

Montanaro Asset Management Ltd

**Public disclosures under the
FCA's Investment Firms
Prudential Regime ("IFPR")**

30 September 2023

(Prepared based on data as at 31 December 2022)



MONTANARO

INTRODUCTION AND CONTEXT

The Investment Firms Prudential Regime (IFPR) is the FCA's new prudential regime for MiFID investment firms which aims to streamline and simplify the prudential requirements for UK investment firms. IFPR came into effect on 1st January 2022, and its provisions apply to Montanaro Asset Management Limited (MAM or the firm) as an FCA authorized and regulated firm.

The public disclosure requirements of IFPR are set out in MIFIDPRU 8, replacing the previous Pillar 3 requirements under BIPRU 11.

MAM can be classified as a non-SNI firm given it breaches at least one of the requirements set out in MIFIDPRU 1.2.1 R to qualify as an SNI firm. In this case, the firm has crossed the following threshold:

- Average AUM of MiFID business exceeds the FCA's threshold of £1.2 billion

However, MAM qualifies as a smaller non-SNI, due to the average balance sheet size being less than £100 million over the previous four-year period.

MAM is required to disclose the following information:

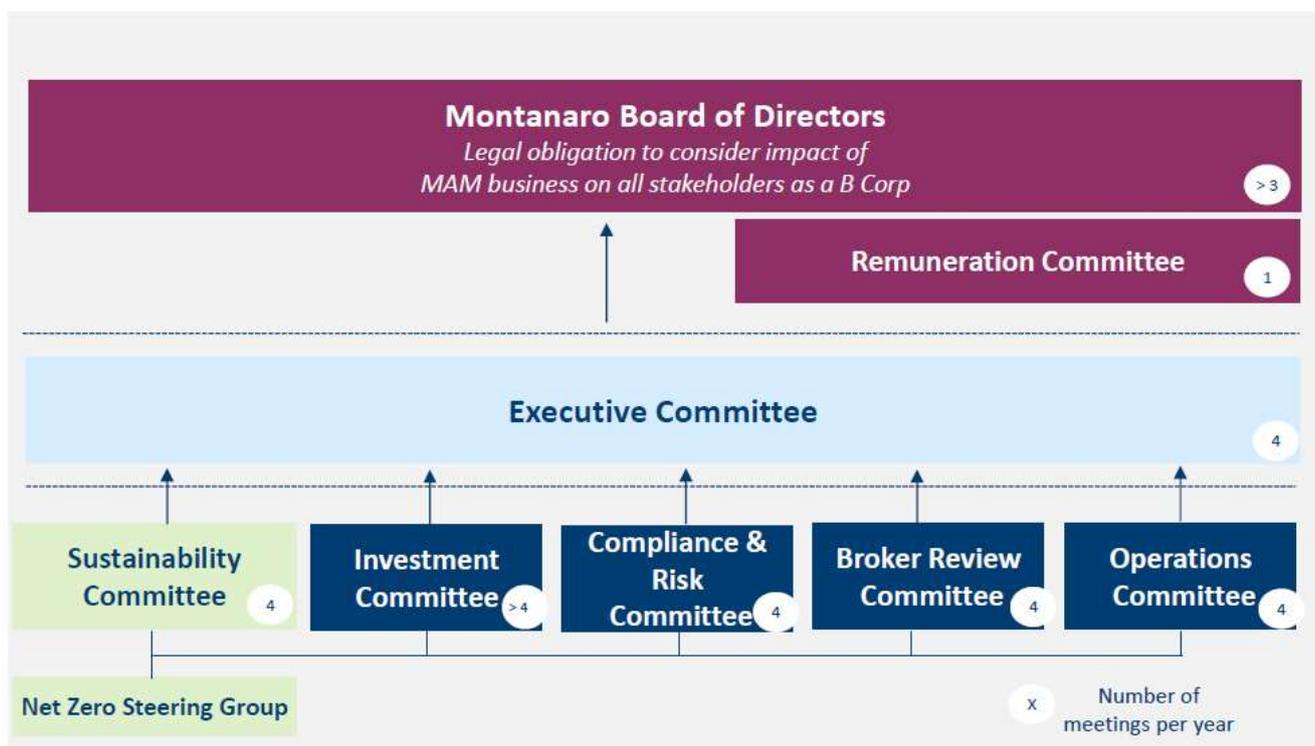
- **Governance arrangements** (MIFIDPRU 8.3): non-SNI firms are required to disclose certain information including:
 - An overview of the firm's governance arrangements;
 - The number of directorships held by each member of the governing body (this only applies to directorships of commercial enterprises, charities and directorships of other group entities are excluded);
 - A summary of the firm's policy on promoting diversity in the governing body;
 - Whether the firm has established a risk committee .
- **Own Funds** (MIFIDPRU 8.4): firms must provide details of their Own Funds (using the template provided in MIFIDPRU 8 Annex 1R), and a reconciliation of the same information in the firm's report and accounts (where available).
- **Own Funds Requirements** (MIFIDPRU 8.5): firms must disclose details of their Own Funds Requirements including the Fixed Overhead Requirement (FOR) and a breakdown of their K-factor requirements (non-SNI only). All firms are also required to disclose their approach to assessing their compliance with the overall financial adequacy rule (MIFIDPRU 7.4.7R).
- **Risk Management** (MIFIDPRU 8.2): firms must disclose their risk management objectives and policies in respect of the following categories of risk addressed by:
 - MIFIDPRU 4: Own Funds Requirements;
 - MIFIDPRU 5: Concentration Risk; and
 - MIFIDPRU 6: Liquidity.

