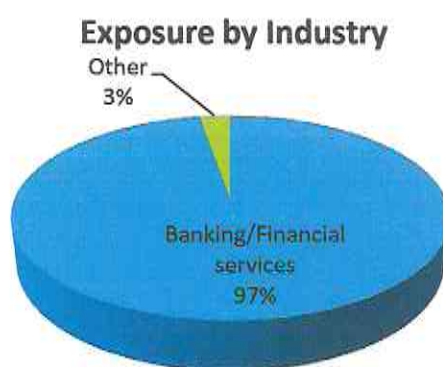
NA

### 5.1.5. Credit Risk – Distribution of exposures by industry

The Company shall disclose the distribution of the exposures by industry or counterparty type, broken down by exposure classes, including specifying exposure to SMEs, and further detailed if appropriate as follows:

**Table 9: Exposures by industry**

Exposure class	Banking/Financial services	Other	Total
	€000	€000	€000
Institutions	242	-	242
Other Items	-	7	7
<b>Total</b>	<b>242</b>	<b>7</b>	<b>249</b>



### 5.1.6 Residual maturity broken down by exposure classes

The Company shall disclose the residual maturity breakdown of all the exposures, broken down by exposure classes, as follows:

**Table 10: Residual maturity broken down by exposure class**

Exposure	Residual Maturity ≤ 3 months	Residual Maturity > 3 months	Total
	€000	€000	€000
Institutions	242	-	242
Other Items	-	7	7
<b>Total</b>	<b>242</b>	<b>7</b>	<b>249</b>

## 5.2. Use of ECAIs

The Company shall disclose the names of the nominated External Credit Assessment Institutions (“ECAIs”) and the exposure values along with the association of the external rating with the credit quality steps.

The Company uses external credit ratings from Moody’s. These ratings are used for all relevant exposure classes. The general ECAI association with each credit quality step is as follows:



**Table 11: ECAI Association with each credit quality step**

Credit Quality Step	Moody's Rating	Corporate	Institutions			Sovereign
			Sovereign method	Credit Assessment method		
				Maturity > 3 months	Maturity 3 months or less	
1	Aaa to Aa3	20%	20%	20%	20%	0%
2	A1 to A3	50%	50%	50%	20%	20%
3	Baa1 to Baa3	100%	100%	50%	20%	50%
4	Ba1 to Ba3	100%	100%	100%	50%	100%
5	B1 to B3	150%	100%	100%	50%	100%
6	Caa1 and below	150%	150%	150%	150%	150%

Exposures to unrated institutions are assigned a risk weight according to the credit quality step to which exposures to the central government of the jurisdiction in which the institution is incorporated, as specified in Article 121 of CRR. Notwithstanding the general treatment mentioned above, short term exposures to institutions could receive a favourable risk weight of 20% if specific conditions are met.

The Other Items category includes tangible assets, debtors and prepayments risk weighted at 100%, cash items in the process of collection risk weighted at 20% and cash in hand risk weighted at 0%.

Exposures to corporate clients were risk weighted by 100% risk factor since they were all unrated and were incorporated in countries with no credit rating or with credit assessment up to credit quality step 5.

**Table 12: Breakdown of exposures by asset class and risk weight under the Standardised approach**

Exposure Class	Risk Weight		Total	Of which unrated
	20%	100%		
	€000	€000	€000	€000
Institutions	242	-	242	-
Other Items	-	7	7	7
<b>Total</b>	<b>242</b>	<b>7</b>	<b>249</b>	<b>7</b>

### 5.2.1. Credit Risk Exposures by credit quality step pre and post credit risk mitigation

The table below indicates the exposure amounts before and after credit risk mitigation for each Credit Quality Step (CQS).

**Table 23: Exposures before and after credit risk mitigation as at 31 December 2018**

Credit Quality Step	Exposure values before credit risk mitigation €000	Exposure values after credit risk mitigation €000
CQS 5	242	242
Unrated	7	7
<b>Total</b>	<b>279</b>	<b>279</b>

### 5.3. Market Risk

Market risk can be defined as the risk of losses in on and off-balance sheet positions arising from adverse movements in market prices. From a regulatory perspective, market risk stems from all foreign exchange risk positions in the whole balance sheet.

