

# **HIROSE FINANCIAL UK Ltd- Pillar 3 Disclosures as at 31<sup>st</sup> March 2021**

## **1. Overview**

### 1.1 Regulatory Requirements for Pillar 3 Disclosures

The Capital Requirements Directive (CRD) and the Capital Requirement Regulation (CRR) (collectively “CRD IV”) implements the Basel III agreement in the EU and establishes a regulatory framework consisting of three “Pillars”:

Pillar 1: sets out minimum capital requirements firms are required to meet for credit, market and operational risk.

Pillar 2: requires firms and their regulatory supervisors to consider whether a firm should hold additional capital against risk not covered in Pillar 1. In the UK, this is implemented through the Internal Capital Adequacy Assessment Process (ICAAP) undertaken by the firm and through the subsequent Supervisory Review and Evaluation Process (SREP) undertaken by the Financial Conduct Authority (FCA).

Pillar 3: requires firms to publicly disclose certain details of their risks, capital, and risk management arrangements. The Pillar 3 disclosure requirements are contained in Articles 431 – 455 of the Capital Requirements Regulation (CRR).

The objective of this disclosure is for HIROSE FINANCIAL UK LIMITED (the “Firm”) to meet its CRR Pillar 3 disclosure requirements.

### 1.2 Solo Basis of Disclosures

The disclosures included herein relate to the Firm, which is a BIPRU 125k Limited Licence Firm-FCA FRN 540244

The firm is wholly owned by Hirose Tusyo Inc., based in Japan.

The disclosures included herein describe the Firm’s overall risk management arrangements and its approach to assessing its capital and liquidity adequacy.

### 1.3 Materiality

CRR Article 432(1) provides that a firm may omit one or more of the required disclosures if the information provided by such disclosures is not regarded as material.

Per Article 432(1), the criterion for materiality is that a firm must regard 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.

### 1.4 Proprietary or Confidential Information

CRR Article 432(2) provides that a firm may omit one or more items of information included in the required disclosures if those items include information which is regarded as proprietary or confidential.

Per Article 432(2), the criterion for proprietary information is that a firm must regard information as proprietary information if sharing that information with the public would undermine its competitive position, where such proprietary information may include information on products or systems which, if shared with competitors, would render a firm's investments therein less valuable.

Per Article 432(2), the criterion for confidential information is that a firm must regard information as confidential if there are obligations to customers or other counterparty relationships binding the firm to confidentiality.

### 1.5 Frequency of Disclosures

These disclosures will be published at least once a year and as soon as practicable following material updates to the Firm's internal capital adequacy assessments. The annual disclosure will be published on the company's website. Given its size and complexity, the Firm assesses that this annual publication meets its disclosure requirements.

### 1.6 Means of Disclosures

These disclosures have been prepared solely for the purpose of fulfilling the Firm's Pillar 3 disclosure requirements and are not used by management for any other purpose. They have not been audited nor do they constitute any form of audited financial statement.

The Firm's Board of Directors are ultimately responsible for the Firm's systems and controls and for reviewing the effectiveness of those arrangements. However, such arrangements are designed to mitigate, not eliminate, risk and therefore can provide only reasonable, but not absolute, assurance against material losses or financial misstatements.

These disclosures have been reviewed and approved by the Firm's Board of Directors.

These disclosures will be published on the Firm's public website ([www.Hiroseuk .com](http://www.Hiroseuk.com)).

## **2. Risk Management Objectives and Policies**

The Firm's risk management objectives and policies are supported by its corporate governance arrangements, its risk management framework and its risk management processes, including its processes establishing risk appetite and for mitigating and monitoring risk within that appetite.

### 2.1 Corporate Governance Arrangements

#### **Board Composition and Diversity**

The current and future needs of the UK business including equality and diversity are considered in the recruitment processes as set out in the UK Equality and Diversity Policy.

Board membership and succession planning for the Board draws upon a range of criteria including relevant skills and expertise, suitability for the role, knowledge of the business, and is cognisant of the business benefits of diversity of gender to maintain a balanced board capable of discharging its responsibilities effectively.

#### **Board of Directors**

The Firm's Board of Directors are expected to be aware of the major aspects of the Firm's risks, especially those risks for which it may need to set aside capital. To that end, the Board periodically review the effectiveness of their systems and controls, including the Risk Management Framework, which establishes the principles of how risk is to be identified, assessed, monitored and controlled/mitigated.