- **Remuneration Policy and practices** (MIFIDPRU 8.6)
 - Provision of quantitative and qualitative disclosures in respect of the firm’s remuneration arrangements.

GOVERNANCE ARRANGEMENTS

The Board

The Board has adopted a risk management governance structure comprising of the board and management committees to provide review, challenge and oversight of the firm’s risks. The link between the Board and its committees is shown below:



Source: Internal.

MAM’s Board of Directors is composed of two independent Non-Executive Directors, Heather Manners and Katrina Hart, and four Executive Directors, Charles Montanaro (Chair), Cédric Durant des Aulnois, Mark Rogers and George Cooke.

In addition, the Board benefits from the counsel of Debbie Hewitt, an independent adviser with a wealth of experience across multiple industries.

The Board meets formally at least three times a year and informally at least once. Meetings are typically held in:

- January – The Board discusses the strategic priorities for the year included in the State of the Nation presentation given to all staff at the start of each year. In addition, the Remuneration Committee meets to review and approve the remuneration of the Executive.
- April – Approval of the year-end accounts.

- September
- December (informal meeting).

Additional Board Meetings are held as required.

The Directors review all aspects of the business including personnel decisions, remuneration, product and business strategy, investment performance, financial reporting, risk management, compliance and cyber-security risk.

Special matters may also arise at any given Board Meeting such as the approval of interim / year-end Financial Statements or the appointment of Auditors.

Committees

The **Remuneration Committee**, comprised of Charles Montanaro, Cédric Durant des Aulnois, Heather Manners (Chair) and Katrina Hart, meets every year in January to review the remuneration of the Executive. The Committee is chaired by Heather Manners.

The **Executive Committee**, composed of Cédric Durant des Aulnois (Chair), Charles Montanaro, Mark Rogers, George Cooke, Tom Norman-Butler, Ed Heaven and Matthew Francis, meets at least four times a year to discuss matters arising in the management of the business.

The **Investment Committee**, composed of Charles Montanaro (Chair), Mark Rogers, George Cooke and Alex Magni, meets at least four times a year to review key changes to the Portfolios. In addition, the Investment Committee closely reviews all new investment ideas and has the ultimate authority for companies to be added to the Approved List.

The **Sustainability Committee**, composed of Ed Heaven (Chair), Cedric Durant des Aulnois, Mark Rogers, Nere Asumendi, Sarah Bridges, Kate Hewitt, Manroop Bal and Rachel Herry, sets all ESG and ethical policies, monitors engagement with companies and reviews voting procedures.

The **Compliance & Risk Committee**, composed of Matthew Francis (Chair), Jeremy Law, Sarah Bridges and Laura Denny, meets at least four times a year to review all aspects relating to investment risk, regulation and compliance.

The **Operations Committee**, composed of John Ensor (Chair), Gareth Bateman and Mark Petar, reviews all operational aspects relating to fund administration, technology and cyber-security.

The **Broker Review Committee**, composed of Gareth Bateman (Chair), Cedric Durant des Aulnois, Mark Rogers, Matthew Francis, George Cooke and John Ensor, reviews MAM's relationships with brokers, monitors the quality of execution, reviews trading costs and threshold disclosures.

