



# CMC Markets Plc Pillar 3 Disclosure



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# 1.0 Overview

These disclosures are made in order to comply with FSA's rules which implement in the UK the EU directives that give effect to the revised capital adequacy framework agreed by the Basel Committee on Banking Supervision in 2004 and subsequently published in comprehensive form in 2006.

Basel II is organised around three "pillars" which the Basel Committee considers to be complementary:

- Pillar 1: minimum capital requirements;
- Pillar 2: supervisory review;
- Pillar 3: market discipline.

To facilitate market discipline Pillar 3 contains requirements for firms to publish specified information on the basis on which Basel II applies to them, their capital resources and capital requirements and their risk exposures and risk management.

FSA's rules for implementing Pillar 3 as incorporated in the EU Capital Requirements Directive are contained in Chapter 11 of The Prudential Sourcebook for Banks, Building Societies and Investment Firms.

In this document we disclose information in accordance with the following BIPRU 11.5 Rules unless it has been determined as immaterial or of a proprietary or confidential nature:

- BIPRU 11.5.1R on our risk management objectives and policies.
- BIPRU 11.5.2R on the scope of application of directive requirements.
- BIPRU 11.5.3R on our capital resources.
- BIPRU 11.5.4R (subsections 1, 2, 4 (a) (i), (ii), (v), (vi), 4 (b) (i) and (ii) and 5) on our compliance with the rules of BIPRU and on Pillar 2 requirements.
- BIPRU 11.5.7R on exposure to counterparty credit risk.
- BIPRU 11.5.8R on exposure to credit risk.
- BIPRU 11.5.12R (subsections 1(a), (b), (e) and (f) and 2 (a) and (b)) on market risk.
- BIPRU 11.5.14R on exposure to operational risk; and
- BIPRU 11.5.16R on exposure to interest rate risk in the non-trading book.

## 2.0 Frequency and location of disclosure

The Board of Directors of CMC Markets Plc ("the Board") do not consider that the Pillar 3 disclosures should be made any more frequently than annually unless there has been a material change in the approaches or permissions used to calculate regulatory capital. The Board believe that the publication of these disclosures on CMC Markets' website is the most appropriate medium.

These disclosures are based on the position as at 31 March 2008. Future disclosures will be issued on an annual basis in accordance with the requirements of Pillar 3.

Pillar 2 capital requirements are excluded from this disclosure but can be material in determining total capital requirements and any available surplus capital. They are therefore reviewed at least monthly at the CMC Markets' Group ICAAP Committee meetings.

## 3.0 Verification

These disclosures have been reviewed by the Board and are published on CMC Markets' corporate website ([www.cmcmarketsplc.com](http://www.cmcmarketsplc.com)). These disclosures are not subject to audit except where they are equivalent to those prepared under accounting requirements for inclusion in CMC Markets' Annual Report.



## 4.0 Scope of application

The disclosures in this document are made in respect of the CMC Markets Plc Group ("CMC Markets" or "the Group") which provides spread betting and CFD trading as well as financial information and stockbroking services to retail and institutional clients.

This is a UK Consolidated Group under the BIPRU 8 Rules of the Financial Services Authority (FSA) and subject to consolidated supervision by the FSA. The entities consolidated, all 100% controlled by the CMC Markets, are shown in the table below. These are the same legal entities that are consolidated in the CMC Markets' 2008 Annual Report.

<b>CMC Markets Entity:</b>	<b>Regulated By:</b>
CMC Markets UK Plc.	Financial Services Authority (FSA), Ontario Securities Commission (OSC)
- Austria Branch	FSA, Finanzmarktaufsicht
- Beijing Representative Office	China Banking and Regulatory Commission
- Germany Branch	FSA, Bundesanstalt für Finanzdienstleistungsaufsicht
- Ireland Branch	FSA, Financial Regulator
- Sweden Branch	FSA, Finansinspektionen
CMC Spreadbet Plc.	FSA
- Ireland Branch	FSA, Financial Regulator
CMC Markets Canada Inc.	Investment Dealers Association of Canada, OSC, British Columbia Securities Commission
CMC Markets (US) LLC	US Commodity Futures Trading Commission, National Futures Association
CMC Markets Asia Pacific Pty Ltd.	Australian Securities and Investments Commission (ASIC), OSC
CMC Markets Pty Ltd.	ASIC
Andrew West & Co. Ltd.	ASIC, Australian Stock Exchange
CMC Markets NZ Ltd.	New Zealand Securities Commission
CMC Markets Asia Ltd.	Securities and Futures Commission (Hong Kong)
CMC Markets Singapore Pte Ltd.	Monetary Authority of Singapore
CMC Markets Japan KK	Financial Services Agency, Financial Futures Association of Japan, Japanese Securities Dealers Association



There are no known current or foreseen practical or legal impediments to the prompt transfer of capital resources or repayments of liabilities between parent and subsidiary undertakings and there are no subsidiary undertakings where actual capital resources are less than the required minimum. We do not rely on the provisions of BIPRU 2.1

# 5.0 Risk management objectives and policies

The Board sets the strategy and policies for managing risks and delegates the monitoring and management of them to various committees as detailed below.