The Board have delegated the day-to-day management of risk to the Firm Compliance Director and Money Laundering Reporting Officer Shion Ikizake with the exception of certain reserved matters for the Board which include but are not limited to:

- Establishing the Firm's overall strategy
- Setting the Firm's "risk appetite"
- Assessing and approving the Firm's capital adequacy (e.g. ICAAP) and liquidity adequacy.

Given the limited size, scale and complexity of the Firm, the Board have not established a separate risk committee, but instead deal with these matters directly. The Board provide oversight on:

- Identifying risks relating to all of the activities, systems and processes of the Firm
- Setting the level of risk tolerated by the Firm
- Managing the risks identified (within any risk tolerance)
- Monitoring the effectiveness of risk management policies and procedures, including compliance with such policies and remedial actions.

The Board is also responsible for the review and approval of new products and segregated accounts (or material changes to such existing products) offered by HIROSE FINANCIAL UK LTD.

In view of the global nature of our business and how quickly crisis events can unfold, the Board acts as a Crisis Management Committee and the Firm maintains its own business continuity and disaster recovery plans.

The Board is responsible for establishing, implementing and maintaining remuneration policies, procedures and practices that are consistent with and promote sound and effective risk management and for ensuring the Firm's compliance with the UK FCA's Remuneration Code.

The Board is also responsible for evaluating potential conflicts of interest, maintaining appropriate records and conflict management including providing ongoing oversight of the Firm's processes for identifying, assessing, mitigating and monitoring potential conflicts of interest throughout the Firm.

Shion Ikizake reports to the Board and is responsible for the development, implementation and maintenance of the Firm's Information Security programme and provides regular reports on the results of the risk assessment process, risk management and control decisions, monitoring and testing, security breaches and resolutions, both internally and with respect to third-party service providers.

## 2.2 Risk Management Framework: Three Lines of Defence

The Firm has adopted a "three lines of defence" model which can be summarised as follows:

### **First Line of Defence**

The first line of defence is the Board responsible for the Firm's business units and who are primarily responsible for identifying and managing risks in their area and for developing and communicating policies, guidance, and procedures necessary to manage those risks.

### **Second Line of Defence**

The second line of defence is primarily comprised of the Compliance director/MLRO and the outsourced Finance function in its parent company responsible for certain financial systems and controls.

The Compliance function is responsible for facilitating the development, implementation and embedding of processes whereby management identifies assesses, monitors, controls and mitigates the risks in their areas and for monitoring adherence to regulatory standards and for reporting its findings to relevant senior management and to the Board. It is also responsible for the provision of technical regulatory/compliance advice and support.

### **Third Line of Defence**

The third line of defence is comprised of the Parent Company's Board which undertakes on-going Audit and Oversight to provide independent assurance of the suitability and effectiveness of the Firm's risk management framework, including management's execution of its responsibilities to ensure an effective system of internal controls, risk management, and compliance is embedded throughout the Firm.

## 2.3 Risk Appetite

The Firm's approach to setting risk appetite first considers the risks inherent in each of its strategies and objectives and then evaluates the most effective way to provide for these risks. For the key risks which cannot be perfectly controlled, the residual risks are quantified and a determination is made whether to provide for each risk with financial planning buffers or with capital (or a combination of both). Generally, expected losses are provided for with financial planning and P&L buffers and unexpected or extreme losses are provided for with capital. These quantifications of risk appetite are the basis on which the Firm's individual capital adequacy assessment (ICAAP) is developed.

## 2.4 Risk Management by Category of Risks

As for other FX firms, risk is inherent in the nature of the Firm's business and activities. The key categories of risks to which the Firm is exposed are:

- operational risks in relation to how it conducts its business activities, and
- Foreign Exchange risk in relation to the exposure of its financials to adverse movements in foreign exchange rates.

The Firm has clear risk management policies and practices in place to manage each category of risk which are described in further detail below.

### **Operational Risk**

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. The Firm undertakes the ongoing identification, assessment, monitoring, controlling and mitigation of risks. Key risks are escalated to the Board for consideration which are in turn developed into scenarios for capital modelling purposes at a 99.5% (1 in 200) confidence level over a one year period.

Other elements of the Firm's operational risk management framework include:

- Quarterly Key Risk Indicator (KRI) assessments and monitoring for any key trends that should be reported to management and the Board.
- Errors Management which involves collecting and analysing loss events (errors) and workflow to ensure swift resolution and senior management attention. The Compliance Director/MLRO is responsible for analysing the impact and cause of any material errors recorded and agreeing any remedial action required with the relevant business function heads.
- Reporting and Analysis - the Risk function is responsible for consolidating and reporting operational risk issues to the Board at their regular meetings taking into consideration KRIs, Errors, and any material issues identified through the external Compliance Consultants.

