Hayfin Emerald Management LLP

MIFIDPRU 8 Disclosure

October 2024

1. Introduction

The Financial Conduct Authority ("FCA" or "Regulator") in its Prudential Sourcebook for MiFID Investment Firms ("MIFIDPRU"), sets out the detailed prudential requirements that apply to Hayfin Emerald Management LLP ("HEM" or the "Firm"). In particular, Chapter 8 of MIFIDPRU ("MIFIDPRU 8" or the "public disclosures requirements") sets out public disclosure obligations with which the Firm must comply.

Hayfin Emerald Management LLP ("HEM") is classified under MIFIDPRU as a non-small and non-interconnected investment firm ("non-SNI MIFIDPRU investment firm"). Accordingly, MIFIDPRU 8 requires the Firm to disclose information on the following areas:

- Risk management objectives and policies;
- Governance arrangements;
- Own funds;
- Own funds requirements; and
- Remuneration policy and practices.

This document has been prepared by HEM in accordance with the requirements of MIFPRU 8. Unless otherwise stated, all figures are current as at the 31 December financial year-end.

2. Risk Management Objectives and Policies

This section describes HEM's risk management objectives and policies for the following categories of risk.

- Own funds requirement;
- Concentration risks; and
- Liquidity.

Business Strategy

HEM acts as an originator and investment manager of European collateralised loan obligation ("CLO") vehicles. Appointments as manager to CLO vehicles are governed by Collateral Management Agreements ("CMA") which, inter alia, set the investment criteria, management fees payable and notice periods. Appointments to warehoused vehicles are governed by Warehouse Agreements, which do not yield management fees. The CMA may only be terminated for cause, which is narrowly defined to include such conduct as wilful breach, fraud or insolvency of the manager.

HEM is a MiFID regulated investment manager and typically satisfies risk retention requirements via the manager originator route. HEM complies with applicable EU risk retention requirements by holding at least a 5% net economic interest in the CLO vehicles that it manages. HEM has the flexibility to hold vertical or horizontal retention strips of CLO structures, but generally holds the retention vertically.

HEM considers that the duality of its position of both acting as investment manager to and holding the risk retention in CLO vehicles, is complementary such that HEM is best placed to maximise performance on behalf of clients. A positive outcome also serves to maximise revenues receivable by HEM as well as preserve HEM's on-balance sheet exposure.

HEM is part of Hayfin Capital Management group, the ultimate parent company of which is Hayfin Capital Holdings Limited ("Hayfin"). Hayfin is a private credit alternative asset manager, headquartered in London. HEM has an intercompany agreement with HCM, a member of the Hayfin group, which provides services to HEM including employees, operations, technology infrastructure and office space.

The Firm's costs are carefully controlled to maintain and ensure long-term profitability with investments made, as appropriate, to expand the business and associated systems and controls.

Considering the Firm's business model, controls, and controls assessment, it is the conclusion of the Firm that its overall potential for harm is low.

Risk management

HEM has established a risk management framework to ensure that it has effective systems and controls in place to identify, assess, manage, monitor and report risks arising in the business. The Executive Committee has ultimate responsibility for the effectiveness of risk management in Hayfin. The overall responsibility for oversight of the non-investment risk framework lies with the Audit and Risk Committee. The day-to-day implementation of the risk management framework, together with the responsibility for the implementation and enforcement of the Firm's risk principles, is overseen by the Risk and Compliance Committee. The Risk and Compliance functions provide independent oversight of the business areas and management. This includes monitoring non-compliance with risk appetite-based limits and any failure to manage, mitigate and escalate risk events appropriately. The Risk and Compliance teams produce management information that is provided to the risk committees to assist in supporting these control functions

To provide a uniform and structured approach to identification and classification of risk across Hayfin, risks are categorised under Strategy/Business, Investment, Financial and Operational Risks. HEM's approach is to identify and assess specific risks within these groups, mitigate and manage these risks, and monitor and report against these risks which provides the foundation to enable us to deliver against our strategic objectives. A library of risks sits below each risk group, and these risks and their definitions are subject to periodic review to ensure they remain relevant to the internal and external environment within which Hayfin operates.

Effective risk management is key to the success of delivering HEM's strategic objectives. The primary objectives of risk management at Hayfin are to ensure that there is:

- A strong risk culture so that employees can identify, assess, manage and report against the key risks the business is faced with;
- An appropriate balance between risk and the cost of control;
- A defined risk appetite within which risks are managed; and

- A swift and effective response to incidents to minimise impact.

