



## UCITS IV: Validation of value-at-risk models

### Looking inside the black box

Under UCITS IV, Internal Risk Models need to be validated by an independent party.

The liquidity crisis of 2007-2008 was also a failure of risk measurement models. In the context of UCITS IV, CSSF Circular 11/512 significantly tightens the requirements for the use of internal risk models.

The CSSF requires that the internal model is validated by a party independent of the model's building

process. The validation needs to ensure that the model is robust and reliable and captures adequately all material risks.

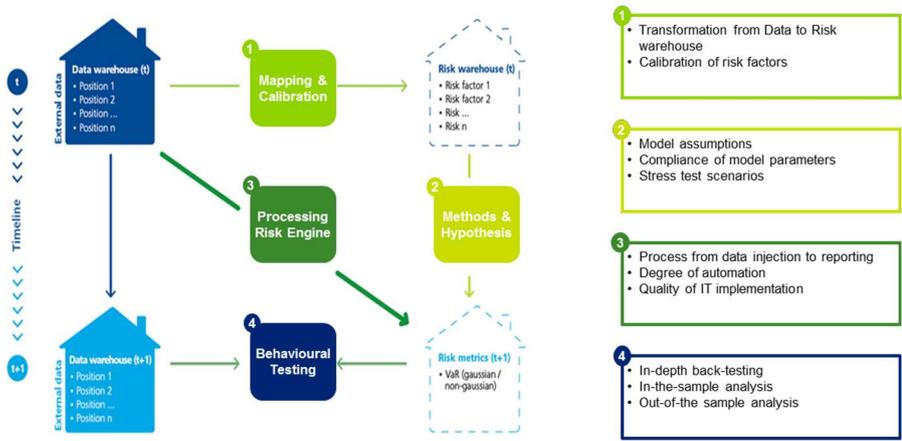
By setting the limit for the acceptable number of backtesting exceptions to four, the need for resilient internal models is even more emphasized:

*"A higher number of 'overshootings' indicate an under-estimate of the VaR. If the back testing results reveal a percentage of exceptions that appears to be too high, the UCITS should review its VaR model and make, appropriate adjustments."<sup>1</sup>*

<sup>1</sup> CESR/10-788

## Our Methodology

Deloitte has developed a model validation approach to ensure that will create confidence in the model's outputs and help you communicate its value throughout your institution. We make sure that the internal model covers all relevant risk factors and produces consistent output:



## Our expertise

We offer you to validate your internal risk model in order to comply with the new requirements under UCITS IV.

Going beyond the regulatory requirements, our validation approach also aims at adding real value for your day-to-day risk management.

This will increase your confidence in the outputs of your internal risk model. Our offer consists of two consequent steps:

- **Gap Analysis Report:** Comprehensive report detailing and summarizing potential gaps
- **Certification (ISAE 3000):** Consequently, we may offer a formal certification that can be communicated to regulators and stakeholders

We take your internal risk model to the lab

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