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Deloitte Valuation Conference

Valuation matters
for conducting
officers and risk
managers

April 2015



Conference Agenda

2015 Valuation Conference Series



1. Valuation for AIFMs

10 February 2015

2. AIFMD valuation requirements for depositary banks & asset servicers

24 February 2015

3. Fund directors: valuation and related risks

12 March 2015

4. Valuation matters for conducting officers and risk managers

23 April 2015

5. Fair Value requirements under IFRS 10 and 13

21 May 2015

6. Sound valuation in credit institutions: more than a regulatory requirement

16 June 2015

7. Valuations for incentive plans

15 October 2015

8. Valuation and Tax considerations

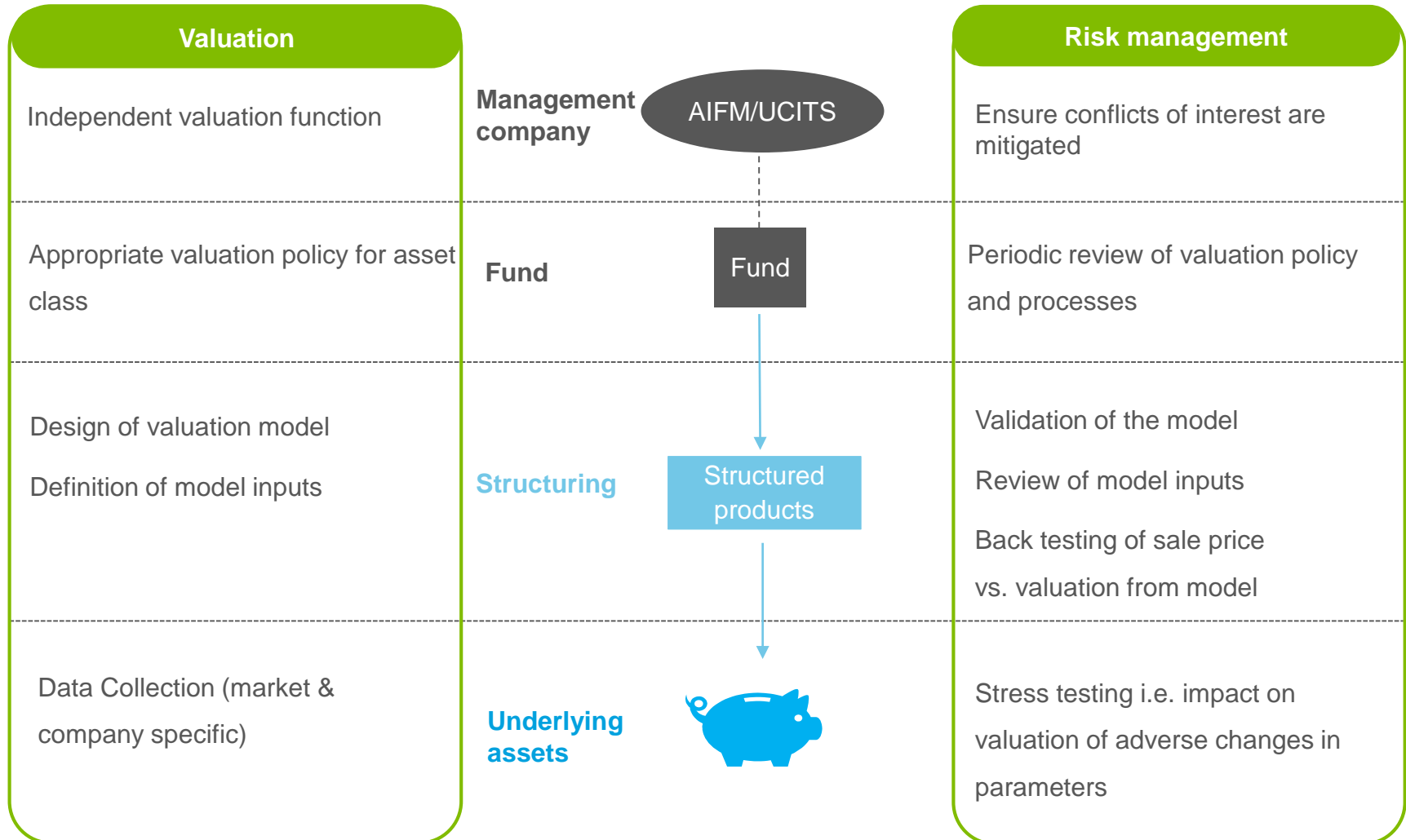
12 November 2015

9. Valuation: How to meet audit requirements

8 December 2015

Valuation matters for conducting officers and risk managers

Interaction between valuation and risk management



Valuation matters for conducting officers and risk managers

UCITS legal framework and principles

UCITS IV Legal Framework

Laws and regulations

UCITS Law 2010
Grand Ducal
regulation 2008
CSSF Circular
08/380
CSSF Regulation
10-04

OTC derivatives
subject to daily
reliable and verifiable
valuation
UCITS should be
able to close
positions at **fair
value**

Principles

- **Fair value** is amount for which asset could be exchanged between knowledgeable willing parties at **arm's length**
- OTC derivatives **fair value** is considered **verifiable** and **reliable** if:
 - valuation is based on up-to-date market value or pricing model using adequate **recognized** methodology; and
 - verification is performed by appropriate **independent** third party or by independent unit from investment manager

Risk management **ensures accurate and independent OTC derivatives valuation**

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AIFMD legal framework and principles