As a “Limited Licence” CIF, the Company does not deal for its own account. Market risk is therefore limited to movements in foreign exchange rates.

The Company’s market risk as at 31 December 2018 was zero.

#### 5.3.1. Foreign Exchange Risk

The Company’s reporting currency is Euro. Foreign exchange risk is the risk that the value of financial instruments will fluctuate due to changes in foreign exchange rates.

If the sum of the Company’s overall net foreign-exchange position and its net gold position exceeds 2% of its total own funds, the Company calculates own funds requirements for foreign exchange risk. The own funds requirement for foreign exchange risk is the sum of its overall net foreign-exchange positions and its net gold position in the reporting currency, multiplied by 8%.

The foreign exchange risk in the Company is effectively managed by setting and controlling foreign exchange risk limits, such as through the establishment of maximum value of exposure to a particular currency pair.

#### Closely Correlated Currencies

Following the EBA’s Final draft Implementing Technical Standards on Closely Correlated Currencies under Article 354 (3) of CRR, the Company may apply lower own funds requirements against positions in relevant closely correlated currencies as those are disclosed by EBA. In this respect, for the calculation of the foreign exchange risk for matched positions on closely correlated currencies, a capital requirement of 4% instead of 8% is used.

As at 31 December 2018, the Company had no exposures emanating from foreign exchange risk.

### 5.4. Fixed Overheads Requirements

Following the CRDIV implementation, Operational Risk is replaced by Fixed Overheads requirements for “Limited Licence” CIFs pursuant to Article 97 of the CRR.

The purpose of this new requirement is to enable CIFs to protect their investors in case of winding down or restructuring their activities and to hold sufficient financial resources to withstand operational expenses over an appropriate period of time. In this respect, CIFs are required to hold eligible capital of at least one-quarter of the fixed overheads of the previous year based on the most recent audited annual financial statements, or projected fixed overheads in the case where a CIF has not completed business for one year.

In addition to holding eligible capital of at least one-quarter of the fixed overheads of the previous year, CIFs have to calculate their total risk exposure based on fixed overheads. In this respect, the total eligible capital is € 223k which is greater than € 50k, the fixed overheads requirement.

CIFs have to calculate their total risk exposure based on fixed overheads of the previous year’s audited expenditures. The Total Risk Exposure Amount for “Limited Licence” CIFs is the greater of the Total risk exposure amount (excluding Operational Risk) and the Fixed Overhead of the preceding year (x 12.5 x 25%).

The Company’s Fixed Overheads Risk Exposure amount is provided by the table below:

**Table 14: Fixed Overheads Risk Exposure amount analysis**

<b>Fixed Overheads</b>	<b>Fixed Overheads Requirements</b>	<b>Fixed Overheads Risk Exposure Amount</b>	<b>Additional Exposure Amount</b>	<b>Total Risk Exposure Amount</b>
<b>€000</b>	<b>€000</b>	<b>€000</b>	<b>€000</b>	<b>€000</b>
198	50	619	564	619

In this respect, the Fixed Overheads risk exposure amount is €619k which is more than the sum of the Credit Risk and Market Risk Exposure amount which is €55k.



## 6. OTHER RISKS

### 6.1. Concentration Risk

Concentration Risk includes large individual exposures and significant exposures to companies whose likelihood of default is driven by common underlying factors such as the economy, geographical location, instrument type etc.

Concentration risk was partly addressed through diversification of counterparties, namely banking institutions.

The Company's experience in the collection of trade receivables has never caused debts which are past due and have to be impaired. The company has a policy in place to monitor debts overdue by preparing debtors ageing reports

#### Large Exposures

Concentration Risk includes large individual exposures and significant exposures to companies whose likelihood of default is driven by common underlying factors such as the economy, geographical location, instrument type etc. Concentration risk was partly addressed through diversification of counterparties, namely banking institutions.

