

# OCH-ZIFF EUROPE LOAN MANAGEMENT LIMITED

## APPENDIX I PILLAR 3 DISCLOSURES – UNAUDITED

### **Regulatory Context**

The Pillar 3 disclosures of the company are set out below as required by the FCA's the Prudential sourcebook for Investment Firms ("IFPRU"), specifically IFPRU 2.2 and has been prepared in accordance with the relevant articles of the Capital Requirements Regulation which came into force on 01 January 2014. The regulatory aim of the disclosures is to improve market discipline.

### **Frequency**

Och-Ziff Europe Loan Management Limited (the "Company") will be making Pillar 3 disclosures annually. The disclosures will be prepared based on the position of the Company as at the accounting reference date.

The Pillar 3 disclosures that appear below are based on the position of the Company as of 31 December 2017.

### **Media and Location**

The disclosure will be published as an appendix to the Company's audited annual accounts.

### **Materiality**

The Company regards information as material in disclosures if its omission or misstatement could change or influence the assessment or decision of a user relying on that information for the purpose of making economic decisions. If the Company deems a certain disclosure to be immaterial, it may be omitted from these disclosures.

### **Confidentiality**

The Company regards information as proprietary if sharing that information with the public would undermine its competitive position. Proprietary information may include information on products or systems which, if shared with competitors, would render the Company's investments therein less valuable. Further, the Company must regard information as confidential if there are obligations to customers or other counterparty relationships binding the Company to confidentiality. In the event that any such information is omitted, the Company shall disclose such and explain the grounds why it has not been disclosed.

### **Risk Management Objective**

The Company's general risk management objective is to ensure that governance arrangements and systems and controls are in place to mitigate risk to a level that only requires the allocation of Pillar 2 capital in very limited circumstances. The senior management of the Company considers it to be of the utmost importance in instilling good corporate governance that risk management is embedded throughout the Company and, consequently, see risk management as a key component of business strategy.

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### **Governance Framework**

The Board of Directors is the governing body of the Company and has the ultimate management and oversight responsibility. As of 31 December 2017, it was composed of:

- Adrian Croxson, Head of European Equities and Group Executive Managing Director

The Company's Board has delegated the day-to-day management of the Company to the Company Chief Executive Officer and the Company's UK Executive Committee.

The Board of Directors is responsible for the entire process of risk management, as well as forming its own opinion on the effectiveness of the process. In addition, the Board, in conjunction with the view of the Company's ultimate parent, Och-Ziff Capital Management Group LLC, and its subsidiaries (collectively, the "Group"), decides the Company's risk appetite or tolerance for risk and ensures that the Company has implemented an effective, on-going process to identify risks, to measure their potential impact and then to ensure that such risks are actively managed.

### **Risk Framework**

Risk within the Company is managed by use of the following:

- The Group Risk Committee
- Daily meetings between portfolio managers and analysts to review risks related to positions
- The Group financial controls group
- The Group internal audit function
- The Group legal and compliance team
- Senior management of the Group, including the OZELM Board

### **Statement of Risk Appetite**

The Company has maintained financial resources since inception in excess of the minimum capital resources requirements. A detailed Risk Appetite statement has been developed for each risk group below rather than an overall top down statement. The "bottom up" approach allows the Company to monitor each risk against risk appetite. Liquidity risk appetite is dealt with in a separate document, namely the Company's "Liquidity Policy."

The Company has developed four (4) statements which collectively make up its Risk Appetite Statement as presented below.

### ***Operational Risk***

As the Company has undertaken a robust risk identification and scoring exercise rating all risks on a scale from A to D, with risks that could potentially cause a significant impact on the Company's business on a quarterly to annual basis being assigned an A, to risks that could potentially cause minor to moderate impacts infrequently on the Company's business rated a D. This Risk Appetite statement translates into the acceptance of risks rated C or below. Any risk rated A is deemed to be unacceptable to the Company and must be addressed as a priority to ensure that it is able to receive a B or C rating.

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This position has been communicated to all senior members of the staff and is reinforced on an annual basis.

Senior Management has determined that any risk rated as an A must have a plan to mitigate the risk within 10 working days of identification and implemented within 30 days or have Pillar 2 capital allocated. Any Risk rated as a B must have a plan for treatment developed within 30 days of identification and implemented within 90 days or have Pillar 2 capital allocated.

### ***Business Risk***

As an investment management firm, the Company has assessed business risks and set out appropriate actions to manage them. The Company is generating revenue primarily via management fees and interest yields. As a result, the Company is exposed to fluctuations in assets under management and credit quality of the underlying securitised CLO assets. The Company set out a process to constantly monitor these movements to ensure appropriate and timely risk identification and mitigation.

