

EBA/CP/2024/24

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9 December 2024

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# Consultation Paper

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## Draft Regulatory Technical Standards

amending Delegated Regulation (EU) No 529/2014 supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for assessing the materiality of extensions and changes of the Internal Ratings Based Approach.

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# 1. Responding to this consultation

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The EBA invites comments on all proposals put forward in this paper and in particular on the specific questions summarised in 5.2.

Comments are most helpful if they:

- respond to the question stated;
- indicate the specific point to which a comment relates;
- contain a clear rationale;
- provide evidence to support the views expressed/ rationale proposed; and
- describe any alternative regulatory choices the EBA should consider.

## **Submission of responses**

To submit your comments, click on the 'send your comments' button on the consultation page by 10.03.2025. Please note that comments submitted after this deadline, or submitted via other means may not be processed.

## **Publication of responses**

Please clearly indicate in the consultation form if you wish your comments to be disclosed or to be treated as confidential. A confidential response may be requested from us in accordance with the EBA's rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the EBA's Board of Appeal and the European Ombudsman.

## **Data protection**

The protection of individuals with regard to the processing of personal data by the EBA is based on Regulation (EU) 1725/2018 of the European Parliament and of the Council of 23 October 2018. Further information on data protection can be found under the Legal notice section of the EBA website.

## 2. Executive Summary

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Article 143(1) of the Regulation (EU) No 575/2013 requires approval by competent authorities for institutions to be able to calculate their risk-weighted exposure amounts (RWEA) for credit risk using the Internal Ratings Based Approach (IRB Approach). Institutions must also apply for permission from their competent authorities prior to implementing material extensions and changes to their internal approaches. The permission to use the IRB Approach is granted by the competent authority in accordance with Article 143(1) of Regulation (EU) No 575/2013, where the conditions set out in Chapter 3 Title II, Part III of Regulation (EU) No 575/2013 are met.

To recall, under the IRB Approach, Regulation (EU) No 575/2013 differentiates between material extensions or material changes, which are subject to approval, and other extensions or changes, which are only subject to notification. The Delegated Regulation (EU) No 529/2014 further splits the non-material changes into those that require ex-ante notifications to the competent authorities at least two months before their implementation (i.e., the supervisors have two months to oppose the implementation by reclassifying the model change as material), and extensions and changes that only have to be notified to the competent authorities after their implementation (i.e., ex-post notifications).

Delegated Regulation (EU) No 529/2014 contains in its annex a list of qualitative criteria which provides a classification of changes and extensions into the three categories mentioned above. Furthermore, Delegated Regulation (EU) No 529/2014 also contains quantitative thresholds, based on the reduction of RWEA before and after a change, in addition to the lists of qualitative conditions for determining the materiality of an extension and change.

With the Regulation (EU) 2024/1623 amending Regulation (EU) No 575/2013, the EBA is mandated under Article 143(5) to publish Regulatory Technical Standards (RTS) proposing amendments to the Delegated Regulation (EU) No 529/2014. The amendments proposed in this Consultation Paper stem primarily from two reasons.

First, a review of Delegated Regulation (EU) No 529/2014 is carried out to align this Delegated Regulation with the amendments to Regulation (EU) No 575/2013 from Regulation (EU) 2024/1623. This includes removing references to IRB approach for equity exposures, and to the AMA approach.

Second, amendments are made to enhance the supervisory effectiveness of the approval process of model changes and extensions, by leveraging on 10 years of supervisory experience gathered since publication of the original RTS. Amendments are proposed to the qualitative criteria related to the definition of default, validation framework, and the modelling approaches used for slotting exposures and purchased receivables. Next to that, the framework for extensions and reductions has been updated. Finally, several clarifications on the scope of the RTS and on the calculation of the quantitative criteria are introduced.

## 3. Background and rationale

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### 3.1 Background and mandate

1. Article 143(1) of Regulation (EU) No 575/2013 requires approval by competent authorities for institutions to be able to calculate their risk-weighted exposure amounts (RWEA) for credit risk using the Internal Ratings Based Approach (IRB Approach). Institutions must also apply for permission from their competent authorities prior to implementing material extensions and changes to their internal approaches.
2. The permission to use the IRB Approach is granted by the competent authorities in accordance with Article 143(1) of Regulation (EU) No 575/2013 where the conditions set out are met. Adjustments may be needed to maintain the compliance of these approaches with the regulatory requirements for the calculation of own funds requirements and for their use in accordance with Article 144(1)(b) of Regulation (EU) No 575/2013. The need for adjustments may for example stem from changes in internal or external factors the outcome of the review of estimates, or changes in the business activity or organisational structure of the institution.
3. Article 143(3) of Regulation (EU) No 575/2013 differentiates between material extensions or changes that are subject to approval, and all other changes that are subject to notification per Article 143(4) of Regulation (EU) No 575/2013. Furthermore, Article 143(5) of Regulation (EU) No 575/2013 mandated the EBA to develop draft regulatory technical standards (RTS) to specify the conditions for assessing the materiality of the use of an existing rating system for other additional exposures not already covered by that rating system and changes to rating systems or internal models approaches to equity exposures under the IRB Approach. The EBA has published the draft RTS in December 2013 and the related Commission Delegated Regulation (CDR 529/2014) was adopted in March 2014.
4. This RTS provides (in its annexes) lists of qualitative criteria for the classification of extensions and changes to the internal approaches into one of the following categories:
  - a. Material extensions and changes, which require a permission from the competent authorities;
  - b. Extensions and changes which are not material but still require ex-ante notifications to the competent authorities at least two months before their implementation (i.e., the competent authorities have two months to challenge the adequacy of the materiality classification and/or the compliance with the respective regulatory provisions);
  - c. Extensions and changes that only require ex-post notification to the competent authorities after their implementation.

5. In addition, the RTS also contains quantitative thresholds, based on the RWEA before and after a change, intended as a ‘back-stop’ measure in addition to the lists of qualitative criteria when determining the materiality of an extension and change.
6. With the Regulation (EU) 2024/1623 amending Regulation (EU) No 575/2013, the EBA is mandated under Article 143(5) to revise the RTS. There are two fundamental reasons necessitating amendments to the RTS:
  - a. Amendments to the RTS driven by changes in Regulation (EU) 2024/1623 amending Regulation (EU) No 575/2013 (e.g., IRB approach is no longer allowed for equity exposures).
  - b. Enhancing the RTS by leveraging on 10 years of supervisory experience gathered since publication of the original RTS. This includes clarifications on the scope of the RTS, the qualitative criteria (e.g., amended definition or re-categorizing changes from material to ex-ante and vice versa), and clarifications on the calculation of the quantitative criteria (e.g., in case of scope reductions or changes affecting multiple rating systems).

