

IFPR: MIFIDPRU disclosures

Pepperstone Limited

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IFPR: MIFIDPRU disclosures

1. Introduction

The UK Investment Firm Prudential Regime (“IFPR”) is the new streamlined and simplified regime for the prudential regulation of investment firms in the UK. The IFPR was introduced by the Financial Conduct Authority (FCA) on the 1st of January 2022 in accordance with the new Financial Services Bill and new Part 9C of the Financial Services and Markets Act 2000.

IFPR represents a significant change to how UK investment firms are prudentially regulated. The new requirements seek to capture the potential harm posed by these firms to their clients and the markets in which they operate. It also considers the amount of capital and liquid assets the FCA solo regulated investment firm should hold so that if it does have to wind-down or exit the market, it can do so in an orderly way.

The impact areas of the IFPR can be put into the following categories:

- Firm Categorisation
- Capital Requirements
- Liquidity Requirements
- Financial Threshold Conditions
- Risk Management
- Governance
- FCA Supervisory Intervention Points
- Remuneration Code
- Regulatory Reporting
- Public Disclosures
- Rulebook

The new prudential sourcebook, MIFIDPRU, replaces BIPRU and IFPRU prudential sourcebooks.

Background

Pepperstone Limited ('the Firm' or 'the Company') is a limited liability company incorporated in the United Kingdom on 28 March 2014. The Company is part of the Pepperstone Group of companies, headquartered in Australia ('Pepperstone Group' or 'the Group'). The Company's principal activity is to onboard retail and professional clients for the purpose of providing a platform for clients to buy and sell leveraged spot Foreign Exchange ("FX") and Contract-For-Difference ("CFD") products.

Frequency of Publication

The disclosures are reviewed on an annual basis at a minimum and, where deemed necessary, more frequently. It is published in conjunction with the date of publication of the financial statements.

Scope of Disclosure

The Firm prepares its disclosures on a solo basis.

Regulatory Environment

The Company adheres to the capital adequacy and overall risk management requirements that apply under the prudential rules established in the FCA's IFPR. This document is prepared on the basis of MIFIDPRU8.1 which sets out the new requirements for disclosures by investment firms. It replaces 'Pillar III' requirements although the objectives are broadly similar.

Given that the Company's total on and off-balance sheet assets are on average less than £100 million over the four-year period immediately preceding the given financial year, the Company has no obligation to disclose any information relating to MIFIDPRU 8.7 (Investment Policy).

2. Risk Management Objectives and Policies

Risk Management Framework and Structure

The Company considers risk management as a core component of proper business management and sound corporate governance. The Company's ability to identify and address risk is central to achieving its corporate objectives and the process of risk management shall be ongoing.

The Company's Risk Management Policy sets out the high-level principles that the Company applies in order to manage its key risks. This policy describes the Company's risk management system relating to its operations, defined as the systematic method of establishing the context, identifying, analysing, evaluating, treating, monitoring and communicating risks to minimise losses and maximise opportunities. The main risks covered are Credit risk, Market risk, Liquidity risk, Operational risk and Compliance risk.

The overall risk management framework of the Company aims to embed risk management in a practical way into business processes and it is implemented through policies, limits, operational guidelines, as well as defined procedures and controls for risk monitoring, measuring and reporting. Risk is a continuous and developing process which runs throughout the Company's strategy and the implementation of that strategy. It addresses methodically all the risks surrounding the Company's activities past, present and especially future.

Risk management refers to a coordinated set of activities and methods that is used to direct the Company and to control the many risks that can affect its ability to achieve objectives. The term "risk management" also refers to the programme that is used to manage risk. This programme includes risk management principles, a risk management framework and a risk management process of identifying, monitoring, assessing and controlling threats to the Company's capital and earnings.

The Firm is a matched principal brokerage for CFDs and Spreadbet products with a straightforward business model and considers that its financial and operational control continue to be adequate and effective for a business of its size and complexity. The Firm does not have regulatory permission to take proprietary trading risk and has an established risk management framework that gives accountability and clarity of the risks that are consistent with the pursuit of the Firm's profitability and other strategic objectives. The Firm hires highly talented and experienced professionals who have a good understanding

of markets as well as operational and regulatory obligations. The Firm's financial management is conducted by the Head of Finance in the UK. The Firm has implemented controls over approval of expenditure, and management accounts and budgets are produced periodically and reviewed by the Board. The Head of Finance also oversees the collation of the Firm's regulatory and prudential reporting to the FCA. The Board retains overall responsibility for the risk management processes within the Firm.