### ***Credit Risk***

Credit risk is the risk that one party to a financial instrument will cause a financial loss for that other party by failing to discharge an obligation.

The Company is exposed to credit risk as it is required to make investments in CLOs it manages for risk retention purposes. The investments in CLOs may not be sold and are held in non-trading book. The risk associated with the investments is assessed using the standardised approach. The Company will be taking a vertical slice approach to its risk retention requirements.

The Company is also exposed to credit risk to the extent that investment management fees cannot be collected. Additionally, the Company has exposure to the bank where collected revenues are deposited. As the Company's credit risk appetite is low, the Company holds all cash balances with banks with assigned credit ratings of A or higher. The Group's treasury department monitors the credit ratings and other events affecting creditworthiness and financial health of the bank.

### ***Market Risk***

As an investment management firm, the Company does not have a trading book. The Company's only potential exposures are non-trading book exposures to foreign currency assets or liabilities held on its balance sheet. The Company's foreign currency risk appetite is generally limited to major currencies such as the Euro and U.S. Dollar. The largest foreign currency exposure on the Company's balance sheet is denominated in Euro, which the Company believes is a stable currency and exposes the Company to little risk. The Company's limit on Euro exposure is generally equal to the amount of CLO Investments, CLO Investments Debt and liquid assets needed to support its maximum three-month outflow projected over the coming year under its Liquidity Policy, with a prudent buffer as needed. Other exposures in Euro and from time-to-time other major currencies arise in the ordinary course of business (e.g., trade payables, intercompany items related to secondment agreements, etc.). These exposures are generally immaterial and/or short-term in nature. The Company's market risk appetite is low and the Company monitors its exposure on a regular basis. Any material exposures other than those discussed above would be communicated to the board on a timely basis.

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All investment decisions are based on thorough research involving extensive due diligence as well as qualitative and quantitative analysis. Risk management has been a core foundation of the the Company's investment management business since inception.

### *Risk Appetite Enforcement*

The risk appetite is reviewed by the Company's Compliance Officer before it is reviewed and signed off by the Board in the first four months of each year, at the same time as it reviews and signs off the Internal Capital Adequacy Assessment Process ("ICAAP").

### IFPRU 4 - Standardised Credit Risk

For its Pillar 1 regulatory capital calculation of Credit Risk, under the credit risk capital component the Company has adopted the standardised approach (IFPRU 4.2) and the simplified method of calculating risk weights.

The following table sets forth the Company's credit risk capital requirement calculation as of 31 December 2017:

Credit Risk Capital Requirement	Rule	Pillar I Requirement £
Credit risk capital component	CRR Article 119/120	5,776,517
Counterparty risk capital component	CRR Article 271/274	1,895,113
<b>Total</b>		<b>7,671,630</b>

The following table sets forth the Company's credit risk capital component calculation, inclusive of risk weighting assigned to different tranches of the Company's CLO Investments, as of 31 December 2017:

Exposure Type	Rule	Exposure £	Weight	Risk-Weighted Exposure Amount £
Institutions	Article 119 - 121 CRR	4,445,940	20%	889,188
Notes with credit quality 1	Article 251 CRR	26,168,488	20%	5,233,698
Notes with credit quality 2	Article 251 CRR	2,178,082	50%	1,089,041
Notes with credit quality 3	Article 251 CRR	1,687,778	100%	1,687,778
Notes with credit quality 4	Article 251 CRR	2,146,227	350%	7,511,795
Notes with credit quality 5	Article 251 CRR	4,373,428	1,250%	54,667,850
Prepayments and accrued income	Article 134 CRR	1,127,108	100%	1,127,108
<b>Total</b>		<b>42,127,051</b>		<b>72,206,458</b>
<b>Credit Risk Capital Component</b>	8% of risk-weighted exposure			<b>5,776,517</b>

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### Overall Pillar 2 Rule

The Company has adopted the “structured” approach to the calculation of its ICAAP capital resources requirement as outlined in the Committee of European Banking Supervisors Paper, 27th March 2006.

The ICAAP assessment is reviewed by the Company’s UK Executive Committee and amended where necessary, on a quarterly basis or when a material change to the business occurs. The Company’s compliance officer presents the ICAAP document to the Board of Directors of the Company which reviews and endorses the risk management objective each year or when a material change to the business occurs at the same time as reviewing and approving the ICAAP document.