AIFMD Legal Framework

Laws and regulations

AIFM Directive
AIFM Regulation
AIFM Law 2013
SIF Law 2007

Valuation of AIF's assets based on the **fair value** unless otherwise specified

Principles

- AIFM's procedures should ensure **proper** and **independent** valuation can be performed
- Where **models** are used, they should be validated by internal or external individuals not involved in the building process
- Damages from failure to carry out sufficient due diligence, including **valuation improperly carried out**, trigger AIFM's **professional liabilities**

Risk manager **should review the documentation of the valuation process** and, when necessary, **provide support**

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Roles and responsibilities in the valuation value chain

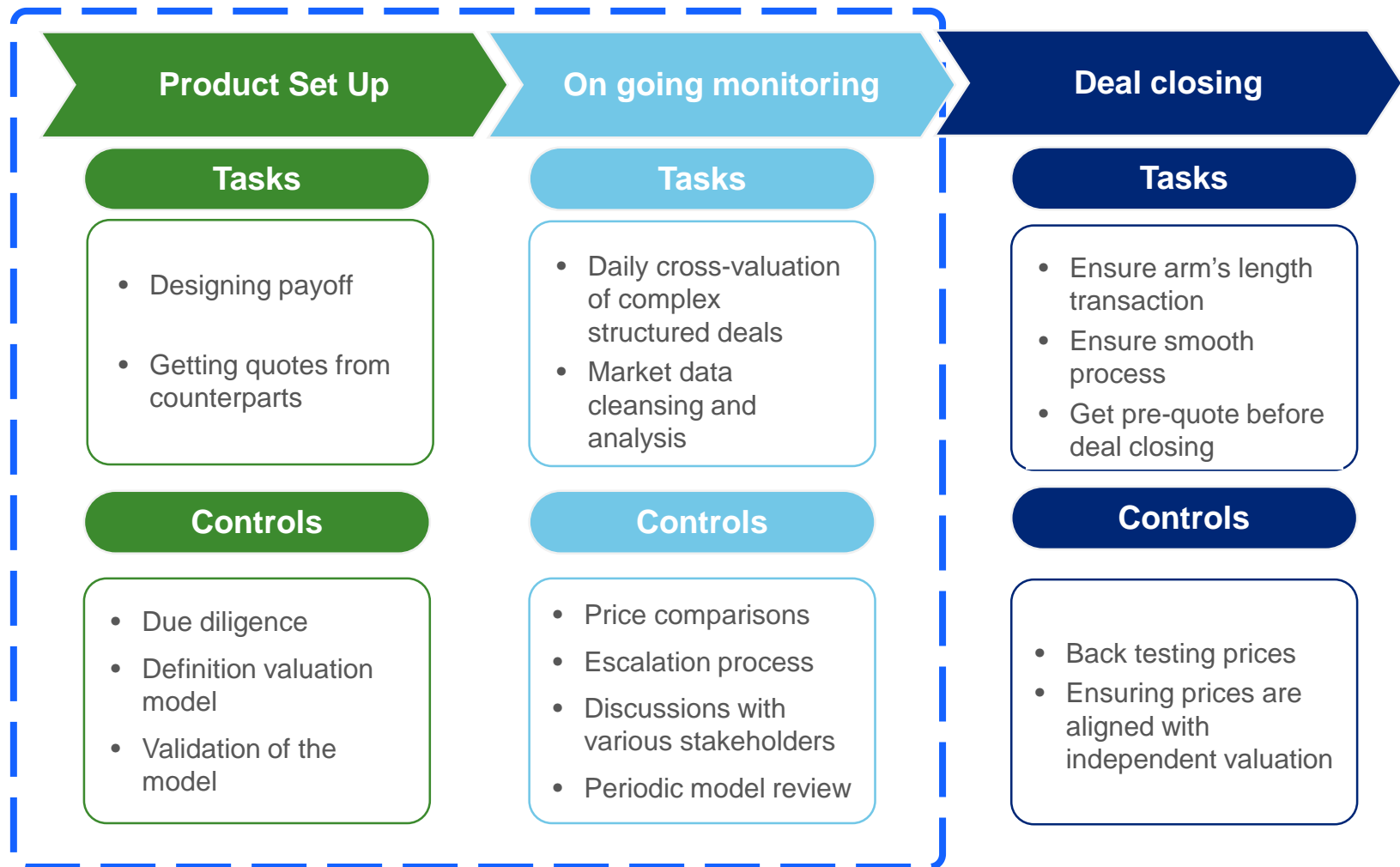


<p>Board of Directors conducting officers and/or Valuation committee</p>	<ul style="list-style-type: none"> • Ultimately responsible for valuation • Understand and approve model and policy for each asset class 	<ul style="list-style-type: none"> • Make decisions on valuation issues following escalation process 	<ul style="list-style-type: none"> • Perform due diligence on models and delegates 	<ul style="list-style-type: none"> • Ensure escalation process is in place • Make decisions based on escalation • Liaise with Auditors and valuation delegates 	<ul style="list-style-type: none"> • Oversight of Fund Administration delegate
<p>Risk Manager</p>	<ul style="list-style-type: none"> • Review valuation model and policy appropriateness vs. AIF risk profile 	<ul style="list-style-type: none"> • Has to provide technical support in case of issue 	<ul style="list-style-type: none"> • Ensure Depository Bank can perform oversight vs. risk profile of the fund (information flow) 	<ul style="list-style-type: none"> • Be involved in the escalation process and intervention 	<ul style="list-style-type: none"> • Ensure NAV process is appropriate

