DRAFT

AUTORITÉ DES MARCHÉS FINANCIERS

RISK DATA AGGREGATION AND RISK REPORTING GUIDELINE

February 2016

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Preamble

The *Autorité des marchés financiers* (“AMF”) establishes guidelines setting out its expectations with respect to financial institutions’ legal requirement to follow sound and prudent management practices. This guideline therefore covers the interpretation, execution and application of this requirement.

The AMF favours a principles-based approach rather than a specific rules-based approach. As such, the guidelines provide financial institutions with the necessary latitude to determine the requisite strategies, policies and procedures for implementation of such management principles and to apply sound practices based on the nature, size and complexity of their activities. In this regard, this guideline illustrates how to comply with the stated principles.

AMF note

The AMF considers governance, integrated risk management and compliance (GRC) as the foundation stones for the sound and prudent management and sound commercial practices of financial institutions and, consequently, as the basis for the prudential framework provided by the AMF.

This guideline is part of this approach and sets out the AMF’s expectations regarding risk data aggregation and risk disclosure practices.

Scope

The *Risk Data Aggregation and Risk Reporting Guideline* is applicable to federations of credit unions governed by the *Act respecting financial services cooperatives*, CQLR, c. C-67.3.

The generic terms “financial institution” and “institution” refer to any federation of credit unions and its financial group, as applicable, covered by the scope of this guideline.

Coming into effect and updating

The *Risk Data Aggregation and Risk Reporting Guideline* is effective as of February 1, 2016.

With respect to the legal requirement of institutions to follow sound and prudent management practices, the AMF expects them to be implemented as soon as this guideline is published. Where an institution has already implemented such a framework, the AMF may verify whether such a framework enables it to comply with the legal requirements.

This guideline will be updated based on risk data aggregation and risk disclosure developments and observations noted during the monitoring of the financial institutions covered.

Introduction

During the latest global financial crisis, many major institutions had difficulty disclosing their risk data, which was often required with little lead time by regulators or other market participants such as rating agencies. The inadequacy of the information technology used by systemically important financial institutions with respect to the financial risks they faced as well as the capability of these institutions to incorporate all the information on risks from the various business lines, were strongly questioned. The result was that the viability of some of these institutions and the stability of their markets were jeopardized.

In response to this crisis, the Basel Committee on Banking Supervision ("Basel Committee") undertook a series of reforms so as to optimize the industry's regulatory, monitoring and risk management practices.

Strengthening the transparency and disclosure of institutions are among the objectives of these reforms. In this context, the Basel Committee published the document titled *Principles for effective risk data aggregation and risk reporting*[1] so as to strengthen the capability of systemic institutions to aggregate and disclose their risk data. The document presents 14 principles covering the following topics: governance and infrastructure, risk data aggregation capabilities, risk disclosure practices and supervisor's role.

From this perspective, as outlined in the *Integrated Risk Management Guideline,*[2] it is important for the AMF and the various market participants to be able to access integrated reports on the major risks to which institutions are exposed, especially those for which any threat to their viability could provoke a systemic crisis.

The AMF adheres to the principles of the main regulatory bodies, including those of the Basel Committee on Banking Supervision and of the International Association of Insurance Supervisors (IAIS), which foster better integration and disclosure of information on risks, allowing financial institutions to better anticipate issues likely to affect their viability.

Therefore, so as to adapt the Basel Committee document to federations of credit unions, the AMF considers it essential to establish guidance as to the governance and infrastructure required for the optimization of processes, as well as specific guidance on risk data aggregation capabilities and practices for disclosing these risks.

Pursuant to the authority conferred upon it under the *Act respecting financial services cooperatives* ("FSCA"),[3] the AMF is issuing this guideline expressly to inform federations of credit unions of its expectations regarding risk data aggregation and the disclosure of these risks.

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1 Basel Committee on Banking Supervision. *Principles for effective risk data aggregation and risk reporting*, January 2013.

2 Autorité des marchés financiers. *Integrated Risk Management Guideline*, April 2009, updated May 2015.

3 *An Act respecting financial services cooperatives.* CQLR, c. C-67.3, s. 565.

General observations

The AMF expects financial institutions to implement a framework allowing them to properly aggregate all material risks and to disclose them to market participants in an accurate, timely manner and appropriate to the circumstances. Once implemented, this framework should enable the institutions to optimize their integrated risk management.