Own Funds Requirement

HEM is required to always maintain own funds that are at least equal to the Firm's own funds requirement. The own funds requirements are the higher of the Firm's:

- **Permanent minimum capital requirement ("PMR")**: The PMR is the minimum level of own funds required to operate at all times and, based on the MiFID investment services and activities the Firm currently has permission to undertake, is set at €75,000;
- **Fixed overhead requirement ("FOR"):** The FOR is intended to calculate a minimum amount of capital that HEM would need available to absorb losses if it has cause to wind-down or exit the market, and is equal to one quarter of the Firm's relevant expenditure; and
- **K-Factor requirement ("KFR"):** The KFR is intended to calculate a minimum amount of capital that HEM would need available for the ongoing operations of its business. The K-factor that applies to the Firm's business is K-AUM (calculated on the basis of the Firm's AUM).

HEM's own funds requirement is currently set by its KFR, as this is the highest of the three metrics. The potential for harm associated with HEM's business strategy, based on the Firm's own funds requirement, is low. This is due to the relatively stable revenues and asset base.

One of the strategies adopted to manage adherence to the Firm's own funds requirement is by maintaining a healthy own funds surplus above the own funds requirement. If own funds drop to an amount equal to 110% of the Firm's own funds threshold requirement, the Firm will immediately notify its management body, as well as the regulator. The management body will consider the necessary steps to be taken to increase the own funds buffer; which may include injecting more own funds into the Firm.

The below table illustrates the various components of the HEM's own funds requirement:

Requirement	**€'000**
(A) Permanent Minimum Capital Requirement ("PMR")	75
(B) Fixed Overhead Requirement ("FOR")	983
(C) K-factor requirement ("KFR")	891
- K-AUM – *risk arising from managing and advising on investments*	891
- K-COH – *risk from order execution and reception and transmission of orders*	-
(D) Own Funds Requirement (Max[A; B; C])	983
[redacted]	

HEM is also required to comply with overall financial adequacy rule ("OFAR"). This is an obligation on HEM to hold own funds and liquid assets which are adequate, both as to their amount and quality, to ensure that:

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

Where HEM determines that the FOR is insufficient to mitigate the risk of a disorderly wind down, the Firm must maintain an 'additional own funds required for winding down', above the FOR, that is deemed necessary to mitigate this risk. Similarly, where the Firm determines that the KFR is insufficient to mitigate the risk of harm from ongoing operations, the Firm must maintain an ‘own funds required for ongoing operations’, above the KFR, that is deemed sufficient to ensure the viability of the Firm throughout economic cycles.

The Firm’s own funds threshold requirement is the higher of:

- the Firm’s PMR;
- the sum of the Firm’s FOR and its additional own funds required for winding down; and
- the sum of the Firm’s KFR and its additional own funds required for ongoing operations.

This is the amount of own funds that HEM is required to maintain at any given time to comply with the OFAR.

Concentration Risk

Concentration risk for HEM means an exposure to a limited set of CLO vintages, where loss of these revenue streams without replacement would lead to a significant reduction in firm profitability or eventual loss. HEM continues to launch new CLO vehicles reducing concentration. Given the Intercompany Agreement, there is a concentration risk with HCM. HCM is part of the Hayfin Group of companies and is a stable, long-term, well capitalised and reliable partner to HEM.

Liquidity

HEM’s liquidity risk is limited to the material harm that it cannot meet its financial obligations as they fall due. HEM’s management fees are drawn quarterly in line with set payment dates for each investment vehicle managed. The management fee received by HEM is split between a part which is contracted irrespective of the performance of the CLOs (the senior management fee) and a part that fluctuates subject to performance (the junior management fee). The senior management fee is sufficient to cover all operating costs of HEM. HEM has contracted with HCM whose services including employees, operations, technology infrastructure and office; the cost and impact on HEM’s liquidity is predictable.

3. Governance Arrangements

Overview

HEM believes that effective governance arrangements help the Firm achieve its strategic objectives while also ensuring that risks to the Firm, its stakeholders and the wider market are identified, assessed, managed and mitigated.

The Executive Committee sits at the level of Hayfin Capital Holdings Limited, the ultimate parent company of the Hayfin group. The Executive Committee is responsible for making all decisions regarding the day to day management of the Hayfin group, including without limitation to HEM, which do not fall within the scope of responsibilities of the Audit and Risk Committee and the Remuneration Committee, and is therefore responsible for defining and overseeing the governance arrangements at the Firm.

