

Internal Risk Policy Update

Documentation for June 2025

Table of Contents

1. Introduction
2. Scope and Governance Structure
3. Policy Summary
4. Policy Update Details
5. Risk Limits Tightening
6. Implementation Procedures
7. Incident Notes and Timeline
8. Rationale and Expected Impact
9. Metadata and References
10. Appendices

1. Introduction

This document provides a comprehensive account of the recent updates to the internal risk management policy implemented by Northbridge Capital, a subsidiary of Fairfax Financial Holding, effective June 18, 2025. It serves as official documentation reflecting the modifications to risk thresholds, governance procedures, and related compliance requirements. The purpose of this documentation is to ensure clarity, transparency, and accessibility for internal stakeholders, auditors, and regulatory review processes.

The update aligns with current risk management standards and incorporates feedback from recent internal audits and market stress scenario analyses. The policy change, identified under policy ID **POL-20250618-001**, is part of our ongoing commitment to maintaining robust risk controls and ensuring adaptive responses to changing market conditions.

2. Scope and Governance Structure

2.1 Scope

The policy update applies across all investment portfolios managed under Northbridge Capital, including proprietary trading desks and client-managed funds. It encompasses all risk measurement activities related to Value at Risk (VAR) calculations, gamma exposure limits, and other related risk metrics.

Specifically, the policy governs:

- Operational risk assessments within portfolio management systems.
- Quantitative risk thresholds for VAR and gamma exposure.
- Stress testing procedures aligned with current market volatility.
- Reporting and escalation procedures for breach events.

2.2 Governance Structure

The governance of the risk policy involves multilevel oversight:

1. **Risk Committee:** Provides strategic oversight, approves policy updates, and reviews breach incidents on a quarterly basis.
2. **Compliance Department:** Ensures adherence to internal standards and external regulatory requirements, conducting periodic audits.
3. **Trading and Portfolio Teams:** Implement risk controls at the operational level, monitor limit breaches, and escalate issues promptly.
4. **Internal Audit:** Performs independent reviews of risk management activities and reports findings to senior management.

3. Policy Summary

This section summarizes the key components of the internal risk policy as of June 2025, prior to the latest update.

Aspect	Description
Policy ID	POL-20250618-001
Effective Date	June 18, 2025
Applicable Entities	Northbridge Capital portfolios, proprietary and managed funds

Main Focus	Maintaining risk exposure within specified VAR and gamma thresholds, enhancing stress testing protocols
Key Metrics	VAR, gamma exposure, slippage_bps, quote_spread_bps
Breach Codes	BR-20250618-001 (VAR breach), BR-20250618-002 (Gamma breach)

Overall, the policy aims to maintain portfolio risk levels aligned with enterprise risk appetite, while enabling responsive management under volatile market conditions.

4. Policy Update Details

4.1 Change Overview

The primary change introduced in the June 2025 update involves a tightening of risk thresholds to mitigate exposure during high volatility periods. The key adjustments include:

- **VAR Thresholds:** Reduction from the previous 99% VaR limit of 2.5% to 2.0%.
- **Gamma Limits:** Tightened from 1.5 to 1.0 gamma exposure units.

These changes respond to recent market stress indicators and internal stress testing results indicating increased tail risk exposure.

4.2 Policy ID and Version

Each policy update is assigned a unique identifier for traceability:

- **Policy ID:** POL-20250618-001
- **Version:** 2.0 (reflecting second major revision)

5. Risk Limits Tightening

5.1 Variance at Risk (VAR)

The VAR limit was decreased to better control potential losses during market downturns. The new threshold details are:

Parameter	Previous Limit	Updated Limit
99% VaR Limit	2.5%	2.0%
Maximum allowable breach frequency	Monthly breaches not to exceed 2	Monthly breaches not to exceed 1

5.2 Gamma Exposure

Gamma limits were also reduced to mitigate excessive convexity risks:

Parameter	Previous Limit	Updated Limit
Gamma Units	1.5	1.0

These thresholds are monitored continuously using automated alerts, with breaches triggering immediate review and escalation processes.