The AMF expects the information on risks that is disclosed by institutions to be effectively aggregated, for all business lines in which they operate. This information must be communicated to market participants in a timely manner, in accordance with the nature of the risks they face, and their impact on the institution’s risk profile.

Risk data aggregation and disclosure must be possible at any time, in particular in times of crisis or of major organizational change, such as mergers and acquisitions. The board of directors and senior management could use it to determine whether the new products and services offer negatively affects the institution’s risk profile, for instance.

The AMF also expects financial institutions to optimize their control procedure as regards the quality of information disclosed so as to present the most accurate information possible on their aggregated risk exposure. This procedure must be standardized in the various legal persons that are part of the institution, even those stemming from a merger process.

Furthermore, the AMF expects the risk data aggregation and disclosure process to adapt on an ongoing basis, so that financial institutions can produce *ad hoc* reports based on the available risk information infrastructure. This adaptation capability is also relevant when presenting the impact of emerging risks.

The implementation of this guideline should ultimately allow the optimization of integrated risk management and serve as an important strategic decision-making tool.

1. Governance and infrastructure

The AMF expects the implementation of a risk data aggregation and disclosure initiative to rely on the participation of authorities with responsibility for these data. Furthermore, the AMF expects institutions to appoint a function in charge of monitoring the management of the data quality controls for risks throughout their life cycle.

This guidance should be part of a financial institution's governance program, as stated in the *Governance Guideline.*[4] The board of directors should insure that senior management relies on expertise in the management of information technology. Since senior management is in charge of seeing to the effectiveness of the organizational structure, it should, in this respect, ensure the coherence between the supervision measures to be implemented for integrated risk reports and the efficiency desired for the disclosure of these risks.

The board of directors and senior management of the institution should ensure the implementation of a policy to protect data confidentiality, availability and integrity. This policy will enable the standardization of the risk data aggregation and disclosure processes.

As the implementation of a risk data aggregation and disclosure initiative involves the entire organization, it is desirable to ensure the participation of all authorities with responsibility for these data, including risk management, compliance, information technology management, and finance and control functions.

The institution should also rely on an independent function for the validation of its risk data aggregation and disclosure processes. This function should be able to confirm that these processes correspond to the institution's risk profile and that the risk data protection policy is observed by all stakeholders, including managers, employees, consultants and third parties. Furthermore, the independent function should coordinate its work with that of the chief risk officer, or member of senior management in charge of this mandate.

Given that the risk data aggregation capability could be modified by a major organizational change (i.e. cession, acquisition, merger, modification of the information technology architecture) or by the development and implementation of a new product, the board of directors and senior management should take these changes into account as part of the due diligence processes. The aggregation capability should be preserved in all business lines where the institution is present. Any major limitation detected in this capability will have to be reported to the board of directors and senior management.

As for infrastructure, the AMF expects the institution to appoint a function in charge of monitoring the management of risk data quality control throughout their life cycle. This function could be performed by a member of senior management, who will have to be independent of the units that generate income for the institution.

[4] Autorité des marchés financiers. *Governance Guideline*, April 2009.

This function should also guarantee the reliability of the technology infrastructure required to manage the data, both in periods of normal operation as well as times of crisis. Although the AMF does not expect the institution to use a single data model, the function in charge of data quality should oversee that sound reconciliation procedures are implemented, in the event that the institution uses different data models. The standardization of data identifiers (e.g. clients, number of accounts) and the information on the risk data characteristics in all the applications used by the institution should be included in these procedures. The progress of this standardization project will have to be documented, validated and made available to the AMF.

Given the importance of counting on a solid technology infrastructure for the successful aggregation and disclosure of risk data, the AMF expects the institutions to optimize their information technology infrastructure.

That optimization could be achieved by limiting the production of manual reports, and also by facilitating data flow between the different business lines and between the jurisdictions in which the institution operates, as applicable. The evolution of such initiative will have to be validated by the independent function, while making sure the heads of all the business lines are on board.

The institution's business continuity plan should consider the potential impact of major incidents on the confidentiality, availability and integrity of risk data.[5] This impact should be quantified by using techniques such as crisis simulations, recovery time objective indicators and update processes.

[5] Autorité des marchés financiers. *Business Continuity Management Guideline*, April 2010.

2. Risk data aggregation capabilities

> The AMF expects financial institutions to ensure the accuracy, timeliness and adaptability of risk data, based on the implementation of a control framework for the aggregation process of this data. Furthermore, the AMF expects the risk data aggregation capability to be effective at all times, even in a crisis.

