

**KKR Credit Advisors (Ireland)**

**PILLAR 3 DISCLOSURES**

**JANUARY 2016**

## **1. Background**

The European Union Capital Requirements Directive (“CRD” or “the Directive”) as amended, sets out the regulatory framework governing the amount of capital which must be maintained by credit institutions and investment firms in Europe.

As an authorised MIFID regulated investment Firm in Ireland, the CRD applies to KKR Credit Advisors (Ireland), hereafter “KKR CAI” or “the Firm”. The regulatory framework comprises three Pillars:

- Pillar 1 sets out the minimum capital requirements that a Firm is required to meet;
- Pillar 2 requires the Firm to assess the amount of capital that would be adequate to cover the risks that the Firm has or may be exposed to (Internal Capital Adequacy Assessment Process) which are not adequately covered by Pillar 1; and
- Pillar 3 requires the Firm to disclose its risk management strategies, policies and processes, capital resources, capital requirements and the Firm’s approach to assessing capital adequacy.

The purpose of this document is to provide the Pillar 3 disclosures required for KKR CAI as at 31 December 2015. The requirements provide for the omission of one or more of the required disclosures if such information is considered to be immaterial, proprietary or confidential.

Information shall be regarded as material in disclosures if its omission or misstatement could change or influence the assessment or decision of a user relying on that information for the purpose of making economic decisions.

Information shall be regarded as proprietary to a firm if sharing that information with the public would undermine its competitive position. It may include information on products or systems which, if shared with competitors, would render a firm’s investments therein less valuable.

Information shall be regarded as confidential if there are obligations to customers or other counterparty relationships binding a firm to confidentiality.

KKR CAI is a consolidated subsidiary of KKR & Co L.P. (“KKR”), a Delaware entity, (NYSE: KKR).

KKR CAI’s primary regulatory activity is the portfolio management of securitisation vehicles, alternative investment funds and separate managed accounts.

## **2. Scope of Application**

KKR CAI is regulated by the Central Bank of Ireland (“CBOI”) on a stand-alone basis and is not subject to consolidated supervision. The Pillar 3 disclosures contained within this document therefore apply to KKR CAI on an individual basis.

### **3. Frequency of Disclosure**

The Firm publishes Pillar 3 disclosures on at least an annual basis in conjunction with the date of its financial statements. Given the scale and range of its operations and complexity, the Firm assesses that there is no need to publish some or all of its disclosures more frequently than annually.

### **4. Risk Management**

The Firm's risk management policies and processes are comprehensive and proportionate to the nature and scale of KKR CAI's activities.

KKR CAI Board of Directors has ultimate responsibility for the wider risk management of the Firm and has appointed a member of the Board of KCAI with responsibility for implementing and maintaining risk management within the Firm. The KKR Global Risk Committee is responsible for identifying, prioritising and monitoring risk for KKR on a global basis and is accountable to KKR's Global Management Committee, which is responsible for KKR's global operations.

The Firm's risk management function is part of the Firm's 'three lines of defence' internal governance model.

Board of Directors:

The KKR CAI Board of Directors places a high priority on a strong risk management culture within the Firm. The Board recognises that risk is inherent in the Firm's business and the markets in which it operates. Effective risk management and strong internal controls are therefore central to the Firm's business model. The KKR CAI Board is ultimately responsible for the Firm's risk management and is responsible for challenging the outcome of the ongoing risk assessments and risk reporting.

Audit and Risk Committee:

The Audit and Risk Committee meets on a quarterly basis and reviews inter alia the reports submitted by the Internal Audit, Finance, Compliance, IT and Risk Management functions. The Audit and Risk Committee is responsible for monitoring and making recommendations to the Board regarding risk, financial reporting, external audit, internal controls and certain other regulatory and compliance matters as they arise. The Audit and Risk Committee reports to the Board of Directors of the Firm.

Senior Management:

Senior management, as subject matter experts and owners of business lines, take an active involvement in the assessment of the risks that the Firm faces. This involves completing an assessment under the guidance and oversight of the Board, or providing support and information to the Firm's Compliance and Risk Management functions in their assessments of risk.

Internal Audit:

KKR globally has an internal audit function. KKR CAI is in scope for internal audit reviews from time to time.

## **Identified Risks**

The following risks are considered to be the most significant business risks:

### **a) Business and Strategic and fund performance risk**

*The risk that strategic business decisions prove to be ill-founded or poorly executed (e.g. performance, investment decisions, moves into new markets, products, or regions; changing the operating model), or there is a failure to anticipate / react to a more general shift in the economic environment or the loss of key personnel).*

Fund performance risk is controlled and managed by ensuring that all new investments are approved by the KKR CAI Investment Committee. Business risk is controlled and managed through all new strategic initiatives being approved by the Board. KKR CAI considers the risks in its' business carefully and seeks to reduce and mitigate risks so as to ensure it maintains an appropriate capital position.

*Risk regarding the ability to attract and retain appropriate investors into the KKR Funds and the management of investor relations.*

To manage the risks regarding the ability to attract and retain appropriate investors into the KKR Funds and to successfully manage investor relations, a team of individuals with solid experience in capital raising and investor relations manage the KKR Funds and manage investor relationships.