Valuation matters for conducting officers and risk managers

Case study 1 – AIF investing in illiquid structured products

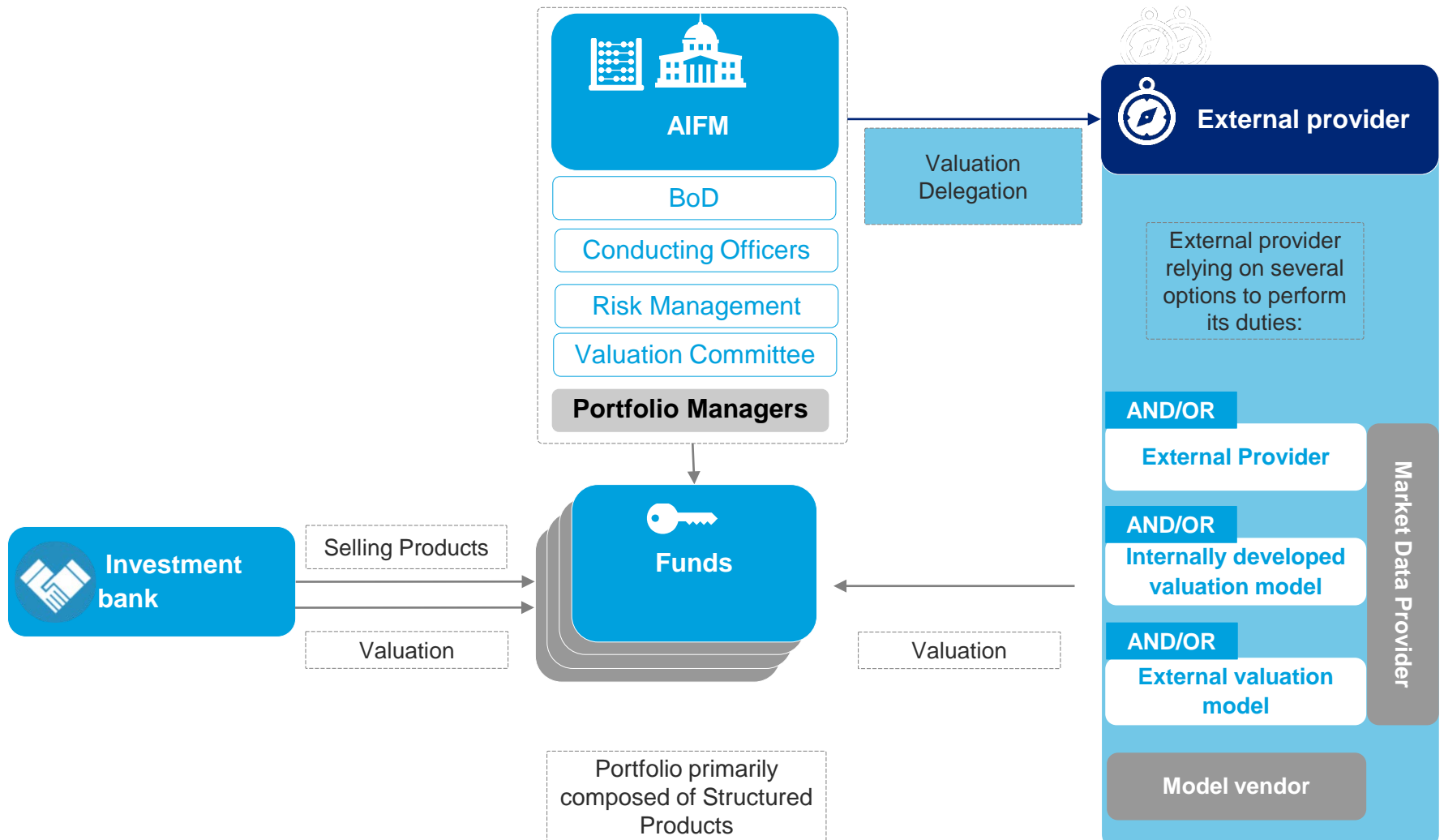
Setting the scene (1/5) : Product life cycle and related controls



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Case study 1 – AIF investing in illiquid structured products