The Board is responsible for:

- governing CMC Markets’ strategic direction and defining and monitoring acceptable risk parameters for CMC Markets;
- ensuring that the necessary financial and human resources are in place for CMC Markets to meet its objectives;
- monitoring the operating and financial results against plans and budgets.

The Board has an agreed set of delegated authorities granted to individuals and committees while having a formal schedule of matters reserved for its attention.

The principal Board committees are the Audit, Remuneration, Nominations, Group Risk and Executive Committees whose terms of reference, duties and responsibilities have been agreed and adopted by the Board.

The Group Risk Management Committee reports to the Board and comprises members of the Executive Committee and various heads of department. It submits reports to each Board meeting. Other committees include the Group ICAAP Committee, which manages the Internal Capital Adequacy Assessment Process (ICAAP) and reviews the requirements of the Capital Requirements Directive; the Credit Committee, which examines all issues relating to credit risk; and the Group Treasury Committee which reviews treasury operations, policies and procedures.

CMC Markets has an established global risk management function and a ‘Global Risk Management Framework’ has been approved by the Board to define key responsibilities, reporting requirements and mechanisms for managing operational and other risks throughout the business.

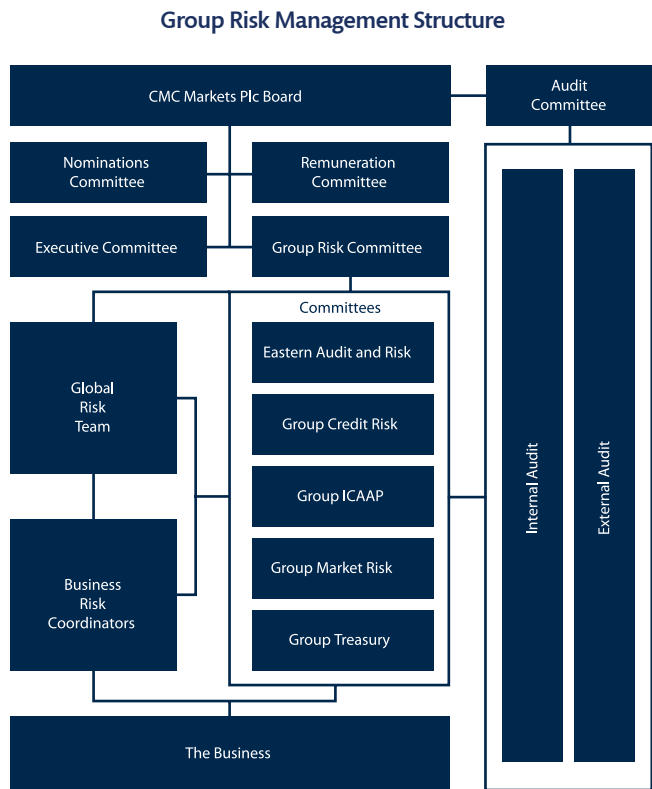
The framework draws from accepted best practice in risk management standards, and is designed to support compliance with regulatory requirements in all jurisdictions in which the business operates. As well as detailing those responsibilities held by the Group’s individual risk committees (Group Audit Committee, Group Risk Committee, etc.), the framework promotes the routine identification, evaluation and management of risks and opportunities by all employees and consultants as part of a risk-aware culture.

The Board has responsibility for sanctioning the global risk management policies and procedures and for determining CMC Markets’ risk appetite and communicating that to the Global Risk Committee. The Audit Committee also plays a formal role in evaluating the reasonableness of the risk appetite and making recommendations to the Board.

The Group Risk Committee meets monthly and considers risk incidents, monthly residual risk assessments, key risk indicators, and market and credit risk exposures.

Both Eastern and Western regions of the business produce a ‘risk register’. These registers detail risks identified from discussions that the Eastern and Western risk management functions undertake with the various regional business managers, and from other reviews.

The Group Risk Management Structure is illustrated below:



The most significant risk types to which CMC Markets is exposed are discussed on the next page.