Furthermore, also embedded to the core of the Company's operations is the Internal Capital Adequacy and Risk Assessment process (ICARA), which serves as a valuable risk management tool that ensures that the Company's Risk Management framework receives the necessary attention from all the related functions and personnel of the Company.

The Board of the Company and the Senior Management ensure the appropriate design, adoption and implementation of this process, by performing their related duties and responsibilities.

Due to the size of the firm a Risk Manager is not required. The Risk Management procedures are further strengthened by the following functions:

- a) Compliance
- b) Money Laundering Reporting Officer
- d) Legal (local and Group)
- e) Finance & Accounting
- f) Enterprise Risk Management

Compliance Officer

The Compliance Officer of the Company is responsible to:

- a) review on an annual basis (and when deemed necessary on an ad-hoc basis) the risk management policies and procedures and ensure that the Company is compliant with relevant rules and regulations; and
- b) report to Senior Management all instances of non-compliance for immediate action.

Money Laundering Reporting Officer (MLRO)

The MLRO has overall responsibility for the establishment and maintenance of effective Anti Money Laundering ('AML') systems and controls. The MLRO is also responsible for designing and implementing risk-based approach policies for money laundering and due diligence procedures for new clients.

Legal Function

The Company utilises the local and Group legal team to ensure that local regulatory obligations and legal issues are appropriately identified, addressed and managed.

Head of Finance & Accounting Department

The Company retains a qualified and experienced person as the Head of Finance & Accounting Department. The Head of the Finance & Accounting Department shall also be responsible for supervising the rest of the staff in the said department, in addition to the below:

- a) Capital Adequacy Planning & Monitoring;
- b) Regulatory Compliance regarding Financial Information;
- c) Monthly, Quarterly & Annual Financial Statements; and
- d) Monitoring and supervising the reconciliation of the Client Financial Information, and General Ledger Account balances.

Risk to Client (RtC)

The Company calculates Risk-to-Client ("RtC") capital requirements, based on the following formula as per the IFPR:

RtC capital requirements = K- Assets Under Management (K- AUM) + K- Client Money Held (K- CMH) + K- Assets Safeguarded and Administered (K- ASA) + K- Client Orders Handled (K- COH).

The Company is only subject to K-CMH. RtC K-Factor definitions and applicability to the Company are detailed below:

- K-AUM captures the risk of harm to clients from incorrect discretionary management of client portfolios or poor execution and provides reassurance and client benefits in terms of the continuity of service of ongoing portfolio management and investment advice. The Company is not subject to K-AUM since it does not provide discretionary portfolio management for its clients or non-discretionary arrangements constituting investment advice of an ongoing nature.
- K-ASA captures the risk of safeguarding and administering client assets and ensures that investment firms hold capital in proportion to such balances, regardless of whether they are on their own Balance Sheet or in third-party accounts. The Company is not subject to K-ASA since it does not provide safeguarding and administration for clients' financial instruments other than CFDs (Note: custodianship of clients' CFDs is provided and is considered to be captured under K-CMH due to the intrinsic nature of the CFDs).
- K-COH captures the potential risk to clients of an investment firm that executes orders (in the name of the client, and not in the name of the investment firm itself), for example as part of execution-only services to clients or when an investment firm is part of a chain for client orders. The Company is not subject to K-COH since it does not execute orders in the name of the client, on an agency basis (i.e. all client orders are executed on a principal basis).
- K-CMH means the amount of client money that the Company holds, taking into account the legal arrangements in relation to asset segregation and irrespective of the national accounting regime applicable to client money held by the Company. K-CMH captures the risk of potential for harm where an investment firm holds the money of its clients, taking into account whether they are on its own Balance Sheet or in third-party accounts and arrangements under applicable national law provided that client money is safeguarded in the event of bankruptcy, insolvency, or entry into resolution or administration of the Company.