For the purposes of calculating large exposures, exposures means any asset or off-balance sheet item without application of the risk weights or degrees of risk there provided for. Exposures arising from derivative instruments are calculated in accordance with the treatment for Counterparty Credit Risk (CCR) applied by each Investment firm.

The Company is not subject to the Large Exposures regime, in accordance with Article 388 of the CRR due to the fact that it is a Limited Licence CIF (under Article 95(1) of the CRR). Nevertheless, according to Directive DI144-2014-14, Prudential Supervision of Investment Firms, Paragraph 61, Limitations on exposures to directors and shareholders, a CIF is not allowed to have exposures to all directors more than 1% and to all shareholders that are not an institution, more than 2% of its eligible capital. Exposures to shareholders and directors are monitored and kept within the limits.

Furthermore, the allowable limits to institutions (100% of the total eligible capital) and to non-institutions (25% of the total eligible capital) are closely monitored and controlled. As at 31 December 2018, the Company had no exposures over the allowable limit.

The Company maintains proper accounting controls in order to identify, monitor and control of all exposures including clients' balances and the value of the assets held as financial instruments under pledge.

### 6.2. Reputation Risk

Reputation risk is the current or prospective risk to earnings and capital arising from an adverse perception of the image of the Company on the part of customers, counterparties, shareholders, investors or regulators. Reputation risk could be triggered by poor performance, the loss of one or more of the Company's key directors, the loss of large customers, poor customer service, fraud or theft, customer claims, legal action and regulatory fines.

The Company has transparent policies and procedures in place when dealing with possible customer complaints in order to provide the best possible assistance and service under such circumstances. The

possibility of having to deal with customer claims is very low as the Company provides high quality services to customers.

### **6.3. Strategic Risk**

Strategic Risk could occur as a result of adverse business decisions, improper implementation of decisions or lack of responsiveness to changes in the business environment. The Company's exposure to strategic risk is moderate as policies and procedures to minimize this type of risk are implemented in the overall strategy of the Company.

### **6.4. Business Risk**

Business Risk includes the current or prospective risk to earnings and capital arising from changes in the business environment including the effects of deterioration in economic conditions. Research on economic and market forecasts are conducted with a view to minimize the Company's exposure to business risk. These are analyzed and taken into consideration when implementing the Company's strategy.

### **6.5. Capital Risk Management**

Capital Risk is the risk that the Company will not comply with capital adequacy requirements. The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders. The Company has a regulatory obligation to monitor and implement policies and procedures for capital risk management. Specifically, the Company is required to test its capital against regulatory requirements and has to maintain a minimum level of capital. This ultimately ensures the going concern of the Company. Such procedures are explained in the Procedures Manual of the Company.

The Company is further required to report on its capital adequacy quarterly and has to maintain at all times a minimum total capital adequacy ratio which is set at 8%. The capital adequacy ratio expresses the capital base of the Company as a proportion of the total risk weighted assets. Management monitors such reporting and has policies and procedures in place to help meet the specific regulatory requirements. This is achieved through the preparation on a monthly basis of management accounts to monitor the financial and capital position of the Company.

### **6.6. Regulatory Risk**

Regulatory risk is the risk the Company faces by not complying with relevant Laws and Directives issued by its supervisory body. If materialized, regulatory risk could trigger the effects of reputation and strategic risk. The Company has documented procedures and policies based on the requirements of relevant Laws and Directives issued by the Commission; these can be found in the Procedures Manual. Compliance with these procedures and policies are further assessed and reviewed by the Company's Internal Auditors and suggestions for improvement are implemented by management. The Internal Auditors evaluate and test the effectiveness of the Company's control framework at least annually. Therefore the risk of non-compliance is very low.

