Commission Directive 2010/43/EU of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards organisational requirements, conflicts of interest, conduct of business, risk management and content of the agreement between a depositary and a management company (Text with EEA relevance)

CHAPTER VI

RISK MANAGEMENT

(Article 51(1) of Directive 2009/65/EC)

SECTION 1

Risk management policy and risk measurement

Article 38

Risk management policy

1 Member States shall require management companies to establish, implement and maintain an adequate and documented risk management policy which identifies the risks the UCITS they manage are or might be exposed to.

The risk management policy shall comprise such procedures as are necessary to enable the management company to assess for each UCITS it manages the exposure of that UCITS to market, liquidity and counterparty risks, and the exposure of the UCITS to all other risks, including operational risks, which may be material for each UCITS it manages.

Member States shall require management companies to address at least the following elements in the risk management policy:

a the techniques, tools and arrangements that enable them to comply with the obligations set out in Articles 40 and 41;

b the allocation of responsibilities within the management company pertaining to risk management.

2 Member States shall require management companies to ensure that the risk management policy referred to in paragraph 1 states the terms, contents and frequency of reporting of the risk management function referred to in Article 12 to the board of directors and to senior management and, where appropriate, to the supervisory function.

3 For the purposes of paragraphs 1 and 2, Member States shall ensure that management companies take into account the nature, scale and complexity of their business and of the UCITS they manage.

Article 39

Assessment, monitoring and review of risk management policy

1 Member States shall require management companies to assess, monitor and periodically review:

a the adequacy and effectiveness of the risk management policy and of the arrangements, processes and techniques referred to in Articles 40 and 41;

b the level of compliance by the management company with the risk management policy and with arrangements, processes and techniques referred to in Articles 40 and 41;

c the adequacy and effectiveness of measures taken to address any deficiencies in the performance of the risk management process.

2 Member States shall require management companies to notify to competent authorities of their home Member State any material changes to the risk management process.

3 Members States shall ensure that requirements laid down in paragraph 1 are subject to review by the competent authorities of the management company's home Member State on an on-going basis and accordingly when granting authorisation.

SECTION 2

Risk management processes, Counterparty risk exposure and issuer concentration

Article 40

Measurement and management of risk

1 Member States shall require management companies to adopt adequate and effective arrangements, processes and techniques in order to:

a measure and manage at any time the risks which the UCITS they manage are or might be exposed to;

b ensure compliance with limits concerning global exposure and counterparty risk, in accordance with Articles 41 and 43.

Those arrangements, processes and techniques shall be proportionate to the nature, scale and complexity of the business of the management companies and of the UCITS they manage and be consistent with the UCITS risk profile.

2 For the purposes of paragraph 1, Member States shall require management companies to take the following actions for each UCITS they manage:

a put in place such risk measurement arrangements, processes and techniques as are necessary to ensure that the risks of taken positions and their contribution to the overall risk profile are accurately measured on the basis of sound and reliable data and that the risk measurement arrangements, processes and techniques are adequately documented;

b conduct, where appropriate, periodic back-tests in order to review the validity of risk measurement arrangements which include model-based forecasts and estimates;

c conduct, where appropriate, periodic stress tests and scenario analyses to address risks arising from potential changes in market conditions that might adversely impact the UCITS;

d establish, implement and maintain a documented system of internal limits concerning the measures used to manage and control the relevant risks for each UCITS taking into account all risks which may be material to the UCITS as referred to in Article 38 and ensuring consistency with the UCITS risk-profile;

e ensure that the current level of risk complies with the risk limit system as set out in point (d) for each UCITS;

f establish, implement and maintain adequate procedures that, in the event of actual or anticipated breaches to the risk limit system of the UCITS, result in timely remedial actions in the best interests of unit-holders.

3 Member States shall ensure that management companies employ an appropriate liquidity risk management process in order to ensure that each UCITS they manage is able to comply at any time with Article 84(1) of Directive 2009/65/EC.

Where appropriate, management companies shall conduct stress tests which enable assessment of the liquidity risk of the UCITS under exceptional circumstances.

4 Member States shall require management companies to ensure that for each UCITS they manage the liquidity profile of the investments of the UCITS is appropriate to the redemption policy laid down in the fund rules or the instruments of incorporation or the prospectus.

Article 41

Calculation of global exposure

1 Member States shall require management companies to calculate the global exposure of a managed UCITS as referred to in Article 51(3) of Directive 2009/65/EC as either of the following:

a the incremental exposure and leverage generated by the managed UCITS through the use of financial derivative instruments including embedded derivatives pursuant to the fourth subparagraph of Article 51(3) of Directive 2009/65/EC, which may not exceed the total of the UCITS net asset value;

b the market risk of the UCITS portfolio.

2 Member States shall require management companies to calculate the UCITS global exposure on at least a daily basis.

3 Member States may allow management companies to calculate global exposure by using the commitment approach, the value at risk approach or other advanced risk measurement methodologies as may be appropriate. For the purposes of this provision, ‘value at risk’ shall mean a measure of the maximum expected loss at a given confidence level over a specific time period.

