IRRBB & CSRBB - Regulatory Updates

Regulatory Technical Standards for risks arising from potential changes in interest rates – an overview and impact assessment of recently published regulations.

May 2024

In this update, we have outlined the impact of recently published regulations as applied to the Pillar 2 interest rate risk (IRRBB) and credit spread risk (CSRBB) approach and reporting requirements on all banks within the EU.

I. Regulatory Landscape

As outlined by the European Banking Authority (EBA), the amendments outlined below supplement the implementing Regulation EU 2021/451 (Rules on Supervisory reporting of IRRBB), and Directive 2013/36/EU (CRD IV).

The relevant risk measures for non-trading book activities are the economic value of equity (EVE), and the net interest income (NII).

II. List of Amendments

- Amendments to **the technical standards applying to IRRBB supervisory reporting (CIR EU 2024/855)**
- A supplement outlining the shock scenarios to be implemented as part of the **Supervisory Outlier Test (SOT) on interest rates (CDR EU 2024/856)**
- A supplement outlining **a standardised approach to the evaluation of interest Rate Risk (CDR EU 2024/857)**

III. Impact of New Regulations on Existing Regulatory Framework

Pillar II Risk	IRRBB			CSRBB
Established Guidelines	CRD VI Directive 2013/36/EU – (Transposing Basel III Regulations into EU Law)		CIR 2021/451 – (Rules on Supervisory Reporting)	EBA/GL/2022/14
Subject Area	Supervisory Outlier Test (SOT)	Standardised approach for the evaluation of interest rate risk	Technical Standards on the supervisory reporting of IRRBB	Requirements for Internal CSRBB Management
Amendment & Summary of Impact	CDR EU 2024/856	CDR EU 2024/857	CIR EU 2024/855	Status Quo
	• Definition of six supervisory shock scenarios. • Parametric specifications for supervisory shock scenarios. • Calculating changes in an Institutions EVE and NII with regard to the shock scenarios. • Quantitative definition of a “Large Decline” in NII. • Quantitative definition of outlier significance criterion for changes in EVE.	• Definition of a standardised methodology for evaluating EVE and NII of an institutions non trading book activities. • Definition and parametrisation for the calculation of the Standardised EVE and NII risk measures. • Definition and parametrisation of a simplified standardised methodology for EVE and NII.	• Specification of uniform reporting formats, templates, instructions, and methodologies. • Inserts a new article, Article 20a, detailing reporting requirements for interest rate risk in the banking book, specifying reporting frequencies for different types of institutions.	• CSRBB Guidelines have not been directly impacted by the new regulations discussed here.
	In effect: **May 2024**	In effect: **May 2024**	First Reporting Date: **Sept 2024**	Already in effect

IV. Supervisory Outlier Testing (SOT)

Published in December 2023; in effect from May 2024. As part of IRRBB guidelines in CRD IV, banks must determine the impact of **six** supervisory shock scenarios (Fig. 1a, 1b, 1c) on their economic value of equity (**EVE**) and **two** supervisory shock scenarios (Fig. 1a) on their net interest income (**NII**) as part of the SOT process. These shock scenarios are applied to the risk-free interest rate and can be grouped into three categories, illustrated in Figure 1.

V. Significance Thresholds

In addition to defining these scenarios, CRD 2024/856 sets thresholds for the significance of quantified risk. Banks must classify their interest rate risk as significant if the impact of any of these six scenarios on EVE exceeds **15% of Tier 1 Capital** (assuming a run-off balance sheet) or if the impact on NII is large. This amendment gives specific details on these shock scenarios, including appropriate assumptions, parametric instructions for implementing shocks, and the definition of a "large" impact on NII (**>5% of Tier 1 Capital** over a one-year period assuming a constant balance sheet).

VI. Examples of Supervisory Shock Scenarios

In the SOT document, the quantities $R_{parallel,\,c}$, $R_{short,\,c}$ and $R_{long,\,c}$ are specified for various currencies (c). For example, in euros, these respective quantities are defined as 2%, 2.5%, and 1.5%.