Diversity

MAM is committed to providing a workplace that seeks and respects diversity and inclusion at every level of the business including the executive and non-executing Board members. We believe that anyone who joins the business should benefit from the opportunity to develop, progress, and succeed within the company. We are at the start of this journey and recognise that recruiting and retaining a truly diverse and inclusive workforce requires long term commitment from across the business.

Directorships

The following directors have held office in executive and non-executive functions throughout the financial year ending 31st December 2022. Please note that MAM is a solo entity.

Name	Group Directorship	Other Directorship in scope of MIFIDPRU 8.3.1R(2)
Charles Montanaro Chair	N/A	0
Cedric Durant des Aulnois CEO	N/A	0
Mark Rogers Head of Investments	N/A	0
George Cooke Head of Fund Management	N/A	0
Katrina Hart Non-Executive Director	N/A	5
Heather Manners Non-Executive Director	N/A	4

RISK MANAGEMENT

Approach to Risk Management

Risk management at MAM is the joint responsibility of the Compliance & Risk Committee and the Head of Compliance, Risk & Administration, Matthew Francis (who also chairs the Committee). Matthew is a permanent member of the Executive Committee and reports directly to the Board of Directors.

The Compliance & Risk Committee meets quarterly to review all aspects of Company-level and investment risk. The members of the Committee are:

- Matthew Francis (Chairman);
- Sarah Bridges (Compliance Manager);
- Laura Denny (Compliance Analyst);
- Jeremy Law (Risk Analyst).

In addition, the following people typically attend the meetings for certain agenda items:

- Cédric Durant des Aulnois (Chief Executive Officer);
- Mark Rogers (Head of Investments);
- Gareth Bateman (Chair of the Broker Review Committee).

The Committee reviews all aspects linked to regulatory risk, investment risk and threshold crossing disclosures. The Committee also reviews and updates the Risk Register.

In addition, the Joint Liquidity Committee, which is a sub-committee of the Compliance and Risk Committee, meets quarterly to monitor stock specific liquidity and set appropriate internal restrictions on illiquid holdings. The Joint Liquidity Committee comprises members of the Risk and Compliance Committee the Investment Committee, and the CEO.

Separately, MAM has an Operations Committee which is chaired by John Ensor, Head of Operations. This Committee also meets quarterly and reviews other aspects of operational risk including: risk relation to fund administration matters, trading risk and IT & Cyber risk. Matthew Francis attends Operations Committee meetings.

The minutes of both the Compliance & Risk Committee and the Operations Committee are reviewed by the Executive Committee.

As risk-averse investors, we do not use derivatives; do not engage in hedging; do not engage in short-selling; do not lend stock; and do not invest in any asset classes other than quoted global Small & MidCap.

Risk Appetite Setting

The main risks to MAM are a loss of client assets or a decline in Stock Markets (as most fee income is based on portfolio valuations), either or both of which would result in reduced revenues. This might impact the ability to invest in MAM as required and to retain staff.

Given the cyclical nature of its business, MAM has always been managed conservatively. The business has no bank debt or debt due to other external third parties. It maintains significant cash balances at all times.

In addition, MAM does NOT:

- make use of derivatives;
- engage in hedging;
- engage in short-selling;
- lend out shares held by its open-ended Funds or investment trusts;
- invest in MicroCap companies;
- invest in private or unquoted assets;
- invest in any asset classes other than quoted global Small & MidCap.

MAM far exceeds its basic regulatory capital requirements which are necessary for the prudential running of its business. This is because of the following factors:

- MAM holds cash balances many times greater than its fixed overhead requirement;
- within its regulated activities, MAM assumes no market risk;
- MAM has a diverse and growing client base; and
- MAM's clients are geographically well diversified.

MAM has a low appetite for risk which will not change in future.

Key Risks

We have identified the potential risks and harms to MAM's clients, the markets, and to MAM itself by considering plausible hypothetical scenarios that might occur in relation to the activities that MAM carries out. These are recorded in our Risk Register, which is maintained by the Compliance & Risk Committee and formally reviewed annually by the Board.

The primary material risks to clients and to MAM are due to poor performance, either due to the markets or the under-performance of MAM's Funds. This would lead to lower returns and a loss of capital for investors, and in turn to a reduction in fee income to MAM. This could impact the quality of MAM's service and ability to retain staff, and reputational damage would also make it more difficult to attract and retain new investors, compounding the issue and eventually leading to the business becoming unviable.

There is also the risk of cyber-crime causing a significant financial loss to both clients and to MAM.

A summary of the potential material risks and harms to clients and to MAM itself is below. Due to the size and nature of the business, it is unlikely that MAM would cause material harm to the markets.