### 3.2 Scope of the RTS

7. Recital 7 of the current CDR 529/2014 states that *‘The permission of competent authorities relates to the methods, processes, controls, data collection and IT systems of the approaches, therefore on-going alignment of the models to the calculation dataset used, based on the approved methods, processes, controls, data collection and IT systems, should not be covered by this Regulation’*. This recital gave rise to a number of interpretative questions from different stakeholders.
8. The EBA deems it necessary to clarify that recital 7 in the current RTS, specifically pertaining to the *‘on-going alignment of the models to the calculation data-set used’*, relates to the ongoing application of the rating systems, and not to changes due to the alignment of development and calibration processes to the approved rating system methods. As the permission of competent authorities relates to the methods, processes, controls, data collection and IT systems of the approaches, updates to the data for the application portfolio used in the ongoing application of the rating systems in order to calculate the RWEA for the application portfolio, based on the approved methods, processes, controls, data collection and IT systems, should not be considered to fall within the scope of this RTS. On the contrary, changes to development and calibration processes (including the respective reference datasets) to align with the approved methods, processes, controls, data collection and IT systems, should be covered by this RTS.
9. In that regard, the EBA deems it necessary to introduce a new recital in the updated RTS clarifying that *‘Changes to rating systems as defined in Regulation (EU) No 575/2013 may have a potential impact on the internal risk estimates used for risk weighted exposure amount calculation, and as such include changes affecting the range of application of a rating system, the rating methodology*

*for IRB systems, the definition of default and the validation framework as well as changes to relevant processes, data and the use of the models. Updates to the data used in the development and calibration of the rating systems should therefore be covered by this Regulation. However, updates to the data used in the ongoing application of the rating systems in order to calculate the risk weight exposure amount for the application portfolio should not be covered by this Regulation.'*

10. In a similar vein, an additional recital is introduced in the updated RTS clarifying that *'New origination of facilities that are of a type of exposure already rated under the IRB approach should not be seen as an extension of a rating system and should therefore not be covered by this Regulation'*.
11. Changes to aspects outside of the rating systems applicable under the IRB approach should not be considered falling within the scope of the RTS on model change, even if they may have a potential impact on the RWEA calculation. This implies that changes in the parameters Maturity (M), Total Annual Sales (S) and the SA-CCF assignment to off-balance sheet items which solely affect the formula used for RWEA calculation should not be within the scope of the RTS on model change as they do not directly affect aspects within the scope of a rating system. On the contrary, the methodology for assigning exposures to exposure classes continues to fall within the scope of the RTS on model change as changes to this methodology may also affect the internal risk estimates used for RWEA calculation and not only the formula used for RWEA calculation itself.
12. Institutions are required to assess and categorize any changes coming from the implementation of Regulation (EU) 2024/1623 that impact the performance of a rating system and bundle them for permission or notification. The prioritisation of the implementation of these changes and any related remediation plans and actions, including possible temporary mitigation measures, should be discussed with the competent authorities. However, the EBA considers that mandatory changes coming from a direct implementation of Regulation (EU) 2024/1623 and that do not impact the performance of a rating system should not be considered under the scope of this RTS. As such, they neither require an authorisation from the competent authorities nor a notification. These changes include the application of new regulatory values (new PD, LGD and CCF input floors, new LGD and CCF regulatory values and new parameters in the credit risk mitigation framework) and updates in relation to the risk weight function (e.g. deletion of the 1,06 factor).

**Consultation box 1.**

Question 1. Do you have any comments on the clarification of the scope of the revised draft regulatory technical standards to specify the conditions for assessing the materiality of the use of an existing rating system for other additional exposures not already covered by that rating system and changes to rating systems under the IRB Approach?

### 3.3 Qualitative criteria for assessing the materiality of changes

#### 3.3.1 Clarifications on the qualitative criteria

13. Where institutions make changes to the rating criteria, the RTS requires having an appropriate framework to assess the significance of (i) changes to the rank ordering; and (ii) changes to the distribution of obligors, facilities or exposures across grades or pools. In both cases, the RTS requires institutions to define the adequate metrics or measure(s) and an appropriate level. The EBA deems it relevant to provide a general clarification that these metrics should be measured on the final ratings or risk parameters (of the approved and of the changed models). This also implies that, in the case where exposures are grouped in pools or grades, the rank ordering should be derived from the final estimates associated with the grades or pools, and not based on intermediate (continuous) scores or other estimates of these exposures. In case of the supervisory slotting criteria approach (SSCA), the rank ordering should be derived from the allocation to the risk weight buckets.

#### 3.3.2 Qualitative changes recategorized from material change to ex ante notification

14. The EBA deems it necessary to make amendments to the definition of certain qualitative criteria in the updated RTS including re-classifying some aspects from material changes requiring prior permission to changes requiring notifications. Although no longer classified as material (unless the quantitative criteria are triggered), the EBA still considers these changes to be important to the extent that an ex-ante notification is required.

15. First, a revision is made to limit the material changes related to the Definition of Default (DoD) to aspects where the implementation of the changes may be more complex and may imply a higher risk of non-compliance pertaining to the identification of defaulted exposures as referred to in Article 178 of Regulation (EU) No 575/2013. It is also noted that a change of the definition of default alone does not change the risk weighting of non-defaulted exposures. With that, it is understood that DoD changes impacting the model performance to the extent that a new model would need to be developed, or a new calibration is necessary, would be captured via other criteria in the RTS. With this objective in mind, the EBA identified four areas where the implementation of the DoD related to the identification of defaulted exposures may be more complex. This includes changes to the method to identify if the obligor is more than 90 days past due on any material credit obligation according to Article 178(1)(b) of Regulation (EU) No 575/2013, changes to the level of application of the definition of default for retail exposures according to CRR Article 178(1), changes to the use of external data according to Article 178(4), and changes whether an indication of Unlikelihood to Pay results in an automatic or in a manual default reclassification. Nevertheless, these criteria may not capture all changes of higher complexity. Therefore, a backstop measure is added: a change related to DoD is deemed material when it impacts the default classification of the exposures in the range of application of a rating system in a significant manner. Similarly to other criteria in the RTS (e.g. change in the fundamental methodology for risk quantification),



there are no prescribed metrics and thresholds, but these will have to be defined by the institution itself.

