The Safest Place To Trade

# FX PRIMUS EUROPE (CY) LTD

# PILLAR III DISCLOSURES AND MARKET DISCIPLINE

## 28 April 2017

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# 1. INTRODUCTION

FX PRIMUS Europe (CY) Ltd (the “Company”) is an Investment Firm authorized to operate and regulated by the Cyprus Securities and Exchange Commission (the “CySEC”) under the license with no. 261/14.

The report is prepared in accordance with the requirements of Directive DI144-2007-05 of 2012 and relevant regulations of CySEC for the Capital Requirements of Investment Firms. The said Directive is based on three pillars:

1. Pillar I has to do with the standards that set out the minimum regulatory capital requirements.
2. Pillar II covers the Supervisory Review Process which assesses the internal capital adequacy processes.
3. **Pillar III covers transparency and relates to the obligation of investment firms to publicly disclose information with respect to their risks, their capital and the risk management structures, policies and procedures they have in place.**

The Company makes this report available publicly on its website annually. This report relates to the year ended 31 December 2016 (the “Reporting reference date”) and to the Pillar III of the said Directive. Finally, the disclosures in this report are verified on a sample basis by the external auditor of the Company, Messrs Anthimos Leonidou & Partners LTD.

Any information not contained in this report was either not applicable based on the Company’s business and activities, or such information is considered as proprietary to the Company. Sharing such information with the public would possibly undermine the Company’s competitive position.

# 2. COMPANY SERVICES AND BRIEF ORGANIZATIONAL STRUCTURE

In accordance to the provisions of the Investment Services and Activities and Regulated Markets Law of 2012 (the “Law”), the Company is licensed to conduct the following services:

**Investment services:**

- Execution of Orders on Behalf of clients

**Ancillary services:**

- Safekeeping and administration of financial services, including custodianship and related services
- Granting credits or loans to one or more financial instruments
- Foreign exchange services where these are connected to the provision of investment services
- Investment research and financial analysis

More specifically, the Company enables traders to trade through the MT4 platform in Contracts for Differences, with underlying assets various currency pairs, stocks, metals, commodities and indices. The orders received from traders in the above mentioned instruments are executed on a variety of liquidity providers the Company is working with.

# 3. RISK MANAGEMENT STRUCTURE

The Company is exposed to a variety of risks referred to below in this present report. The Company actively manages the risks it is exposed with the involvement of a series of functions within, so as to protect both investor and company interests.

From the level of Board of Directors and Senior Management, and their relevant Risk Management Committee, to the independent Internal Audit function, and down to the additional defense line of the Risk Management function, the Company identifies, assesses, manages and monitors risks taking into account the nature, scale and complexity of the activities undertaken in the course of business.

## 3.1. BOARD OF DIRECTORS AND SENIOR MANAGEMENT

The Board of Directors is ultimately responsible for overlooking and directing the operations of the Company, based on the approved objectives and strategic directions, as detailed in the Company's approved Internal Operations Manual (the "IOM"). It carries the overall responsibility for the establishment of a robust control environment and a sound risk management framework that will safeguard the operations of the Company and will ensure it creates value for its stakeholders.

The selection basis for the Directors of the Company includes previous relevant experience in senior positions in the Fintech industry, which will ensure they are equipped with the necessary know-how that their duties demand, so as to competently excel in their everyday work. It also brings fresh ideas in the Company and state-of-the art practices widely applied by the competition.

## 3.2. RISK MANAGEMENT COMMITTEE

The Risk Management Committee is composed as required by members of the Company's control functions, Senior Management and Board of Directors, entitled to oversee the overall risk management system in place, establish relevant policies, and direct key risk management related decisions, as detailed in the Company's IOM.

The Composition of this Committee includes 1 executive and 2 non-executive directors.

## 3.3. RISK MANAGEMENT FUNCTION

The risk management function is operating with the necessary expertise and follows the required processes as detailed in the Company's IOM for implementation and monitoring of Risk Management policies and needs.

The Risk Manager is heading the risk management function and reports at least annually to the Risk Management Committee and the Board of Directors.

