M E M O R A N D U M

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More efficient handling of applications to use the IRB approach for credit risk

Summary

It is Finansinspektionen's (FI) goal to conclude all applications for permission to use the IRB approach for credit risk within six months of the date the application was submitted. [1] The goal has currently been for FI to have sent its first assessment within six months. In addition to the higher demands this change will place on FI's handling procedures, it also means that firms submitting an application must show that the models meet the requirements of the Capital Requirements Regulation in all material respects already at the time the application is submitted. In other words, it will no longer be possible for firms to repeatedly rectify deficiencies identified by FI during the application process, which is the procedure today.

Background

Many of the largest Swedish banks use the IRB approach to calculate their capital requirement for credit risk. Every year, FI handles several relatively extensive applications from firms to start using the IRB approach or expand or alter their existing methodology.

The Capital Requirements Regulation takes the position in general that applications to use the IRB approach normally should be concluded by the supervisory authority within six months. Furthermore, the Administration Act states that all matters handled by government authorities should be handled as simply, quickly and cost-efficiently as possible without comprising the legality of the decision. A general expectation of a six-month limit is also expressed in the new Administration Act, which will go into effect on 1 July 2018.

During the more than ten years that FI has handled applications for the IRB approach, however, a procedure has been established that entails significantly longer handling periods for these types of applications, often stretching beyond the one-year mark. One of the primary reasons for the long handling periods is

[1] The six-month deadline goes into effect from the day the application is complete and the application fee has been paid.

that FI allows firms to rectify the deficiencies in their models until the models eventually meet the requirements of the Capital Requirements Regulation. These supplements are often extensive in both number and scope. This procedure is inefficient for both FI and the firms, and it does not meet the legislator's expectation of a fast, simple and cost-efficient handling process.

In order to achieve a more efficient and predictable handling process, FI will therefore place higher requirements on the firms in that they must meet the requirements of the Capital Requirements Regulation in all material respects at the time the application is submitted. In the event the approach to which the application refers contains minor deficiencies that are judged to be able to be rectified within the six-month deadline, firms will be given an opportunity to adjust their applications. Deficiencies in the approach that are of such an extent that major changes are needed will result in a rejection of the application. During the handling process, FI will apply technical standards[2] and guidelines[3] from EBA, which can also serve as guidance for firms when preparing their application.

This change does not alter the conditions for permission, but rather only alters FI's handling procedures. The new handling procedures will be applied to all applications for permission to use the IRB approach received by FI after 1 January 2018.

FINANSINSPEKTIONEN

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[2] The technical standards from EBA have not yet entered into force, but they have been sent to the European Commission for approval. FI will continue to use EBA's proposals as a guideline since they are an expression of a joint view within the European supervision collective on how the firms' approaches should be assessed.
https://www.eba.europa.eu/documents/10180/1525916/Final+Draft+RTS+on+Assessment+Methodology+for+IRB.pdf/e8373cbc-cc4b-4dd9-83b5-93c9657a39f0

http://www.eba.europa.eu/documents/10180/1597002/Final+draft+RTS+on+the+materiality+threshold+for+credit+obligations+%28EBA-RTS-2016-06%29.pdf

[3] Guidelines on the application of the definition of default under Article 178 of Regulation (EU) No 575/2013 (EBA/GL/2016/07)

Guidelines on PD estimation, LGD estimation and the treatment of defaulted exposures EBA/GL/2017/16