16. It is clarified that only those changes in the validation methodology and/or validation processes are considered material when they lead to a more lenient judgment within the institution of the accuracy and consistency of the estimation of the relevant risk parameters, the rating processes or the performance of their rating systems according to Article 185(a) of Regulation (EU) No 575/2013. Other changes in the internal validation methodology according to Article 185 of the CRR are deemed not material, but instead require an ex-ante notification. This refers to those changes to the validation framework resulting in validation assessments that are at least as critical compared to the assessments resulting from the validation framework before the change, under different scenarios. For example, changes to traffic light thresholds of test metrics leading to a more positive validation result are deemed a material change; however, where such changes lead to an equally strict or more conservative validation result, an ex-ante notification is deemed appropriate. For this purpose, institutions should carefully consider the impact of the change on aggregated test outcomes where thresholds are set at a level higher than an individual test metric.

### 3.3.3 Qualitative changes removed from ex ante notification

17. Based on the qualitative criteria in the current RTS, changes to the supervisory slotting criteria approach (SSCA) according to Article 153(5), and changes in the treatment of purchased receivables according to Article 153(6) and (7) and Article 154(5) of Regulation (EU) No 575/2013 are being classified as requiring an ex-ante notification. This implies that a material change can only occur with respect to the SSCA or the treatment of purchased receivables if the quantitative criteria are exceeded. However, the EBA is of the opinion that there is limited reason to treat the SSCA and purchased receivables in a different manner compared to other rating systems. Therefore, the general materiality criteria should be applied in the updated RTS (i.e., in particular the changes in the rating criteria under item (2)(d) clarifying that the ranking and distribution should be considered in relation to the risk weight buckets).

#### Consultation box 2.

**Question 2.** Do you have any comments on the clarifications and revisions made to the qualitative criteria for assessing the materiality of changes as described in the Annex I, part II, Section 1 and Annex I, part II, Section 2?

## 3.4 Qualitative criteria for assessing the materiality of extensions and reductions

18. Annex I, Part I, Section 1, point 1 related to the classification of material extensions was updated on four accounts.

19. First, the distinction between the extensions covered by article 148(1) of Regulation (EU) 2024/1623 and the scope of this RTS is clarified. The current RTS already clarified that changes to

the permanent partial use of internal approaches or, where applicable, to the sequential implementation of internal approaches are covered by Articles 148 and 150 of Regulation (EU) No 575/2013 for IRB approach and those types of changes should not be covered by this Regulation. As such, in accordance with Article 148(1) of Regulation (EU) 2024/1623, additional exposures that were not risk weighted by another rating system (i.e. under the Standardized Approach or by F-IRB if the scope of an LGD model is extended) require in any case an approval by the competent authority and are not within scope of this RTS. As already mentioned in paragraph 10, it is clarified that new origination of facilities that are of a type of exposure already rated under the IRB approach should not be seen as an extension of a rating system and should therefore not be covered by this Regulation.

20. Second, the categorization of types of extensions is simplified, requiring approval for extensions to additional exposures, unless the institution can prove representativeness of the rating system for the extended exposures.
21. As a third revision, the concept of representativeness in this RTS which needs to be demonstrated by the institution in order to apply the derogation described in paragraph 20 is linked to the requirements on representativeness in the Commission Delegated Regulation (EU) 2022/439, namely to Article 37(2) pertaining to the risk differentiation capacity of the rating system, and to Article 42(2) pertaining to the risk quantification capacity of the rating system.
22. Finally, changes in the methodology used for assigning exposures to different exposure classes are reclassified as requiring an ex-ante notification. Although it is noted that such a change may potentially affect RWEA, the change in RWEA stemming from a change in the assignment methodology would stem from applying a different prescribed RWEA formula, input floor or other regulatory prescribed input (i.e., CRR3 requirements) rather than changes to the rating systems themselves. Similarly, changes in the methodology used for assigning an obligor or a transaction to a rating system are reclassified as requiring an ex-ante notification. This is because the implied changes to the affected rating systems are covered by other aspects of the RTS. In particular, the following changes would remain categorised as material model changes:
- a. changes stemming from an extension of the range of application of a rating system to additional exposures as described in paragraphs 19 to 21;
  - b. changes that would lead to a breach of quantitative thresholds, described in article 4(1)(c) and 4(1)(d) of the RTS on model change.

**Consultation box 3.**

**Question 3.** Do you have any comments on the clarifications and revisions made to the qualitative criteria for assessing the materiality of extensions and reductions as described in the Annex I, Part I, Section 1 and Annex I, Part I, Section 2?

## 3.5 Quantitative metrics for material changes and extensions

### 3.5.1 Quantitative metrics for material changes to rating systems

23. Changes have been made to the quantitative thresholds, where it was deemed necessary to on the one hand clarify the intension of the RTS regarding quantitative thresholds for changes to rating systems, and on the other hand to revise the quantitative thresholds that are related to extensions and reductions of the ranges of application of rating systems.
24. Regarding the quantitative thresholds for changes to rating systems, one aspect that was considered is the granularity which should be applied to define a model extension or change, i.e. whether a group of modifications affecting a single rating system should be considered as a single model change or as different changes. Modifications that are similar in nature should be grouped together as one change. With that, the timing of the changes should not be considered as a reason to justify the splitting of modifications into several model changes. For example, if the methodology to take into account recoveries from collateral is changed in a phased approach, where the methodological change is first applied to some collateral types and subsequently to others, such modifications constitute one change, if they constitute the same change to the approved methods, processes, controls, data collection, and IT systems used. As a consequence, one materiality assessment should be performed encompassing all such modifications.
25. As a second clarification, it is clarified that one change affecting multiple rating systems should be considered as a single change to rating systems in the IRB Approach. Institution should not split the change into separate changes to the different rating system affected by the change. Instead, the institution should assess the materiality by considering it as a single change when assessing the threshold described in Article 4(1)(c)(i) of this RTS. For example, the materiality of a change in the DoD affecting several rating systems is assessed for Article 4(1)(c)(i) by aggregating the RWEA impact of the DoD change across the rating systems affected. This was deemed relevant to ensure that this quantitative threshold, related to the impact of the change on the overall impact of the framework, is not diluted by assessing the threshold for each rating system individually.

#### **Consultation box 4.**

Instead of clarifying the quantitative thresholds for material changes to rating systems stating that one change affecting multiple rating systems should be considered as a single change to rating systems in the IRB Approach, it was also considered to revise this quantitative threshold to require institutions to assess the threshold for each rating system individually. This would imply that one change affecting multiple rating systems would be considered as separate changes to each individual rating system. Under this revision, for each rating system affected, the impact of the change would be calculated separately and the materiality of that change assessed against the threshold described in Article 4(1)(c)(i) separately.