Institutions should have a strict control framework for the entire risk data production process. This framework should include controls on the data generated by external suppliers, which will have to offer their services by respecting the governance principles of outsourcing arrangements.[6]

In cases where an institution works in different business lines, or even in different jurisdictions, it is recommended establishing common parameters to determine whether risks are material. It is also desirable to adopt a permanent reconciliation procedure between the data from different sources and between different types of data. This procedure must facilitate the analysis of differences between sources (qualitative and quantitative) in order to proceed with the necessary depurations before the data aggregation.

The independent function responsible for the validation of the risk data aggregation and disclosure processes mentioned in the previous section will need to have special and permanent access to all the software used for risk data production for the institution. In the event that considerable gaps between these processes and the validated reports are observed, senior management will have to be quickly informed so that corrective actions can be implemented as soon as possible.

Moreover, the independent function will have to continuously oversee that risks are presented consistently, but without necessarily targeting the standardization of risk measurement units. In addition, AMF expects institutions to report any risk disclosure errors or omissions, and that a procedure be implemented to mitigate the frequency and impact of this type of errors.

On an ongoing basis and more specifically during a crisis, the institution will have to make sure it can effectively meet all risk data aggregation requests, which may come from the AMF or other market participants such as the central bank or rating agencies.

The integrated risk management framework should allow the institution to quickly generate information on the material risks it is exposed to. To do so, it is desirable that timelines required for the production of each risk report to be specified beforehand. However, note that agility with respect to the disclosure of risk data should never interfere with the accuracy, integrity, completeness and adaptability of this data.

As risk information requests come from various participants, and that special needs do not necessarily observe the same parameters and timeframes, the institution must make sure its systems and procedures can effectively adapt to enable customized reports (e.g. by business line, region, and method of distribution). This adaptability is crucial when

[6] Autorité des marchés financiers. *Outsourcing Risk Management Guideline*, December 2010.

considering new situations with the potential to adversely affect the institution's risk profile.

3. Risk disclosure practices

The AMF expects risk reports, especially those intended for decision-making bodies, to reflect the financial institution's risk appetite and tolerance level. These reports must also clearly allow stakeholders to track the institution's risk exposure, along with the effectiveness and efficiency of risk management measures.

Given that reports on risks are used by senior management and the board of directors, mainly for strategic decision making, their expectations concerning the granularity required for information on risks, and the timeframes for its presentation, will have to be formally disclosed to all stakeholders.

The greater an institution's complexity, the less manual systems for risk disclosure will be tolerated. However, regardless of the degree of automation of the systems used, all institutions will have to properly document their risk disclosure requirements, including an explanation of the use of manual systems, as applicable, and the effect of this choice on the accuracy of the information generated and the actions planned to mitigate the associated inherent risks. This documentation will have to be validated by the independent function to ensure that any major anomaly is presented to senior management and the board of directors.

These reports must also track the evolution of each institution's risk exposure, along with the effectiveness and efficiency of risk management measures. It is essential that the presentation of data showing this evolution be accompanied by an analysis adapted to the various recipients, including, as applicable, an explanation of the limitations related to the disclosure of risk data and of the measures planned to mitigate them. The board of directors and senior management, as well as any other recipient of these reports, will have to report those that do not meet expectations or that do not reflect the institution's risk tolerance and appetite.

Moreover, it is critical that the body responsible for generating these reports check the accuracy of the information to be disclosed. As previously mentioned, these reports may come from a multitude of information sources. The institution is responsible for aggregating and presenting them clearly and adapted to the target audience. To do so, the institution should develop and implement all the necessary validation rules to guarantee the consistency of the risk data presented. As these rules are necessarily dynamic, due to the continually changing sources, controls will have to be implemented for these rules, and their effectiveness validated by the independent function. These controls will have to be incorporated into the institution's internal control framework and be supported by the description of the rules in effect, using simple, specific conventions.

4. Supervision of sound and prudent management practices

To foster the establishment of sound and prudent management practices within financial institutions, the AMF, as part of its supervisory activities, intends to assess the degree of compliance with the principles and guidance set forth in this guideline.

Accordingly, it will examine the effectiveness and relevance of the adopted strategies, policies and procedures, the quality of supervision, and the control exercised by the board of directors and senior management.

Risk data aggregation and disclosure practices are constantly evolving. The AMF expects financial institution's decision-making bodies to remain current with best practices and to adopt them, to the extent that they address their needs.