Neptune Investment Management Limited
("Neptune" or "the Company")

Pillar 3 Disclosures 2017

Approved by the Board of Neptune on 26th June 2018

Contents

1. Overview

1.1 Background

The Capital Requirements Directive ("**CRD**") of the European Union (as amended from time to time) establishes a regulatory capital framework across Europe governing the amount and nature of capital that credit institutions and investment firms must maintain, including requirements relating to the remuneration paid by such firms. In the United Kingdom, the CRD has been implemented by the Financial Conduct Authority ("**FCA**") through rules and guidance set out in the General Prudential Sourcebook ("**GENPRU**"), the Prudential Sourcebook for Banks, Building Societies and Investment Firms ("**BIPRU**") and the Senior Management Systems and Controls Sourcebook ("**SYSC**"), each of which forms part of the FCA Handbook.

The European framework under the CRD consists of three "Pillars":

- Pillar 1 sets out the minimum capital requirements firms will require in order to meet credit, market and operational risk;

- Pillar 2 requires firms and supervisors to consider whether additional capital should be held to cover risks not covered in Pillar 1 requirements; and

- Pillar 3 seeks to improve market discipline by requiring firms to disclose certain details of their risks, capital and risk management.

1.2 Basis of Disclosure

Neptune is a company registered in England and Wales. The business of the Company is investment management. Within the UK, Neptune's investment management, OEIC and Unit Trust activities are regulated by the FCA.

In accordance with Part Eight of the Capital Requirements Regulation (Regulation No. 575/2013), disclosures ("Pillar 3") must be made on an annual basis as a minimum, and more frequently when appropriate. Neptune has an accounting year end of 31 December, and these disclosures are made as at 31 December 2017.

Disclosures will be made on an annual basis and made available shortly after the publication of Neptune's statutory accounts.

1.3 Scope

The disclosures have not been audited and do not form part of the annual audited financial statements of the Group (being Neptune and its 100% owned subsidiary, Neptune Investment Contracts Limited. They do not constitute any form of financial statement and should not be relied upon in making any judgement about the financial position of the Company.

1.4 Approval and Publication

These Pillar 3 disclosures were approved by the Board of Neptune on 26th June 2018 and will subsequently be published on the firm's website (www.neptunefunds.com).

The disclosures are also available on request in writing from the Chief Financial Officer, Neptune Investment Management Limited, 3 Shortlands, Hammersmith, London W6 8DA.

2. Risk Management Objectives and Policies

2.1 Risk Appetite of Neptune

The key risks to Neptune's business are considered to be investment performance, adverse market conditions and loss of key staff.

Neptune manages these risks through diversity of client and product range and by ensuring that the remuneration packages for key staff are both competitive and appropriate.

At all times the business would look to mitigate any losses, however small, by internal systems and controls.

2.1.1 OEIC, Unit Trust and ISA Products

It is Neptune's objective to sell suitable OEIC, Unit Trust and ISA products successfully to clients in both the retail, professional and institutional markets, primarily through fund supermarkets, life assurance companies, family offices and by direct contact with financial advisers, whilst providing good value, straightforward design and products that perform as clients and prospective clients have been led to expect.

2.1.2 Investment Management

Neptune seeks to provide these services by minimising its risk exposure as follows:

- Neptune as a company has no direct market/investment performance risk;
- the Neptune Funds' market/investment performance risk directly impacts the business's income and is mitigated through a stop-loss discipline triggered by a 20% fall in the price of a stock, at which point the relevant fund manager reviews the investment rationale for holding the stock. In a volatile market, the fund manager may use his / her discretion as price moves can be more dramatic;
- operational risk exposure is primarily through the outsourcing of: (i) transfer agency functions to a subsidiary of DST Systems Group, which is a leading global provider of investor and policy holder solutions; and (ii) custody and fund accounting functions to relevant subsidiaries of State Street Corporation, one of the world's leading providers of financial services to institutional investors; and

- Neptune has a low risk approach to selling practices, does not offer advice to customers and deals solely on an execution only basis when selling OEIC, Unit Trust and ISA products.

Neptune aims to minimise its risks through a combination of: (i) the structure and design of its products; and (ii) its strategy of appointing business partners with the relevant expertise, on whom strenuous due diligence and risk assessments have been, and continue to be, carried out. In addition, Neptune maintains appropriate insurance cover against a number of major operational risks.

At all times Neptune ensures that its capital resources do not fall below the regulatory required level at any point in the economic cycle. The monthly information pack reviewed at the regular Board meetings includes a three-year financial projection, which is regularly updated, and periodically includes severely stress-tested scenario modeling of a severe business downturn, plus an appropriate margin to allow for the normal variability in timings of cash flows.

