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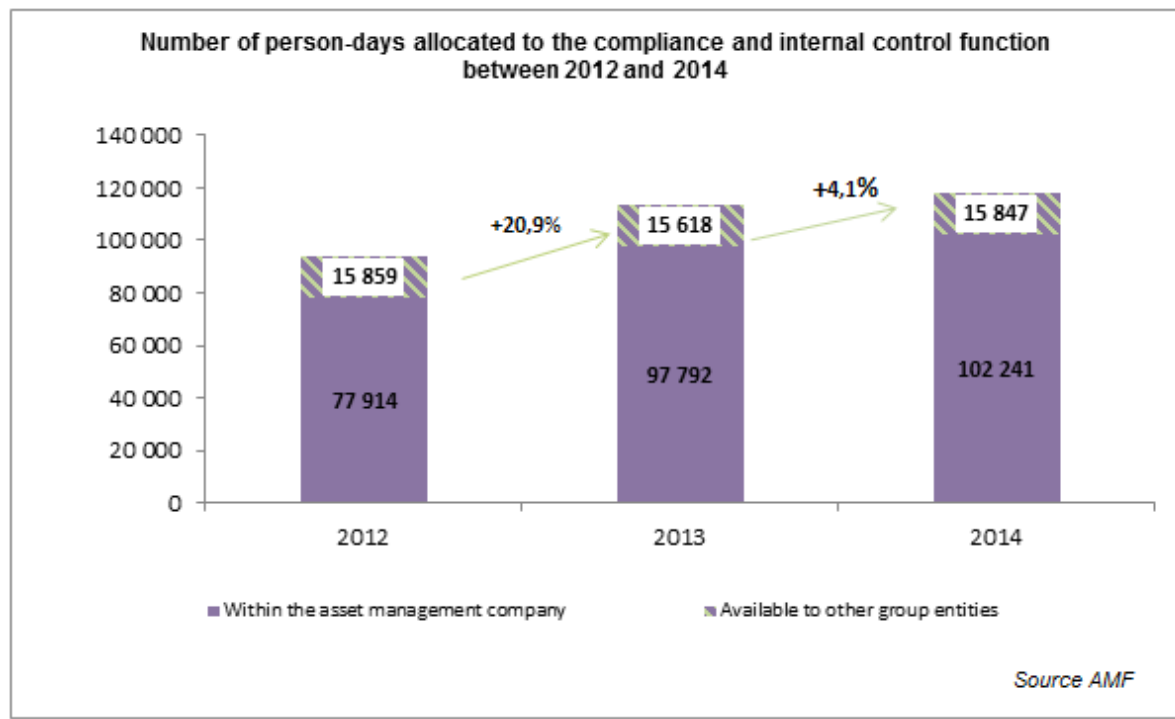
10 February 2016

Key figures for asset management in 2014 - Control systems in asset management companies

The French asset management industry strengthened its control systems in 2014. The number of person-days allocated to the compliance and internal control function increased from 93,773 to 118,088 between 2012 and 2014 (up 25.9%). The level at which asset management companies outsourced their permanent control function was 55%, for the periodic control function, this figure was 79%. This report examines the organisation of the control systems in place at these firms in 2014.

