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## CHANGES TO THE IRB APPROACH

### PART I

## CHANGES TO THE RANGE OF APPLICATION OF RATING SYSTEMS OR INTERNAL MODELS APPROACHES TO EQUITY EXPOSURES

### SECTION 1

#### Changes requiring competent authorities' approval ('material')

1. Extending the range of application of a rating system to:
  - (a) exposures in an additional business unit, that are of the same type of product or obligor;
  - (b) exposures of an additional type of product or obligor unless the additional type of product or obligor falls within the range of application of an approved rating system based on the criteria as referred to in points (c)(i) and (ii);
  - (c) additional exposures related to the lending decision of a third party to the group, unless the institution can prove that the additional exposures fall within the range of application of an approved rating system, based on all of the following criteria:
    - (i) the 'representativeness' of the data used to build the model to assign exposures to grades or pools with respect to the key characteristics of the institution's additional exposures where the lending decision has been taken by a third party, according to Article 174(c) of Regulation (EU) No 575/2013;
    - (ii) the 'comparability' of the population of exposures represented in the data used for estimation, the lending standards used when the data was generated and other relevant characteristics with the ones of the additional exposures where the lending decision has been taken by a third party, according to Article 179(1)(d) of Regulation (EU) No 575/2013.

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

2. Extending the range of application of an internal models approach to equity exposures, to one of the following type of exposures:
  - (a) to the Simple risk weight method according to Article 155(2) of Regulation (EU) No 575/2013;
  - (b) to the PD/LGD approach according to Article 155(3) of Regulation (EU) No 575/2013;
  - (c) to the temporary partial use provision according to Article 495 of Regulation (EU) No 575/2013;
  - (d) to the same type of product in an additional business unit;

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- (e) ~~amendments to an additional type of product under the institution's approval that it falls within the range of application of an existing internal models approach to equity exposures.~~

## SECTION 2

### Changes requiring prior notification to competent authorities

1. Reducing the range of application or the scope of use of a rating system.
2. Reducing the range of application of an internal models approach to equity exposures.
3. Extending the range of application of a rating system for which it can be shown that it does not fall under Part I, Section 1, point 1 of this Annex.
4. Extending the range of application of an internal models approach to equity exposures where such extension does not fall under Part I, Section 1, point 2 of this Annex.

## PART II

### CHANGES TO RATING SYSTEMS OR AN INTERNAL MODELS APPROACH TO EQUITY EXPOSURES

## SECTION 1

### Changes requiring competent authorities' approval ('material')

1. Changes in the methodology of assigning exposures to exposure classes and rating systems. These include:
  - (a) changes in the methodology used for assigning exposures to different exposure classes according to Article 147 of Regulation (EU) No 575/2013;
  - (b) 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.
2. The following changes in the algorithms and procedures used for: assigning obligors to obligor grades or pools; for assigning exposures to facility grades or pools; or for quantifying the risk of obligor default or associated loss ('changes in the rating methodology for IRB systems'):
  - (a) changes of the modelling approach for assigning an obligor to grades or pools and/or exposures to facility grades or pools according to Article 171(1) and Article 172(1) (a) to (d) of Regulation (EU) No 575/2013;
  - (b) changes to the institution's approach to the 'one-obligor-one-rating principle' according to Article 172(1)(e) of Regulation (EU) No 575/2013;
  - (c) changes in the rating system's assumptions behind ratings relating to the extent by which a change in economic conditions is expected to result in a net migration of a large number of exposures, obligors or facilities across grades or pools of the model, as opposed to migration of only some exposures, obligors or facilities due only to their individual characteristics the measure and significance levels of which are defined by the institution;

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- (d) changes to the rating criteria as referred to in Article 170(1)(c) and (3)(c) and Article 170(4) 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.
  - (e) introduction or withdrawal of an external rating as a primary factor determining an internal rating assignment according to Article 171(2) of Regulation (EU) No 575/2013;
  - (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 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;
  - (g) inclusion of additional types of collateral into the LGD estimation according to Article 181(1)(c) to (g) of Regulation (EU) No 575/2013 if their treatment differs from procedures that have already been approved.
3. Changes in the definition of default according to Article 178 of Regulation (EU) No 575/2013.
  4. Changes in the validation methodology and/or validation processes which lead to 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.
  5. Changes in the internal models approach to equity exposures. These include:
    - (a) changes in the value-at-risk modelling approach to estimate risk weighted exposure amounts for equity exposures according to Article 155(4) of Regulation (EU) No 575/2013;
    - (b) changes in the methodology for adjusting estimates of potential loss to achieve appropriate levels of realism and/or conservatism, or changes in the analytical method to convert shorter horizon period data to quarterly data according to Article 186(a) of Regulation (EU) No 575/2013;
    - (c) changes in the model capture of material risk drivers considering the specific risk profile and complexity, including non-linearity's of the institution's equity portfolio according to Article 186(b) and (c) of Regulation (EU) No 575/2013;
    - (d) changes in the fundamental methodology for mapping of individual positions to proxies, market indices or risk factors according to Article 186(d) of Regulation (EU) No 575/2013.