## 5.1 Operational risk

Operational risk is the risk of loss or negative impact to CMC Markets resulting from inadequate or failed internal process, people and systems or from external factors such as regulation and key suppliers; it includes legal and financial crime risks but excludes strategic, reputation and business risks.

The following have been identified as the main sources of operational risk:

### 5.1.1 Business continuity

There are potentially a number of events that may result in the invocation of the CMC Markets' 'Business Continuity Plan' (BCP) and/or the disaster recovery procedure.

Examples of the events that are likely to occur to require partial to full disaster recovery of people and IT systems and infrastructure are as follows:

- Fire;
- Bomb threat;
- Power outage; and
- Server room environment incident.

The business continuity management arrangements created for CMC Markets should ensure that 'business as usual' impact is kept to a minimum. The business continuity key documents include:

- Group Crisis Management Policy;
- Group Business Continuity Plans;
- Business Continuity Incident Escalation Procedure.

### 5.1.2 Fraud

Fraud is defined as the risk that client or company assets may be misappropriated.

The controls that CMC Markets has in relation to controlling internal fraud in relation to payments, payroll, purchasing and treasury are designed to prevent and detect errors. CMC Markets' treasury monitoring, daily cash reconciliations and authorisation procedures are key controls designed to detect material fraudulent activities promptly.

Purchasing (budgetary and approval controls) and dealing activity monitoring are also set to minimise the possibility of fraudulent activity.

The primary area for external fraud to be perpetrated against CMC Markets is in relation to credit card fraud with payment monitoring procedures and chargeback protection procedures designed to identify such activity at an early stage.

### 5.1.3 Information technology

Failure of IT strategy or implementation would have an adverse impact on the business. The Board has overall responsibility for ensuring an effective IT strategy to ensure that IT solutions are prioritised to meet business strategic requirements.

### 5.1.4 Administration and dealing errors

Extensive management information is prepared monthly for the Group Risk Committee. Although administration errors and dealing errors are inherent in the scale of CMC Markets' operations, the Board considers that effective controls are in place to mitigate such risks.

### 5.1.5 Regulatory action

CMC Markets endeavours to maintain good working relations with regulators within each jurisdiction in which it operates. This is achieved via a global compliance function that ensures CMC Markets has experienced compliance professionals in place to ensure timely compliance with local and consolidated regulatory requirements.

## 5.2 Market risk

CMC Markets does not hold proprietary trading positions based on expectations of future market movements but to hedge open client positions.

Market risk is analysed as market price risk, interest rate risk and currency risk.

### 5.2.1 Market price risk

This is the risk that the fair value of a financial instrument will fluctuate due to changes in market prices other than due to currency or interest rate risk.

Market risk arises from CMC Markets' clients spread betting and trading contracts for difference (CFDs) which are based on underlying equities and indices on world stock markets, foreign currencies, commodities and interest rates and the derivative (OTC and exchange-traded) or physical positions CMC Markets takes to hedge these client positions. All derivatives used to hedge client positions are margin-traded so the profit or loss arising on the position is settled on a daily basis. The use of derivative financial instruments is governed by Group policies approved by the Board which provide written principles on their use consistent with the Group's risk management strategy.

CMC Markets monitors its market risk on these client positions against internally approved limits and hedges these client positions based on a number of internally agreed metrics to manage its net exposure. These metrics include the size of the client position, CMC Markets' view of current market conditions and the volatility and liquidity of the underlying instrument in which its clients are spread betting or trading CFDs.

These positions are monitored on a global basis so all open positions held by CMC Markets' clients are combined to calculate CMC Markets' total net client exposure to ensure optimal hedging decisions are made.

The diversity of our product range and global distribution significantly reduces CMC Markets' revenue sensitivity to individual asset classes and instruments. The direct result is consistent historical revenue performance throughout periods of varying market movements and volatility levels.

### 5.2.2 Interest rate risk

This consists of cash flow interest rate risk (the risk that future cash flows of a financial instrument will vary due to changes in market interest rates) and fair value interest rate risk (the risk that the value of a financial instrument will vary due to changes in market interest rates).

Interest rate risk arises from unhedged client positions where the underlying instrument is subject to cash flow or fair value interest rate risk. These positions are managed subject to internally approved limits that are set in accordance with CMC Markets' risk appetite.

Interest rate risk also arises from the mismatch between the repricing of financial assets and liabilities. Financial assets and liabilities are predominantly short-term. These short-term mismatches are managed according to parameters determined by the Group Treasury Committee.