2.2 Governance and Enterprise Risk Management Framework

The Enterprise Risk Management framework is part of the corporate governance arrangements within Neptune, which operate in a manner appropriate to the Company's risks, scale and nature of operations. The framework demonstrates control of the business, whilst facilitating transparency for Neptune's shareholders and clients.

2.3 Risk Management Processes

The risk management process is defined below. The risk appetite is set by the Board (see **2.1**), which receives, on a monthly basis, a management information pack designed to ensure that all relevant matters are considered and discussed. The framework that Neptune's directors and senior management follow to manage risks is:

- Board level (top-down) risk assessment, covering an analysis of corporate level risks that threaten the achievement of corporate and strategic goals and how these risks are mitigated.

- Internal Capital Adequacy Assessment Process ("**ICAAP**") that summarises the management of capital, including allocations to cover operational, and other, risks that could threaten capital adequacy.

- Risk appetite providing a benchmark level of acceptable risk against which residual risk levels should be compared.

- Department level (Bottom-up) Risk and Control Assessment, highlighting inherent and residual risks and how they are mitigated.

- Control Risk Self-Assessment, providing half-yearly positive assurance to the Board on the continuing adequacy of internal controls.

- Change Risk Assessment, which enables all business change to be risk assessed to ensure it is within Neptune's risk appetite and to ensure the ICAAP reflects any new risk level appropriately; and

- an Operations & Risk Committee consisting of at least two main board directors, together with representatives from Operations, Compliance, Finance, Legal, Human Resources, Investment, Fund Administration, Investor Services, Sales and Marketing departments.

2.4 Risk Management by Category of Risk

2.4.1 Credit Risk

Neptune has the following exposures to credit risk (that is, the risk that a party will default on a financial agreement):

- UK authorised banks in relation to cash reserves; and
- clients not settling management fees.

To mitigate these risks, Neptune:

- performs due diligence checks prior to entering into a material contract with counterparties;
- monitors on an on-going basis the financial strength of the credit institutions with whom it banks; and
- monitors receipt of income against agreed service level agreements.

Neptune applies the standardised approach to credit risk, applying 8% to the risk weighted exposure amounts, consisting mainly of investment management fees due but not paid and bank balances.

The capital requirement of Neptune is calculated as being the higher of its Base Capital resources requirement and its Variable Capital requirement.

For Neptune, this is its Variable Capital requirement, which is calculated as being the higher of its fixed overhead requirement ("**FOR**"), and the sum of its market and credit risk requirements. As detailed in **2.4.2** Neptune is currently not exposed to any material market risks.

2.4.2 Market Risk

Neptune has a low direct exposure to market risk in relation to stock market investments (market risk being the risks that arise from fluctuations in values of, or income from, assets or interest or exchange rates). This exposure arises from investment into seeding new funds and is monitored at the regular Board meetings. All new investment or divestment from a Neptune fund is authorised at Board level.

The assets under Neptune's control in respect of the authorised OEICs and Unit Trusts are held independently by trustees, for the benefit of the unitholders of those funds. The assets under Neptune's control in respect of the discretionary accounts are held independently by the custodians of each institutional client, for the benefit of each scheme.

Neptune's exposure to Market Risk relates to foreign exchange risk on outstanding debtors and accrued income. Neptune applies the standardised approach of 8% to the outstanding debts (see **2.4.1**).

Neptune manages clients' assets and the impact of market movements on managed assets is considered under **2.1**.

2.4.3 Operational Risk

As a limited licence firm, Neptune is not required to hold capital at Pillar 1 under the FCA's standardised approach to operational risk. Operational risk is defined by the FCA as the risk of loss resulting from inadequate or failed internal processes, people or systems or from external events, including legal risk.

At Neptune these risks are mitigated through an operational framework that comprises both policy and procedures that provide identification, assessment, mitigation, monitoring and reporting to the Board.

Such procedures are designed to protect Neptune from losses of a financial and reputational nature, in turn protecting shareholders, customers and staff. The framework is designed to ensure that the Company meets its regulatory requirements, as outlined in the FCA's High Level Standards, in particular SYSC.

Operational risks are recorded on Risk and Control Matrices and are reviewed half-yearly by senior management. The review will include all controls and their continuing adequacy and effectiveness. Neptune's Head of Operational Risk will collate the information and provide a summary to the Board for formal sign-off as required by the FCA.

If a residual risk for an area is outside the risk appetite of Neptune for the relevant risk type then management is required to implement mitigating actions to return the exposure to within the required tolerances. Additional mitigating actions or controls may also be implemented, after their consideration by the Board.

2.4.4 Securitisation Risk

Neptune does not have securitised assets and does not intend to securitise any assets in the foreseeable future and consequently has no exposure to securitisation risk.