The Company implements a number of policies and procedures in order to properly safeguard and minimise the risk of loss of any clients' money held under custody.

Specifically, according to these policies and procedures the Company shall, on receiving any Client funds, promptly place those funds into one or more accounts opened with any of the following:

- a) central bank
- b) credit institution
- c) bank authorised in a third country
- d) qualifying money market fund.

In the event that the Company decides not to deposit Client funds with a central bank, it shall exercise all due skill, care and diligence in the selection, appointment and periodic review of the credit institution, bank or money market fund where the funds are placed and the arrangements for the holding of those funds. The Company shall take into account the expertise and market reputation of such institutions or money market funds with a view to ensuring the protection of Clients' rights, as well as any legal or regulatory requirements or market practices related to the holding of Client funds that could adversely affect Clients' rights.

The Head of Finance shall be responsible for implementing the provisions arising from the above by

- opening separate bank accounts for Clients and the Company.
- performing due diligence over the operational adequacy of the third parties so as to ensure that separate bank accounts are maintained for holding Client assets and Company assets through the review of (indicatively):
 - i. the terms of business
 - ii. expertise
 - iii. credit ratings
 - iv. reputation
 - v. references

- vi. availability of authorisation/specialised licenses, granted by the supervisory authority of the country of origin of the third party for the provision of services
- vii. availability of suitable staff members employed by the third party, in this respect
- viii. availability of information on shareholders, financial position and top managers of the third party
- ix. ability of third parties to maintain segregation of assets between Clients and the Company.

Further to the above, the Head of Finance shall be responsible for ensuring that the Company does not mix its own funds with its Clients' funds. In this respect, the bank account(s) containing Client funds should be labeled as "Clients' Account" with appropriate trust letters as required under the Client money rules.

For the year ended 30 June 2022, all Client funds were kept in tier 1 UK credit institutions.

Risk to Market (RtM)

The RtM K-factor requirement for the trading book positions of an investment firm dealing on own account, whether for itself or on behalf of a client shall be either the K-Net Position Risk (K-NPR) calculated in accordance with MIFIDPRU 4.12.2R or the K-Clearing Margin Given (K-CMG) calculated in accordance with MIFIDPRU 4.13.5R. The RtM K-factor requirement applies to all Trading Book positions, which include in particular positions in debt instruments, equity instruments, collective investment undertakings ('CIU's), foreign exchange and gold, and commodities (including emission allowances). Furthermore, for the purposes of calculating RtM K-Factor requirement an investment firm shall include positions other than trading book positions where those give rise to Foreign Exchange risk or Commodity risk.

For the purposes of calculating RtM the Company has elected to apply K-NPR instead of K-CMG, since K-CMG applies in the case where the execution and settlement of transactions of an investment firm dealing on own account take place under the responsibility of a clearing member or a qualifying central counterparty, which is not relevant for the Company.

For the purpose of calculating K-NPR the Company applies the Standardised Approach set out in Title IV of Part Three of the UK Capital Requirements Regulation ('CRR').

The Company may incur Market risk from its Trading Book transactions in FX, equity and commodity CFDs, as well as from exchange rate fluctuations on all its Banking Book assets and liabilities held in foreign currencies. As a match principal brokerage, the Company does not incur market risk as all transactions are automatically hedged on a back to back basis with its liquidity provider(s) (currently a Group affiliated and regulated entity). The Company also regularly analyses its currency groups by netting each currency's cash balances with the respective client liabilities. If the net position of a currency group is in deficit, funds from a currency group that is in surplus may be converted and transferred to bring the deficit currency group into surplus.

Risk to Firm (Rtf)

RtF capital requirements = K- Trading Counterparty Default (K- TCD) + K- Daily Trading Flow (K- DTF) + K- Concentration (K- CON).

K-TCD

In accordance with MIFIDPRU 4.14, "Trading Counterparty Default" or "TCD" is an amount equal to the sum of the TCD own funds requirement for all transactions specified in MIFIDPRU 4.14.3R.