## 3.4. COMPLIANCE FUNCTION

The compliance function possesses the necessary expertise and follows the required processes as detailed in the Company's IOM. Specifically, it is implementing a compliance monitoring program to ensure the overall compliance of the Company with laws and relevant directives imposed by the CySEC. The Company operated its compliance function for the year of 2016 with an outsourced expert service arrangement.



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### 3.5. INTERNAL AUDIT FUNCTION

The internal audit function has the necessary expertise and follows the required processes as detailed in the Company's IOM. Specifically, it is implementing an internal audit program to independently review the Company's functions and activities and their adherence to processes, controls and requirements. The internal audit program involves desktop and physical audits, including surprise visits.

The Board of Directors is satisfied that the risk management arrangements of the Company are proportional to its scale of operations.

# 4. RISK MANAGEMENT RELATED POLICIES FOR MITIGATING RISK

The Company has various policies, embedded in its documentations and governing its operations, which aid to mitigate risks; the main being:

- Internal Procedures Manual
- Additional Departmental Manuals/Procedures
- Anti- Money Laundering and Terrorist Financing Manual
- On Information Security, Access/Password Protection, Backup
- Business Continuity Plan
- On Employees' Personal Transactions
- On Customer Complaint Handling
- ICAAP: Internal Capital Adequacy Assessment Process

# 5. CAPITAL ADEQUACY AND CAPITAL MANAGEMENT

A fundamental objective of the Company's management of capital is to ensure that the Company complies with regulatory/externally imposed capital requirements and that the Company maintains such compliant healthy capital ratios at all times/continuously.

According to the Directive DI144-2007-05 of 2012 of the CySEC regarding Capital Adequacy of Investment Firms, the Company is obliged to submit to CySEC quarterly capital adequacy reports.

The CySEC may revise or impose additional capital requirements for risks not covered by Pillar I.

### 5.1. CAPITAL ADEQUACY RATIO AND RISK WEIGHTED ASSETS

The Company's capital adequacy ratio as of end of year was as follows and the Company's Risk Weighted Assets were concentrated on the categories a., b., and c. below:

| **Eligible Own Funds (I, II, III) & Capital Requirements /Risk Weighted Assets (a, b, c, d)** | **USD '000** |
|---|---|
| I. Original Own Funds (Tier 1 Capital) | 2.448 |
| II. Applicable Deductions | (32) |
| **III. Total Eligible Own Funds** | **2.416** |
| **a.** Risk Weighted exposure amounts for credit, counterparty credit and dilution risks and free deliveries | 217 |
| **b.** Total Risk exposure amount for fx risk | 33 |
| **c.** Additional Risk exposure amount due to fixed overheads (fraction of annual fixed overheads expenditure) | 1.534 |
| **d. Total Risk Exposure Amount** | **1.784** |
| **Minimum Capital Adequacy Ratio** | **10.83%** |

The Company employs a real-time budgeting process to assess the adequacy of its internal capital to support the current and future activities.

### 5.2. COMPANY OWN FUNDS - CAPITAL BASE

The composition of the capital base of the Company as of end of year was as follows:

| **Capital (Original Own Funds): Tier 1 (none of Tier 2)** | USD '000 |
|---|---|
| Share Capital | 317 |
| Share Premium | 1.446 |
| Reserves (Retained Earnings) | 685 |
| **Total Original own funds (before deductions)** | **2.448** |
| Deductions | (32) |
| **Total Own Funds** | **2.416** |

The share capital of the Company consists of 300 002 fully-paid ordinary shares of EUR1 each. The ordinary shares of the Company carry the same voting and dividend distribution rights.


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# 6. MAIN RISKS

## 6.1. CREDIT RISK

Credit Risk arises mainly from the inability of counterparties to honor contractual obligations or change in the credit premium that the market demands as an effect of the market perception of increased default risk.

Banks, Custodian-type third parties and Trading counterparts of the Company have been risk-assessed on credit worthiness. To minimize potential risks, the Company was using, for its own purposes/funds, reliable (EU and/or investment-grade) and diversified financial institutions in the EU region. The Company did not have any own financial instruments/positions.