2.4.5 Pension Obligation Risk

Neptune does not have a defined benefit pension scheme and as such is not exposed to the risks associated with the valuation of future pension liabilities. Therefore this is not considered to be a relevant risk.

2.4.6 Liquidity Risk

Liquidity risk is the risk that a firm, although solvent, either does not have available sufficient financial resources to enable it to meet its obligations as they fall due, or can secure them only at excessive cost.

Neptune holds only limited principal positions in relation to its seed investments (see 2.4.2), has no borrowing and has benefitted from continued generation of liquid cash reserves. These reserves and surplus of working capital requirements are held in cash and are readily realisable. Neptune has a liquidity policy to ensure it maintains sufficient liquid assets to meet expected cash flow requirements of the business. A rolling 12-month cash flow forecast is reviewed by the Board at its regular meetings.

It is the opinion of the Board that Neptune maintains liquid resources which are adequate, both as to amount and quality to ensure that there is no significant risk that its liabilities cannot be met as they fall due.

2.5 Assurance process

On an annual basis, Neptune commissions an independent firm of external auditors to perform testing on the integrity of the control environment. Neptune reports against the framework set out in the technical release AAF 01/06 issued by the Audit and Assurance Faculty of the Institute of Chartered Accountants in England and Wales.

The last review undertaken was for the year to 20 June 2017. A copy of the final report is available on request in writing from the Chief Financial Officer, Neptune Investment Management Limited, 3 Shortlands, Hammersmith, London W6 8DA.

3. Capital Resources

3.1 Regulatory capital as at 31 December 2017

Common Equity Tier 1	£7,763,000

Neptune does not hold any other form of capital (Additional Tier 1, Tier 2)

3.2 Common Equity Tier 1 Capital

Common Equity Tier 1 capital represents Ordinary Share Capital, Share Premium Account, Distributable Reserves and accumulated Profit and Loss Account balances as at 31 December 2017 and is reduced for any foreseeable losses and dividends.

3.3 Transferability of capital

There are currently no foreseen impediments to the prompt transfer of capital within the Group or payment of Group liabilities.

4. Capital Adequacy

4.1 Internal Capital Adequacy Assessment Process (“ICAAP”)

Under Pillar 2 of the CRD the FCA sets regulatory obligations that require all firms to have an ICAAP.

This requires Neptune to:

- carry out regular assessments of the amounts, types and distribution of financial resources, capital resources and internal capital that it considers adequate to cover the nature and level of the risks to which it is or might be exposed;
- identify the major sources of risk to its ability to meet its liabilities as they fall due;
- conduct stress and scenario tests;
- ensure that the processes, strategies and systems required by the overall Pillar 2 rule, and used within its ICAAP, are both comprehensive and proportionate to the nature, scale and complexity of Neptune’s activities; and
- document its ICAAP.

The Neptune ICAAP is integrated into the business by:

- a half-yearly review of the departmental risk and control matrices and consideration of whether any changes warrant review of the ICAAP; alongside the normal cycle of FCA financial reporting;
- an annual update of the ICAAP within the annual strategy and budgeting process, including a fundamental review of risk assumptions and revised strategic targets;
- review and challenge of the annual ICAAP by the Audit Committee and the Board;
- immediate update of the ICAAP if there are material changes to Neptune’s risks;
- consideration of individual ICAAP guidance from the FCA; and
- consideration of updated ICAAP guidance from peer practices and industry bodies.

4.2 Minimum Capital Requirement – Pillar 1

As a limited licence BIPRU firm, Neptune’s Pillar 1 requirement is its Variable Capital requirement and is determined as the higher of its FOR, or sum of market and credit risk requirements (see **2.4** above). As at 31 March 2018 the capital resources requirement of the Firm was the FOR.

4.3 Pillar 2 Assessment

As part of its ICAAP review and as required by the FCA Rules, Neptune has carried out a detailed internal assessment of the risks it faces and resultant capital that it believes it should hold. The risks considered can be classified under the heading of credit and operational risks. The Company has very low exposure to market risk, as investment assets predominantly belong to the unitholders, rather than Neptune (see **2.4.2**).

Neptune's assessment of capital required at Pillar 2 concludes that no additional capital was required over and above the Pillar 1 assessment. Internal models have been used rather than the FCA's standardised approach to evaluate these risks, including stress testing, scenario, and a wind down analysis.

5. Remuneration Code

5.1 Remuneration code disclosure

Neptune is subject to the FCA's Remuneration Code (the "**Code**"), as set out in SYSC of the FCA Handbook. The Code sets out a number of requirements and principles in respect of the total remuneration received by staff of firms that are governed by the Code, including both fixed and variable remuneration. Neptune incentivises its staff through a combination of the two.

