



WHITE PAPER

EBA ISSUES FINAL GUIDELINES FOR IRRBB AND CSRBB

December 2022

INTRODUCTION

In October 2022, the European Banking Authority (EBA) published the new final guidelines focusing on overhauling the rulebook for the management of Interest Rate Risk in the Banking Book (IRRBB). In addition to the amendments relating to Interest Rate Risk, the EBA have confirmed and further clarified its increased focus on Credit Spread Risk in the Banking Book (CSRBB) and Fair Valuation impacts. While the changes relating to **IRRBB are becoming effective from June 30th 2023**, the regulator leaves some breathing space for banks with implementation of **CSRBB becoming binding from December 31st 2023**.

The regulatory guidelines consist of three papers structured as follows:

- **Final guidelines for IRRBB and CSRBB** (EBA/GL/2022/14) internal stress testing representing an integral part of ICAAP
- Standards specifying **the supervisory outlier tests (SOTs)** for EVE and newly introduced standards for NII SOTs
- **New standardized methodologies both for EVE and NII**, which can be requested by competent authorities if internal systems are deemed to be “insufficient”

The new regulatory package is relevant for EU banks, while the PRA may follow suit, and therefore will be of interest to U.K. domestic banks.

Amended guidelines for IRRBB and CSRBB

One specific focus of the new guidelines is the identification and **assessment of Credit Spread Risk in the Banking Book (CSRBB) impacting NII and EVE** of a financial institution.

The guidelines specify that any instruments sensitive to CSRBB, irrespective of their accounting treatment, are in scope. Additionally, the EBA emphasizes that as a minimum requirement, institutions should include **all positions measured at Fair Value into the CSRBB** assessment and should not exclude any off-balance sheet positions bearing credit spread risk in the non-trading book. To avoid misinterpretation, the EBA does not specifically limit CSRBB to corporate/governments bonds and other securities usually measured at Fair Value through OCI but rather encompasses all on and off balance sheet positions which may give rise to an EVE and NII impact. Any exclusions from the scope of CSRBB must be documented accordingly. Institutions may include **idiosyncratic credit spread** components (own credit, geography, industry, etc.) to the extent they lead to more conservative results.

Furthermore, in the **new NII definition** the EBA **introduces financial instruments carried at fair value** in addition to the existing interest expense and interest income only components.

Hence, the new NII definition de facto moves closer to a more comprehensive earnings view, which the regulator expects to embed into the limit setting framework.

Besides, the EBA clarified that **the full amount of non-financial deposits will be part of the five-year non-maturing deposits cap scope**. This means that in future the modelling of the non-core deposit part will be allowed, while previously the non-core part was deemed to be overnight.

“Reflections will be valid for IRRBB models... How they capture the changes in the current interest rate environment, the way banks will adapt the models and underlying assumptions, the way they will adapt the hedging strategies, will be very important for us to understand.”

Delphine Reymondon, Head of Liquidity, Leverage and Capital Unit, EBA
Risk.net, October 2022

Supervisory Outlier Tests (SOTs)

The six BCBS scenarios for the supervisory SOT continue to be valid for the EVE calculation. However, the new standards additionally **introduce a prescribed SOT for NII, based on the two supervisory parallel up and down shocks (+/-200bps)**. The one-year horizon as well as the constant balance sheet assumption for the NII projection remain in place.

Furthermore, the EBA decided to remain with the **“narrow” NII definition for the SOT** calculations and dropped the initially suggested inclusion of Fair Valuation impacts in order to preserve comparability across banks.

Finally, the **floor** in the new standards is moved from -100 basis points to **-150 basis points** for the shortest maturity, linearly raised to 0% at 50 years.

New standardized models for IRRBB

Competent authorities are entitled to require banks to apply a standardized methodology, provided their internal models are not sufficiently capturing the interest rate risk in the banking book. Hence, the EBA has developed a **standardized (SA) and simplified standardized approach (s-SA) for EVE and NII** based on slotting of cash flows.

Fair Valuation impacts (through PnL or OCI) are confirmed to be in scope when assessing NII using the standardized models.

The standardized approaches, however, are expected to remain a transitory fallback option or a means of “validation” of results rather than business-as-usual, long-term solutions.

FIS preliminary assessment

Overall, the new guidelines provide valuable clarification and additions to IRRBB and CSRBB. They address some of the regulatory uncertainties which crystalized over the past years in practice.

While the determination of the credit spread risk component for debt instruments is not an area of concern, the isolation of the idiosyncratic risk might prove more challenging in certain instances.

When assessing IRRBB/CSRBB for internal management, the incorporation of fair value effects for credit and interest rate sensitive instruments will require banks to re-assess balance sheet positions which might have been previously out of scope. Potential examples include:

CSRBB for EVE and NII metrics:

- Debt instruments at amortized cost (AC)
- Debt instruments at FVPL/FVOCI
- Off Balance Sheet items

IRRBB for NII metric:

- Banking book positions held at amortized cost, which are economically hedged with swaps (FVPL) and mitigated by hedge accounting

Depending on the structure, complexity and applicable accounting standard of a given bank, the inclusion of interest-rate sensitive fair value impacts into the NII definition might result in overlapping effects with the EVE calculation.