Material risks and harms to Clients		
Risk	Potential Harm	Recovery Action/Additional Own Funds
Prolonged underperformance in one or more products	<i>Reduced returns and loss of capital</i>	<i>Review and/or replace Fund Manager, review strategy/investment process/Approved List.</i>
Lower markets (which could lead to the above underperformance)	<i>Reduced returns and loss of capital</i>	<i>Communication with existing clients, increased marketing activity. All clients in MAM's open-ended Funds have the option to redeem without any notice. MAM's investment trust clients can sell their shares on the secondary market. MAM's segregated mandate clients can typically redeem part of their investment with little notice.</i>
Prolonged absence of Charles Montanaro	<i>Pre-emptive redemptions from clients</i>	<i>Communication with existing clients, increased marketing activity.</i>
Cyber Crime	<i>Client may suffer system outages, client data could be compromised / lost, clients may be unable to place trades or loss of assets through fraud</i>	<i>Note: MAM does not hold client cash or client assets so there is minimal risk of a financial loss to clients originating from MAM's own systems being compromised.</i>

	<i>involving MAM service providers (administrator, custodian, Charles River).</i>	<i>All clients may need to be contacted. Potential legal action against MAM's service providers. Although MAM has recently invested in best-in-class systems which reduce the likelihood and scope of a potential cyber attack, further investments may be warranted. Similarly, additional staff training may be required.</i>
Material risks and harms to MAM		
Risk	Potential Harm	Remedial Actions/Additional Own Funds
Prolonged underperformance in one or more products	<i>Reduced fee income, reputational damage, more difficult to attract and retain clients, loss of clients</i>	<i>Review and/or replace Fund Manager, review strategy/investment process/Approved List. Consider closing fund if in the interest of shareholders.</i>
Lower markets (which could lead to the above underperformance)	<i>Reduced assets leading to reduced fee income, more difficult to attract and retain clients, loss of clients</i>	<i>Increased cost control (including reduction in staff bonuses). Reduction in discretionary investments e.g. advertising. Stress tests demonstrate that MAM could comfortably continue to operate following a 50% reduction in revenue year-on-year for at least 3 years.</i>
Strategy becomes unattractive (which could be as a result of the above)	<i>More difficult to attract and retain clients, loss of clients leads to reduced assets and a reduction in fee income</i>	<i>Launch of new products; changes to existing products to increase their attractiveness to investors. Increased cost control (including reduction in staff bonuses). Stress tests demonstrate that MAM could comfortably continue to operate following a 50% reduction in revenue year-on-year for at least 3 years.</i>
Significant client withdrawals (which could be a result of the above, or could be due to a single large investor withdrawing for another reason, for example if their business fails)	<i>Reduced assets, leading to a reduction in fee income</i>	<i>Increased cost control (including reduction in staff bonuses). Reduction in discretionary investments e.g. advertising. Stress tests demonstrate that MAM could comfortably continue to operate following a 50% reduction in revenue year-on-year for at least 3 years.</i>

Decline in fees (which could be as a result of the above risks)	<i>A decline in fees is the main risk to MAM as this is where the company's income comes from and would impact whether the business continued to be viable</i>	<i>Increased cost control (including reduction in staff bonuses). Reduction in discretionary investments e.g. advertising. Stress tests demonstrate that MAM could comfortably continue to operate following a 50% reduction in revenue year-on-year for at least 3 years.</i>
Prolonged absence of Charles Montanaro	<i>More difficult to attract and retain clients, loss of clients leads to reduced assets and a reduction in fee income</i>	<i>Investment Committee and Co- / Back-up Fund Managers to provide cover for Charles. Significant increase in client communication and marketing effort. Stress tests demonstrate that MAM could comfortably continue to operate following a 50% reduction in revenue year-on-year for at least 3 years.</i>
Cyber-crime	<i>System outages, data compromised or lost, financial loss through fraud or blackmail, fines, reputational damage</i>	<i>Note: MAM does not hold client cash or client assets so there is minimal risk of a financial loss to clients originating from MAM's own systems being compromised. All clients may need to be contacted. Potential legal action against MAM's service providers. Although MAM has recently invested in best-in-class systems which reduce the likelihood and scope of a potential cyber attack, further investments may be warranted. Similarly, additional staff training may be required.</i>
Material risks and harms to the Market		
None identified		

Approach to assessing the effectiveness of the Risk Management Function

The risk framework detailing the key risks to MAM, clients and the markets and the mitigation in place is drawn up by the Risk Team. The MAM Board review this formally at least once a year and will question anything they feel requires further investigation. The risks are monitored by the Compliance and Risk Committee, who review the framework at the quarterly Committee meetings. Any new risks arising during the year or any changes to the existing ones are discussed, as well as whether the mitigation measures in place remain sufficient.