### **6.7. Legal and Compliance Risk**

Legal and Compliance Risk could arise as a result of breaches or non-compliance with legislation, regulations, agreements or ethical standards and have an effect on earnings and capital. Following the replacement of the Law 144(I)/2007 by Law 87(I)/2017 for the purpose of harmonization with MIFID II, several regulatory changes were applied that may cause the Company's exposure to compliance

risk. The Company among others, is also exposed to legal and compliance risk arising from inability or inadequate arrangements to comply with the requirements related to the:

- Product Governance (Circular C236, Directive DI87-01),
- New rules governing derivatives on virtual currencies (Circular C268),
- Commission Delegated Regulation of 8 June 2016 of the European Parliament and of the Council with regard to regulatory technical standards for the annual publication by investment firms of information on the identity of execution venues and on the quality of execution,
- Policy Statement on the Risk Management Arrangements of Cyprus Investment Firms Providing Investment Services in CFDs,
- European Securities and Markets Authority Decision (EU) 2019/155 of 23 January 2019 renewing the product intervention measures relating to the marketing, distribution or sale of contracts for differences to retail clients,
- Provisions of the General Data Protection Regulation (GDPR) 2016/679 and
- 4<sup>th</sup> AML Directive (Directive (EU) 2015/849)

The probability of such risks occurring is relatively low due to the detailed internal procedures and policies implemented by the Company and regular reviews by the Internal Auditors. The structure of the Company is such to promote clear coordination of duties and the management consists of individuals of suitable professional experience, ethos and integrity, who have accepted responsibility for setting and achieving the Company's strategic targets and goals. In addition, the Board meets at least annually to discuss such issues and any suggestions to enhance compliance are implemented by management. Finally and with respect the Implications of NBP, the Company has contractual agreements with solely with European Economic Area regulated entities and as such is not required to maintain a minimum additional capital buffer.

#### **6.8. IT Risk**

IT risk could occur as a result of inadequate information technology and processing, or arise from an inadequate IT strategy and policy or inadequate use of the Company's information technology. Specifically, policies have been implemented regarding back-up procedures, software maintenance, hardware maintenance, use of the internet and anti-virus procedures. Materialization of this risk has been minimized to the lowest possible level.

#### **6.9. Risk Reporting**

The Company maintains a system in place to record any risk event incurred on a special form duly completed by personnel of each department and is submitted to the Compliance officer and Risk manager when such event occur.

#### **6.10. Liquidity Risk**

Liquidity risk is defined as the risk when the maturity of assets and liabilities does not match. An unmatched position potentially enhances profitability, but can also increase the risk of losses. The Company has policies and procedures with the object of minimizing such losses.

#### **6.11. Conduct Risk**

Conduct risk is defined as the risk of an action, by an individual, financial institution or the industry as a whole, which leads to customer detriment or, undermines market integrity. This can bring sanctions and negative publicity. Moreover, EBA has defined conduct risk as the current or

prospective risk of losses to an institution arising from inappropriate supply of financial services including cases of wilful or negligent misconduct. Consequently, conduct risk arises from failures of designated liquidity providers located in third countries associated with the Company.

Additionally, the Company is exposed to negative balances with its Liquidity Providers, in case of fast-paced volatile market, where the LP cannot close a position at the Company's stop out limit. Therefore, the Company may be exposed to conduct risk arising from inadequate agreements with the Liquidity Providers and/or with the third parties that hold client's funds.

As part of risk management policy and tools, the Company has procedures in place to diversify its liquidity providers and monitor their financial position on an on-going basis. The financial soundness of the liquidity providers is closely monitored and the company is ready to switch to alternative LPs, if necessary. Furthermore, the receivable/payable amounts with the LPs are monitored on a daily basis. In particular, the Company examines its existing procedures and arrangements with respect to the products offered and services provided.

Further to the above, the agreement of MoUs between CySEC and FCA is expected to maintain investors' protection via the appropriate communications channels between the two competent authorities and as such may have negative impact on the Company's risk profile due to hard Brexit Scenario is mitigated.

#### **ESMA's Adopts Final Product Intervention Measures on CFDs and Binary Options**

The European Securities and Markets Authority (ESMA) on 23 January 2019 adopted Decision 2019/155, under Article 40 of Regulation (EU) No 600/2014 to restrict the marketing, distribution or sale of contracts for differences (CFDs) to retail clients. The Decision renews and amends ESMA Decision (EU) 2018/7962 on the same terms as the previous renewal decision, ESMA Decision (EU) 2018/16363.