More staff dedicated to the compliance and internal control function

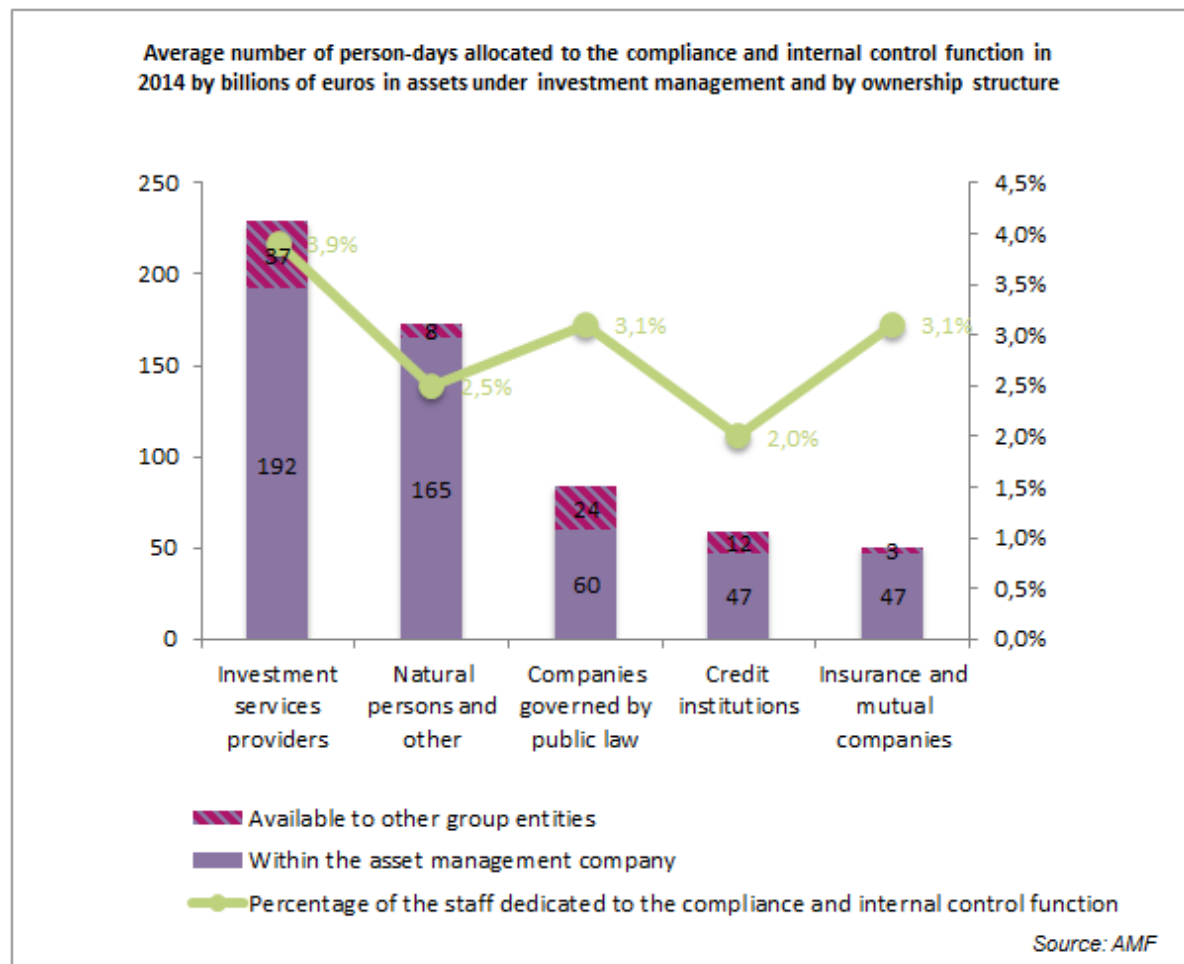
At 31 December 2014, the number of person-days dedicated to the compliance and internal control function was 118,088, up 4.1% from 2013.



This growth was driven largely by the increase in compliance and internal control staff within management companies, as well as by the resources asset management companies made available to other parent group entities. The number of person-days made available by asset management companies to other group entities⁽¹⁾ for the compliance and control function remained fairly stable over the three-year period.

The rise in the number of person-days allocated to the compliance and internal control function stems in part from the natural rise in the number of asset management companies created and, consequently, the broadened scope of the study⁽²⁾. It also reflects the implementation of a series of directives designed to strengthen the financial system following the subprime crisis.

A closer analysis of the compliance and internal control function reveals that the number of person-days allocated varies by ownership structure. However, the percentage of staff dedicated to the compliance and internal control functions remained relatively similar for all asset management companies, regardless of ownership structure.



On average, management companies that are subsidiaries of investment services providers and boutique management companies allocated more person-days to the compliance and internal control function by billions of euros in assets under management (averaging 229 and 173 person-days, respectively, in 2014).