OWN FUNDS

Composition of Own Funds

Template OF1 - Composition of regulatory own funds		
Item	Amount {GBP thousands}	Source based on reference numbers/letters of the balance sheet in the audited financial statements
OWN FUNDS	66,927	
Tier 1 Capital	66,927	
Common Equity Tier 1 Capital	66,927	
Fully paid-up capital instruments	578	Note 22
Share premium	1,805	Note 23
Retained earnings	64,544	Statement of change in equity
Accumulated other comprehensive income		
Other reserves		
Adjustments to CET1 due to prudential filters		
Other funds		
(-) TOTAL DEDUCTIONS FROM COMMON EQUITY TIER 1	0	
CET1: Other capital elements, deductions, and adjustments		
Additional Tier 1 Capital	0	
Fully paid up, directly issued capital instruments		
Share premium		
(-) TOTAL DEDUCTIONS FROM ADDITIONAL TIER 1		
Additional Tier 1: Other capital elements, deductions, and adjustments		

Tier 2 Capital	0	
Fully paid up, directly issued capital instruments		
Share premium		
(-) TOTAL DEDUCTIONS FROM TIER 2		
Tier 2: Other capital elements, deductions, and adjustments		

Reconciliation to audited financial information

The table below shows a reconciliation with own funds in the balance sheet where assets and liabilities have been broken down by asset and liabilities classes respectively. The information in the table below reflects the balance sheet in the audited financial statements.

Template OF2: Own funds: reconciliation of regulatory own funds to balance sheet in the audited financial statements				
Flexible template - rows to be reported in line with the balance sheet included in the audited financial statements of the investment firm. Columns should be kept fixed, unless the investment firm has the same accounting and regulatory scope of consolidation, in which case the volumes should be entered in column (a) only. Figures should be given in GBP thousands unless noted otherwise.				
		a	b	c
		Balance sheet as in published/audited financial statements	Under regulatory scope of consolidation	Cross reference to template OF1
		As at period end	As at period end	
Assets - Breakdown by asset classes according to the balance sheet in the audited financial statements				
1	Tangible fixed assets	1,257		
2	Investments	50		
3	Debtors-within one year	10,946		
4	Current asset investments	47,502		
5	Cash at bank and in hand	27,114		

	Total Assets	86,869		
Liabilities - Breakdown by liability classes according to the balance sheet in the audited financial statements				
1	Creditors – due within one year	14,738		
2	Creditors – due more than one year	2,644		
3	Deferred taxation	2,560		
	Total Liabilities	19,942		
Shareholders' Equity				
1	Called up share capital	578		
2	Share premium	1,805		
3	Retained earnings	64,544		
	Total Shareholders' equity	66,927		

Main features of MAM's Own Funds instruments

The table below provides information on the CET1 Instruments used by Montanaro Asset Management Ltd. These are the only capital instruments.

Table: main features of own instruments issued by the Firm:

Public or private placement	Private
Instrument type	Ordinary share
Amount recognised in regulatory capital (GBP thousands, as of most recent reporting date)	£578k
Nominal amount of instrument	£578k
Issue price	£1 / 10p
Redemption price	N/A
Accounting classification	Called Up share capital
Maturity date	N/A
Dividends	Fully Discretionary

OWN FUNDS REQUIREMENT

REQUIREMENT	[£'S]
PERMANENT MINIMUM REQUIREMENT	75,000
FIXED OVERHEAD REQUIREMENT	2,038,000
TOTAL K-FACTOR REQUIREMENT	726,000
SUM OF K-AUM, K-CMH AND K-ASA	726,000
SUM OF K-COH AND K-DTF	0
SUM K-NPR, K-CMG, KTCO AND K-CON	0

Overall Financial Adequacy

The internal capital adequacy and risk assessment process (the “ICARA process”) is the core risk management process for FCA investment firms. The ICARA process is a continuous assessment of the harm a firm may pose to clients and markets as part of its ongoing business and during wind-down.

The ICARA process document and associated external disclosures have been reviewed in detail by senior management and therefore has had senior management input throughout the document’s development.