- Derivatives contracts;
- Exchange-traded derivative contracts; and
- Derivative contracts held for hedging a position of the firm resulting from an activity outside the Trading Book
-

For the Firm, TCD risk arises from its trading activities in Over-The-Counter ("OTC") CFD derivative contracts when acting as Principal for the purposes of executing its clients' transactions

K-DTF

Furthermore, "Daily Trading Flow" or "K-DTF" is defined by MIFIDPRU 4.15.2G as "the daily value of transactions that an investment firm enters through Dealing on Own Account or the Execution of orders on behalf of clients in its own name. Pepperstone Limited is subject to DTF risk as the firm acts as principal, however, as the firm's model is matched principal all trades are automatically passed to its liquidity providers.

The Company strives to manage, control and minimize Rtf category risks by implementing the following measures:

- Client margins are monitored on a daily basis so that minimum risk exposure occurs. Moreover, as at 30 June 2022 the Company held all cash with top-tier UK banks after undertaking an initial assessment of the credit rating of the bank.

- The Company enters into OTC financial derivatives contracts with its clients only if such contracts are supported by sufficient margin collateral. The Company is required to apply margin requirements as a minimum to support the clients' investments and any other trading activities performed through the Company. Any open positions held by the clients in OTC derivatives will be included with 100% of their prevailing mark-to-market values (i.e. including the unrealised profit or loss related to each such position), in support of the clients' margin collateral requirements at any time.

- The Company monitors and controls on an ongoing basis the clients' Net Free Equity and related margin requirements, where Net Free Equity for a client is the sum of the below:
 - The value-dated cash balance of the client's trading accounts,
 - plus (or minus) any unrealised profits (or losses) from the client's open contracts,
 - minus any margin required for financing the client's open positions.

K-CON

- The Company assesses Concentration risk on a continuous basis by actively monitoring its open positions with its clients and with its hedging counterparty and group affiliate entity, Pepperstone Group Limited (ASIC regulated). As at 30 June 2022, the Company had no significant concentration of Trading Counterparty Default risk (Counterparty Credit risk under the CRR framework) to any single counterparty, or of Issuer risk to issuers of equities underlying its own positions in equity CFDs.

The Firm operates as a matched principal broker. All market exposure arising from client transactions is passed to the Pepperstone Group's centralised risk book in Australia.

The Firm's retail customers benefit from a no-negative-balance guarantee. The management of this guarantee is also underwritten by the Group's central risk book. Because these client's accounts can not go negative, there is no credit risk to the Firm in relation to them.

Credit exposures to non-retail customers are mitigated through margin deposits. Margin requirements are regularly reviewed by the Firm to ensure that they remain appropriate in light of market conditions.

There is some risk that our clients' ability to trade and to manage their market risk could be impacted by operational problems within the Firm. The Board of Directors has implemented a comprehensive operational risk management framework to identify, monitor and manage such risks.

Over-exposure to a single counterparty or a single source of earnings has the potential to destabilise the Firm in the event of disruption to the counterparty/client.

The Firm's senior management team monitors the Firm's exposures and sources of earnings on an ongoing basis to ensure that they are sufficiently diversified in accordance with the Firm's risk appetite.

A shortage of liquidity has the potential to interrupt the normal operation of the business. In extreme circumstances it could result in a disorderly failure of the Firm.

The Firm undertakes an analysis, as part of its overall ICARA process, of the amount of liquidity required to maintain normal business operations or, if necessary, to facilitate an orderly wind down of the firm. The Firm's available liquid resources are monitored on an ongoing level against a trigger level set in excess of the identified requirements. The Board of Directors has identified a number of steps that could be taken in those circumstances to increase the Firm's liquidity. The Firm has processes in place to wind down the business on an orderly basis should this become necessary.

3. Governance arrangements

3.1 Board of Directors

For the year ended 30 June 2022 the Board consisted of 3 members, of which 1 was a Non-Executive Director and 2 were Executive Directors. The Company ensures that the management body has overall responsibility for the firm and complies with the requirements outlined in SYSC 4.3A.1R. Board meetings are held every quarter.