Comparing the threshold in Article 4(1)(c)(i) against the change for each rating system individually might lower the burden and complexity for institutions. The change might be material for one rating system but not for another. Both in relation to the quantitative and qualitative criteria that include significance levels, this could be an effective way to reduce the burden on the institutions, because prior approval is required only for those rating systems where the change is material. However, this argument can be challenged, as a decision on the classification would need to be taken for each rating system, leading to potentially different outcomes per rating system. It was therefore considered most effective to clarify that one change affecting multiple rating systems should be considered as a single change to rating systems in the IRB Approach.

**Question 4.** Do you have any comments on the introduced clarification on the implementation of the quantitative threshold described in Article 4(1)(c)(i) and 4(1)(d)(i)?

### 3.5.2 Quantitative metrics for extensions and reductions to the range of application of rating systems

26. In relation to the quantitative threshold for reductions of the range of application of rating systems, the framework is adapted to capture the risks associated with such changes.
27. First, it is clarified that the quantitative threshold does not need to be applied to reductions of the range of application of rating systems, where the EBA deems ex-ante notifications for reductions as sufficient in accordance with Section 2 of Part 1 of Annex 1. Furthermore, the risks associated with reductions of the range of application of rating systems are understood to be captured elsewhere in the framework. Reductions due to reversals to less sophisticated approaches are captured by Article 149 of the Regulation (EU) 2024/1623. Reductions stemming from exposures moving to other rating systems under the IRB approach are captured in the framework for extensions of the range of application of those other rating systems. The threshold described in Article 4(1)(d) that applies to these extensions is considered to be appropriate to capture any risks stemming from the corresponding reductions of the range of application of rating systems.
28. With respect to extensions, it is furthermore clarified that the 15% threshold described in Article 4(1)(c)(ii) does not cover the risk that a rating system might not perform adequately for the additional exposures to which the range of application of the rating system is extended. This risk of this weak model performance on the new exposures becomes more pressing the larger the extensions of range of application of the rating system is in comparison to the existing range of application. Instead, the EBA considers that a different quantitative threshold is required for extensions, taking into account these specific risks concerned with extensions. The new threshold is described in an added point Article 4(1)(d)(ii). The threshold is calculated as the ratio of the risk-weighted exposure amounts of the additional exposures to the range of application of the rating system (i.e. the set of exposures to which the rating system is extended rated by this rating system) divided by the risk-weighted exposure of the existing range of application of the rating system prior to the extension.

**Consultation box 5:**

Instead of calculating the threshold as the ratio of the risk-weighted exposure amounts of the additional exposures to the range of application of the rating system, it was also considered to maintain the threshold described in the current Delegated Regulation (EU) No 529/2014. Under this approach, the numerator was calculated as the difference between the RWEA assigned by the extended rating system and the RWEA assigned to the set of exposures before the extensions.

**Question 5.** Do you have any comments on the revised 15% threshold described in Article 4(1)(d)(ii) related to the materiality of extensions of the range of application of rating systems?

### 3.6 Alignment with CRR 3

29. In Regulation (EU) 2024/1623, Article 183 refers to the requirements for assessing the effect of unfunded credit protection (UFCP) for exposures to central governments and central banks, exposures to regional governments, local authorities and public sector entities, and exposures to corporates, where own estimates of LGD are used and for retail exposures. To align this RTS with the Regulation (EU) 2024/1623, the EBA considers it appropriate to broadening the scope of paragraph 2(i), by referring generally to changes to UFCP effecting an institution's own estimates of LGD. It is the understanding of the EBA that this relates primarily to changes made by institutions within their discretion under Article 183(1a) of Regulation (EU) 2024/1623, which stipulates that institutions may recognise unfunded credit protection by using either the PD/LGD modelling adjustment approach or the substitution of risk parameters approach under A-IRB (in accordance with Article 236a and subject to the eligibility requirements of Chapter 4). As such, changes from a modelling approach to a substitution approach and vice versa would entail an ex-ante notification.

30. In addition, considering that Article 150(1)(a) of Regulation (EU) 2024/1623 imposes the use of the Standardised approach for the exposures assigned to the exposure class referred to in Article 147(2), point (e) (equity exposure class), all references to the internal models approach to equity exposures are removed. Similarly, the use of Advanced Measurement Approach (AMA) for the operational risk is no longer possible under Regulation (EU) 2024/1623, and therefore all reference to this approach are removed.

### 3.7 IT and Documentation requirements

31. On the expectations in relation to the IT implementation of the rating system, a technical clarification is made by adding a reference to Article 144(1)(g) of Regulation (EU) No 575/2013 to Article 3(5) of the updated RTS. This requires institutions to calculate under the IRB Approach the own funds requirements resulting from its risk parameter estimates and to be able to submit the reporting as required by Article 430 of Regulation (EU) No 575/2013. This implies that institutions should have conducted the preparatory work for the IT implementation of the rating systems. The

intention is to further clarify that institutions are not only required to be able to calculate RWEA but also to report accordingly under COREP based on the approved extension or change from the date specified in the new permission. Introducing the cross-reference to Article 144(1)(g) of Regulation (EU) No 575/2013 therefore provides further transparency and clarity on the requirements regarding the implementation of material changes post approval by the CAs.

32. A final revision is made that stipulates that for an extension all documentation referred to in Article 8(1) of this RTS should be submitted, irrespective of whether the extension requires approval from the competent authority or is subject to notification prior to implementation. This implies that institutions should include in the documentation also the assessment report of the validation function and the technical documentation related to the extension. Furthermore, the institution should also deliver documentation vis-à-vis the model performance of the rating system on the extended scope of application. This allows competent authorities to be more effective in challenging the materiality classification of a given extension.

**Consultation box 6:**

It was considered that validation processes of institutions may be hampered if they are required to provide, for extensions that require prior notification, also the technical documentation and the assessment report of the validation function. In particular, this implies that an institution either has to wait for the periodical validation process before submitting the extension notification, or perform an ad-hoc assessment by the validation function in order to submit the extension for prior notification.

**Question 6.** Do you have any comments on the documentation requirement for extensions that require prior notification?

## 4. Draft regulatory technical standards

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## COMMISSION DELEGATED REGULATION (EU)

of XXX

amending the regulatory technical standards laid down in Commission Delegated Regulation (EU) No 529/2014 supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for assessing the materiality of extensions and changes of the Internal Ratings Based Approach.