### **Foreign Exchange Risk**

Foreign Exchange Risk is the exposure of the Firm's financial condition to adverse movements in exchange rates. The Firm is primarily exposed to foreign exchange movements from its non-sterling revenue and expense streams and from its non-sterling assets and liabilities such as cash and net

counterparty trade debtors and creditors. The Firm does not actively hedge its Profit and Loss exposure to foreign exchange movements at the UK Ltd company level, this exposure may be managed on a global basis at the HIROSE Tusyo Inc. level.

### **Interest Rate Risk**

Interest rate risk is the exposure of a Firm's financial condition to adverse movements in interest rates. Changes in interest rates do not affect the Firm's earnings by materially changing its net interest income nor the level of other interest-sensitive income and operating expenses. Such a movement in interest rates does not affect the underlying value of the Firm's assets and liabilities nor materially change the present value of future cash flows.

The Firm does not rely on interest income to fund its operations and has no material debt and as a result would not be materially affected by a 200-basis point movement in interest rates. Therefore, the Firm considers that interest rate risk is not material.

### **Credit Risk**

The Firm's credit risk arises from its cash deposits with banks and financial institutions, as well as credit exposures to debtors in respect of outstanding receivables. Cash deposits are diversified among several high-quality institutions (Barclays and Citibank) which are regularly monitored. The Firm does not have a history of bad debts arising from clients and does not consider such risk material.

### **Liquidity Risk**

Liquidity risk is the risk that current assets are not readily convertible to cash, that funds are either not available to service day-to-day funding requirements or are only available at a high cost, or need to be arranged at a time when market conditions are unfavourable and consequently the terms are onerous.

The liquidity requirements for the Firm arise from day-to-day routine financial activities including the settlement of non-trading book creditors, accounts payable and payroll, offset by the receipt of non-trading book receivables, particularly periodic capital injections from the Parent Company.

Whilst a certain amount of cash volatility is an inevitable consequence of general business activities, the Firm maintains controls to reduce this volatility through cash forecasting. The Firm retains a mixture of substantial cash balances and is confident of being able to settle transactions and continue operations even in the most difficult foreseeable circumstances. Cash requirements are monitored and forecast on a regular basis.

The Firm is not exposed to any significant liquidity risk and considers that liquidity risk is not material.

### **Other Risks**

Insurance risk, concentration risk, residual risk and securitisation risk have also been considered. These risks are not deemed to be material.

### **3. Internal Capital Adequacy Assessment Process and Capital Resources**

The Firm undertakes its Internal Capital Adequacy Assessment Process (ICAAP) at least once annually (or as material changes in conditions warrant) in fulfilment of its Pillar 2 requirements. The Firm's most recent ICAAP document was approved by the Board in September 2021.

#### **3.1 Internal Capital Adequacy Assessment Process (ICAAP)**

The ICAAP is the process under which the management oversees and regularly assesses:

- the Firm's processes, strategies and systems
- the material risks to the Firm's ability to meet its liabilities as they fall due
- the results of internal stress testing of these risks
- the amounts and types of financial and capital resources and whether they are adequate to cover the nature and level of the risks to which the Firm is exposed.

The ICAAP document describes the framework under which the Board carry out their assessment of the adequacy of the Firm's capital and liquidity resources. In particular the document sets out:

- the Firm's internal organisation and governance structure
- the risk management framework
- the Firm's risk appetite
- the key risk areas relevant to the Firm's capital and liquidity
- financial, capital and liquidity projections
- the adequacy of capital and liquidity resources in relation to the overall risk profile and certain stress and scenario events, including reverse stress tests.
- an orderly wind-down scenario
- the way in which the ICAAP is used in the business, including the process of challenge and adoption.

The ICAAP is undertaken on a proportionate basis, taking into account the Firm's size, and the nature and complexity of its activities.

#### **3.2 Approach to IFPRU Capital Requirements**

The Firm's total capital resources requirements with respect to Pillar 1 are the higher of the base capital requirement or the higher of:

- The sum of Market Risk Capital Requirements ("MR") and Credit Risk Capital Requirements ("CR"), or
- A Fixed Overhead Requirement ("FOR").

### 3.3 Capital Requirements and Resources

#### **Capital Resources**

The firm has a simple capital structure and does not use any exotic capital instruments, with all capital held as Tier 1 capital. As of 31<sup>st</sup> March 2021, the Firm held total net core Tier 1 capital of £2,357,408, which exceeds both its Pillar 1 and Pillar 2 capital requirements.