The ICARA will be refreshed on at least an annual basis, typically in conjunction with the annual budgeting process, and in the event of a material change in the business activities or operating model of the Company.

To ensure MAM meets its ongoing capital needs and liquidity requirements, these will be reviewed each month in the management accounts which are distributed to the Management Committees and the Board.

On this basis the Board are satisfied that MAM has sufficient own funds and liquid assets to meet its Overall Financial Adequacy Rule (OFAR) both as to amount and quality to ensure that:

- a) it is able to remain financially viable throughout the economic cycle, with the ability to address material potential harm that may result from its ongoing activities; and
- b) its business can be wound down in an orderly manner, minimising harm to consumers or to other market participants.

REMUNERATION

Qualitative Disclosures

The aim of MAM's Remuneration Policy is to ensure that the remuneration arrangements reward employees appropriately, but also promote sound and effective risk management. In particular, the remuneration arrangements aim to avoid rewarding excessive risk-taking, (either on behalf of MAM, or on behalf of any funds or mandates we manage for customers). It is also designed to ensure that, when taking decisions about remuneration, the impact of reward arrangements on MAM's long-term sustainability are considered.

The total variable remuneration pool is set at the start of each calendar year and determined based on MAM's financial performance in the prior year. In addition to their base salary, employees may be eligible to receive variable compensation that reflects performance in excess of that required to fulfil their job description and terms of employment.

All employees are eligible to receive a bonus. However, bonuses are by nature entirely discretionary and must reflect the individual's performance in the previous year.

Employees may receive:

1. An Ordinary Discretionary Bonus ("OB") made up of the following:
 - a) Up to 30% of their Base Salary in recognition of MAM's overall performance and outlook. This figure is determined by the REMCO.
 - b) Up to 70% of their Base Salary in recognition of personal achievement during the year (as agreed with the individual Line Manager and documented in the year-end appraisal form).
2. An Extraordinary Discretionary Bonus ("EB") in the event that MAM receives a Performance Fee during the year (one third of any Performance Fees are distributed to staff). The EB is made up of two components:
 - a) A Cash Extraordinary Bonus;
 - b) A 3-year Loyalty Bonus ("LB") – such bonus is to be invested in units of Funds or Investment Trusts managed by MAM. The recipient decides how to allocate their LB. Fund Managers must allocate up to 75% of their LB towards Funds or Investment Trusts they manage personally. On the third anniversary of award, the employee may choose to either: i) receive the units; or ii) receive the cash equivalent of the value of the units at the time.

Employees are entitled to receive the deferred portion of variable remuneration only if they remain employed with MAM at the time of vesting. Loyalty Bonuses are subject to clawback to the extent that part or all of the Bonus can be clawed back should the recipient become the subject of a disciplinary hearing.

MAM will base the total amount of remuneration on an assessment of the performance of the employee, the business unit and the Firm's overall results.

When assessing individual performance, both financial and non-financial criteria will be taken into account, including effective risk management, compliance with regulations and appropriate conduct in line with the Firm's values. Poor performance in non-financial criteria will impact financial performance metrics.

MAM will not award guaranteed variable remuneration for employees unless:

- It is on an exceptional basis;
- It is for a new appointment;
- It is limited to the first year of service.

MAM will ensure that any remuneration packages relating to compensation for, or buy out from, an employee's contract with a previous employer, is in the long-term interests of the company and is subject to retention, deferral, performance, and claw back arrangements.

MAM will also ensure that any payments relating to early termination of a contract reflect the performance achieved over time and do not reward failure or misconduct.

The Remuneration Committee, a sub-committee of the Board of MAM, ensures that the total variable compensation paid out in any given year is consistent with the company's financial performance in the previous year. Variable compensation will only be awarded when it is sustainable to the Firm's overall financial situation and taking into account any known future events, the performance of the company, the business unit, and the employee.

Quantitative Disclosures

	Fixed remuneration	Variable remuneration	Total remuneration
Senior Management	1,330,000	1,580,000	2,910,000
Other Material Risk Takers	677,500	685,000	1,362,500
Other staff	1,776,500	1,545,000	3,321,500
Total	3,784,000	3,810,000	7,594,000

	Total amount of guaranteed variable remuneration awarded	Number of Individuals
Senior Management	N/A	0
Other Material Risk Takers	N/A	0

	Total amount of severance payments awarded	Number of individuals
Senior Management	N/A	0
Other Material Risk Takers	N/A	0

Highest severance payment awarded to an individual Material Risk Taker	N/A
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