Member States shall require management companies to ensure that the method selected to measure global exposure is appropriate, taking into account the investment strategy pursued by the UCITS and the types and complexities of the financial derivative instruments used, and the proportion of the UCITS portfolio which comprises financial derivative instruments.

4 Where a UCITS in accordance with Article 51(2) of Directive 2009/65/EC employs techniques and instruments including repurchase agreements or securities lending transactions in order to generate additional leverage or exposure to market risk, Member States shall require

management companies to take these transactions into consideration when calculating global exposure.

Article 42

Commitment approach

1 Where the commitment approach is used for the calculation of global exposure, Member States shall require management companies to apply this approach to all financial derivative instrument positions including embedded derivatives as referred to in the fourth subparagraph of Article 51(3) of Directive 2009/65/EC, whether used as part of the UCITS general investment policy, for purposes of risk reduction or for the purposes of efficient portfolio management as referred to in Article 51(2) of that Directive.

2 Where the commitment approach is used for the calculation of global exposure, Member States shall require management companies to convert each financial derivative instrument position into the market value of an equivalent position in the underlying asset of that derivative (standard commitment approach).

Member States may allow management companies to apply other calculation methods which are equivalent to the standard commitment approach.

3 Member States may allow a management company to take account of netting and hedging arrangements when calculating global exposure, where these arrangements do not disregard obvious and material risks and result in a clear reduction in risk exposure.

4 Where the use of financial derivative instruments does not generate incremental exposure for the UCITS, the underlying exposure need not be included in the commitment calculation.

5 Where the commitment approach is used, temporary borrowing arrangements entered into on behalf of the UCITS in accordance with Article 83 of Directive 2009/65/EC need not be included in the global exposure calculation.

Article 43

Counterparty risk and issuer concentration

1 Member States shall require management companies to ensure that counterparty risk arising from an over-the-counter (OTC) financial derivative instrument is subject to the limits set out in Article 52 of Directive 2009/65/EC.

2 When calculating the UCITS exposure to a counterparty in accordance with the limits as referred to in Article 52(1) of Directive 2009/65/EC, management companies shall use the positive mark-to-market value of the OTC derivative contract with that counterparty.

Management companies may net the derivative positions of a UCITS with the same counterparty, provided that they are able to legally enforce netting agreements with the counterparty on behalf of the UCITS. Netting shall only be permissible with respect to OTC derivative instruments with the same counterparty and not in relation to any other exposures the UCITS may have with that same counterparty.

3 Member States may allow management companies to reduce the UCITS exposure to a counterparty of an OTC derivative transaction through the receipt of collateral. Collateral

received shall be sufficiently liquid so that it can be sold quickly at a price that is close to its pre-sale valuation.

4 Member States shall require management companies to take collateral into account in calculating exposure to counterparty risk as referred to in Article 52(1) of Directive 2009/65/EC when the management company passes collateral to OTC counterparty on behalf of the UCITS. Collateral passed may be taken into account on a net basis only if the management company is able to legally enforce netting arrangements with this counterparty on behalf of the UCITS.

5 Member States shall require management companies to calculate issuer concentration limits as referred to in Article 52 of Directive 2009/65/EC on the basis of the underlying exposure created through the use of financial derivative instruments pursuant to the commitment approach.

6 With respect to the exposure arising from OTC derivatives transactions as referred to in Article 52(2) of Directive 2009/65/EC, Member States shall require management companies to include in the calculation any exposure to OTC derivative counterparty risk.

SECTION 3

Procedures for the valuation of the OTC derivatives

Article 44

Procedures for the assessment of the value of OTC derivatives

1 Member States shall require management companies to verify that UCITS exposures to OTC derivatives are assigned fair values that do not rely only on market quotations by the counterparties of the OTC transactions and which fulfil the criteria set out in Article 8(4) of Directive 2007/16/EC.

2 For the purposes of paragraph 1, management companies shall establish, implement and maintain arrangements and procedures which ensure appropriate, transparent and fair valuation of UCITS exposures to OTC derivatives.

Member States shall require management companies to ensure that the fair value of OTC derivatives is subject to adequate, accurate and independent assessment.

The valuation arrangements and procedures shall be adequate and proportionate to the nature and complexity of the OTC derivatives concerned.

Management companies shall comply with the requirements set out in Article 5(2) and in the second subparagraph of Article 23(4) when arrangements and procedures concerning the valuation of OTC derivatives involve the performance of certain activities by third parties.

3 For the purposes of paragraphs 1 and 2, the risk management function shall be appointed with specific duties and responsibilities.

4 The valuation arrangements and procedures referred to in paragraph 2 shall be adequately documented.

SECTION 4

Transmission of information on derivative instruments

Article 45

Reports on derivative instruments

1 Member States shall require management companies to deliver to the competent authorities of their home Member State, at least on an annual basis, reports containing information which reflects a true and fair view of the types of derivative instruments used for each managed UCITS, the underlying risks, the quantitative limits and the methods which are chosen to estimate the risks associated with the derivative transactions.

2 Member States shall ensure that the competent authorities of the management company's home Member State review the regularity and completeness of information referred to in paragraph 1 and that they have an opportunity to intervene where appropriate.