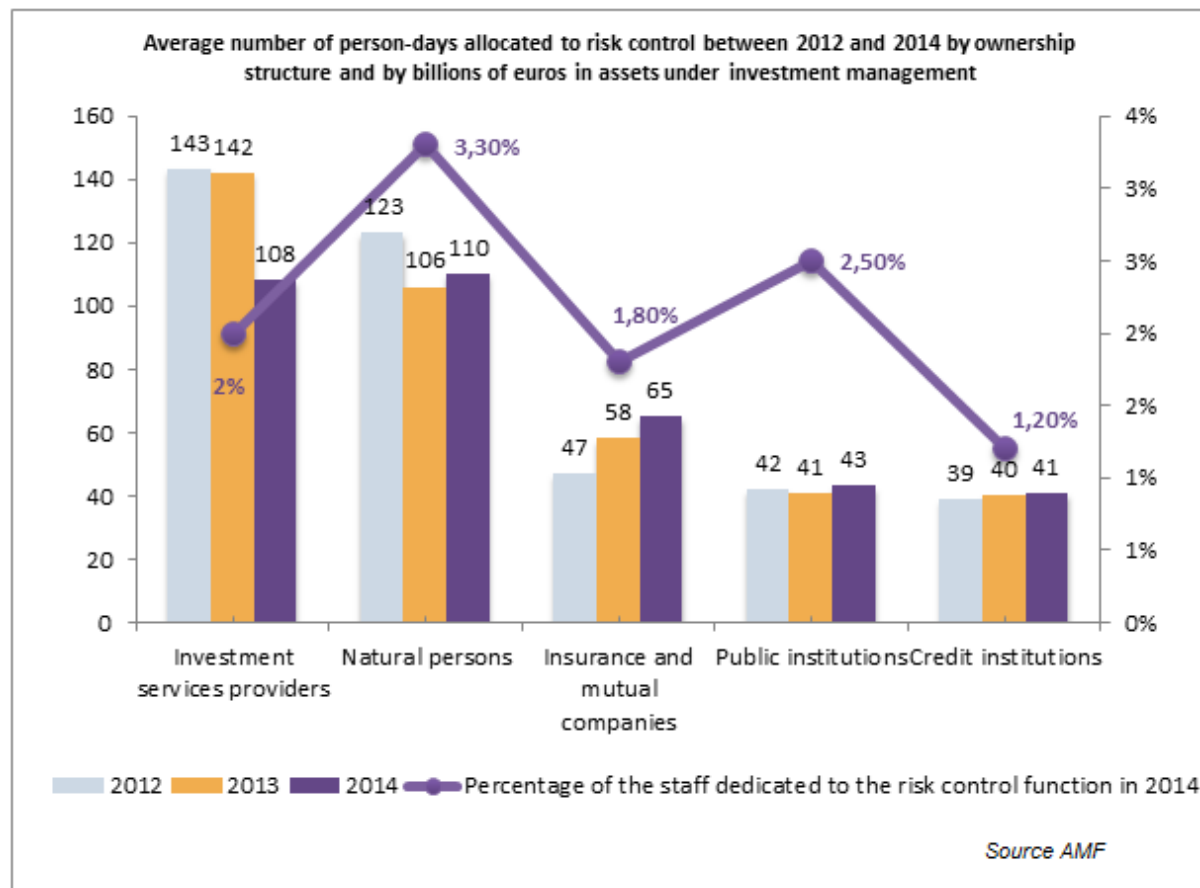
Companies that are subsidiaries of credit institutions and of insurance and mutual companies allocated fewer person-days by billions of euros in assets under management (averaging 59 and 50 person-days, respectively). These companies are generally large firms, both in terms of number of accounts and volume of assets under management (87.2% of assets in 2014) and with respect to staff (on average 72 and 67 people, respectively, in 2014 per company). This means they benefit from economies of scale in managing their compliance and internal control needs and can optimise their human and technical resources, for example, with regard to their information systems.