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 575/2013 of 26 June 2013 on prudential requirements for credit institutions and amending Commission Delegated Regulation (EU) No 529/2014<sup>1</sup> [please insert footnotes with OJ reference] in particular Article 143(5), third subparagraph thereof,,

Whereas:

- (1) Commission Delegated Regulation (EU) No 529/2014 which specifies the technical standards for assessing the materiality of extensions and changes of the IRB Approach and the Advanced Measurement Approach should be amended to reflect the changes in the legal framework which occurred since its entry into force, with particular reference to the introduction of the provisions concerning the repeal of the exclusion of IRB approaches to equity exposures and the repeal of the provisions of Regulation (EU) No 575/2013 concerning the Advanced Measurement Approach (AMA) for operational risk. Furthermore, several elements of Commission Delegated Regulation (EU) No 529/2014 should be enhanced by leveraging on the supervisory experience gathered since the publication of the Delegated Regulation (EU) No 529/2014.
- (2) Changes to rating systems as defined in Regulation (EU) No 575/2013 may have a potential impact on the internal risk estimates used for risk weighted exposure amount calculation, and as such include changes affecting the range of application of a rating system, the rating methodology for IRB systems, the definition of default and the validation framework as well as changes to relevant processes, data and the use of the models. Updates to the data used in the development and calibration of the rating systems should therefore be covered by this Regulation. However, updates to the data used in the

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<sup>1</sup> OJ L 176, 27.6.2013, p. 1.



ongoing application of the rating systems in order to calculate the risk weight exposure amount for the application portfolio should not be covered by this Regulation.

- (3) In accordance with article 148(1) of Regulation (EU) No 575/2013, extensions of additional exposures that were not risk weighted by another rating system before the change are not covered by Delegated Regulation (EU) No 529/2014. This includes extensions to additional exposures that were risk-weighted under the Standardised Approach before the extension or, where it relates to the extension of the range of application of an LGD model, additional exposures that were risk-weighted under a rating system without own LGD estimates before the extension.
- (4) ‘New origination of facilities that are of a type of exposure already rated under the IRB Approach should not be seen as an extension of a rating system and should therefore not be covered by this Regulation’
- (5) To improve efficiency and lower the burden for supervisors and institutions whilst maintaining a prudent approach to classifying model changes, certain qualitative criteria described in Annex I of this Regulation should be amended, re-classifying aspects from material changes requiring prior permission to changes requiring notifications. Although no longer classified as material (unless the quantitative criteria are triggered), these changes should be deemed important to the extent that a prior notification is required.
- (6) A revision should be made to limit the material changes related to the definition of default to aspects where the implementation of the changes may be more complex and may imply a higher risk of non-compliance pertaining to the identification of defaulted exposures in accordance with Regulation (EU) No 575/2013. However, it is not possible to establish an exhaustive list of types of changes that may lead to an incorrect estimation of the risk-weighted exposure amount stemming from an incorrect implementation. Instead, four types of changes are identified that require approval due to the potentially high impact stemming from an incorrect implementation. This is complemented by a backstop measure to ensure appropriate implementation of any change to the definition of default of institutions where an incorrect implementation may have a potentially high impact on risk-weighted exposure amounts.
- (7) For changes to the rating criteria, this Regulation should require having an appropriate framework to assess the significance of (i) changes to the ranking; and (ii) changes to the distribution of obligors, facilities or exposures across grades or pools. Institutions should define the adequate metrics or measures and an appropriate level. To ensure a harmonised implementation of these metrics, it is clarified that these metrics should be measured on the final ratings or risk parameters, of both the approved and of the changed models. In the case where exposures are grouped in pools or grades, the ranking should

be derived from the final estimates associated with the grades or pools, and not based on intermediate continuous scores or other estimates of these exposures. In case of exposures risk weighted according to Article 153(5) of Regulation (EU) No 575/2013, the rank ordering should be derived from the allocation to the risk weight buckets.

- (8) A revision to this Regulation should be made to ensure that institutions can update their validation framework in a timely manner when it does not entail a risk of missing deficiencies in the rating system. Therefore, the changes in the validation methodology and validation processes are considered as material only in the case where they lead to a more lenient assessment within the institution.
- (9) A revision to the framework should be made such that changes to the treatment of exposures that are risk weighted according to Article 153(5), and changes in the treatment of purchased receivables according to Article 153(6) and (7) and Article 154(5) of Regulation (EU) No 575/2013 are classified according to the general materiality criteria applied for other rating systems. It is thereafter no longer necessary to explicitly mention them in the list of changes requiring an ex-ante notification.
- (10) The quantitative threshold for changes to the rating system should be clarified to ensure a harmonised implementation amongst competent authorities and institutions. It is clarified thereafter that where one change affects multiple rating systems, for example a change in the definition of default, the quantitative threshold in Article 4(1)(c)(i) in this Regulation relates to the aggregate impact of the change across the different rating systems. Next to that, the quantitative thresholds that apply to changes to the range of application of rating systems have been revised to align them with the risks stemming from such changes under the IRB Approach. First, it is clarified that the quantitative thresholds do not apply to reductions of the range of application of a rating system because the risk of exposures moving to other rating systems is covered by the quantitative threshold that applies to extensions of the range of application of these other rating systems. To extend the range of application of rating systems, the quantitative threshold in Article 4(1)(c) in this Regulation is considered inappropriate, such that a new threshold should be introduced. This is because a rating system might not perform adequately for the additional exposures to which the range of application of the rating system is extended, irrespective of the rating system that was used to risk-weight the exposures before the change. The risk of this weak model performance on the new exposures is considered to be proportionate to the magnitude of the extension of range of application of the rating system in comparison to the range of application of the rating system prior to the change.
- (11) The documentation to be submitted by institutions to competent authorities at the time of the application for approval of a change or notification of an extension should

also include the information related to the performance of the rating system after the change to the IRB Approach, which is in particular relevant for extensions of rating systems to additional exposures. This clarification should be introduced to ensure effective supervision on changes to the IRB Approach, in particular in the context of potential changes in the model landscape of institutions.

- (12) This Regulation is based on the draft regulatory technical standards submitted by the European Banking Authority to the Commission.
- (13) The European Banking Authority has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits, and requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council<sup>2</sup>.

HAS ADOPTED THIS REGULATION:

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<sup>2</sup> Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12).

*Article 1*

Commission Delegated Regulation (EU) No 529/2014 is amended as follows:

(1) Article 1 is replaced by the following:

*‘Article 1*

**Subject matter**

This Regulation lays down the conditions for assessing the materiality of extensions and changes to the Internal Rating Based approaches and the Internal Models Approach permitted in accordance with Regulation (EU) No 575/2013, including the modalities of the notifications of such changes and extensions.’