6. Implementation Procedures

6.1 Prerequisites

- Updated risk management software with latest policy parameters
- Training sessions for portfolio managers and risk analysts
- Notification protocols in place for breach escalation

6.2 Step-by-Step Process

1. Ensure risk calculation models are updated with new thresholds and parameters.
2. Perform dry-run stress tests to validate model adjustments.
3. Implement risk limits in trading systems, ensuring real-time monitoring capabilities.
4. Distribute updated policy documentation and conduct training sessions with relevant teams.
5. Activate automated alert systems for breach detection based on updated thresholds.
6. Establish regular review sessions to monitor adherence and assess breach incidents.

6.3 Verification

Post-implementation, verification involves simulated breaches and review of automated alerts to ensure system responsiveness. Regular audits are scheduled to confirm compliance with the new thresholds.

7. Incident Notes and Timeline

7.1 Timeline of Events

Date	Event	Description
2025-06-18	Policy Update Deployment	Implementation of tightened VAR and gamma thresholds as per policy ID POL-20250618-001.
2025-06-18	Initial Breach Detection	First instance of VAR breach recorded at 2.2%, triggering automated alert.
2025-06-19	Escalation	Risk team conducted review; identified causes related to increased market volatility.
2025-06-20	Mitigation Action	Position adjustments made to reduce gamma exposure; risk limits reaffirmed.
2025-06-21	Review	Follow-up assessment confirmed system accuracy and compliance with new thresholds.

7.2 Root Cause Analysis

The initial breach was caused by a sudden spike in market volatility affecting equity options positions, resulting in gamma exposure exceeding the new limit. The rapid escalation underscored the need for tighter risk thresholds and more responsive monitoring.

8. Rationale and Expected Impact

The primary rationale for tightening risk limits is to mitigate tail risk exposure during turbulent market conditions, thereby safeguarding portfolio integrity and reducing potential for significant losses.

Expected impacts include:

- Enhanced risk control leading to lower probability of large drawdowns.
- Improved early warning systems and faster response times to breaches.
- Alignment with evolving regulatory standards emphasizing prudential risk management.
- Potential reduction in return margins due to conservative limit settings, balanced against risk mitigation benefits.

Simulations suggest that, under stress scenarios, the new thresholds reduce tail losses by up to 15-20% compared to previous policies.

9. Metadata and References

9.1 Document Metadata

- **Model:** POLICY-2025-06-03
- **Document Date:** June 18, 2025
- **Version:** 2.0
- **Path:** /Volumes/demo_generator/
saswata_sengupta_agneticportfoliomanager/raw_data/incoming_data/
Investor_Report/interim_report.pdf

9.2 References

- Internal Risk Management Framework v4.2
- Market Stress Testing Guidelines, June 2025
- Regulatory Compliance Standards for Risk Control, Basel III, 2024
- Recent incident reports and breach logs (e.g., BR-20250618-001,
BR-20250618-002)

10. Appendices

10.1 Glossary of Terms

Term	Definition
VAR (Value at Risk)	A statistical measure quantifying the maximum expected loss at a specified confidence level within a given time horizon.

Gamma Exposure	The measure of convexity or second-order risk in options portfolios, indicating sensitivity to underlying asset price changes.
Slippage_bps	Basis points reflecting the difference between expected and executed prices during trading.
Quote Spread_bps	The difference in basis points between the bid and ask prices, indicating liquidity costs.

10.2 Relevant Policy Documents

- Risk Management Framework, June 2024
- Market Stress Testing Procedures, March 2025
- Internal Compliance Guidelines, 2023

This document is an authoritative record of the internal risk policy update as of June 2025. For additional information, contact the Risk Management Department at Northbridge Capital.