Pursuant to article 40 of MiFIR for CFDs, product intervention measure include:

1. Leverage limits on the opening of a CFD by a retail client from 30:1 to 2:1, which vary according to the volatility of the underlying:
  - 30:1 for major currency pairs;
  - 20:1 for non-major currency pairs, gold and major indices;
  - 10:1 for commodities other than gold and non - major equity indices;
  - 5:1 for individual equities and other reference values;
  - 2:1 for cryptocurrencies;
2. Margin close out rule on a per account basis,
3. Negative balance protection on a per account basis,
4. A restriction on the incentives offered to trade CFDs,
5. A firm specific risk warning.

The Company has complied with all the above measures adopted by ESMA within the specified deadline.

## 6.12. Operational Risk

Operational risk is the risk of loss arising from fraud, unauthorized activities, error, omission, inefficiency, systems failure or external events. It is inherent in every business organization and covers a wide range of issues.

The Company manages operational risk through a control-based environment in which processes are documented and transactions are reconciled and monitored. This is supported by continuous monitoring of operational risk incidents to ensure that past failures are not repeated.

Furthermore, the Company has in place policies and processes whose implementation assists with the evaluation and management of any exposures to operational risk.

The Company has implemented an operational risk management framework designed to ensure that operational risks are assessed, mitigated and reported in a consistent manner consisting of, inter alia, the following components:

- Maintaining a four-eye structure and implementing board oversight over the strategic decisions made by the heads of departments;
  - A Disaster Recovery Plan has been designed in order to be used in the event of a force majeure affecting the Company's internal systems and databases; and
  - Maintenance of Risk Registers in the Context of the ICAAP;
  - A Business Continuity Plan has been implemented which helps protect all of the Company's information databases including data, records and facilities.
  - The majority of actions occurring in the Company's systems are automated and therefore it is less likely that a human error will occur;
  - Review of risks and controls as part of the Internal Audit function;
- Regular review and updating of the Company's policies;





## 7. REMUNERATION POLICY

The Company has established a remuneration policy, which its purpose is to set out the remuneration practices of the Company taking into consideration the salaries and benefits of the staff, in accordance with the provisions of Directive as well as the Circular 031 (Circular 031 has been issued in place of Guidelines GD-IF-07 for the correct filing purposes) on remuneration policies and practices, where these comply with specific principles in a way and to the extent that is appropriate to the Company's size, internal organization and the nature, scope and complexity of its activities. Furthermore, the Company's remuneration strategy is designed to reward and motivate the people who are committed to maintaining a long term career with the Company and performing their role in the interests of the Company.

The design of the Policy is approved by the people who effectively direct the business of the Company, after taking advice from the compliance function, and implemented by appropriate functions to promote effective corporate governance. The people who effectively direct the business are responsible for the implementation of remuneration policies and practices and for preventing and dealing with any relevant risks, that remuneration policies and practices can create. The Board discusses remuneration policy matters at least annually.

Furthermore, the Policy also benefits from the full support of senior management or, where appropriate, the supervisory function, so that necessary steps can be taken to ensure that relevant persons effectively comply with the conflicts of interest and conduct of business policies and procedures.

Finally, the Policy adopts and maintains measures enabling them to effectively identify where the relevant person fails to act in the best interest of the client and to take remedial action.

### 7.1. Remuneration System

The Company's remuneration system and policy is concerned with practices of the Company for those categories of staff whose professional activities have a material impact on its risk profile, i.e. the Senior Management and members of the Board; the said practices are established to ensure that the rewards for the "executive management" are linked to the Company's performance, to provide an incentive to achieve the key business aims and deliver an appropriate link between reward and performance whilst ensuring base salary levels are not set at artificially low levels. The Company uses remuneration as a significant method of attracting and retaining key employees whose talent can contribute to the Company's short and long term success.