A key report that is reviewed, discussed and ratified by the senior management at least annually is the Senior Management Systems and Controls ("SYSC") document, as this demonstrates how the Firm has met its governance arrangement requirement. The SYSC document provides the Executive Committee with information on the functioning and performance of all aspects of the Firm, including the following areas:

- general organizational requirements, including steps taken by the Firm to ensure continuity and regularity in the performance of its regulated activities and the Firm's account policies;
- employees, including steps taken by the Firm to ensure that employees have the necessary skills, knowledge and expertise for the discharge of the responsibilities allocated to them, and to ensure that they are fit and proper persons;
- regulatory framework for meeting compliance and financial crime requirements;
- internal capital adequacy and risk assessment process;
- outsourcing of critical or material operating functions or activities;
- record-keeping controls and arrangements;
- conflicts of interest management;
- remuneration policies and practices; and
- whistleblowing controls.

In line with MIFIDPRU 8.3.1 (2), the below table sets out the number of directorships, both executive and non-executive, held by each member of the Executive Committee:

Management body member	Position at HEM	Number of directorships held	
		Executive	Non-Executive
Timothy B Flynn	Chief Executive (SMF 1) Partner (SMF 27)	1	0
Mark James Tognolini	Partner (SMF 27)	1	0
Alex Wolfman		0	0

Executive Committee

Hayfin ensures that the Executive Committee:

- has overall responsibility for the FCA Firms;
- approves and oversees implementation of the FCA Firms' strategic objectives, risk strategy and internal governance;
- ensures the integrity of the FCA Firms' accounting and financial reporting systems, including financial and operational controls and compliance with the regulatory system;
- oversees the process of disclosure and communications;
- has responsibility for providing effective oversight of senior management;
- monitors and periodically assesses:
  - the adequacy and the implementation of the FCA Firms' strategic objectives in the provision of investment services and/or activities and ancillary services;
  - the effectiveness of the FCA Firms' governance arrangements; and
  - the adequacy of the policies relating to the provision of services to Clients; and take appropriate steps to address any deficiencies and
- has adequate access to information and documents which are needed to oversee and monitor management decision-making.

Hayfin ensures that the Executive Committee defines, approves and oversees:

- the organisation of the FCA Firms, including the skills, knowledge and expertise required by staff as well as the FCA Firms' resources, procedures and arrangements;
- a policy regarding the services, activities, products and operations offered or provided, in accordance with the risk tolerance of the FCA Firms and the characteristics and needs of the FCA Firms' Clients, including carrying out stress testing, where appropriate; and
- a remuneration policy that aims to encourage responsible business conduct, fair treatment of Clients as well as avoiding conflicts of interest in the relationships with Clients.

Audit and Risk Committee

HEM has established an independent Audit and Risk Committee ("ARC"). The Audit and Risk Committee is responsible for the oversight of the non-investment risk framework at the Hayfin Group, including but not limited to HEM. Its primary responsibilities are to review key financial and operational risk metrics and to assist management in reviewing and periodically assessing the Hayfin's group's risk management framework. The ARC's other main duties shall be to oversee the integrity of the Hayfin group's financial reports and the effectiveness of the Hayfin group's systems and controls. As the ultimate constitutional body responsible for oversight of non-investment risk, it approves this ICARA annually. Members of the Audit and Risk Committee have the appropriate knowledge, skills and expertise to fully understand, assess, manage and monitor the risk strategy and risk appetite of the Firm.

4. Own Funds

As at 31 December 2023, HEM maintained own funds of €84.85 million. The below regulator-prescribed tables provide a breakdown of the Firm's own funds:

Composition of regulatory own funds			
	Item	**Amount (EUR thousands)**	**Source based on reference numbers/letters of the balance sheet in the audited financial statements**
1	**OWN FUNDS**	**84,846**	
2	**TIER 1 CAPITAL**	**84,846**	
3	**COMMON EQUITY TIER 1 CAPITAL**	**84,846**	
4	Fully paid up capital instruments	84,818	1
5	Share premium	-	
6	Retained earnings	-	
7	Accumulated other comprehensive income	-	
8	Other reserves	28	1
9	Accumulated other comprehensive income	-	
10	Accumulated other comprehensive income	-	
11	(-)TOTAL DEDUCTIONS FROM COMMON EQUITY TIER 1	-	
19	CET1: Other capital elements, deductions and adjustments	-	
20	**ADDITIONAL TIER 1 CAPITAL**	-	
21	Fully paid up, directly issued capital instruments	-	
22	Share premium	-	
23	(-) TOTAL DEDUCTIONS FROM ADDITIONAL TIER 1	-	
24	Additional Tier 1: Other capital elements, deductions and adjustments	-	
25	**TIER 2 CAPITAL**	-	
26	Fully paid up, directly issued capital instruments	-	
27	Share premium	-	
28	(-) TOTAL DEDUCTIONS FROM TIER 2	-	
29	Tier 2: Other capital elements, deductions and adjustments	-	

Own funds: reconciliation of regulatory own funds to balance sheet in the audited financial statements				
		Balance sheet as in published/audited financial statements	**Under regulatory scope of consolidation**	**Cross-reference to above template**
		As at 31 December 2023	As at 31 December 2023	
Assets - Breakdown by asset classes according to the balance sheet in the audited financial statements (in €'000)				
1	Financial assets at fair value through profit and loss	163,473	163,568	
2	Trade and other receivables	5,222	99,841	
3	Amounts due from members	43,972	50,802	
4	Cash and cash equivalents	1,264	8,089	
5	Right of use asset		32,517	
6	Property, plant and equipment		2,445	
7	Intangible assets		5,703	
8	Investments in subsidiaries		320,673	
9	Restricted cash and deposits		8,089	
	Total Assets	**213,932**	**367,700**	
Liabilities - Breakdown by liability classes according to the balance sheet in the audited financial statements (in €'000)				
1	Trade and other payable	613	15,770	
2	Borrowings	124,856	150,856	
3	Lease liabilities		39,146	
4	Amounts due to Members	3,616	17,948	
	Total Liabilities	**129,085**	**223,721**	
Shareholders' Equity (in €'000)				
1	Eligible Members' LLP capital	84,818		1
2	Share capital		145,008	
3	Retained earnings	101	101	8
4	Cumulative translation adjustment	(72)	(72)	8
	Total Shareholders' equity	**84,846**	**144,979**	

Own funds: main features of own instruments issued by the Firm	
HEM's own funds consists solely of Common Equity Tier 1 Capital. The main features of the own funds issued by the Firm issued are highlighted below:	
Placement	*Private*
Instrument type	*Eligible Members' LLP capital*
Amount recognised in regulatory capital (EUR thousands, as of most recent reporting date)	*84,818*
Accounting classification	*Equity*
Perpetual or dated	*Perpetual*
Write-down features	*Ranks last on winding up*

Remuneration Policy and Practices

Overview

As a non-SNI MIFIDPRU investment firm, HEM is subject to the 'basic' and 'standard' requirements of the MIFIDPRU Remuneration code. The purpose of the requirements on remuneration are to:

- promote effective risk management in the long-term interests of the Firm and its clients;
- ensure alignment between risk and individual reward;
- support positive behaviours and healthy firm cultures; and
- discourage behaviours that can lead to misconduct and poor customer outcomes.

The objective of HEM's remuneration policies and practices are to establish, implement and maintain a culture that is consistent with, and promotes, sound and effective risk management and does not encourage risk-taking which is inconsistent with the risk profile of the Firm and the services that it provides to its clients.

In addition, HEM recognises that remuneration is a key component in how the Firm attracts, motivates and retains staff and sustains consistently high levels of performance, productivity and results. As such, the Firm's remuneration philosophy is consistent with the belief that its people are the most important asset and greatest competitive advantage.

HEM is committed to excellence, teamwork, ethical behaviour and the pursuit of exceptional outcomes for clients. From a remuneration perspective, this means performance is determined through the assessment of various factors that relate to these values, and by making considered and informed decisions that reward effort, attitude and results.

Characteristics of the remuneration policy and practices

Remuneration at HEM is made up of fixed and variable components.

The fixed component of the remuneration comprises salary, which is permanent, pre-determined, non-discretionary, non-revocable and which is not dependent on the performance of the individual. The fixed component is set in line with market competitiveness at a level to attract and retain skilled staff.