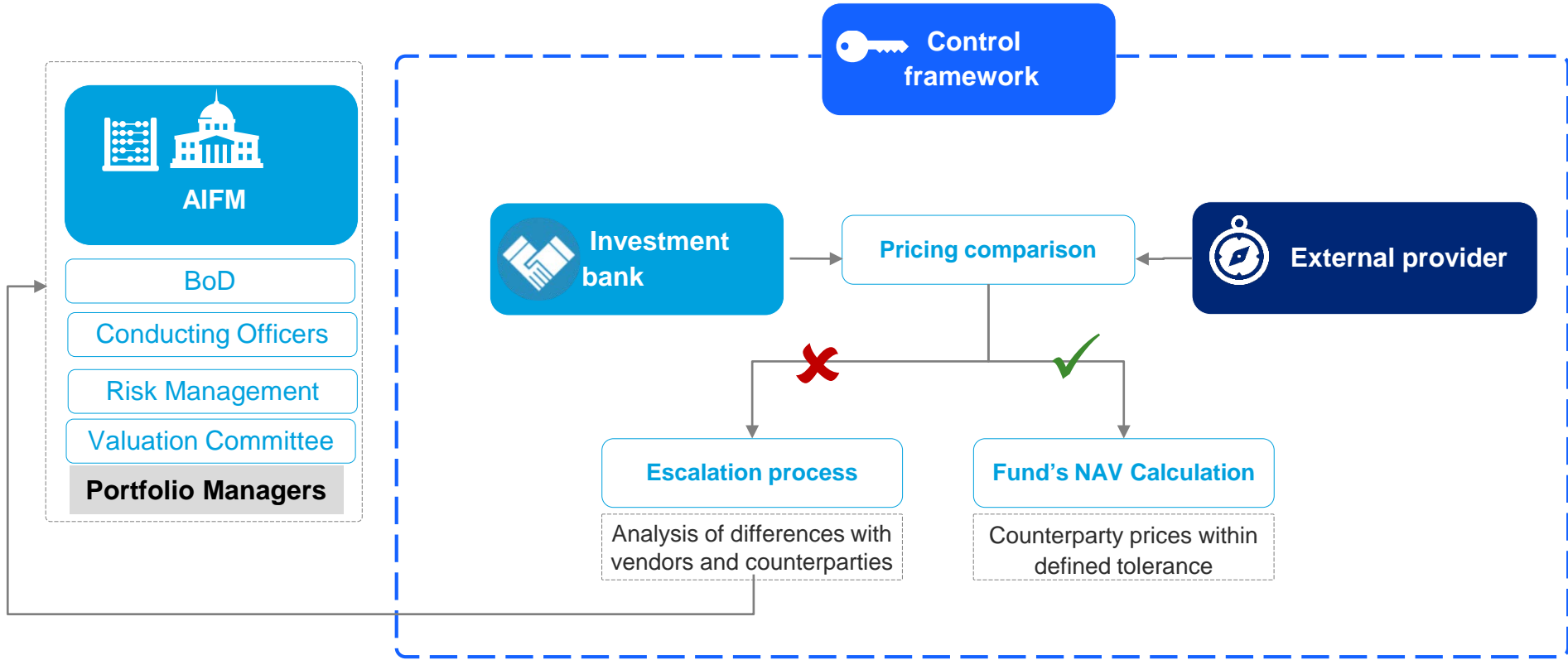
Setting the scene (2/5) : Various stakeholders



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Case study 1 – AIF investing in illiquid structured products

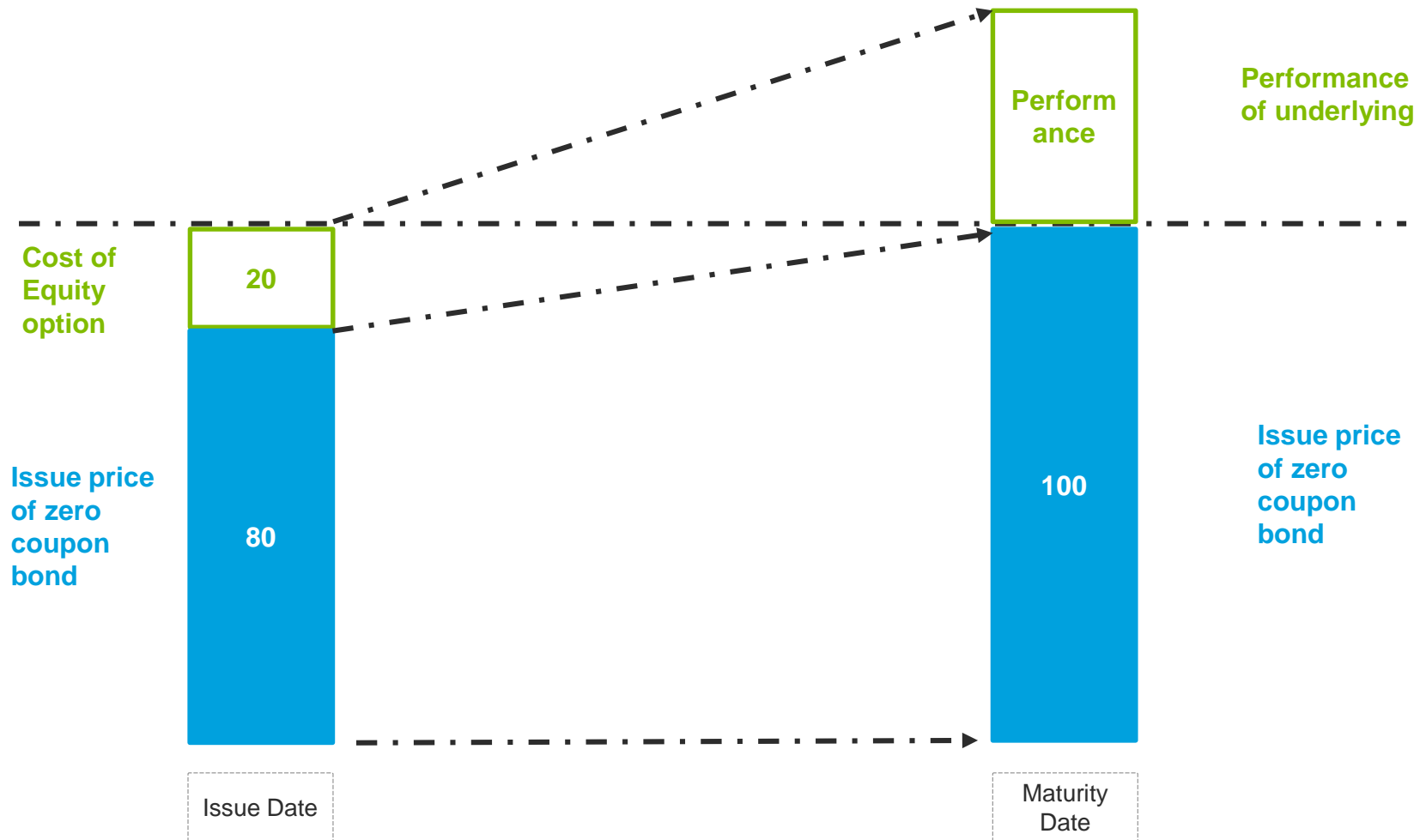
Setting the scene (3/5) : Control framework