The remuneration mechanisms employed are well known management and human resources tools that take into account the following factors in order to determine the remuneration of each staff member:

- a) knowledge and skills,
- b) the adding value to the business,
- c) the demands (physical and mental) of the job,
- d) amount of training and/or experience needed,
- e) working conditions,
- f) the importance and the amount of responsibility,
- g) market dynamics such as the supply and demand for labour,
- h) financial viability of the Company,



- i) economic performance of the country in which the Company operates,
- j) employee's personal goals and performance evaluation in relation to the objectives set up at the beginning of the period,
- k) employee's professional conduct with clients.
- l) Staff's skills, experience and performance, whilst supporting at the same time the long-term business objectives.

The Company's remuneration system takes into account the highly competitive sector in which the Company operates, and the considerable amount of resources the Company invests in each member of the staff. The remuneration includes all forms of benefits provided by the Company to its staff and can be Financial or non-Financial remuneration.

It is noted that the Company has taken into account its size, internal organisation and the nature, the scope and the complexity of its activities and it does not deem necessary the establishment of a specific remuneration committee. Decisions on these matters are taken on a Board level while the remuneration policy is periodically reviewed.

The remuneration varies for different positions/roles depending on each position's actual functional requirements, and it is set at levels which reflect the educational level, experience, accountability, and responsibility needed for a staff member to perform each position/role. The remuneration is also set in comparison with standard market practices employed by the other market participants/competitors. Furthermore, the employee's personal goals and performance evaluation in relation to the objectives set up at the beginning of the period and the employee's professional conduct with clients are taken into account in order to determine the remuneration.

The total remuneration of staff currently consists of a fixed and a variable component. On the one hand, the Fixed Remuneration (FR) has purpose to attract and retain Company's employees. This fixed amount of remuneration includes salary, fixed pay allowance and other cash allowances and all are determined based on the role and position of each employee, taking into account the experience, seniority, education, responsibility, and market conditions. On the other hand, the variable remuneration is a performance-based remuneration which motivated and rewards staff members based on their results in relation with the targets set in the beginning of the year. This kind of remuneration is not guaranteed and the BoD has determined a maximum percentage of variable remuneration relative to the fixed remuneration in order to ensure a compliant ratio between these two kinds of remuneration. Although, the maximum limit on variable remuneration set at 100% of fixed salary, the limit could be set at 200% upon shareholders' approval according to the Article 94 of Directive 2013/36/EU.

Furthermore there no remuneration is payable under deferral arrangements (with vested or unvested portions). Finally the Company did not pay any non-cash remuneration for the year under review, since the Company does not have non-cash instrument, such as shares or other equivalent non-cash instrument, in place.

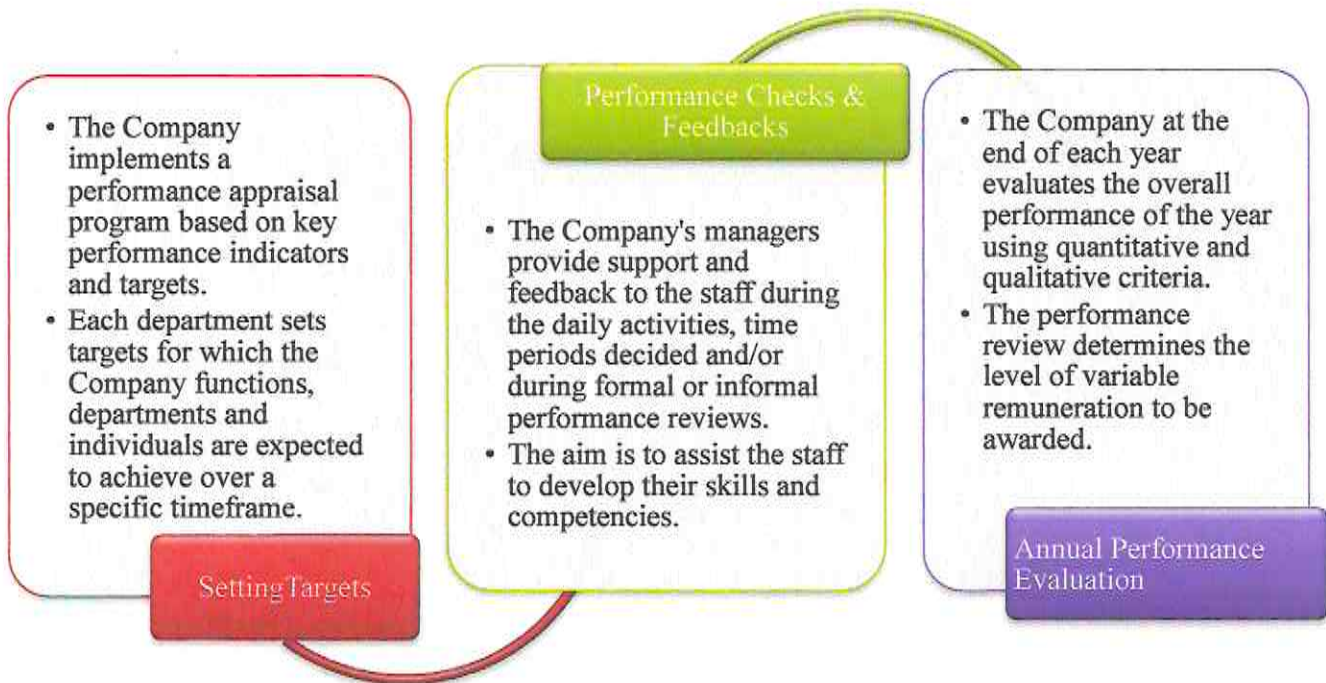
The Company recognizes that its remuneration system have some features that increases the mis-selling risk. Therefore, the Company applies effective mitigation controls for each part of the remuneration system.