Under Senior Managers and Certification Regime (SM&CR) the board members hold the following responsibilities:

- Responsibility for the Firm's performance of its obligations under the Certification Regime;
- Responsibility for the Firm's obligations in respect of notifications and training of the Conduct Rules;
- Responsibility for the Firm's policies and procedures for countering the risk that the firm might be used to further financial crime;
- Responsibility for the Firm's compliance with CASS;
- Responsibility for the Firm's performance of its obligations under the SM&CR, including implementation and oversight.

3.2 Diversity Policy

With a view to achieving a sustainable and balanced development, the Company sees increasing diversity at Board level as an essential element in supporting the attainment of its strategic objectives and its sustainable development. In designing the Board's composition, Board diversity has been considered from a number of aspects, including but not limited to gender, age, cultural and educational background, professional experience, skills, knowledge and length of service. The members of the Board of Directors shall at all times be of appropriately good repute and possess sufficient knowledge, skills and experience to perform their duties.

The ultimate objective is to have a Board that offers a broad range of perspectives that are directly relevant to the business and organisational needs. The Company ensures that a broad set of qualities and competences exists when recruiting members to its Board.

The overall composition of the Company's Board shall reflect an adequately broad range of experiences and knowledge such as investment banking and finance, human resources, legal, risk management, etc.

Due to its size Pepperstone is not required to have Risk, remuneration, and nomination committees in line with MIFIDPRU 7.1.4R.

3.3 Number of directorships held by members of the Board

The table below provides the number of directorships each member of the management body of the Company currently holds at the same time in other entities outside of the Group. Directorships in organisations that do not pursue predominantly commercial objectives, such as non-profit-making or

charitable organisations, or are held in entities within the same group are not taken into account for the purposes of the below.

Name of Director	Position within the Company	Directorships- Executive	Directorships- Non-Executive
Tamas Szabo	Non- Executive	0	0
Savvakis (Zack) Ioannou	Executive	0	0
Robert Bowen	Executive	0	0

Note: The information in this table is based only on representations made by the directors of the Company

As the firm does not meet any of the following criteria under the definition of an SYSC Significant firm found in SYSC 1.5.2R a waiver for the directors to hold additional directorships under SYSC 4.3A.6R from the FCA is not necessary.

4. Capital Management and Preservation

The Company's eligible Own Funds at year-end comprised entirely of Common Equity Tier 1 Capital. As at 30 of June 2022, the Company's eligible Own Funds consisted of the following:

Composition of regulatory own funds			
	Item	Amount (GBP thousands)	Source based on reference numbers/letters of

			the balance sheet in the audited financial statements
1	Own Funds	7,231	
2	Tier 1 Capital	7,231	
3	Common Equity Tier 1 Capital	7,231	
4	Fully paid up capital instruments	956	Face of Balance Sheet ("Called- up share capital")
6	Retained Earnings	6,326	Face of Balance Sheet ("Retained earnings")
9	Adjustments to CET1 due to prudential filters	(3)	Prudent deduction not shown on Balance Sheet
11	Total deductions from Common Equity Tier	(48)	Face of Balance Sheet ("Intangible assets")
20	Additional Tier 1 Capital	-	N/A
25	Tier 2 Capital	-	N/A

The Company's Capital Adequacy Ratio as at 30 June 2022 was 646.61% which was above the IFPR regulatory threshold of 100% for Total Capital Requirements.

The primary objective of the Company's capital management is to ensure that it has sufficient capital to enable it to effectively fund its operations on a going-concern basis and maximise shareholder value by taking advantage of growth opportunities. The Company does not leverage through the use of debt finance in order to generate returns on equity. The Company manages its capital structure and makes adjustments to it, in light of changes in economic conditions. To maintain or adjust its capital structure, the Company may adjust the dividend payment to shareholders, return capital to shareholders or issue new shares.

5. Capital Requirements

5.1 Own Funds Requirements

The Company's policy is to monitor Own fund requirements on a continuous basis. The Company complies with MIFIDPRU 4.3.2R stating that the Company shall at all times have Own Funds which amounts to at least the highest of the following:

- a) Its permanent minimum capital requirements under MIFIDPRU 4.4;
- b) Its fixed overheads requirement under MIFIDPRU 4.5; or
- c) its K-factor requirement under MIFIDPRU 4.6.