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Case study 1 – AIF investing in illiquid structured products

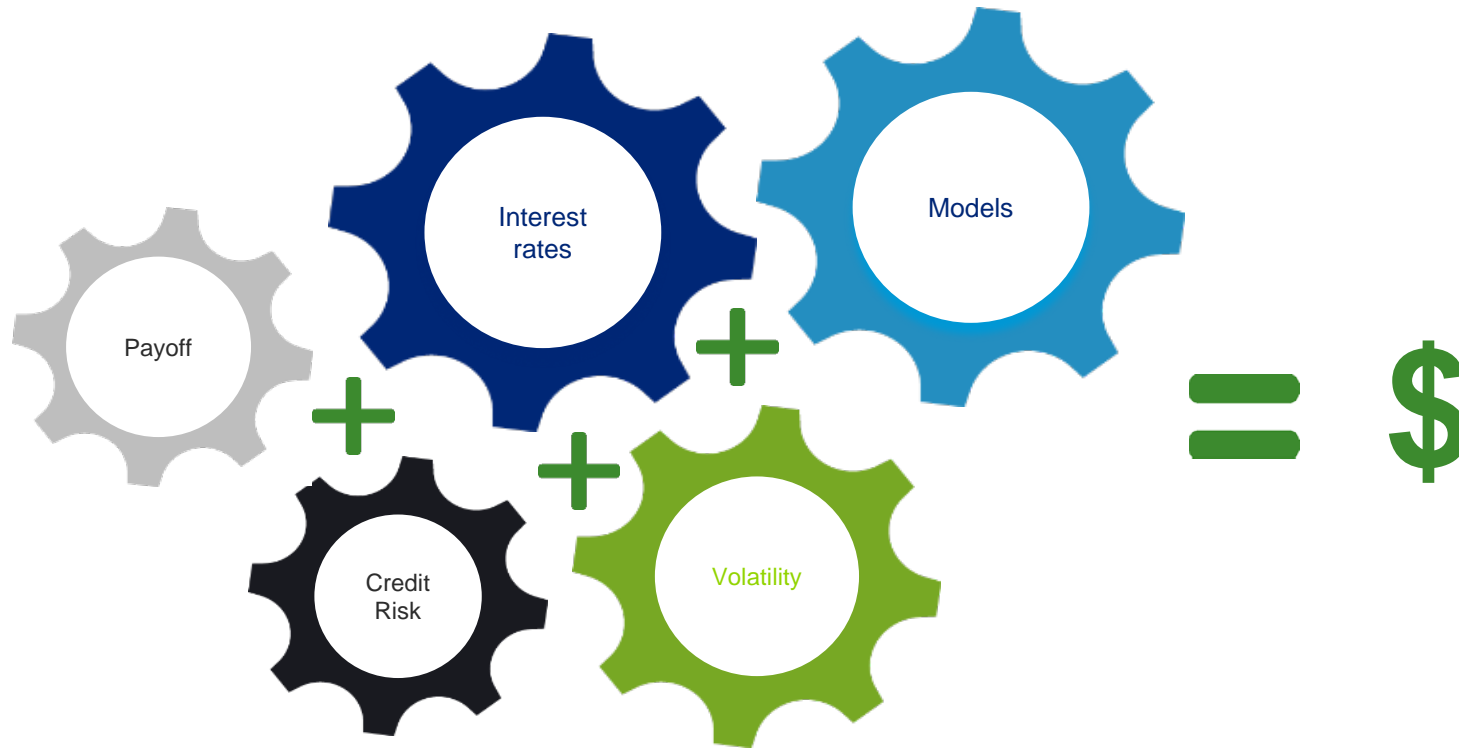
Setting the scene (4/5) : Capital guaranteed product



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Case study 1 – AIF investing in illiquid structured products