### Credit Risk and Dilution Risk

The Company is exposed to credit risk as it is required to make investments in CLOs it manages for risk retention purposes. The investments in CLOs may not be sold and are held in non-trading book. The risk associated with the investments is assessed using the standardised approach.

The Company is also exposed to credit risk to the extent that investment management fees cannot be collected. Additionally, the Company has exposure to banks where collected revenues are deposited. As the Company’s credit risk appetite is low, the Company holds all cash balances with banks with assigned credit ratings of A or higher. The Group’s treasury department monitors the credit ratings and other events affecting these creditworthiness and financial health of the banks.

The Company does not, as at the accounting reference date, have any past due or impaired assets. A financial asset is past due when a counterparty has failed to make a payment when contractually due. Impairment is defined as a reduction in the carrying amount of an asset.

### Market Risk

The Company only has non-trading book potential exposure (CRR Article 352). The following table sets forth the Company’s market risk capital requirement calculation as of 31 December 2017:

Exposure Type	Rule	Exposure £	Weight	Risk-Weighted Exposure Amount £
Foreign currency positional risk requirement	Article 352 of CRR	7,684,098	8%	614,728
		<b>7,684,098</b>		<b>614,728</b>

### Operational Risk

As an IFPRU firm, the Company is not subject to an operational risk requirement. However, the Company is required to maintain capital resources equal to at least its Fixed Overhead Requirement (“FOR”). The Company’s 2017 FOR was £357,363.

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### Consolidation

The Company is not a member of a U.K. or non-EEA consolidation group and consequently, does not report on a consolidated basis for accounting or prudential purposes.

### Capital Resources

The Company is an IFPRU firm without an Investment Firm Consolidation Waiver deducting Material Holdings (GENPRU 2 Annex 4). The Company's Tier 1 Capital is comprised of its parent's investment in the form of shares and share premium accounts and audited reserves and reflects an adjustment due to prudential filers. The Company has no Tier 2 or 3 capital nor any deductions from its capital. The Company's Tier 1 capital resources as of the accounting reference date were £10,773,155.

### Encumbered Assets

The Company's CLO Investments Loan (see Note 9) is collateralized with the Company's Investment in CLO (see Note 6). Beyond that, none of the Company's assets are encumbered from any activity related to derivatives, securities lending, rehypothecation, covered bond issuances, or securitisations.

### Remuneration

The Company is required to comply with the remuneration rules for IFPRU firms which are set out in SYSC 19A. As a firm subject to the IFPRU remuneration rules, the Company has, in accordance with the FCA's guidance publication entitled "General Guidance on Proportionality: The Remuneration Code (SYSC 19A)" (the "SYSC19A Proportionality Guidance"), concluded, in light of its structure and the nature of its activities, that it does not need to appoint a remuneration committee. Instead, the Company's Board of Directors sets, and oversees compliance with, the Company's remuneration policy including reviewing the terms of the policy at least annually. As of the accounting reference date, the Company currently sets the variable remuneration of its staff in a manner which takes into account staff and firm performance, by reference to individual employee performance; performance of the individual's business unit or department and the overall results of the Company. As permitted for IFPRU firms, in accordance with the SYSC19A Firm Proportionality Guidance, the Company takes into account the specific nature of its own activities in conducting any *ex-ante* risk adjustments to awards of variable remuneration and, given the nature of its business, has disapplied the requirement under the Code to make *ex-post* risk adjustments.

The Company only has one "business area," namely its collateralised loan obligation management business. The Company is required to identify those staff whose professional activities have a material impact on the Company's risk profile in accordance with Regulation (EU) 604/2014 (Regulatory technical standards to identify staff who are material risk takers) (the "MRT Regulations") ("Code Staff"). The MRT Regulations permit firms to exclude from the list of Code Staff, staff who would otherwise fall within the definition where the institution determines that the professional activities of the staff member do not have a material impact on the institution's risk profile because the staff member either: (a) only carries out professional activities and has authorities in a business unit which is not a material business unit; or (b) has no material impact on the risk profile of a material business unit through professional activities carried out (the "MRT exclusion"). Where a firm wishes to exclude an individual on the basis of the MRT exclusion, for individuals that earn over EUR 500,000 but less than

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EUR 750,000, the firm must make a notification to the FCA. For individuals that earn over EUR 750,000, the firm must seek prior approval from the FCA to exclude such individuals from its Code Staff.

The Company has identified eight individuals to be excluded from its Code Staff on the basis of the MRT exclusion and has made relevant notifications and applications for approval from the FCA, as applicable. The total “remuneration” (as defined in the FCA Rules) awarded to the Code Staff in 2017 was £731,541.