
Public Hearing on CP draft RTS on the materiality of extensions and changes to the use of FRTB IMA and changes to the subset of modellable risk factors

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EBA Roadmap on MKR & CCR mandates under CRR2

Priorities	EBA regulatory products	Mandate in CRR	Legal Deadline	Status
Phase 1: Implementation of the SA-CCR and of essential parts of the FRTB revisions for the IMA	<u>Report on the impact of the FRTB</u>	Art. 519b(1)	30 Sep 2019	Delivered
	<u>RTS on mapping of derivatives transactions to risk categories under the SA-CCR</u>	Art. 277(5)(a) and (b)	28 Dec 2019	In force
	<u>RTS on the supervisory delta formula for interest rate options and determination of long or short positions under the SA-CCR</u>	Art. 279a(3)(a) and (b)	28 Dec 2019	In force
	<u>RTS on liquidity horizons for the IMA</u>	Art. 325bd(7)(a),(b),(c),(d)	28 Mar 2020	In force
	<u>RTS on backtesting requirements and PLA requirements under the IMA</u>	Art. 325bf(9) and 325bg(4)	28 Mar 2020	In force
Phase 2: Implementation of FRTB (SA) reporting requirements and of essential parts of IMA FRTB revisions and for the treatment of non-trading book positions subject to FX or comm risk	<u>RTS on assessment of risk factor modellability under the IMA</u>	Art. 325be(3)	28 Mar 2020	In force
	<u>ITS on specific reporting requirements for market risk (FRTB SA)</u>	Art. 430b(6)	30 Jun 2020	In force / Finalisation
	<u>RTS on a stress scenario risk measure for non-modellable risk factors under the IMA</u>	Art. 325bk(3)(a)(b)(c)(d)	28 Sep 2020	Delivered
	<u>GL on criteria for the use of data inputs in the risk-measurement model under the IMA</u>	Art. 325bh(3)	28 Sep 2020	In force
	<u>RTS on PDs and LGDs for the default risk model under the IMA</u>	Art. 325bp(12)	28 Sep 2020	In force
Phase 3: Implementation of FRTB (IMA) reporting requirements and of FRTB SA regulatory products	<u>RTS on treatment of non-trading book positions subject to FX or commodity risk</u>	Art. 325(9)	28 Sep 2020	In force
	<u>ITS on specific reporting requirements for market risk (FRTB IMA)</u>	Art. 430b(6)	30 Jun 2020	Finalisation
	<u>RTS on instruments exposed to residual risk</u>	Art. 325u(5)	28 Jun 2021	In force
	<u>RTS on emerging markets and advanced economies</u>	Art. 325ap(3)	28 Jun 2021	In force
	<u>RTS on gross jump-to-default (JTD) amounts</u>	Art. 325w(8)(a),(b),(c)	28 Jun 2021	In force
Phase 4: Regulatory products whose substance will be derived from the monitoring of the application of the revised frameworks	<u>RTS on material extensions and changes under the IMA</u>	Art. 325az(8)(a)	28 Jun 2024	Under consultation
	<u>RTS on the assessment methodology for the IMA</u>	Art. 325az(8)(b)	28 Jun 2024	Delivered
	<u>RTS on extraordinary circumstances for being permitted to continue using the IMA</u>	Art. 325az(9)(a)	28 Jun 2024	Finalisation
	<u>RTS on extraordinary circumstances for being permitted to limit the backtesting add-on</u>	Art. 325az(9)(b)	28 Jun 2024	Finalisation
	<u>GL on the meaning of exceptional circumstances for the reclassification of a position</u>	Art. 104a(1)	28 Jun 2024	Postponed
	<u>Report on the impact and relative calibration of the SA-CCR, simplified SA-CCR and OEM</u>	Art. 541(1)	28 Jun 2023	Delivered

Art. 325az(8)(a) - Alternative internal model approach and permission to use alternative internal models

EBA shall develop draft regulatory technical standards to specify the **conditions for assessing the materiality of extensions and changes to the use of alternative internal models and changes to the subset of the modellable risk factors** (MRF) referred to in Art. 325bc.

EBA shall submit the draft RTS to the Commission by 28 Jun 2024.

Similarities with the mandate under Art. 363(4)(a)

The mandate in Art. 325az(8)(a) is very similar to the one in Art. 363(4)(a), which is the legal basis for the **existing RTS on market risk model extension and changes**. The existing RTS are used as a **starting point** for developing the new ones, adapting the provisions where needed.

