



Derivative Operational Risk Assessment

SCENARIO TYPE	Asset Manager – Multi-Asset Absolute Return (UCITS)
ASSET CLASS	Multi-asset derivatives – equity futures/options, IRS/swaptions, FX forwards, CDS, variance swaps, commodity futures
RISK FOCUS	Trade capture completeness, valuation control, reconciliation timeliness, margin disputes, regulatory reporting, control design vs scale
PRIMARY OFFER	Derivatives Portfolio Review™
RELEVANT SERVICES	Derivatives operations risk assessment · Control remediation roadmap · IPV governance · Daily controls design · Exception reporting framework · Board / regulator narrative pack

THE SITUATION

A high-quality institutional manager running liquid, uncorrelated absolute return strategies through a derivatives engine. The strategy set was credible, the team experienced, and the funds had grown fast. The derivatives book had evolved the way these books always evolve – from a few futures and FX forwards into a genuinely multi-asset machine spanning multiple funds, prime brokers, OTC dealers, and clearing venues.

The problem was not market risk. The operating system underneath the derivatives book was still built for the earlier chapter. By the time the firm reached scale, execution and control drift had become the real risk.

The trigger was not a blow-up. It was something worse – a formal audit finding that turned a messy internal reality into an external fact. External audit flagged a large set of control deficiencies across trade capture, valuation, reconciliation, and reporting. Once written down, it stopped being an internal inconvenience and became a regulatory exposure.

HOW THE DRIFT SETS IN

A derivatives programme scales because it works. It adds instruments, counterparties, strategies, and turnover. The P&L engine gets bigger. The operational design does not. Nobody chooses to run a weak control environment – the system rewards growth and postpones infrastructure.

The hidden tax appears in predictable places. Trade capture becomes probabilistic – manual ticketing and inbox-based confirmation workflows work until they do not. Valuation becomes trust-based – counterparty marks entered because the day needs to close, not because they are validated. Reconciliation becomes a lagging indicator – when it is two months late, it stops being a control and becomes a historical record of past mistakes.

At scale, the failure mode is not one big error. It is a steady accumulation of small survivable breaks that eventually become a regulatory event.

WHAT TYPICALLY BREAKS

Trade capture breaks the moment it is email-driven

If the truth source depends on traders remembering to send tickets and ops manually keying them, missing trades are not an edge case – they are an eventual certainty. Email-based confirmation workflows cannot survive at institutional derivatives scale.

Reconciliation backlog is a design failure, not a workload issue

If month-end reconciliation takes six weeks, you do not have reconciliation – you have delayed discovery. Margin disputes and credit escalation become the detection mechanism for missing trades and mis-marks.

Valuation errors are human, not exotic

Once marks are entered manually across multiple dealers and products, the real risk is data entry, stale marks, and the absence of tolerance checks – not bad models. IPV exists in name but not in practice.

Regulatory reporting failure is downstream, not primary

Late EMIR reporting, CASS stress, and UCITS valuation concerns are symptoms. The root is trade capture integrity and record completeness. Fixing the downstream without fixing the upstream produces clean reports on an unreliable book.

THE STRUCTURAL INSIGHT

This was not a Hedge Rebuild. It was the paid review that identifies what is broken, where the risk sits, and what must change – before spending money on platforms, making commitments to a regulator, or assuming the problem is smaller than it is.

The work mapped control failures by failure mode rather than by department: how errors occur, how they are detected, how long detection takes, and what happens if detection fails. This separated immediate stabilisers (controls implementable without a platform change) from medium-term redesign and structural remediation.

A minimum viable control pack was defined as the Monday morning interventions – confirmation matching discipline with escalation rules, IPV tolerance checks with exception workflows, break ageing with ownership and deadlines, and a daily sign-off cadence. These stopped the bleeding without requiring a platform decision.

A remediation roadmap was then built that a board, auditor, and regulator could understand: what changes now, what changes next, what depends on platform uplift, what resourcing is required, and what evidence will exist that controls are operating effectively.

INTENDED OUTCOMES

- ▶ A book that can be proven complete – not assumed complete because no one has raised an exception recently.
- ▶ Valuations that can be defended – not accepted because a dealer emailed a PDF and the day needed to close.
- ▶ Reconciliations that function as controls – not archaeology catching errors that already settled incorrectly.
- ▶ Margin and collateral that stop being surprises – disputes cease to be the primary detection mechanism for missing trades.
- ▶ A remediation plan that reduces enforcement risk because it is evidence-based, sequenced, and credible under scrutiny from boards, auditors, and regulators.

WHERE THIS APPLIES

Most relevant where derivatives usage has scaled faster than middle-office design; multiple dealers, cleared and OTC mix, and multi-asset instruments are in play; NAV integrity and valuation governance matter to institutional allocators; reconciliations run with material lag; and audit findings, board scrutiny, or regulatory engagement is imminent.

Less relevant where the book is small and listed-only; controls are automated and reconciliations are timely with real IPV; or there is no institutional governance layer requiring audited funds, trustee oversight, or regulatory reporting.

TYPICAL ENGAGEMENT PATH

Derivatives Portfolio Review™ – derivatives operating risk assessment, control failure map, immediate stabilisers, and remediation roadmap.

Secondary: Platform selection support, IPV governance pack, daily controls design, exception reporting framework, regulator and board narrative support.