

## Citadel Europe LLP

### Pillar 3 disclosures for the year ended 31 December 2009

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#### 1. Introduction: pillar 3

Basel II is structured around three 'pillars': pillar 1 on minimum capital requirements; pillar 2 on the supervisory review process; and pillar 3 on market discipline.

Pillar 3 aims to encourage market discipline by developing a set of disclosure requirements which will allow market participants to assess key pieces of information on a firm's capital resources, risk exposures and risk assessment process. The disclosures contained in this document cover the qualitative and quantitative disclosure requirements of pillar 3 and are based on audited data as at 31 December 2009.

These pillar 3 disclosures have been prepared solely to comply with regulatory requirements to provide public information on the Partnership's risk management objectives and policies, its capital position, its approach to assessing the adequacy of its capital and its exposure to credit, market and operational risks.

The disclosures are made in accordance with the Partnership's disclosure policy and are not audited. Disclosures will be issued as a minimum on an annual basis and will be published on the Citadel group website [www.citadelgroup.com](http://www.citadelgroup.com) as soon as practicable after the publication of the Partnership's annual report and financial statements.

If you have any questions on this document, please write to the Partnership Secretary, Citadel Europe LLP, Moor House, 120 London Wall, London EC2Y 5ET.

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#### **2. Risk Management framework and policies**

##### ***Business Overview***

Citadel Europe LLP ("CELP") is a limited licence firm regulated by the FSA, and is not authorised to undertake proprietary trading. CELP advises on investment decisions taken by Citadel's global flagship funds, known as Kensington and Wellington. CELP operates from a single location, in the City of London.

The controlling partner of CELP is Citadel Investment Group (Europe) Limited ("CIGE"). Prior to 29 January 2009, CIGE was the regulated investment management firm. With effect from 29 January 2009 CELP became the regulated investment management firm. The financial data disclosed in this report is taken from the consolidated report and financial statements of CIGE and CELP for the year ended 31 December 2009.

##### ***Risk Management framework***

Risk Management is the process of identifying the principal risks to the Partnership achieving its strategic objectives, establishing appropriate controls to manage those risks and ensuring that appropriate monitoring and reporting systems are in place to ensure that controls remain robust and evolve with the changing risk profile of the Partnership.

The Partnership's operations expose it to certain financial risks such as credit risk, liquidity risk and foreign exchange risk. The Partnership considers financial risks regularly and seeks to limit the adverse effects on the financial performance of the Partnership. The risk management infrastructure, computer systems, and back office are global functions supported by the US parent entity from Chicago and were rated OQ2+ in 2008 by Moody's.

The Partnership has conducted a comprehensive risk identification exercise by risk category by function head across the business to ensure that all significant risks have been identified and captured by the risk management infrastructure. All significant risks have been documented, scored and level of exposure estimated using a matrix of parameters.

The London Operations Committee ("LOC") meets monthly and considers risk management on an ongoing basis. The LOC consists of the local business heads across front and back office.

CELP's management committee, consisting of senior UK and US management, reviews and endorses the risk management framework of the Partnership.

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#### ***Risk Management framework (continued)***

The high level summary of the key risk assessments for CELP is as follows:

#### ***Operational Risk***

Operational risk is the inherent risk of material loss or other adverse impact resulting from inadequate internal processes, people or systems or from external events. CELP has a low operational risk appetite and has in place a robust control framework, as evidenced by the OQ2+ group operational risk rating received from Moody's.

This various risks associated with employees are addressed by human resource policies to ensure that the Partnership recruits and retains staff with the appropriate skills, by offering an attractive work place environment and highly competitive remuneration packages.

#### ***Business Risk***

Business risk is the risk that the Partnership will not have adequate cash flow to meet its operating expenses. CELP has a low risk appetite, reflected in the existing fee structure that ensures fee income covers all costs. This structure provides CELP management with a level of comfort and CELP would be able to reduce its cost base in a controlled fashion if necessary.

#### ***Credit Risk***

Credit risk is the risk of loss if another party fails to perform its obligations, and arises in the normal course of business. The principal credit risk for CELP is exposure to receivable balances from group undertakings. Fee income receivable from the US parent company is estimated and called monthly in advance to mitigate this risk. CELP bank balances are segregated from those of the group and placed with highly rated counterparties. The bank accounts are managed and controlled locally, independent of the group cash position.