(2) Article 2 is amended as follows:

(a) paragraph 1 is replaced by the following:

‘1. The materiality of changes to the range of application of a rating system, or of changes to the rating systems for the Internal Rating Based approach (‘changes in the IRB approach’) or of the materiality of the extensions and changes for the Internal Models Approach (‘extensions and changes in the IMA’) shall be classified into one of the following categories:

- a. material extensions and changes, which, according to Articles 143(3) and 363(3) of Regulation (EU) No 575/2013, require permission from the competent authorities;
- b. other extensions and changes, which require notification to the competent authorities.’

(3) Article 3 is amended as follows:

(a) in Article 3(1), subparagraph 2 is deleted.

(b) paragraph 2, point (c), is replaced by the following:

‘(c). for changes having no direct quantitative impact, no quantitative impact as laid down in Article 4(1)(c) and Article 4(1)(d) for the IRB approach or Article 7a(1)(c) for IMA shall be calculated.’

(c) paragraph 2 point (d) is added:

‘(d). for reductions to the range of application of a rating system no quantitative impact as laid down in Article 4(1)(c) or Article 4(1)(d) for the IRB approach shall be calculated.’

(d) paragraph 3 is replaced by the following:

‘3. One material extension or change shall not be split into several changes or extensions of lower materiality. In particular, the following modifications shall be assessed as one extension or change:

(a) modifications of a different nature are made simultaneously to the same rating system

(b) modifications of the same nature and to the same rating system that are implemented sequentially over time.

(c) only for the assessment of changes referred to in Article 4(1)(a), 4(1)(c)(i), and 4(1)(d)(i), one modification affecting multiple rating systems.

(e) paragraph 5 is replaced by the following:

‘5. Where competent authorities have provided their permission in relation to a material extension or change, institutions shall calculate the own funds requirements in accordance with Article 144(1)(g) of Regulation (EU) No 575/2013 based on the approved extension or change from the date specified in the new permission which shall replace the prior one. The non-implementation on the date specified in the new permission of an extension or change for which permission from competent authorities has been given, shall require a new permission from competent authorities which shall be applied for without undue delay.’

(4) Article 4 is amended as follows:

(a) paragraph 1 is amended as follows:

(i) point (a) is replaced by the following:

‘(a) they fall under any of the changes to the range of application of a rating system described in Annex I, Part I, Section 1;’

(ii) point (b) is replaced by the following:

‘(b) they fall under any changes to the rating systems described in Annex I, Part II, Section 1;’

(iii) point (c) is replaced by the following:

‘(c) they are changes to rating systems that result in either of the following:

(i) a decrease of 1,5 % or more of either of the following:

- the overall EU parent institution's consolidated risk-weighted exposure amounts for credit and dilution risk,
- the overall risk-weighted exposure amounts for credit and dilution risk in the case of an institution which is neither a parent institution, nor a subsidiary;

(ii) a decrease of 15 % or more of the risk-weighted exposure amounts for credit and dilution risk associated with the range of application of the internal rating system.’

(iv) point (d) is added:

‘(d) they are extensions of the range of application of a rating system that result in either of the following:

(i) a decrease of 1,5 % or more of either of the following:

- the overall EU parent institution's consolidated risk-weighted exposure amounts for credit and dilution risk,
- the overall risk-weighted exposure amounts for credit and dilution risk in the case of an institution which is neither a parent institution, nor a subsidiary;

(ii) an increase of 15% or more of the risk-weighted exposure amounts for credit and dilution risk associated with the range of application of the internal rating system.’

(b) paragraph 2 is replaced by the following:

‘2. For the purposes of paragraph (1)(c)(i) and paragraph (1)(d)(i) of this Article, and in accordance with Article 3(2), the impact of the change shall be assessed as a ratio calculated as follows:

(a) in the numerator, the difference in the risk-weighted exposure amounts for credit and dilution risk associated with the range of application of all internal rating systems impacted by the change before and after the change at the EU parent institution's consolidated level or at the institution level which is neither a parent institution, nor a subsidiary;

(b) in the denominator the overall risk-weighted exposure amounts for credit and dilution risk before the change at the EU parent institution's consolidated level or, respectively, at the institution level which is neither a parent institution, nor a subsidiary.’

(c) paragraph 3 is amended as follows:

(i) point (a) is replaced by the following:

‘(a) in the numerator, the difference in the risk-weighted exposure amounts for credit and dilution risk associated with the range of application of the internal rating system before and after the change;’

(ii) point (b) is replaced by the following:

‘(b). in the denominator, the risk-weighted exposure amounts for credit and dilution risk before the change associated with the range of application of the rating system.’

(d) paragraph 4 is added as follows:

‘4. For the purposes of paragraph (1)(d)(ii) of this Article, and in accordance with Article 3(2), the impact of the change shall be assessed as a ratio calculated as follows:

(a) in the numerator, the risk-weighted exposure amounts for credit and dilution risk after the change associated with the additional exposures on to which the range of application of the internal rating system is extended.

(b) in the denominator, the risk-weighted exposure amounts for credit and dilution risk before the extension associated with the range of application of the rating system.

The calculation shall refer to the same point in time.’

(5) Article 5 is amended as follows:

(a) paragraph 1, point (a)(iii) is replaced by the following:

‘(iii) changes which result in a decrease of at least 5 % of the risk-weighted exposure amounts for credit and dilution risk associated with the range of application of the internal rating system.’

(b) paragraph 2 is amended as follows:

(i) point (a) is replaced by the following:

‘(a) in the numerator, the difference in the risk-weighted exposure amounts for credit and dilution risk associated with the range of application of the internal rating system before and after the change;’

(ii) point (b) is replaced by the following:

‘(b) in the denominator, the risk-weighted exposure amounts for credit and dilution risk before the change associated with the range of application of the rating system.’

(6) Article 6 is deleted.

(7) Article 7 is deleted.

(8) Article 8 is amended as follows:

(a) paragraph 1 is replaced by the following:

‘1. For extensions and changes to the IRB approach classified as requiring competent authorities' approval, and for extensions requiring prior notification, institutions shall submit, together with the application, the following documentation:

(a) description of the extension or change, its rationale and objective;

(b) implementation date;

(c) scope of application affected by the model extension or change, with volume characteristics;

(d) technical and process document(s),

(e) reports of the institution's assessment of the model performance of the rating system after the change;

(f) reports of the institutions' independent review or validation;

(g) confirmation that the extension or change has been approved through the institution's approval processes by the competent bodies and date of approval;

(h) where applicable, the quantitative impact of the change or extension on the risk weighted exposure amounts or on the own funds requirements, or on the relevant risk numbers or sum of relevant own funds requirements and risk numbers;

(i) records of the institution's current and previous version number of internal models which are subject to approval, where applicable.’