Scope of the RTS

Model extensions, model changes and changes to the subset of MRF

Modifications to the IMA performed at bank's initiative or triggered by the regulatory framework should generally be considered as model extension or changes and are covered under the scope of these RTS, if they constitute a **change of the approved methods, processes, controls, data collection, organisation of the risk management and internal validation function, and IT systems used.**

The choice of the subset of MRF referred to in Art. 325bc should be part of the institution's approved and documented set of internal policies and procedures. **Modifications to such policies and procedures are considered as changes to the choice of the subset of MRF.**

Ongoing alignment of the IMA to the dataset used, correction of errors or day-to-day model maintenance (occurring within the approved methods, processes, controls, data collection and IT systems and recorded accordingly) do not constitute model changes.

Categorisation of model extensions and changes

Material model extensions and changes and changes to the subset of MRF

According to the CRR, material extensions and changes shall be approved by the competent authority.

Non-material model extensions and changes and changes to the subset of MRF

According to the CRR, non-material extensions and changes shall be notified to the competent authority.

The proposed draft RTS further divide non-material extensions and changes into two sub-categories:

- **non-material extensions and changes requiring additional information;**
- **other non-material extensions and changes.**

For non-material extensions and changes having a significant impact, additional information is required to enable competent authorities to adequately review and take actions outside the formal approval process.

Q1. What are your views on requiring additional information for specific extensions and changes?

Identification of material model extensions and changes (1)

Qualitative criteria for model extensions and changes

- Significant changes to the structure or organisation of the trading desks under the IMA, e.g. significant changes to the business strategy (including where internal risk transfers is applied for the first time), the booking models or the risk management structure;
- Inclusion of a trading desk in the IMA scope, which was not part of the existing permission;
- Reverse extensions where an institution aims at applying the standardised approach to trading desks under the existing IMA permission;
- Changes in the fundamental approach to calculate the IMA partial expected shortfall measures, e.g. changes between historical simulation, parametric or Monte Carlo approach;
- Changes in the fundamental approach to calculate the default risk charge (DRC), e.g. significant changes to the choice of the systematic risk factors or the correlation structure of the model.

Q10. Do you agree with the proposed qualitative criteria to identify material extensions and changes, as set out in Part I of the Annex?

Identification of material model extensions and changes (2)

Quantitative criteria for model extensions and changes

- Material model changes: changes that produce an impact in the IMA own funds requirements (OFR) above +15% or below -10%, or changes that produce an impact in at least one measure among the Expected Shortfall (ES), the Stress Scenario risk measure (SS) and the DRC, above +20% or below -15%.
- Material model extensions: extensions that produce an impact in the IMA OFR above +10% or below -10%, or extensions that produce an impact in at least one measure among ES, SS and DRC above +15% or below -15%.

Q2. Do you agree with the proposed quantitative conditions for determining the materiality of extensions and changes?

Q3. What are your views on the selected threshold levels?

Identification of material model extensions and changes (3)

Additional specifications related to the quantitative criteria

The quantitative conditions should be calculated for an observation period, representative of the trading and hedging activity under normal market conditions, of 15 consecutive business days, starting from the testing day.

Only the risk measures (ES, SS and DRC) which are relevant (i.e. $>5\%$ of $ES+SS+DRC$) need to be checked.

As in the existing RTS, only the most recent FRTB IMA risk numbers (ES_{t-1} , SS_{t-1} and DRC_{t-1}) need to be checked, disregarding the averages over the preceding 60 business days (i.e. ES_{avg} , SS_{avg} and DRC_{avg}).

As in the existing RTS, a pre-condition is included that exempts from the 15 business days computation of the quantitative conditions if the impact on the relevant risk numbers $<1\%$ in absolute terms on the testing day.

Q4. Do you agree with the proposal to introduce a condition for assessing the relevance of the risk measures to be checked for the materiality assessment of model extensions and changes?

Q5. Do you agree with the proposal to always assess the quantitative conditions on 15 consecutive business days?

Identification of material model extensions and changes (4)

Quantitative criteria for changes to the choice of the subset of MRF

- Material changes to the choice of the subset of MRF: changes that produce an impact in the IMA OFR above +15% or below -10%, or changes that produce an impact on ES above +20% or below -15%, or changes that produce a decrease in the ratio $R = \text{PES}_t^{\text{RC}} / \text{PES}_t^{\text{FC}}$ below a certain threshold.

Two options are included for consultation on the definition of a threshold for the last condition:

(option 1) $R_{\text{change}} \leq 80\%$

(option 2) $R_{\text{change}} - R_{\text{no_change}} \leq -\max\left(1\%, 50\% \cdot (R_{\text{no_change}} - 75\%)\right)$

where R_{change} is the ratio with the change implemented and $R_{\text{no_change}}$ is the ratio without the change.

Q7. Do you agree with the proposed conditions for determining the materiality of changes to the subset of MRF?

Q8. Which option do you think is more appropriate for a quantitative condition based on $\text{PES}_t^{\text{RC}} / \text{PES}_t^{\text{FC}}$?