As at the Reporting reference date:

| **Credit Risks (Standardized Approach) per Counterparty type (on-Balance Sheet):** | USD ‘000 |
|---|---|
| Institutions | 297 |
| Corporates | 1.073 |
| Retail | 993 |
| Other Items | 355 |
| **Total Risk Weighted exposure amounts for credit risk** | **2.718** |

**Capital Requirements**

The Company follows the Standardised Approach for the calculation of the minimum capital requirements for credit risk.

The risk-weighted credit risk exposure against the following counterparties is measured as follows:

***Institutions***

Exposures against institutions are risk weighted based on the risk weight of the credit quality step the institutions are assigned. The assignment of institutions to credit quality steps is made through the use of Moody’s credit ratings.

Moody’s credit ratings correspond to credit quality steps based on the table below:

| Credit Quality Step | Moody’s Assessment |
|---|---|
| 1 | Aaa to Aa3 |
| 2 | A1 to A3 |
| 3 | Baa1 to Baa3 |
| 4 | Ba1 to Ba3 |
| 5 | B1 to B3 |
| 6 | Caa1 and below |


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***Corporates***

All the corporates to which the Company has exposure to are unrated. Therefore the highest between the 100% risk weight and the risk assigned to the central government the corporate is incorporated to is been used.

***Retails***

The exposure to retails is risk weighted with a 75% risk weight. It is consisted of many small balances been the receivable of the Company from the clients' money segregated from the money held by the Company.

***Other items***

Included in this type of exposure are the fixed assets of the Company, various prepayments, other receivables and the cash in hand. The cash in hand are assigned a risk weight of 0%, whereas the rest of the other items are risk weighted at 100%.

The credit risk exposures relate to balances with residual value of less than three months and are mainly receivable from counterparties located within the European Union.

**IMPAIRMENT**

**Financial assets at amortised cost**

The Company assesses at the end of each reporting year whether there is objective evidence that a financial asset or a 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.

The criteria that the Company uses to determine that there is objective evidence of an impairment loss include:

- significant financial difficulty of the issuer or obligor;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- the Company, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that a lender would not otherwise consider;
- it becomes probable that the borrower will enter bankruptcy or other financial reorganisation;
- the disappearance of an active market for that financial asset because of financial difficulties; or
- observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including:

(i) adverse changes in the payment status of borrowers in the portfolio;
(ii) national or local economic conditions that correlate with defaults on the assets in the portfolio.

The Company first assesses whether objective evidence of impairment exists. For loans and receivables category, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognised in profit or loss. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Company may measure impairment on the basis of an instrument's fair value using an observable market price.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the reversal of the previously recognised impairment loss is recognised in profit or loss.

A financial asset is 'past due' when a counterparty fails to make a payment that is contractually due.

## 6.2. MARKET RISK

Market Risk is the risk of losses in on- and off-balance-sheet positions arising from changes in market prices / adverse changes in market factors.

The Company follows the Standardized Approach for calculating the minimum capital requirements for market risk.

The main such risks are detailed below:

### 6.2.1. Currency Risk

Foreign Exchange Market risk is the risk that results from adverse movements in the rate of exchange. Foreign Exchange risk arises from positions (transactions, and recognized assets and liabilities; on- and/or off- balance sheet items) in currencies other than the functional currency of the Company, which is the USD.

The Company mitigates such risk by closely monitoring the balance of its foreign currency obligations versus the balance of its holdings and receivables in foreign currencies. Any currency gaps identified exceeding the limits set by the Risk Management Committee are been rectified accordingly to return back within the tolerable pre-set limits.

The Company had certain assets and liabilities denominated in EUR which were creating a net long currency gap of USD429.000.

### 6.2.2. Interest Rate Risk

Interest Rate Market risk is the risk that arises from adverse movements in interest rates that affect the Company's on- and/or off- balance sheet items.

The Company's management monitors the interest rate fluctuations on a continuous basis and acts accordingly. The Company did not have any own position in securities meaning that its income and operating cash flows are substantially independent of changes in market interest rates. At 31 December 2016 the Company had an interest bearing financial liability, with interest been at normal commercial rates.

#### 6.2.3. Liquidity Risk

Liquidity Risk is the risk that Company's tradable assets become illiquid.

The Company's management monitors liquidity on a continuous basis and acts accordingly. The Company did not have any own financial instruments/positions (securities), other than its cash-form capital, therefore was not exposed to such risk of asset illiquidity.