The variable component of remuneration broadly comprises annual variable remuneration paid in cash and long-term incentives. Long-term incentives are themselves split into three categories: (i) awards of carried interest; and (ii) awards of equity which are made via a restricted share scheme and a management incentive programme. Variable remuneration is paid on a discretionary basis, and takes into consideration the Firm's financial performance, the financial performance of each business unit, and the financial and non-financial performance of the individual in contributing to the Firm's success. All staff members are eligible to receive variable remuneration.

When assessing the level of variable remuneration to be paid, the Firm applies a number of both financial and non-financial performance criteria at the level of the firm, the relevant business unit and the individual to whom the remuneration is payable. At the level of the Firm, in determining the variable remuneration which can be awarded, current and future risks or anticipated risks to the Firm, as well as the Firm's liquidity requirements on a current and a look-forward basis are taken into account. Furthermore, other matters relevant to the long-term success of the Firm such as ensuring that remuneration is aligned with the interests of the Firm's shareholders and its clients and seeking to attract and retain talent, amongst others, are taken into consideration.

As to both the business unit and the individual level, the Firm awards variable remuneration where the employee or the business unit in which the employee sits has contributed to the long-term interests of the Firm, measured against factors such as profitability. Further, at the individual level, no employee shall be encouraged to take or rewarded for taking excessive risks for the purpose of generating short-term profit.

HEM ensures that the variable and fixed components of the total remuneration are appropriately balanced and that the fixed component represents a sufficiently high proportion of the total remuneration. This allows for a fully flexible policy on variable renumeration and the possibility of paying no variable remuneration component, which the Firm would do in certain situations, such as where the Firm's profitability is particularly constrained, or where there is a risk that the Firm may not be able to meet its regulatory capital or liquidity requirements.

Governance and Oversight

The Remuneration Committee is responsible, amongst other things, for any decisions regarding the exercise of any discretion which is conferred on the Remuneration Committee by the legal framework of the Hayfin group; any decisions regarding the implementation of and any changes to the group's compensation plan; any decisions regarding any settlement agreement with a departing employee or member of HEM (where the amount payable exceeds €500,000); and any decisions regarding whether leaver provisions in respect of the incentive plan or annual liquidity window mechanism (whereby it allows employees to buy and sell interests in the Hayfin group)_are to be exercised in relation to any leaver.

Material Risk Takers

HEM is required to identify its material risk takers; that is, those members of staff whose professional activities have a material impact on the risk profile of the Firm and of the assets that the Firm manages. The types of staff that have been identified as material risk takers at HEM are:

- members of the senior management team;
- those with managerial responsibility for a client-facing or client-dealing business unit of the Firm;

- those with managerial responsibilities for the activities of a control function[1];
- those with managerial responsibilities for the prevention of money laundering and terrorist financing;
- those that are responsible for managing a material risk within the Firm;
- those that are responsible for managing information technology; information security; and/or outsourcing arrangements of critical or important functions; and
- those with authority to take decisions approving or vetoing the introduction of new products.

Quantitative Remuneration Disclosures[2]

The below table quantifies the remuneration paid to staff in the financial year 1st January 2023 to 31st December 2023. For these purposes, 'staff' is defined broadly, and includes, for example, employees of the Firm itself, members, employees of other entities in the group, employees of joint service companies, and secondees:

Period: 1st January 2023 – 31st December 2023			
		Senior Management & Other material risk takers	Other staff
Total number of material risk takers		1	
Remuneration Awarded	Fixed (€)	345,834	1,411,950
	Variable (€)	486,884	1,619,346
	Total (€)	832,718	3,501,946
Guaranteed variable remuneration	Amount (€)	0	
	# Staff Awarded	0	
Severance payments	Amount (€)	0	
	# Staff Awarded	0	
Highest severance payment awarded to an individual (€)		0	

[1] A control function is defined as a function (including, but not limited to, a risk management function, compliance function and internal audit function) that is independent from the business units it controls and that is responsible for providing an objective assessment of the Firm's risks, and for reviewing and reporting on those risks.

[2] MIFIDPRU investment firms are typically required to split the quantitative data in the above table, where relevant, into categories for senior management and other material risk takers. The regulator however allows firms to aggregate or altogether omit the information to be disclosed for senior management and other material risk takers, where splitting the information between these two categories would lead to the disclosure of information about one or two people. HCM has relied upon this exemption, MiFIDPRU 8.6.8R(7), and has aggregated the disclosure of fixed/variable/total remuneration awarded and omitted the disclosure of severance payments, in order to prevent the individual identification of a material risk taker.