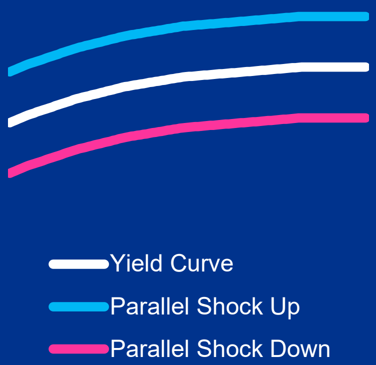

Fig. 1a) Parallel Shocks

$$\Delta R_{parallel,\,c}\,(t_k) = \pm\, R_{parallel,\,c}$$

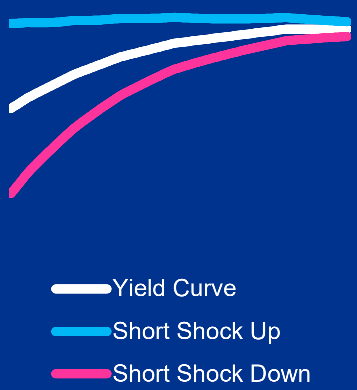

Fig. 1b) Short Rate Shocks

$$\Delta\, R_{short,c}\,(t_k) = \pm\, R_{short,c} \cdot (e^{-tk/4})$$

$$\Delta\, R_{long,c}\,(t_k) = \pm\, R_{long,c} \cdot (1-e^{-tk/4})$$

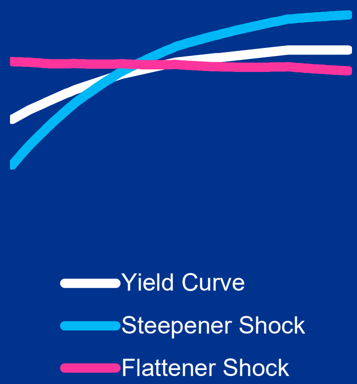

Fig. 1c) Rotation Shocks

$$\Delta R_{steepener,\,c}\,(t_k) = -\,0.65\,|\,\Delta R_{short,c}\,(t_k)\,| + 0.9\,|\Delta R_{long,\,c}\,(t_k)\,|$$

$$\Delta R_{flattener,\,c}\,(t_k) = 0.8\,|\,\Delta R_{short,c}\,(t_k)\,| - 0.6\,|\,\Delta R_{long,\,c}\,(t_k)\,|$$

VII. Standard Approach for Interest Rate Risk

Published in December 2023 and in effect from May 2024, the standardised approach for interest rate risk must be applied if required by an institution's regulator. This amendment suggests an approach to evaluating interest rate risk for banks within the EU, and details the precise requirements in the evaluation of interest rate risk expected of an institution if requested by the regulator.

The standardised approach is outlined for the calculation of the **EVE**, and the **NII** risk measures, as well as simplified approaches for each of these respective measures. Specific instructions are provided for evaluating risk across different interest rate-sensitive asset classes and financial instruments.

- ***Fixed and Floating Rate Instruments***
- ***Non-Maturity Deposits (NMD)***
- ***Fixed Rate Loans Subject to Early Repayment***
- ***Fixed Rate Term Deposits Subject to Early Redemption Risk***
- ***Derivative Instruments Without Optionality***
- ***NPEs and Fixed Rate Loan Commitments to Retail Counterparties***

***The above components are indictive and not exhaustive in nature**

VIII. Updated Reporting Requirements under CRR

This amendment applies to the Commission Implementing Regulation EU 2021/451 technical standards. It specifies the exact reporting requirements for the monitoring of IRRBB by providing reporting templates, which will be filled by each bank within the EU beginning in **September 2024**.

The amendment provides instructions at a field level for the completion of the **five** sets of reporting templates, each of which must be populated by **competent authorities** to identify and report potential excessive losses in a bank's non-trading book activities.

New Article: 20a

CIR 2024/855 inserts a new article, Article 20a, to the Commission Implementing Regulation EU 2021/451. Article 20a details reporting requirements for interest rate risk in the banking book, specifying reporting frequencies for different types of institutions.

IX. Reporting Template Titles and Example Fields Specified Under New Regulations

EVE/NII SOT and MV changes

- Worst case EVE/NII figures
- EVE/NII figures across each shock scenario
- Market Value Changes under Baseline, and parallel shock scenarios

Sensitivity Estimates

- Carrying Amount
- Duration
- Bank Estimates of IRRBB Sensitivities

Repricing Cashflows

- For Fixed and Floating Rate instruments:
- Notional Amounts
- Weighted average yield and maturities
- Optionality Types
- Repricing Schedules

Relevant Parameters

- Notional Amounts
- Optionality Types
- Baseline and Shocked Scenario Parameters

Quantitative Information

- Methodology
- Scope & Materiality
- Additional Quantitative Information

*The above components are indictive and not exhaustive in nature

Key Takeaways

New requirements will impact IRRBB processes starting May 2024

Standardised approaches to NII and EVE stress testing have been defined

Updated reporting requirements accompany each new process

How KPMG Can Help?

Regulatory Gap Assessment & Impact Assessment

Benchmarking & Industry Insights, Regulatory Updates

IRRBB & CSRBB Model development, review & validation

IRRBB & CSRBB Calculation Review & Assurance

IRRBB & CSRBB Regulatory Reporting Assistance

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