(b) paragraph 2 is replaced by the following:



‘2. For changes classified as requiring notification either before or after implementation, institutions shall submit, together with the notification, the documentation referred to in points (a), (b), (c), (g) and (h) of paragraph 1.’

*Article 2*

This Regulation shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

*For the Commission  
The President*

*On behalf of the President*

*[Position]*

**ANNEX**

Annex 1 to Commission Delegated Regulation (EU) No 529/2014 is amended as follows:

(1) Part I is amended as follows:

(a) the title of Part I is replaced by the following:

**‘PART I**

**CHANGES TO THE RANGE OF APPLICATION OF RATING SYSTEMS’**

(b) Section 1 is amended as follows:

(i) point 1 is replaced by the following:

‘1. Extending the range of application of a rating system to additional exposures, unless the institution can prove that;

(i) the data used to build the model to assign exposures to grades or pools is representative with respect to the extended scope of application according to Article 174(c) of Regulation (EU) No 575/2013 and in particular Article 37(2)(a) and 37(2)(b) of Commission Delegated Regulation (EU) 2022/439;

(ii) the data used for risk quantification purposes shall be representative of the extended scope of application according to Article 179(1)(d) of Regulation (EU) No 575/2013 and in particular Article 42(2)(a) and 42(2)(b) of Commission Delegated Regulation (EU) 2022/439.

For the purposes of establishing ‘representativeness’ under points (i) and (ii) of the first paragraph institutions shall provide a complete description of the used criteria and measures.’

(ii) point 2 is deleted.

(c) Section 2 is amended as follows:

(i) point 2 is deleted.

(ii) point 4 is deleted.

(2) Part II is amended as follows:

(a) the title of Part II is replaced by the following:

**‘PART II  
CHANGES TO RATING SYSTEMS’**

(b) Section 1 is amended as follows:

(i) point 1 is deleted.

(ii) point 2(d) is replaced by the following:

‘(d). changes to the rating criteria as referred to in Article 170(1)(c) and (e) and Article 170(4), and 170(2) of Regulation (EU) No 575/2013 and/or their weights, sequence or hierarchy, if any of the following conditions are met:

- (i) they change the rank ordering referred to in Article 170(1)(c) and (3)(c) of Regulation (EU) No 575/2013 in a significant manner, the measure and level of which will have been defined by the institution;
- (ii) they change the distribution of obligors, facilities or exposures across grades or pools according to Article 170(1)(d) and (f) and Article 170(3)(b) of Regulation (EU) No 575/2013 in a significant manner, the measure and level of which will have been defined by the institution.

The measures referred to in point (i) and point (ii) of the first subparagraph are captured according to the final ratings or risk parameters of the approved and of the changed models. In the case where exposures are grouped in pools or grades, the rank ordering measure referred to in point (i) of the first subparagraph should be determined based on the final estimates associated with the grades or pools, and not based on intermediate scores or other estimates for these exposures. For exposures that are risk-weighted according to Article 153(5) of Regulation (EU) No 575/2013 the rank ordering measure referred to in point (i) of the first subparagraph should be determined based on the allocation to the risk weight buckets'

(iii) point 2(f) is replaced by the following:

'(f). change in the fundamental methodology for estimating PDs, LGDs including best estimate of expected loss, and conversion factors according to Articles 180, 181 and 182 of Regulation (EU) No 575/2013, including the methodology for deriving appropriate adjustments in its estimates and including the methodology for deriving a margin of conservatism related to the expected range of estimation errors according to Article 179(1)(f) of Regulation (EU) No 575/2013. For LGDs and conversion factors this includes also changes in the methodology for accounting for an economic downturn according to Articles 181(1)(b) and 182(1)(b) of Regulation (EU) No 575/2013;'

(iv) point 3 is replaced by the following:

'3. Changes in the definition of default according to Article 178 of Regulation (EU) No 575/2013, if any of the following conditions are met:

- (a) they change the method to identify if the obligor is more than 90 days past due on any material credit obligation according to Article 178(1)(b) of Regulation (EU) No 575/2013;

(b) they change the level of application of the definition of default for retail exposures according to Article 178(1), second subparagraph of Regulation (EU) No 575/2013;

(c) they change the use of external data according to Article 178(4) of Regulation (EU) No 575/2013;

(d) they change whether an indication of unlikelihood to pay according to Article 178(3) of Regulation (EU) No 575/2013 results in an automatic or in a manual default reclassification;

(e) they change the default classification in the reference dataset or scope of application of a rating system in a significant manner, the measure and level of which will have been defined by the institution.’

(v) point 4 is replaced by the following:

‘Changes in the validation methodology and/or validation processes which lead to more lenient changes in the institution's judgment of the accuracy and consistency of the estimation of the relevant risk parameters, the rating processes or the performance of their rating systems according to Article 185(a) of Regulation (EU) No 575/2013.’

(vi) point 5 is deleted.

(c) Section 2 is amended as follows:

(i) point 1 is deleted:

(ii) point 2(a) is replaced by the following:

‘(a) Changes in the methodology of assigning exposures to exposure classes and rating systems. These include:

(i) changes in the methodology used for assigning exposures to different exposure classes according to Article 147 of Regulation (EU) No 575/2013;

(ii) changes in the methodology used for assigning an obligor or a transaction to a rating system according to Article 169(1) of Regulation (EU) No 575/2013.’

(iii) point 2(d) is replaced by the following:

‘(d) changes to the rating criteria and/or their weights or hierarchy according to Article 170(1)(c) and (e) and 170(4), and changes to specialised lending exposures according to Articles 153(5) and 170(2) of Regulation (EU) No 575/2013 of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Section 1 of this Annex.’

(iv) point 2(h) is replaced by the following:

‘(h) changes in the methodology for estimating PDs, LGDs including best estimate of expected loss, and conversion factors according to Articles 180, 181 and 182 of Regulation (EU) No 575/2013 including the methodology for deriving appropriate adjustments in its estimates and including the methodology for deriving a margin of conservatism related to the expected range of estimation errors according to Article 179(1)(f) of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Section 1 of this Annex. For LGDs and conversion factors this includes also changes in the methodology for accounting for an economic downturn according to Article 181(1)(b) and Article 182(1)(b) of Regulation (EU) No 575/2013;’

(v) point 2(i) is replaced by the following:

(i) changes in the way or extent to which unfunded credit protection is accounted for in the LGD estimation according to Article 183 of Regulation (EU) No 575/2013;

(vi) point 2a is added to Section 2:

‘2a. Changes in the definition of default according to Article 178 of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Section 1 of this Annex.’