Credit risk and NII fair value impacts in the banking books will continue to be a focus area of the ECB and EBA over the coming years, which already form part of the EBA stress-testing exercises for EU banks. Regulatory requirements, stress testing and internal risk management continue to move toward alignment.

In order to accommodate for the low/negative interest rate environment, banks have adjusted their balance sheets, for example, by deploying excess liquidity and acquiring medium to long-term debt instruments to optimize NII by generating steady interest income. After a prolonged period of persistently low rates, **inflation** has become an area of major concern and **central banks have taken a hawkish stance by increasing reference rates aggressively and at a historical pace**. Hence, we recommend banks to expand the sophistication of their own internal shock scenarios given the current economic outlook and potential shortcomings in the 6 mandatory supervisory shock scenarios (SOT) scenarios as they may prove to be too conservative. It is now key to assess the balance sheet and define strategic steps in order to optimize earnings and financial resources (incl. capital buffers).

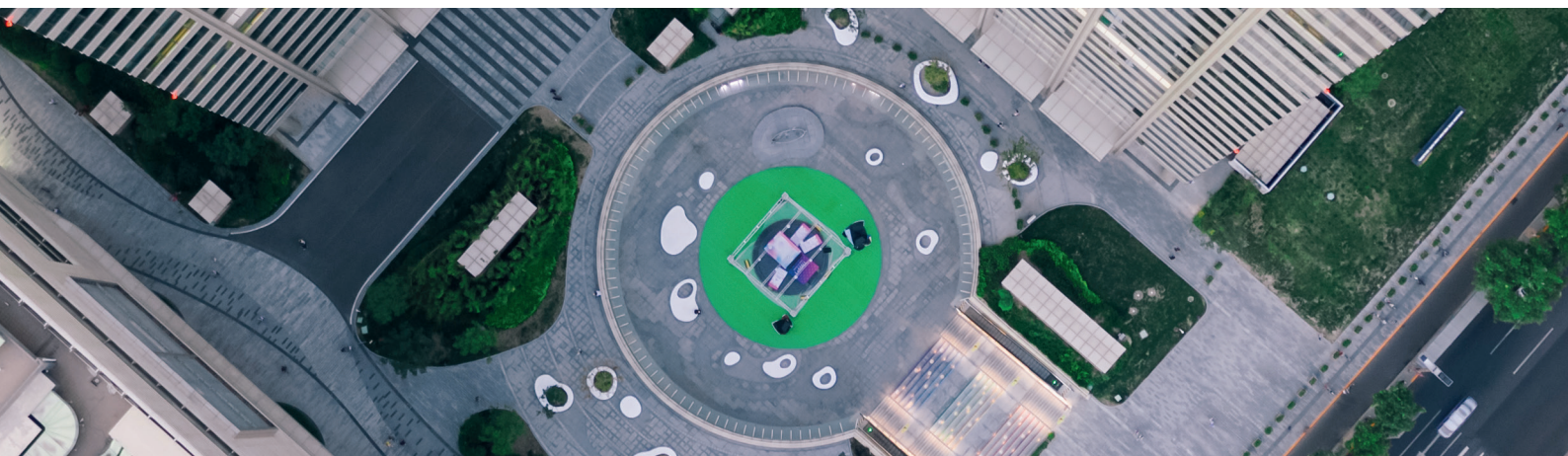
The solution

As a trusted partner of 600+ financial institutions, the FIS® Balance Sheet Manager (formerly Ambit Focus) is already actively used by Treasury, Finance and Risk departments around the globe.

The IRRBB/CSRBB assessment under the new definition and scope requires banks to have resilient, flexible and reliable assessment capabilities in place to evaluate the potential stress impact in different scenarios.

Balance Sheet Manager provides a robust platform which fulfils current IRRBB regulation. Additionally, the platform is also **capable of addressing the specifics of the new IRRBB/CSRBB requirements** in particular:

- Full revaluation stress testing of interest rate, credit and FX sensitive instruments
- Comprehensive NII modelling, including out-of-the-box as well as customizable like-for-like balance sheet modelling, flexible behavioural modelling (e.g., prepayments and replication) and re-hedging simulations
- Flexible scenario definition and capability of handling multiple what-if scenarios
- Modelling of accounting mismatch and hedge accounting results



Besides the IRRBB and simulation coverage, Balance Sheet Manager provides an **integrated modular platform for Treasury, Risk and Finance** for the following subject matters:

- ALM (incl. Stochastic simulations)
- Hedge accounting
- Liquidity risk (incl. NSFR, LCR, ALMM)
- Market risk (incl. EBA Stress Testing)
- IFRS 9 impairment
- Funds Transfer Pricing (FTP)
- Capital management

Our team is experienced in configuring the platform to comply with regulatory standards and meet internal needs. The platform can be easily customized and modified to accommodate for internal management, risk appetite exercises, financial planning and budgeting, reverse stress tests as well as recovery and resolution planning (RRP).

[Find out more about FIS Balance Sheet Manager.](#)

[Guidelines on IRRBB and CSRRB | European Banking Authority \(europa.eu\)](#)

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