#### ***Liquidity Risk***

Liquidity risk is the risk of not being able to meet liabilities as they fall due. The Partnership is not exposed to material liquidity risk. The Partnership has sufficient cash to meet short-term liquidity needs, and lends excess cash to highly rated counterparties on a short-term basis only. Cash flow forecasts are produced on a three month time horizon and are reviewed regularly by senior management.

#### ***Market Risk***

Market risk is the risk of loss that arises from adverse movements in financial markets; CELP is not authorised to undertake proprietary trading and therefore its market risk is limited to foreign exchange exposure on its balance sheet. The functional currency of CELP is sterling; the US parent entities functional currency is US dollars and group performance is measured in US dollars. As a consequence CELP does have a potential exposure to exchange rate movements; this is not actively hedged as certain administrative expenses including performance bonus payments are also denominated in US dollars. However the Partnership actively monitors foreign currency balances and exchange rates and seeks to limit the potential adverse effects of foreign exchange transactions on the financial performance of the Partnership.

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#### 3. Capital Resources and Capital Adequacy

The table below summarises the consolidated regulatory capital position of CELP and CIGE as at 31 December 2009 (pillar 1):

Capital resources	Notes	31 December 2009 GBP 000s
Share Capital		300
Audited retained profits	1	23,805
Core Tier 1 Capital		24,105
<b>Total regulatory capital (A)</b>	2	<b>24,105</b>
Credit risk capital requirement		829
Market risk capital requirement		811
Sum of credit risk and market risk (B)		1,640
Fixed overhead requirement (C)	3	9,551
<b>Surplus of Capital Resources Being (A) less the higher of (B) or (C)</b>	4	<b>14,554</b>

Notes on capital resources table above

1. Audited retained earnings include GBP309K in respect of the year ended 31 December 2009, which was audited subsequent to that date.
2. The Partnership has no tier 2 capital, or any deductions from core tier 1 capital.
3. The fixed overhead requirement calculation is based on the audited 2009 expenses.
4. Stated before any capital set aside arising from pillar 2 or individual capital guidance.

#### **Pillar 1 capital resources**

The Partnership's policy is to remain well capitalised and soundly financed. CELP will maintain a strong capital base to support the development of the business and to ensure regulatory capital requirements are met at all times.

The classification of the Partnership as a limited licence firm means the key capital adequacy measurement is the fixed overhead requirement (25% of the audited fixed cost base) as compared to the audited share capital and retained earnings. As at 31 December 2009, the surplus of capital resources was GBP 14,554K.

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***Pillar 1 capital resources (continued)***

There are no current or foreseen material practical or legal impediments to the prompt transfer of capital resources or repayment of liabilities. There are no plans to distribute retained earnings to the US parent entity by way of dividends.

#### 4. Credit Risk

***Credit risk capital requirement***

CELP adopts the Simplified Standardised Approach to the credit risk capital requirement, and the calculation at 31 December 2009 is as follows:

Asset class	Risk Weight	Exposure GBP 000s
Claims on institutions	20%	31,150
Claims on corporates and partners	100%	2,722
Other items - tax assets	0%	21,844
Other items	100%	1,415
<b>RISK WEIGHTED TOTAL</b>		<b>10,367</b>
<b>Credit risk capital requirement</b>	<b>8%</b>	<b>829</b>

The above analysis gives the breakdown of credit risk by asset class; no further industry analysis of the credit risk capital requirement is considered necessary.

The geographical analysis of exposures by asset class is as follows:

Asset class	UK GBP 000s	Rest of World GBP 000s
Claims on institutions	31,150	-
Claims on corporates and partners	2,705	17
Other items - tax assets	21,844	-
Other items	1,415	-
	<b>10,350</b>	<b>17</b>

Claims on institutions and corporates have a residual maturity of less than 90 days, there being no material amounts falling due after 90 days. The deferred tax assets carry a residual maturity of more than 1 year.

***Past due items and impairment***

The Partnership does not have any material past due or impaired assets on its balance sheet.