These differences in person-days allocated to the compliance and control function by ownership structure should, however, be put into perspective. In fact, the percentage of staff dedicated to the compliance and internal control functions remained relatively similar for all asset management companies, regardless of ownership structure.

All asset management companies have bolstered their risk control

Asset management companies maintain a risk control function in order to formalise "all procedures enabling the investment manager to assess exposure to market, liquidity, counterparty and operational risks for each collective investment scheme or managed portfolio⁽³⁾". In 2014, the number of person-days allocated to risk control rose by 9.2% from 2013 to 78,978.

How the risk control function is fulfilled and the time dedicated to this function by billions of euros in assets under management vary by ownership structure.



All asset management companies have shored up their risk control function. The average number of person-days allocated to risk control at asset management companies, regardless of ownership structure, increased between 2012 and 2014. The size of the company, the nature and complexity of the activities carried out, and the regulatory aspect are the main underlying factors. For EUR 1 billion in assets under management, management companies owned by natural persons and investment services providers dedicated on average 110 and 108 person-days to risk control, while subsidiaries of credit institutions and insurance and mutual companies allocated 41 and 65, respectively.

Moreover, 23.6% of asset management companies are required to maintain a permanent function independent of risk management due to the nature and complexity of their

business⁽⁴⁾. Within this group, 60.4% use the value-at-risk⁽⁵⁾ method to calculate a broad measure of risk exposure, although this practice has become less common (64% in 2013 and 65% in 2012). In 2014, of the 84 firms that used the VaR method, 45.2% were boutique management companies, 36.9% were management companies that are subsidiaries of credit institutions, 11.9% had ties to an insurance or mutual company, and 6% were investment services providers.

The outsourcing and delegation of permanent and periodic control are correlated to AUM

When an asset management company or, more broadly, its parent group "does not reasonably have the financial resources to assign a person to the compliance function"⁽⁶⁾ and the position of compliance officer can only be assigned to a senior manager, then the asset management company must outsource its compliance and internal control tasks. The main reasons for outsourcing and delegation are therefore the size of the asset management company, the nature of its business, and the complexity of the strategy implemented and of the tools used to further this strategy.

In 2014, 55% of asset management companies outsourced tasks related to the permanent control function (19% of which were delegated to an entity in their group) and 79% of French asset management industry actors outsourced their periodic control function tasks (27% of which were delegated to an entity in their group).

An analysis of outsourcing, delegation of permanent and periodic control and the proportion of senior manager compliance officers by ownership structure shows the different ways the control system can be organised.

**IM: insurance and mutual companies; CI: credit institutions; NP: natural persons; Other: investment services providers and companies governed by public law.*

The proportion of management companies reporting at least one senior manager who holds the professional licence for compliance officers rose by 4.6 percentage points between 2012 and 2014 to stand at 48.3% across all asset management companies. This trend reflects the rising number of boutique management companies among Paris financial centre participants and points to an organisational framework for the typical control system. These types of firms represented 80.6% of the increase in the number of asset management companies with at least one senior manager compliance officer between 2012 and 2014.

A majority of the boutique firms have at least one senior manager compliance officer (62.5% in 2014⁽²⁾). At these companies, the senior manager compliance officer generally performs operational duties in addition to his or her control duties. Compliance tasks are therefore outsourced and assigned to an external service provider or a parent group entity. However, asset management companies owned by natural persons do not typically belong to a group, are focused on the core business and therefore delegate some of their "support" functions, including control tasks, to an outside entity. This explains the very high rates of outsourcing of permanent and periodic control among these companies (61% and 75%, respectively).

** This is a special case, i.e., a former securitisation fund (fonds commun de créances) management company which pursued a passive management strategy and outsourced its second-level permanent control.*

Conversely, almost all asset management companies that are subsidiaries of credit institutions have access to their group's internal audit teams, which can perform periodic (and, to a lesser extent, permanent) control tasks. Accordingly, 84% of these companies delegate the operational aspects of these tasks to other group entities (31% for permanent control tasks). When the principle of proportionality applies, requiring a periodic control function that is separate and independent of the other functions, asset management companies that are subsidiaries of credit institutions outsource this function. In 2014, 10% of management companies belonging to a credit institution outsourced periodic control and 12% outsourced permanent control.