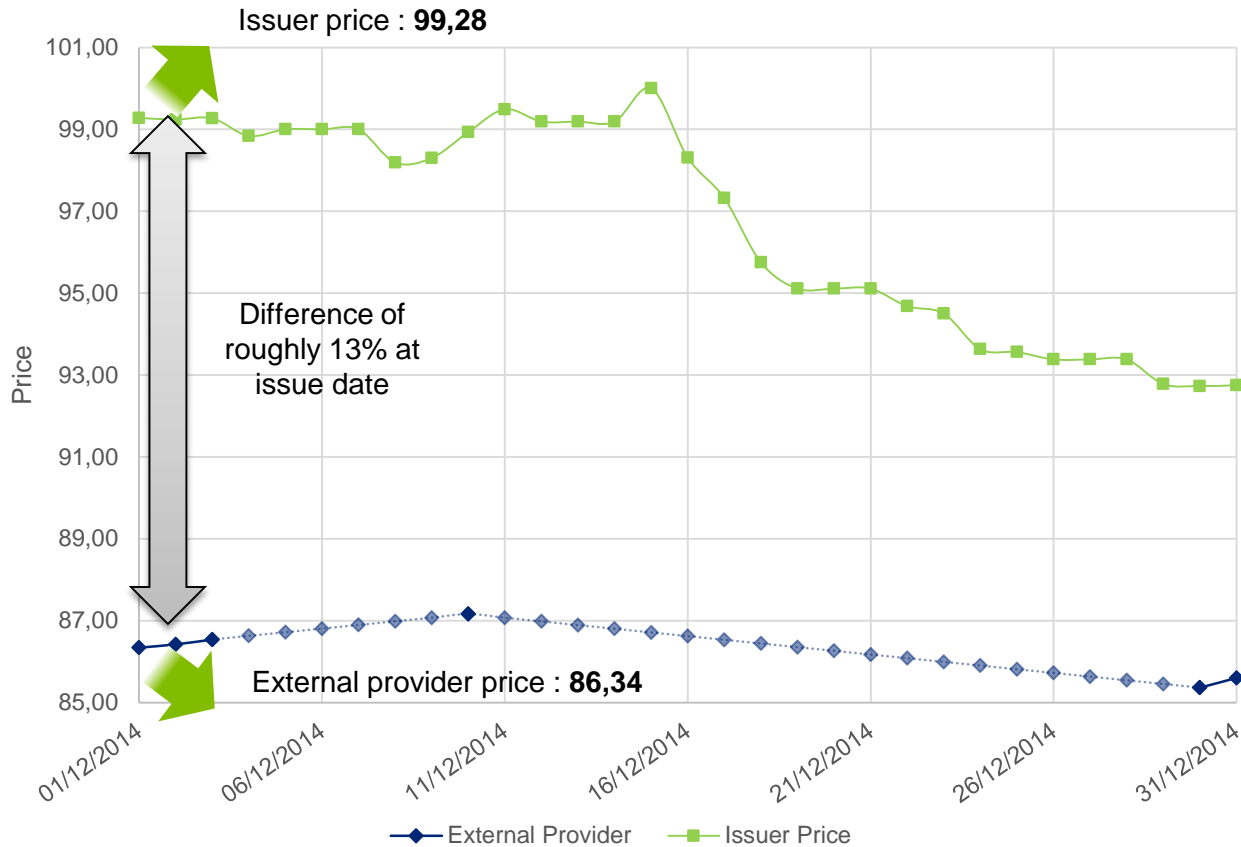
Setting the scene (5/5) : Product life cycle and related controls



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Case study 1 – AIF investing in illiquid structured products

External provider valuation compared with Issuer price



Observations and facts

- Independent valuation took place at the NAV frequency
- Differences above threshold were investigated
- Prices tend to converge but still above the threshold

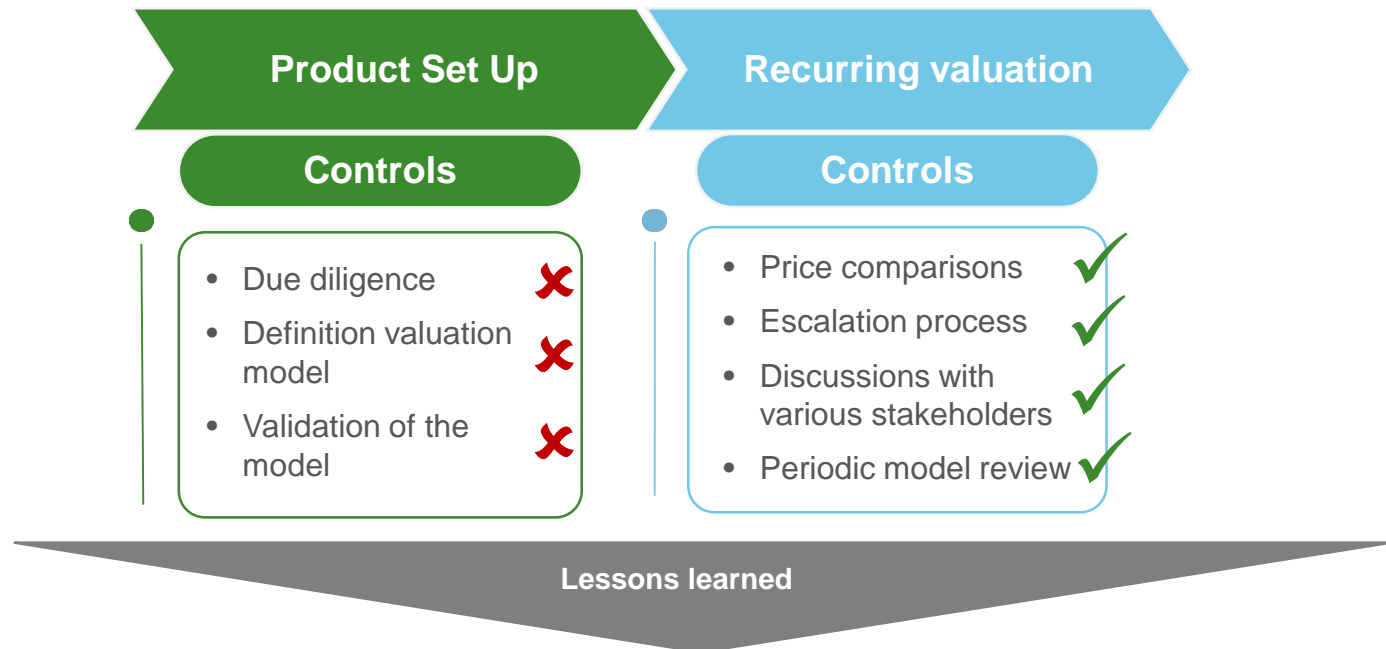
WHAT WENT WRONG ?

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Case study 1 – AIF investing in illiquid structured products

What went wrong ?