### 6.3. OPERATIONAL RISK

Operational Risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or external events. Operational risk is one of the major risks that the Company is facing where errors, fraud or disruptions to service can have monetary or reputational cost.

Particularly, the Company mitigates such risk as it applies the "4-Eyes" Principle as a risk mitigation factor of broad human error. It has also established procedures which ensure business continuity and disaster recovery. Furthermore, the Company applies transaction recording mechanisms, segregation of duties where feasible, and verification as necessary. As the Company falls under the provisions of Article 95 of the Regulation for Investment Firms with limited authorization, it is required to measure this risk with the Fixed Overhead approach. This approach requires the Company to hold eligible capital which is higher than the maximum of the sum of the credit and foreign exchange risk requirements or its fixed overhead requirement.

The Company follows the subtractive approach for calculating the fixed overheads, whereby variable cost items are deducted from the total expenses as calculated according to the International Financial Reporting Standards.

Out of the total expenses the Company has reported for the year ended 31 December 2016, there have been adjustments for non-recurring expenses from non-ordinary activities of the Company, clearing houses costs, commissions paid to intermediary brokers and fully discretionary bonuses.

The additional capital requirement of the Company imposed by the Fixed Overhead approach for the relevant risk measurements, is seen in table of section 5.1 (III.c.).

#### 6.3.1. Operating Cash Flow Liquidity Risk

Operating Cash Flow Liquidity Risk is the risk that the Company will not be able to meet its financial obligations, and may arise, among others, when the maturity of assets and liabilities does not match.

The Company closely monitors cash-flow in real time and strives to be aware, as far as possible, regarding future own financial obligations, to ensure to meet its liabilities when they are due. As at the Reporting reference date, the payables comprising the financial liabilities of the Company were matched by balances available on account(s).

#### 6.3.2. IT Risk

IT risk is the business-impact risk associated with the ownership and operation, as well as involvement with, Information Technology.


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The Company mitigates this risk with adequate arrangements in place regarding back-up procedures, software maintenance, hardware maintenance, use of the internet, and anti-virus safety/safeguarding procedures.

### 6.3.3. Reputational Risk

Reputational risk occurs when negative publicity arising from customers, counterparties, shareholders or regulators regarding the Company's business practices affects the Company.

The Company, in this respect, employs the following mitigation strategies:

- Strive to keep its customers satisfied. The Company has a well-implemented customer complaint handling-policy.
- Information provided to Customers is ensured to be fair, clear and not misleading. The Company reviews and approves any advertising and other material before they are being published.
- Prioritizes compliance with applicable regulations
- Maintains good relationships with counterparties

# 7. REMUNERATION RISK AND POLICY

Remuneration Risk is the risk that the remuneration structure/policy of the Company provides incentives to take risks that exceed the general level of risk tolerated by the Company, or to willingly act against interests of clients, therefore exacerbating excessive risk-taking behavior and giving rise to conflicts of interest with clients.

The Company revised its remuneration policy, which was approved by the Board of Directors in August 2016, and includes certain safeguards directly dealing with the avoidance of the risks elaborated in the preceding paragraph.

The Remuneration policy is in line with the business strategy, objectives, values and long-term interests of the Company, such as sustainable growth prospects, and consistent with the principles relating to the protection of clients/investors in the course of services provided. In this way, the Company mitigates remuneration risk to the best extent feasible.

The remuneration of the Directors and Senior Management of the Company is also governed by the aforesaid policy. It comprises of a basic salary and a fully discretionary variable element.

The remuneration of the Non-Executive Directors of the Company comprises of a fixed annual fee.

As at the Reporting reference date the total remuneration was as follows:

The remuneration paid to the Board of Directors was USD295.304 (No of Beneficiaries: 5). This is analysed as follows:

**Fixed Salary element** total: USD287.516
**Variable Salary element** total: USD7.788

This variable salary element related to a fully discretionary payment made to a Director as a recognition of his contribution to the operations of the Company. No other variable element of remuneration was paid to the Directors and key management personnel of the Company.


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# 8. COMMUNICATION / ENQUIRIES

For any enquiries regarding the contents of this report, please feel free to contact the Company at the contact details stated below.

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