Having considered the forecasted financial position of the Firm and the nature of the risks that the Firm currently faces or is likely to face going forward, the Board have concluded that there is currently, and is expected to be, adequate capital and liquidity given the size, nature and complexity of the Firm and anticipated capital injections from its parent company in Japan.

The capital resources of HIROSE FINANCIAL UK LIMITED are reflected in its audited financial statements for year ending 31st March 2021.

HIROSE FINANCIAL UK LIMITED's Tier 1 Capital Resources are £2,357,408 made up of: -

Issued Share capital	£6,317,000 and
Accumulated Losses	£3,959,592

#### **Summary of Pillar 1 capital requirements**

The Firm's approach to calculating its Pillar 1 Capital Resource Requirement determines the respective Pillar 1 amounts for each of its activities and then aggregates them across by category to calculate the Firm amount for each category. For Pillar 1, the Firm's minimum Capital Resources Requirement is equal to the sum of its Credit Risk Requirement £109,507 and Market Risk Requirement of £1,945 together totalling £111,452 since this amount is greater than both: -

- a) its base capital resources requirement of €125,000 which equates to £106,475 at the 31<sup>st</sup> March 2021 euro sterling exchange rate of 0.8518
- b) its Fixed Overhead Requirement of £60,347.

The Pillar 1 Capital requirements of HIROSE FINANCIAL UK LIMITED are as follows: -

	£000
Credit Risk Capital Requirement (Standardised Approach)	109
Market Risk Capital Requirement ("MR")	2
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<b>Sum of Credit Risk and Market Risk Capital Requirement</b>	<b>111</b>
<b>Fixed Overhead Requirement ("FOR")</b>	<b>60</b>
<b>Base Capital Resource Requirement ("Base CRR")</b>	<b>106</b>
<b><i>Pillar 1 Capital Resource Requirement (Highest of the above)</i></b>	<b><i>111</i></b>

## Summary of Pillar 2 capital requirements

The Firm has prepared an ICAAP which quantifies each of its key risks in order to understand its Pillar 2 capital requirements on a going concern basis. An orderly wind-down analysis has also been prepared which considers the net cash-flows associated with discontinuing the Firm's regulated activities.

These results have been compared to the firm's Pillar 1 requirements in order to determine the overall Pillar 2 capital requirement on a Pillar 1 plus basis and we have conservatively set aside the following amounts against each category of risk:-

Credit Risk	222k
Market Risk	127k
Liquidity Risk	125k
Concentration Risk	38k
Operational Risk	237k
Business Risk	162k
<b>Total Capital Requirement</b>	<b>911k</b>

As at 31<sup>st</sup> March 2021 we had a surplus of capital resources amounting to £1,446k over and above this capital requirement.

## 4. Remuneration

In accordance with the Capital Requirements Regulation remuneration disclosure requirements, as further elaborated in the FCA's General Guidance on Proportionality: The Remuneration Code (SYSC 19A) & Pillar 3 Disclosures on Remuneration (Article 4125 of the Capital Requirements Regulation (CRR)), as an IFPRU limited licence firm, the Firm falls within proportionality level 3 and is required to provide the following disclosures regarding its remuneration policy and practices for those categories of staff whose professional activities have a material impact on its risk profile. FCA's Remuneration Code. Due to the nature, scale and complexity of its business, HIROSE FINANCIAL UK LIMITED has not formally appointed a Remuneration Committee. However, all decisions concerning remuneration are taken by the Board.

### **CRR Article 4125(b): information on link between pay and performance.**

The Firm uses fixed compensation where the fixed component is considered to be a sufficient proportion of the overall remuneration package as to allow the firm to operate a fully flexible bonus policy. The Firm currently sets the variable component in a manner which takes into account individual performance, performance of the individual's business unit and the overall results of the Firm. Staff performance is formally evaluated and documented at least once annually. Such evaluations also consider the staff's contributions in promoting sound and effective risk management where appropriate.

**CRR Article 4125(g): aggregate quantitative information on remuneration, broken down by business area for the financial year ended 31 March 2021.**

CRR Article 4125(h): aggregate quantitative information on remuneration, broken down by senior management and members of staff whose actions have a material impact on the risk profile of the firm. The Firm classifies those staff whose professional activities have a material impact on its risk profile as “Code Staff”. The only Code Staff are the firm’s 2 Executive Directors and its Non-Executive Chairman.

Business Area		Total remuneration
FX margin trading		<b>£31,405</b>
<b>Aggregate quantitative information on remuneration broken down by senior management and members of staff whose actions have a material impact on the risk profile of the firm</b>		
Senior management	Other members of staff	Totals
<b>£31,405</b>	£0	<b>£31,405</b>