The Group's interest-bearing financial assets mature in the short-term, with maturities no longer than 12 months. As a result, CMC Markets is subject to limited exposure to fair value interest rate risk due to fluctuations in the prevailing levels of market interest rates. Excess cash of the Group is invested in short-term cash deposits with the term to maturity no longer than three months.

Exposures to financial liabilities with maturities greater than one year are specifically hedged depending on the Group Treasury Committee's view of medium- to longer-term interest rate movements.

### 5.2.3 Currency risk

This is the risk that the value of assets and liabilities denominated in a foreign currency will fluctuate due to adverse movements in exchange rates. Currency risk arises from unhedged client positions in foreign currencies where the value of the underlying currency fluctuates against Sterling. These positions are managed in accordance with CMC Markets' internally approved limits subject to CMC Markets' risk appetite.

CMC Markets' residual currency risk (excluding risk on client positions denominated in foreign currencies above) relates to balance sheet translation exposure and transactional currency flows arising from earnings in foreign currencies.

These risks are managed by CMC Markets' Group Treasury Committee which regularly reviews them and makes recommendations to the Board regarding their management. Balance sheet translation exposure is actively managed to ensure negligible foreign currency net asset exposure on a group basis.

Forecasted foreign currency earnings are hedged using various hedging instruments including CFDs, currency forwards and options. The percentage of these earnings hedged is determined by the Group Treasury Committee based on guidelines set out in CMC Markets' Global Hedging Policy.

## 5.3 Credit risk

Credit risk is the risk that CMC Markets' clients and counterparties may fail to pay amounts they owe the Group as they become due.

The Group's principal financial assets are deposits and other cash balances held with banks and other financial institutions, trade and other receivables and investments.

### 5.3.1 Deposits and other balances held with banks and other financial institutions

It is CMC Markets' policy to manage credit risk by only placing funds with financial institutions that meet certain short-term and long-term external credit ratings provided by Moody's Investors Service and Fitch Ratings Limited. These exposures are monitored on a daily basis.

Limits are regularly reviewed and CMC Markets does not consider that it has any significant concentration of credit risk as exposure is spread over a range of counterparties. Limits are in place to monitor exposure to individual counterparties or connected groups of counterparties.

Credit risk also arises from deposits and excess funds placed with brokers that CMC Markets uses to hedge its net client positions.

### 5.3.2 Client credit risk

CMC Markets does not offer credit facilities to clients and funds must be deposited in order to open a position. CMC Markets operates a real-time marked-to-market trading platform with client profits and losses being credited and debited automatically to their account.

Credit risk occurs where a client's funds held by CMC Markets (margin and free equity) are insufficient to cover losses incurred by the client upon liquidation.

Client credit risk is therefore monitored daily with reference to the market price movement of the underlying instrument in which the client holds a position and the equity the client holds in relation to the margining requirement calculated for their position.

## 5.4 Liquidity risk

Liquidity risk is the risk that CMC Markets will encounter difficulty in meeting its obligations from its financial liabilities. CMC Markets' policy is to ensure that, as far as possible, it will always have sufficient liquidity to meet its financial liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to its reputation.

CMC Markets maintains a portfolio of short-term deposits to ensure that sufficient liquidity is maintained within the Group as a whole. The liquidity position is monitored on a daily basis and management information provided monthly to the Group Treasury Committee and the Board. All treasury policies and procedures are approved by the Board.

## 6.0 Capital resources

At the 31 March 2008, and throughout the year, CMC Markets has complied with the capital requirements as required by the FSA. The following table provides a breakdown of the capital resources available to meet these requirements:

	March 2008 (£m)
<b>Core Tier 1 capital</b>	
Share capital	64.0
Own shares held in trust	-3.9
Translation reserve	1.5
Merger reserve	-47.8
Retained earnings	90.5
<b>Deductions from Tier 1 capital</b>	
Intangible assets	-69.2
<b>Total Tier 1 capital after deductions</b>	<b>35.1</b>
Lower Tier 2 - Long-term subordinated debt	23.7
<b>Lower Tier 2 - capital after deductions</b>	<b>23.7</b>
<b>Capital resources</b>	<b>58.8</b>

### 6.1 Tier 1 Capital

Tier 1 Capital comprises share capital less own shares held in trust, other audited reserves and retained earnings. CMC Markets has no 'innovative Tier 1' instruments.

An adjustment is also made in respect of intangible assets. For accounting purposes, £50.4m of software development and other costs are capitalised as intangible fixed assets as they meet certain criteria. In addition, £18.8m of goodwill is held as part of intangible assets. However, because intangibles do not qualify as capital for regulatory purposes, a total of £69.2m of intangible assets are therefore deducted from capital.