### **b) Reputational risk**

*The current and prospective impact on earnings (and/or access to liquidity and capital) arising from how KKR CAI is perceived by counterparties, regulators, clients and governments is considered an ongoing risk to the Firm.*

This risk is managed centrally via the KKR Public Affairs team, the KKR client relationship team and locally by the Board of KKR CAI.

### **c) Operational risk**

*The risk of loss resulting from inadequate or failed internal processes relating to back office operations, human resources, legal, compliance, IT systems, financial reporting, public affairs, tax and insurance.*

KKR CAI has processes and controls in place to manage and mitigate operational risks and local controls are supplemented by operational support from KKR.

### **d) Credit and Market risk**

KKR CAI does not have material exposures to credit risk save for fee receivables and risk on banks with which it deposits funds and there are no material net exposures to market risk.

*Foreign exchange risk is the risk that changes in the value of non-euro denominated income and expenses, and assets or liabilities, will adversely impact the capital position of the Firm. The Firm may be exposed to risks associated with fluctuations in exchange rates due to the fact that its revenues and expenses may be denominated in different currencies.*

The Firm has minimal exposures to non-euro assets and liabilities due to its UK Branch activities.

## **5. Capital Resources and Capital Adequacy**

As at 31 December 2015, KKR CAI's capital resources were comprised of Tier 1 capital only, which included audited accumulated profits but does not take into account the unaudited profits of the Firm occurring subsequent to such date.

### **Capital Position as of 31 December 2015 (Amount in €000)**

	<u>€000</u>
Ordinary Share Capital	1
Capital Contribution	154,371
Reserves	32,521
Deductions	(157,936)
Available Tier 1 Capital	28,956

In addition, KKR CAI currently has access to additional capital resources through the Firm's direct parent company and ultimately from the KKR Group.

## **6. Minimum Capital Requirement**

As at 31 December 2015 KKR CAI's minimum regulatory capital requirement was €6,588k. The minimum regulatory capital requirement is calculated as the higher of the Firm's fixed overhead requirement or the sum of its credit risk and market risk requirements plus the Firm's pillar II requirement.

## **7. Oversight**

The Board of Directors monitors the on-going compliance of the Firm with its minimum capital requirements and ensures that the Firm maintains adequate capital to cover its material risks at all times. As at the 31 December 2015 the Firm had adequate capital resources to meet its ongoing regulatory and business requirements.

## **8. Internal Capital Adequacy Assessment Process (“ICAAP”)**

KKR CAI conducts at least annually an internal assessment of the amount of capital that is considered adequate to cover the risks facing the Firm’s current and future activities.

Determination of the business strategy for the Firm includes the projection of financial profitability, capital resources and capital requirements. Stress testing and scenario analysis are also conducted on these projections in order to determine the appropriate level of capital required to be held by the Firm. The key risks to which the business is or might be exposed are considered along with the amount of capital that would be considered adequate to cover the Firm in the event that those risks were to crystallise. In addition, the economic environment and the impact of adverse economic conditions on the Firm’s profitability and capital position are considered, as well as the actions that management would take in those situations.

## **9. Remuneration Code**

KKR CAI is authorised and regulated by the CBOI as a MIFID investment Firm and is subject to the rules on remuneration outlined in the CRD IV and CRR (collectively referred to as “CRD”). The CRD remuneration rules cover an individual’s total remuneration both fixed and variable. KKR CAI, in line with KKR, offers a fixed base salary to its employees and also a variable remuneration, which is dependent on individual and business performance.

KKR CAI’s policy is designed to ensure compliance with the CRD and the Firm’s compensation arrangements:

- Do not encourage excessive risk taking;
- Are consistent with and promote effective risk management;
- Include measures to avoid conflict of interest;
- Are in line with the Firm’s business strategy, objectives and interests.

The CRD requires authorised Firms to apply principles of proportionality when establishing and applying their remuneration policies, having regard to their size, internal organisation, nature, scope and complexity of their activities. The proportionality principles outlined in the CRD and the European Bank Authority Guidelines aims to match the remuneration policies and practices with the individual risk profile, risk appetite and the strategy of the Firm. KKR CAI’s policy and disclosures are made in accordance with these principles.

The remuneration of the KKR CAI senior management is set by the Global Heads of KKR Credit, as appropriate, in conjunction with members of the KKR Management Committee and with the assistance of the Human Resource department, having regard to the principles laid out in the Firm’s Remuneration Policy Statement and the Firm’s Conflict of Interest Policy.

Appropriate measures are taken to ensure that support and control function employees are not placed in a position where their activities could be directly linked to an increase in their variable remuneration. In addition to reporting to KKR CAI CEO, the support and control function employees have independent reporting lines to the

KKR Global Head of the relevant support and control function who also have input to support and control function employee remuneration.

The Remuneration Policy (in accordance with requirements of the CRD) outlines the governance framework supporting the remuneration practices in relation to staff whose professional activities have a material impact on the Firm's risk profile ("Identified Staff"). The schedule of Identified Staff is maintained by Compliance.

Remuneration is made up of fixed and variable elements. Variable remuneration is discretionary and is awarded based on performance against a number of financial and non-financial metrics, in each case taking appropriate consideration of all regulatory guidance, the function of the relevant employees and the impact of their actions on the risk profile of the Firm. Variable remuneration is paid in cash and in certain cases in common units of KKR, which may be subject to a deferral process.

For the year ended 31 December 2015, total remuneration payable to Senior Management who are involved in the KKR CAI business was €5.2m.