(vii) point 7 is deleted.

(9) Annex II to Regulation (EU) No 529/2014 is deleted.

## 5. Accompanying documents

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### 5.1 Draft cost-benefit analysis / impact assessment

33. Article 143(5) of the CRR3 mandates the EBA to revise the RTS on model change to specify the conditions for assessing the materiality of the use of an existing rating system for other additional exposures not already covered by that rating system and changes to rating systems under the IRB Approach. The EBA has published the initial draft RTS in December 2013 and the related Commission Delegated Regulation (CDR 529/2014) was adopted in March 2014.

34. As per Article 10(1) of the EBA regulation (Regulation (EU) No 1093/2010 of the European Parliament and of the Council), any RTS developed by the EBA shall be accompanied by an Impact Assessment (IA) annex which analyses 'the potential related costs and benefits' before submitting to the European Commission. Such annex shall provide the reader with an overview of the findings as regards the problem identification, the options identified to remove the problem and their potential impacts.

35. The EBA has prepared the IA contained in this consultation paper, which analyses the policy options considered. Given the nature of the topic, the IA is qualitative.

#### A. Problem identification

36. The proposed amendments originate mainly from two sources: first, the alignment of the CDR with the corresponding amendments to Regulation (EU) No 575/2013, and second, the enhancement of supervisory effectiveness of the approval process of model changes and extensions. These include, inter alia, amendments to the qualitative criteria related to the definition of default, the validation framework, and the modelling approaches, updates to the framework for extensions and reductions, and clarifications on the calculation of quantitative criteria and the scope of the RTS.

37. In the context of the latter, in particular recital 7 of the current CDR 529/2014: 'The permission of competent authorities relates to the methods, processes, controls, data collection and IT systems of the approaches, therefore on-going alignment of the models to the calculation data-set used, based on the approved methods, processes, controls, data collection and IT systems, should not be covered by this Regulation', gave rise to a number of interpretive questions from various stakeholders.

## B. Policy objectives

38. The main objective of this RTS is to provide alignments corresponding to the updated regulatory framework and clarifications on interpretative issues that have proved to be unduly burdensome for institutions and or/supervisors in order to ultimately ensure a harmonised framework at European level. The review builds on more than 10 years of specific supervisory experience using the currently applicable criteria

## C. Options considered and assessment

39. In preparing this RTS, the EBA considered the clarification of the interpretive issues as one of the main aspects. These include, inter alia, clarifications on the qualitative criteria for assessing the materiality of changes, clarifications on the qualitative criteria for assessing the materiality of extensions, clarifications on the quantitative metrics for material changes and extensions, alignments with CRR3, and IT and documentation requirements.

40. The EBA also assessed the interactions between the quantitative thresholds and the qualitative criteria. Specifically, it considered combining the existing quantitative criteria with the qualitative criteria (i.e. changing the 'or' to an 'and' in the CDR for certain qualitative criteria); in other words, both criteria—quantitative and qualitative—would need to be met in order to trigger the classification as a material model change. To understand whether such a recalibration was needed, the EBA has conducted a survey among national competent authorities and the results showed that most material model changes are in fact due to the qualitative criteria. Members were of the opinion that the changes triggering a qualitative threshold observed were considered to require approval from the national competent authority, irrespective of whether the quantitative trigger was hit. Furthermore, often multiple qualitative triggers were hit without triggering a quantitative threshold, further strengthening the belief that supervisory approval was still needed despite not triggering of the quantitative criteria. This is in line with the philosophy of the original CDR, as the quantitative thresholds were intended as 'backstops' and not as main criteria. It was therefore decided to retain the current principles, with the quantitative criteria serving as a 'backstop'.

41. Consideration was also given to how a change affecting multiple rating systems should be assessed against the 1.5% threshold. In particular, this means that either the threshold is assessed for each individual rating system (option 1) or the threshold is assessed for all affected rating systems, i.e. considered as a single change to the rating systems in the IRB Approach (option 2). The main argument in favour of option 1 is a potential reduction in burden and complexity for institutions, as the change could be material for one rating system but not for another. However, this argument can be challenged as it does not necessarily ensure legal consistency, i.e. the decision on classification leads to a potentially different outcome depending on the rating system. It was therefore considered appropriate to clarify that a change affecting multiple rating systems should be considered as a single change to the rating systems under the IRB Approach.

42. In addition, the quantitative thresholds for extensions to the range of application of rating systems have also been reviewed. It is clarified that the 15% threshold described in Article 4(1)(c)(ii) does not apply to extensions as it does not cover the risk that a rating system might not perform adequately for the additional exposures to which the range of application of the rating system is extended. Hence, a new quantitative threshold for extensions is required that considers the specific risks associated with extensions, which become more pressing the larger the extended scope of range of application is compared to the existing range of application. To reflect such risks associated with extensions, the threshold shall be calculated as the ratio of the risk-weighted exposure amounts of the additional range of application of the rating system (i.e. the set of exposures to which the rating system is extended) divided by the risk-weighted exposure amounts of the existing range of application of the rating system before the extension.
43. In preparing this RTS, the EBA considered it therefore sufficient to maintain the principles of the framework of the current RTS (i.e. the list of qualitative criteria and the quantitative threshold as a 'back-stop' measure) while clarifying the interpretative issues. In addition, a new quantitative threshold is introduced that takes into account specific risks associated with extensions to the range of application of rating systems.



## 5.2 Overview of questions for consultation

**Question 1.** Do you have any comments on the clarification of the scope of the revised draft regulatory technical standards to specify the conditions for assessing the materiality of the use of an existing rating system for other additional exposures not already covered by that rating system and changes to rating systems under the IRB Approach?

**Question 2.** Do you have any comments on the clarifications and revisions made to the qualitative criteria for assessing the materiality of changes as described in the Annex I, part II, Section 1 and Annex I, part II, Section 2?

**Question 3.** Do you have any comments on the clarifications and revisions made to the qualitative criteria for assessing the materiality of extensions and reductions as described in the Annex I, Part I, Section 1 and Annex I, Part I, Section 2?

**Question 4.** Do you have any comments on the introduced clarification on the implementation of the quantitative threshold described in Article 4(1)(c)(i) and 4(1)(d)(i)?

**Question 5.** Do you have any comments on the revised 15% threshold described in Article 4(1)(d)(ii) related to the materiality of extensions of the range of application of rating systems?

**Question 6.** Do you have any comments on the documentation requirement for extensions that require prior notification?