There is a significant positive correlation between the level of assets under management and the rate of delegation of permanent and periodic control to a parent group entity. This is because most asset management companies with more than EUR 1 billion in assets under management are tied to a group, making it possible to delegate these controls to other group entities.

A negative correlation was observed between the level of assets and the percentage of outsourcing of permanent and periodic control to an external service provider. Companies with substantial assets have more significant financial resources and insource the periodic and permanent control functions. This is less frequently the case for companies with less than EUR 150 million in assets. Of the latter, 67% outsource permanent control and 76% periodic control.

Focus on... AIFM reporting – Liquidity of AIF portfolios

The change in the liquidity of alternative investment funds (AIFs) has not been uniform.

The liquidity of funds in the "Other" category remains quite significant in the reporting, as illustrated in the chart below, in which the curves representing the four reports received are overlaid.

Source: AIFM reports received in October 2014 and in January, April and July 2015.

Conversely, the liquidity of hedge funds increased significantly between the third quarter of 2014 and the second quarter of 2015. Fund managers likely focused on more liquid assets in response to the recent stress in the financial markets. The chart below therefore shows that the share of portfolios that can be liquidated in one day increased significantly, at the expense of the share of the portfolio that can be liquidated in 31 to 90 days.

Source: AIFM reports received in October 2014 and in January, April and July 2015.

Source

As part of its monitoring of the asset management sector, the AMF collects annual information forms from asset management companies (AMCs). These forms contain quantitative information about the assets managed and about the revenue and expenses associated with asset management in France. This information enables the Authorisation and Monitoring Department of the AMF's Asset Management Directorate to perform analyses. Since the AIFM Directive entered into force in July 2013, European AIF managers have also been subject to a new reporting requirement. The information gathered mainly concerns the portfolios' exposure to different types of risks and is collected on a quarterly, semi-annual and/or annual basis. Although every care is taken when compiling and processing the data, due to the late receipt of some of the forms and possible data entry errors, the analyses may nevertheless contain inaccuracies.


Key figures for asset management in 2014

Each year, the AMF publishes a series of five articles entitled "Key figures for asset management". These publications are available from the Publications > Reports, research & analysis > Savings & services providers page on the AMF's website. The key figures cover the following topics: the landscape for management companies, their profiles, assets under management, financial data and, lastly, the control mechanism. A compilation of these five publications, plus additional data and tables, is published at a later date.

Notes

- 1 • Some asset management companies make staff available to other group entities to fulfil the compliance and internal control function. Most of these companies are subsidiaries of credit institutions (77.2%).
- 2 • The scope of the study is not constant over time; it varies according to the number of existing companies minus companies whose authorisation is being withdrawn and/or that are in liquidation, companies created during the year, and companies acquired by another asset management company during the year. The scope included 578 companies in 2012, 571 in 2013, and 588 in 2014.
- 3 • Articles 2.1.1. and 2.1.2. of AMF position-recommendation DOC-2014-06 – Guide to arranging risk management systems in asset management companies.
- 4 • Article 3.2.6.2. of AMF position-recommendation DOC-2012-19 – Programme of operations guide for asset management companies and self-managed collective investments.
- 5 • Value at risk (VaR) is a composite indicator that estimates the maximum potential loss a portfolio could incur for a given time frame and a given probability.
- 6 • Article 3.2.6.1. of AMF position-recommendation DOC-2012-19 – Programme of operations guide for asset management companies and self-managed collective investments.
- 7 • There was at least one senior manager compliance officer at 38.3% of investment services providers. This was also the case for 29.4% of companies governed by public law, 25% of insurance and mutual companies, and 12% of subsidiaries of credit institutions in 2014.

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