The product lifecycle and particularly the controls related to the two first phases

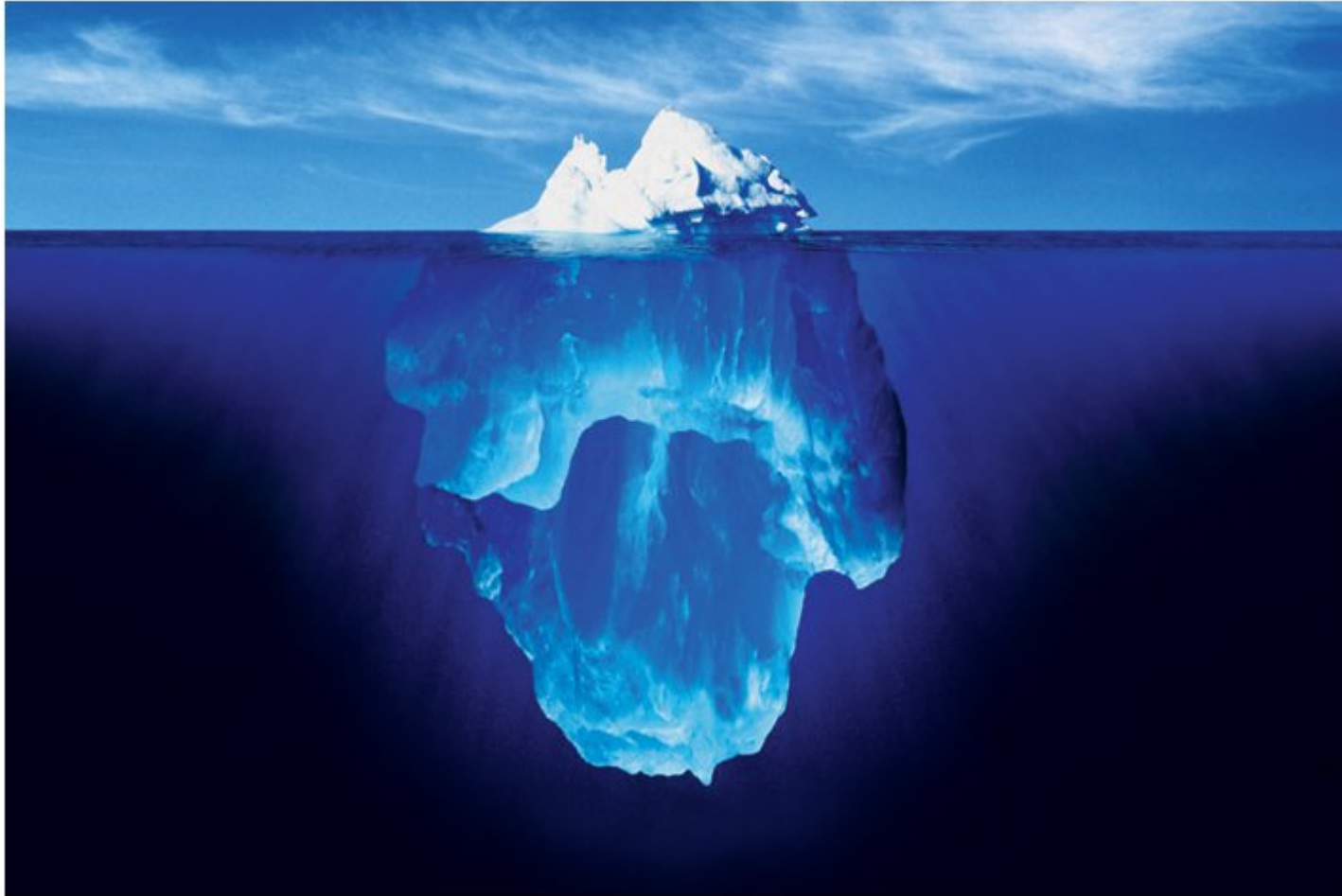


A sound risk management process includes any single piece of the control framework foreseen by the regulations. Missing one part might lead to systemic consequences and that could trigger AIFM's professional liabilities