Neptune's policy is designed to ensure that it complies with the Code and that, in accordance with the Code, its remuneration arrangements:

- are consistent with and promote sound and effective risk management;
- do not encourage excessive risk taking;
- include measures to avoid conflicts of interest; and
- are in line with Neptune's business strategy, objectives, values and long-term interests.

5.2 Proportionality

Enshrined in the CRD's requirements regarding remuneration is the principle of proportionality. The FCA has sought to apply proportionality in the first instance by categorising firms into three levels, depending on their business activities and total amount of regulatory capital that they hold, with certain remuneration requirements applying differently between each tier. Neptune is treated as a "Level 3" firm and this disclosure is made in line with the relevant requirements applicable to such firms.

5.3 Application of the requirements

Neptune is required to disclose certain information on at least an annual basis regarding its remuneration policy and practices for those staff whose professional activities have a material impact on the risk profile of Neptune. This disclosure is made in accordance with Neptune's size, internal organisation and the nature, scope and complexity of its activities.

5.4 Pillar 3 Remuneration Disclosure

Neptune's policy has been agreed by its Remuneration Committee ("RemCo"), which consists of independent non-executive directors, in line with the Code principles laid down by the FCA. The policy is reviewed on an annual basis or as a result of a significant change to the business. The Audit Committee, which is also comprised of independent non-executive directors, receives information on the risk and compliance profile of the Company, including the levels of regulatory capital that it holds. The RemCo takes into account the findings and conclusions of the Audit Committee regarding Neptune's risk and compliance profile when considering individual and aggregate annual awards of variable remuneration.

All staff are remunerated by way of a mixture of fixed and variable compensation. Fixed remuneration is represented by a base salary for each employee, which is reviewed on an annual basis and is targeted around the market median for the respective role. Any increase in fixed compensation is also linked to the performance of the relevant employee, which is assessed through ongoing and annual appraisal processes.

The variable element of an employee's remuneration recognises their performance and the individual's compliance with internal policies and procedures and his/her commitment to the fair treatment of Neptune's customers. The aggregated variable element of the remuneration paid by Neptune is considered in the light of, and tested against, the need to maintain sufficient regulatory capital, deliver an appropriate return to shareholders and ensure the financial stability of the Company.

5.4.1 Bonus schemes

Neptune operates three bonus schemes, one for each of the following teams of staff and management:

a) The Investment team

The annual bonus pool ("**Pool**") is calculated as a percentage of the profits of Neptune. Allocation of the Pool takes account of three components of performance: relative investment performance; fund profitability and; research, including contribution to the team.

b) The Sales team

Sales commission for the team is based on the sales achieved. The bonus pool is discretionary in nature and is allocated based on performance and contribution to the team, including measures to assess adherence to Neptune's Treating Customers Fairly policy and other measurements relating to good team behaviour.

c) The Executive Management, Administration and Operations teams

Members of the above teams are eligible for discretionary annual bonuses related to their individual and team performance. Individual cash bonuses are on an entirely discretionary basis.

d) *Equity Participation Plan*

Under this plan, a significant proportion of the annual bonus awarded to employees can be awarded to them in the form of deferred equity. The deferred equity awards are in the form of a nil-price option to acquire ordinary shares in Neptune. The awards will vest on the third anniversary of the date of grant. The plan provides that additional shares be awarded to participants, on vesting, in respect of dividends paid after the date of grant. The value of each award will typically represent 50% of the participant's variable remuneration.

5.4.2 Executive Incentive Schemes

Neptune currently operates the following employee incentive scheme:

Share Option Plan

All employees of Neptune participate in the Share Option Plan once their probationary period has passed. This is approximately 65 employees in total, with the number of options awarded being linked to seniority of the employee. The award is in the form of an entitlement to buy shares in Neptune at a fixed option exercise price which is determined when the award is granted. There are no performance criteria, but the gain to the participant depends on the extent to which the value of Neptune's shares increases above the exercise price. The earliest an option can be exercised is five years from grant. The participants are not permitted to sell more than a certain number of shares per year once an option has been exercised. This limit is determined by capital adequacy considerations and all transactions require authorization at Board level.

5.4.3 Quantitative remuneration information

Aggregate quantitative information on remuneration for the financial year ended 31 December 2017 was as follows:

Business Area	Investment Management
Aggregate remuneration expense	£10,183,000
Number of staff remunerated	75

Aggregate quantitative information on remuneration for the financial year ended 31 December 2017 for senior management and other members of staff whose actions have a material impact on the risk profile of Neptune was as follows:

Aggregate remuneration expense		£4,742,000
Consisting of:		
Fixed remuneration		£3,059,000
Variable remuneration:	Cash	£1,167,000
	Share-linked	£460,000
	Other	£56,000
Number of senior managers/staff remunerated		14

Neptune Investment Management Limited
26th June 2018