### 7.2. Link between the pay and performance

The Company recognises the responsibility that the Staff has in driving its future success and delivering value for the Company and that remuneration is a key component in motivating and compensating its employees. Furthermore, the overall remuneration policy incorporates an annual variable incentive compensation reflecting individual performance and overall performance.

The individual performance is assessed during the annual appraisal process, which establishes objectives for all staff covering both financial and non-financial factors, specific behavioral competencies including compliance and risk management behaviors with regards to the Company’s procedures.

Further to the above, the Company implements a performance appraisal method, which is based on a set of Key Performance Indicators, developed for each business unit and its target is to promote the healthy competition amongst personnel, analysis of weak and strong sides of each employee performance-based and give feedback to the staff member in order to motivate them to be improved. At the most of the times, the performance appraisal takes place in a multiyear framework in order to ensure that the appraisal process assess employee’s long-term performance. However, sometimes the performance appraisal is performed on medium and short-term basis, and the performance indicators of this type of performance appraisal include quantitative as well as qualitative criteria. The appraisal is being performed as follows:



### 7.3. Remuneration of Senior Management Personnel and Directors

The remuneration policy of the Company is intended to ensure that the Company will attract and retain the most qualified Senior Management Personnel and Directors. As stated in Section 8.2 the criteria used for determining the remuneration of the Company’s directors are segregated into quantitative and the qualitative criteria.



The quantitative remuneration criteria mostly rely on numeric and financial data such as the Company's performance and the individual performance evaluation and ratings of each member of the staff whose professional activities affect the risk profile of the firm. In addition to the quantitative criteria, the Company has put in place qualitative criteria which include compliance with regulatory requirements and internal procedures, fair treatment of clients and client satisfaction.

Moreover, the remuneration of the Company's non-executive directors is fixed and it is set at a level that is market aligned and reflects the qualification and competencies required based on the Company's size and complexity, the responsibilities and the time that the non-executive directors are expected to consume in order to serve the Company.

As at 31 December 2018, the aggregate remuneration of the Company was EUR 27,500 (4 beneficiaries), whilst no variable remuneration was paid.

Furthermore, companies are required to disclose the number of natural persons that are remunerated €1mln or more per financial year, in pay brackets of €1mln, including their job responsibilities, the business area involved and the main elements of salary, bonus, long-term award and pension contribution. Nevertheless, currently there are no natural persons at the Company that are remunerated €1mln or more per financial year and as such the above disclosure is not applicable to the Company. No sign-on payments have been awarded during 2018, while no severance payments were paid during the year.

NA