Identification of non-material model extensions and changes requiring additional information (1)

Qualitative criteria for model extensions and changes requiring additional information

- Inclusion in IMA scope of product classes requiring risk modelling techniques not part of current permission;
- Changes in the methodology used to assess the modellability of risk factors;
- Changes in the methodology for calculating actual or hypothetical profit and loss (P&L), when such changes lead a desk to pass the back-testing requirements;
- Changes in the methodology for calculating hypothetical or theoretical P&L, when such changes lead a desk to changing its classification in accordance with the RTS on P&L attribution (e.g. from yellow to green);
- Fundamental changes in the internal validation methodology, which lead to significant changes in the way the institution assesses the overall performance and integrity of the IMA;
- Structural, organisational or operational changes to core processes in risk management/controlling functions;
- Fundamental extensions and changes in the IT infrastructure relevant for the calculation of the IMA OFR.

Q11. Do you agree with the proposed qualitative criteria to identify extensions and changes requiring additional information, as set out in Part II of the Annex?

Identification of non-material model extensions and changes requiring additional information (2)

Quantitative criteria for model extensions and changes requiring additional information

- Non-material model changes requiring additional information: changes in the IMA OFR that produce an impact between +10% and +15% or between -5% and -10%, or changes in at least one relevant measure among ES, SS and DRC that produce an impact between +15% and +20% or between -10% and -15%.
- Non-material model extensions requiring additional information: extensions that produce an impact in the IMA OFR between +5% and +10% or between -5% and -10%, or extensions that produce an impact in at least one measure among ES, SS and DRC between +10% and +15% or between -10% and -15%.

Quantitative criteria for changes to the subset of MRF requiring additional information

- Non-material changes to the choice of the subset of MRF requiring additional information: changes that produce an impact in the IMA OFR between +10% and +15% or between -5% and -10%, or the ones that produce an impact on ES between +15% and +20% or between -10% and -15%..

General provisions

Notification period for non-material extensions and changes (four weeks in advance).

Clarification on the granularity which should be applied to define a model extension or change, and on the procedure to follow in case of doubt on the correct allocation of an extension or change to the proper category.

Clarification around cases where the implementation of extensions and changes is delayed.

Documentation requirements (for other non-material extensions and changes, only a., b., c., f. and g.):

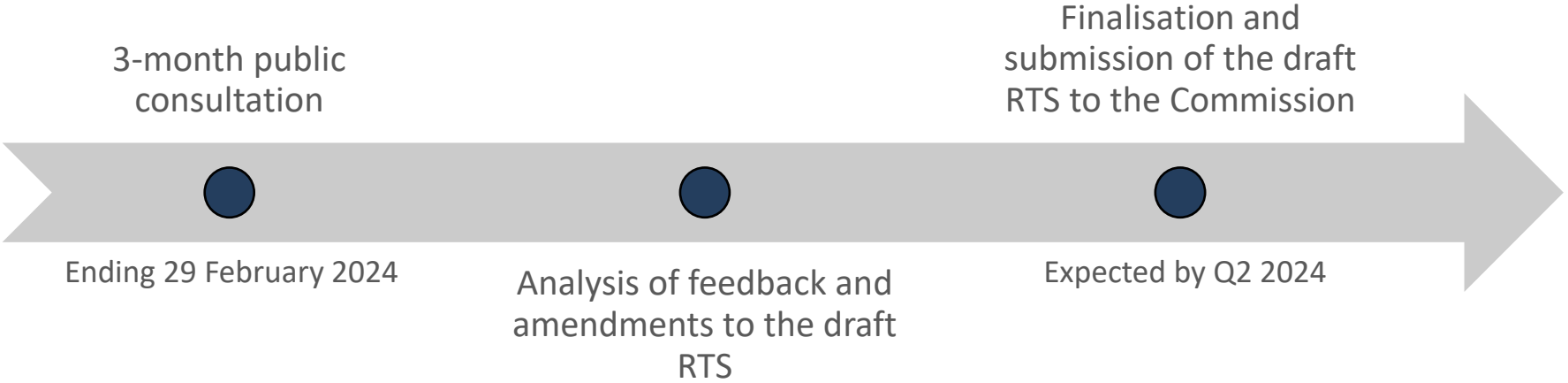
a. Description, rationale and objective of the extension or change; b. implementation date; c. scope of trading desks affected; d. technical and process documents; e. reports of the institutions' independent review or validation; f. confirmation and date of approval through the institution's approval processes; g. where applicable, quantitative impact on the basis of the quantitative conditions applied; h. records of current and previous IMA version number.

Minimum content of the reports of the institutions' independent review or validation (point e. above)

Q6. Do you agree with requiring non-material extensions and changes to be notified four weeks in advance?

Q9. What are your views on the proposed clarification to the content of the reports of the institutions' independent review or validation?

Next steps





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