5.2 Fixed Overheads Requirements

The Company's policy is to monitor Fixed Overheads Requirements on a continuous basis. The Company complies with MIFIDPRU 4.5.1R stating that the Company shall hold Own Funds of at least one-quarter of the fixed overhead expenses of the preceding year. The Fixed Overheads Requirement as of 30 June 2022 amounted to £1,118,000

5.3 Permanent Minimum Capital Requirement

The Company's policy is to monitor on a continuous basis its Own Funds and ensure that they remain above the Permanent Minimum Capital Requirement of £750,000 as per MIFIDPRU 4.4.1R. However, because it is a matched principal broker and was authorised prior to 1 January 2022, the Firm currently benefits from a Transitional Provision which means that it will not be fully subject to this capital requirement until 1st January 2027. The Firm's Transitional Minimum Capital Requirement (TMCR) as at 31 January 2022 was £125,000.

5.4 K-Factor Requirements

The Company's policy is to monitor K-Factor Requirements at least on a continuous basis. The table below presents the K-Factor requirements as at 30 June 2022:

K-factor	Capital requirement (£'000)
K- AUM + K- CMH + K- ASA	£73,000
K- COH + K- DTF	£64,000
K- NPR + K- CMG + K- TCD + K- CON	£527,000
Total	£664,000

5.5 Liquidity risk

Definition

Liquidity risk arises from the possibility that the Company might encounter difficulty in settling its debts or otherwise meeting its obligations relating to financial liabilities. The Company manages this risk through the following mechanisms:

- preparing forecast cash flow analysis in relation to its operational, investing and financial activities, monitored on a quarterly basis; and
- comparing the maturity profile of financial liabilities with the realisation profile of financial assets.

Typically, the Company ensures that it has sufficient cash on demand to meet expected operational expenses by preparing a 12- month cash flow forecast

The Company maintains liquidity levels which are at least one-third of the fixed overhead requirement as per the requirements of MIFIDPRU 6.2.1R

6. Remuneration Policy and Practices

Deferral Policy and Payout in Instruments Policy

The Company does not have a Deferral Policy nor does it maintain a Payout in Instruments Policy. In the event of a Deferred payment or Payout in Instruments, these will be payable in accordance with the applicable employment laws at the time.

The Firm's Board adopts and periodically reviews the general principles of the remunerations policy and is responsible for overseeing its implementation. Decisions with regards to remuneration levels and salary increases of employees are discussed and approved by the Board. In addition to examining these factors, Senior Management hold performance reviews for each staff at the end of each year to assess the employee's performance during the preceding year.

Aside from the monthly fixed salaries, the Firm operates a discretionary annual bonus scheme to recognise an employee's contribution to the success of the Firm. The bonus year runs from 1 July to 30 June.

The FCA defines material risk takers as employees whose professional activities have a material impact on the firm's risk profile including any employee who is deemed to have a material impact on the firm's risk profile. The firm has implemented the new remuneration rules taking effect in January 2022 together with the IFPR and will provide the disclosures pursuant to this requirements in its FY23 disclosures.

There are four material risk takers employed by the firm as of 30th June 2022. The firm does not offer guaranteed variable remuneration and severance pay is offered on a case-by-case basis. Malus and clawback arrangements are in place.


Aggregate Remuneration

During the year ended 30 June 2022, the remuneration structure offered by the Company to management and staff comprised of a fixed salary cash component and non-cash benefits. The Company also paid bonuses in the form of cash to reward outstanding employee performance during the year. Information on the aggregate remuneration to Senior Management and other staff whose actions had a material impact on the Company's risk profile as of 30 June 2022, is provided in the following table:

30 June 2022

Position/ Role	No. of Benefici aries	Fixed Remunerati on £'000	Variable Remunerati on £'000	Total Remuneration £'000
Senior Management	4	625	409	1,034
Other Staff	18	1,065	162	1,227
Total	22	1,690	571	2,261

During the year ended 30 June 2022, the Company did not pay or award any deferred remuneration or severance payments. In addition, all the variable remuneration paid within the year was in the form of cash. No variable remuneration was guaranteed.



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