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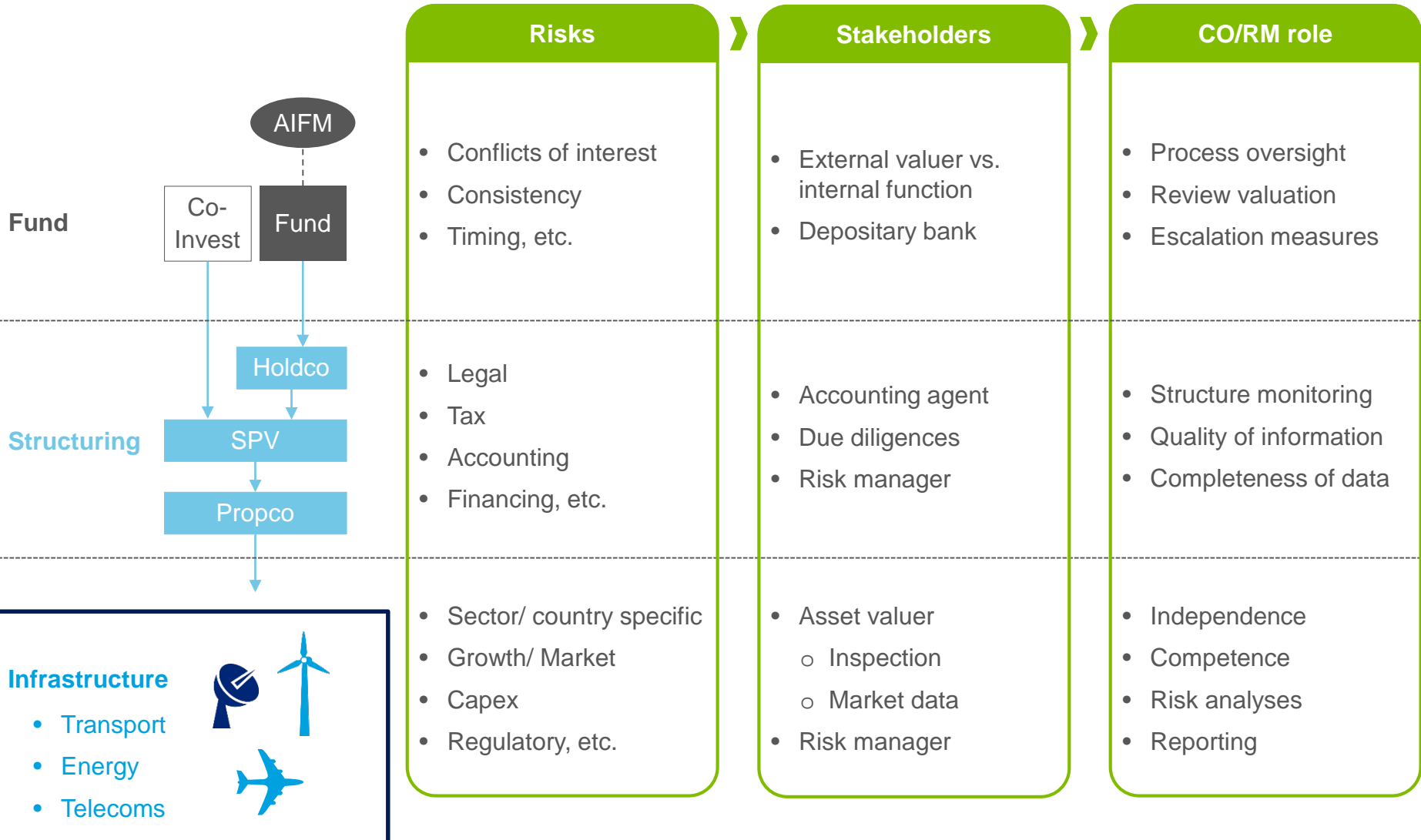
Case study 1 – AIF investing in illiquid structured products

Conclusions : Don't believe what you see



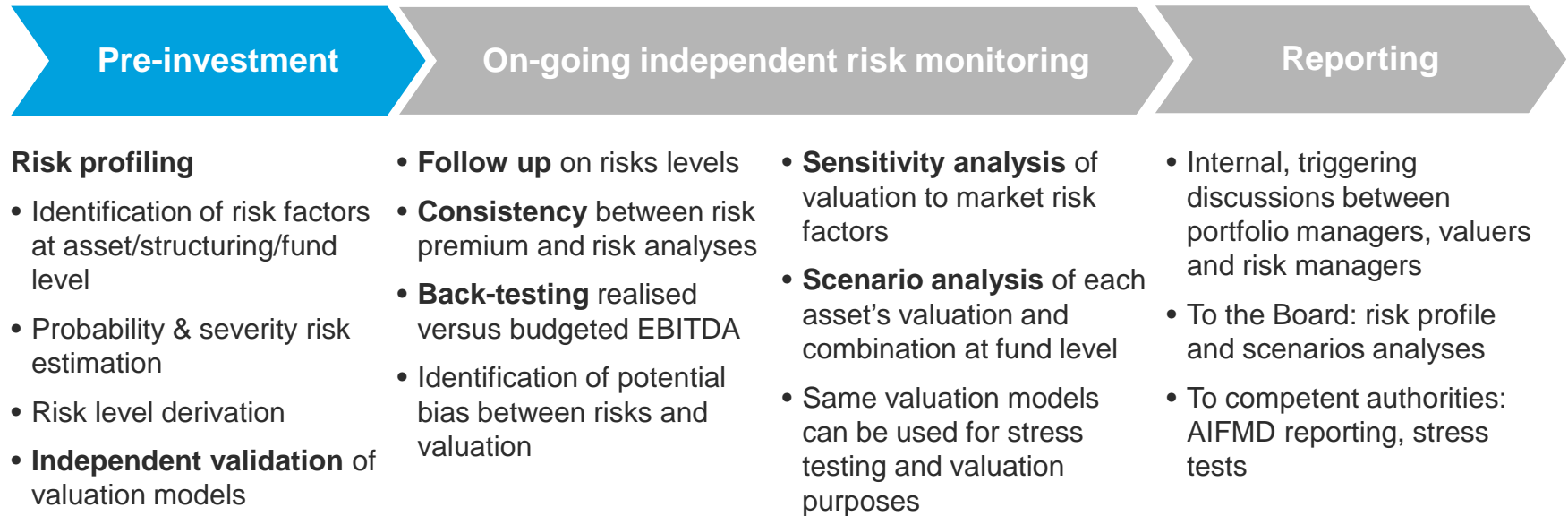
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Case Study 2 – AIF investing in infrastructure



Valuation matters for conducting officers and risk managers

Case Study 2 – AIF investing in infrastructure



Outcomes of independent risk analyses for valuation purposes:

- Bring assurance to conducting officers on the consistency between risks levels and valuations
- Bring a fair picture of the risk profile of the fund, including sensitivities to stressed scenarios
- Identify potential outlier assets from a risk standpoint

Valuation matters for conducting officers and risk managers

Panelists

Enrico Turchi

Managing Director, Pioneer AM

Dr. Luc Neuberg

Conducting Officer, BCEE AM

Michael Derwael

Risk Manager, Lombard Odier Funds (Europe)

Thank you for listening

If you have any questions or comments, please contact valuation@deloitte.lu

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