



1401 H Street, NW, Washington, DC 20005-2148, USA
202/326-5800 www.ici.org

January 12, 2009

Jonathan Stokes, Director
Standards of Practice
CFA Institute
560 Ray C. Hunt Drive
Charlottesville, Virginia 22903

Re: Proposed Risk Management Requirement

Dear Mr. Stokes:

The Investment Company Institute¹ appreciates the opportunity to comment on the CFA Institute's proposed addendum to the *Asset Manager Code of Professional Conduct* ("AMC") relating to risk management. With the increasing importance of risk management to asset managers and their clients, we believe it wholly appropriate to incorporate a requirement relating to this topic in the AMC and we commend the Institute for proposing this new requirement. While we support inclusion of such requirement, we recommend various modifications to the current proposal, which are briefly discussed below.

As proposed, the new requirement would mandate that managers establish a "risk management process" that includes certain functions. We support this requirement. However, consistent with the fact that it will be applicable to investment managers, we recommend that the requirement clarify that the required process relates to "investment risk." Additionally, we recommend that the process include establishing risk tolerances, which is a necessary component of effective risk management. In particular, we recommend that the proposed addendum be revised to read in relevant part as follows²:

¹ The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of \$9.86 trillion and serve over 93 million shareholders.

² Additions are indicated by underscoring; deletions by ~~overstriking~~.

7. **Establish a an investment risk management process that establishes risk tolerances and identifies, monitors, and analyzes the risk position of the Manager . . .**

In addition to this change, we recommend minor revisions to the narrative explaining the proposed requirement. In particular, many members of the Institute's Risk Management Advisory Committee were actively involved a year or so ago with drafting "Risk Principles for Asset Managers" (the "Risk Principles"), which was published by the Buy Side Risk Managers Forum and the Capital Market Risk Advisors in February 2008.³ Like the current CFA Institute's proposal, this document was intended to provide asset managers a set of principles to foster the development of sound risk management practices. In furtherance of this goal, the Risk Principles identify a variety of risks that are relevant to investment managers and establishes principles related to each.

Consistent with the Risk Principles, the Institute recommends that the CFA Institute revise the types of risks listed in the second paragraph of the narrative to read as follows:

The types of risk faced by Managers include, but are not limited to, investment risks, which include market, concentration, leverage, and issuer risks; credit risk;; liquidity risk;; counterparty risk;; operational risk;; valuation risk; and style drift.

We also recommend that the second sentence of this same paragraph be revised. This sentence currently states, in substance, that it is "imperative" that risk management be objective and independent of the portfolio management process in order to understand and control risk. We respectfully disagree that one must be independent of the portfolio management process to understand or control risk. Indeed, in our view, due to their familiarity with risks related to the investment process, portfolio managers can play a valuable role in this process. Moreover, requiring managers to divorce portfolio managers from the process assumes that all managers have the resources to establish risk management processes separate and apart from portfolio managers, which may not be the case, particularly with smaller managers. To address these concerns, we recommend that the CFA Institute replace the word "imperative" in this sentence with either "strongly recommended" or "preferred" and delete "to understanding and controlling these types of risks."

The third sentence of the third paragraph in the narrative notes that the goal of risk and stress testing models is to determine how various changes in market conditions could impact investments. Because models and stress tests test how a variety of conditions beyond "market conditions" might impact investments, we recommend deleting the word "market" from this paragraph. Additionally, we

³ A copy of the Risk Principles is available through the website of the Buy Side Risk Managers Forum at: <http://www.buysiderisk.org>.

