

Press release

22 June 2023

ECB consults on revised Guide to internal models

- ECB invites comments from banks and other stakeholders involved in internal models
- Revision accounts for climate-related risks, clarifies requirements for common definitions of default, counterparty credit risk, default risk in the trading book and ways to return to standardised approach
- Revision further clarifies ECB's understanding of rules on banks' internal models
- Consultation period ends on 15 September 2023

The European Central Bank (ECB) today launches a public consultation on its revised Guide to internal models. The revision reflects updates on the legal framework and builds on the ECB's experience gained over the years in supervising internal models.

In the revised version under consultation, the Guide clarifies how banks should go about including material climate-related and environmental risks in their models. It also provides clarifications for banks that wish to revert to the standardised approach for calculating their risk-weighted assets. Specifically on credit risk, the guide helps all banks to move towards a common definition of default and a consistent treatment of massive disposals. The update of the market risk chapter details how to measure default risk in trading book positions. The Guide also provides clarifications regarding counterparty credit risk, which is the risk that the counterparty to a transaction could default. More details are available in the FAQs.

The Guide explains how the ECB understands the rules applicable to banks when they use internal models to calculate how much capital they need.

With the ECB's permission, banks can use their own [internal models](#) to determine their risk-weighted assets. Risk-weighted assets are a measure of the risks that a bank has on its books and serve as the basis for calculating how much [capital](#) it needs. Supervisors check that banks are complying with the relevant EU banking rules governing the use of internal models.

European Central Bank

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The consultation on this update to the Guide to internal models starts today and ends on 15 September 2023. The ECB will publish the comments received together with a feedback statement and the updated Guide.

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Notes

- A bank's use of internal models to calculate risk-weighted assets is first subject to initial approval by ECB Banking Supervision. Banks' internal models are then subject to internal model investigations and to ongoing model monitoring by ECB Banking Supervision. This is how supervisors check whether the bank continues to meet the requirements for using internal models.
- As of the end of 2022, about 60% of risk-weighted exposure amounts for the credit risk of banks directly supervised by the ECB (significant banks) were calculated using internal models and about 40% using standardised formulas. Altogether, credit risk accounted for about 85% of significant banks' total risk-weighted exposure amounts, which amounted to €8.6 trillion.
- The ECB originally developed the Guide to internal models as part of its targeted review of internal models (TRIM), a one-off, large-scale project to address inconsistencies resulting from the use of complex internal models and to reduce unwarranted (i.e. non-risk-based) variability of outputs.

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