### 6.2 Tier 2 Capital

Tier 2 capital comprises lower Tier 2 long-term subordinated debt. Details of the subordinated note can be found in Note 21 in the 2008 Annual Report.



# 7.0 Capital adequacy

## 7.1 Capital management

CMC Markets has adopted the standardised approach to both credit and operational risk since 1 January 2008 in order to calculate the Basel II Pillar 1 minimum capital requirement under the Capital Requirements Directive.

The Group's objectives for managing capital are as follows:

to comply with the capital requirements set by the FSA and all other regulators to which the Group is subject;

to ensure that all CMC Markets Group entities are able to operate as going concerns and satisfy any minimum externally imposed capital requirements; and

to ensure that the CMC Markets Group maintains a strong capital base to support the development of its business.

## 7.2 Internal Capital Adequacy Assessment Process

CMC Markets undertakes an Internal Capital Adequacy Assessment Process (ICAAP) which is an internal assessment of capital requirements. This is undertaken annually or more frequently if required.

The outcome of the ICAAP is presented as an Internal Capital Assessment (ICA) document covering CMC Markets. The ICA covers all material risks to determine the capital requirement over a three-year horizon and includes stressed scenarios to satisfy regulatory requirements.

The FSA can assess the ICA and set 'Individual Capital Guidance' capital requirements for firms.

## 7.3 Market risk

CMC Markets does not use a VaR model for the calculation of its market capital requirement (although a VaR model is planned to be introduced from 2009). Nor does CMC Markets have any non-trading book exposures in equities.

## 7.4 Operational risk

CMC Markets has adopted the 'basic indicator' approach to calculating the Pillar 1 capital requirements for operational risk. This produces an operational risk capital requirement equivalent to 15% of the three-year average of CMC Markets' net income.

## 7.5 Credit risk

### 7.5.1 Impairment of financial assets

A financial asset or group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of events that occurred after the initial recognition of the asset ("a loss event") and that loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets. Evidence of impairment could include significant evidence that the counterparty will enter bankruptcy or other financial reorganisation.

If there is objective evidence that a loss event has occurred, the amount of the loss is measured as the difference between the carrying amount of the asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The resultant provisions are deducted from the appropriate asset values in the balance sheets.

If in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised the provision is adjusted and the amount or the reversal recognised in the income statement.

Financial assets are written off when it is reasonably certain that receivables are irrecoverable.

### 7.5.2 Past due items

A financial asset is considered to be past due where the recovery of the financial asset is past its due date but no specific event has occurred which the Board consider to deem to have created impairment of the asset.

### 7.5.3 Calculation of impairment provisions

The only financial assets that were subject to an impairment provision at the date of the Pillar 3 Disclosure were amounts due from clients on unsettled transactions. The impairment is calculated as the 'probability of default' (PD) x the 'loss given default' (LGD).

The PD represents the probability that a client receivable will not be recovered. The LGD is calculated as:

the current value of the receivable;

the estimated net recoverable amount.

The LGD is then calculated as the current value of the receivable less the estimated net recoverable amount.

## 8.0 Further enquiries

### 7.5.4 Credit exposures

The Group's Pillar 1 credit risk capital requirement is based on 8% of its risk-weighted assets.

CMC Markets uses external credit assessments provided by Moody's and Fitch. These are all recognised by the FSA as eligible external credit assessment institutions (ECAI) for the purpose of calculating credit risk assessments under the standardised approach.

Funds deposited with various financial institutions are subject to internal concentration risk limits and these are reported regularly to the Board.

Trading book positions with brokers are subject to various netting agreements to mitigate net credit exposure.

All exposures to financial institutions at 31 March 2008 have a maturity of less than 3 months, as detailed in Note 24 of the 2008 Annual Report.

Should you have any queries, please contact:

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London E1 8HG  
Company Number : 5145017

## 7.6 Counterparty credit risk

This arises principally from exposures arising in the trading book due to financial derivative instruments as well as unsettled non-trading book transactions and is calculated as 8% of the total risk-weighted exposure amounts.

## 7.7 Exposures to interest rate risk in the non-trading book

Exposures to interest rate risk in the non-trading book are evaluated by running a number of scenarios based on underlying business cashflows and interest rate assumptions with forecasts adjusted monthly.



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Instrument
1332 Npn Suis (Jp)
1605 Inpex (Jp)
1721 Comsys (Jp)
1801 Taisei (Jp)
1802 Obayashi (Jp)
1803 Shimizu (Jp)
1810 Kajima (Jp)

USDJPY Spot

119.59

LLOY (UK)

551.50