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### Changes requiring *ex ante* notification to competent authorities

1. Changes in the treatment of purchased receivables according to Article 153(6) and (7) and Article 154(5) of Regulation (EU) No 575/2013.
2. The following changes in the rating methodology for IRB systems:
  - (a) changes in the internal procedures and criteria for assigning risk weights to specialised lending exposures according to Articles 153(5) and 170(2) of Regulation (EU) No 575/2013;
  - (b) changes from the use of direct estimates of risk parameters for individual obligors or exposures to the use of a discrete rating scale or vice versa according to Article 169(3) of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Section 1 of this Annex;
  - (c) changes to the rating scale in terms of the number or structure of rating grades according to Article 170(1) of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Section 2 of this Annex;
  - (d) changes to the rating criteria and/or their weights or hierarchy according to Article 170(1)(c) and (e) and 170(4) of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Section 1 of this Annex;
  - (e) changes to the grade or pool definitions or criteria according to Articles 171(1) and 172 of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Section 1 of this Annex;
  - (f) changes in the scope of information used to assign obligors to grades or pools according to Article 171(2) of Regulation (EU) No 575/2013 or inclusion of new or additional information in a model for parameter estimation according to Article 179(1)(d) of Regulation (EU) No 575/2013;
  - (g) changes in the rules and processes for the use of overrides according to Article 172(3) of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Section 1 of this Annex;
  - (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 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;
  - (i) changes in the way or extent to which conditional guarantees are accounted for in the LGD estimation according to Article 183(1)(c) of Regulation (EU) No 575/2013;
  - (j) inclusion of additional types of collateral into the LGD estimation in accordance to Article 181(1)(c) to (g) of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Title I of this Annex;

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- (k) an institution maps its internal grades to the scale used by an ECA and then attributes the default rate observed for the external organisation's grades to the institutions' grades according to Article 180(1)(f) of Regulation (EU) No 575/2013, changes in the mapping used for this purpose unless already classified as material according to Part II, Section 1 of this Annex.
3. Changes in the validation methodology and/or process according to Articles 185 and 188 of Regulation (EU) No 575/2013, unless already classified as material according to Part II, Section 1 of this Annex.
  4. Changes in processes. These include:
    - (a) changes in the credit risk control unit according to Article 190 of Regulation (EU) No 575/2013 as regards its position within the organisation and its responsibilities;
    - (b) changes in the validation unit's position according to Articles 190(1) and (2) of Regulation (EU) No 575/2013 within the organisation and its responsibilities;
    - (c) changes in the internal organisational or control environment or key processes that have an important influence on a rating system.
  5. Changes in the data. These include:
    - (a) if an institution starts or ceases to use data that is pooled across institutions according to Article 179(2) of Regulation (EU) No 575/2013;
    - (b) change of the data sources used in the process of allocating exposures to grades or pools or for parameter estimation according to Articles 176(5)(a) and 175(4)(a) of Regulation (EU) No 575/2013;
    - (c) change in the length and composition of time series used for parameter estimation according to Article 179(1)(a) that goes beyond the annual inclusion of the latest observations, unless already classified as material according to Part II, Section 1 of this Annex.
  6. Changes in the use of models, if an institution starts using risk parameter estimates for internal business purposes that are not those used for regulatory purpose and, where this was previously not the case, within the lines set out according to Article 179(1) of Regulation (EU) No 575/2013.
  7. Changes in the internal models approach to equity exposures. These include:
    - (a) changes of the data used to represent return distributions for equity exposures under the internal models approach according to Article 186(a) of Regulation (EU) No 575/2013;
    - (b) changes in the internal organisational or control environment or key processes that have an important influence on the internal models approach to equity exposures.

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**Changes and effects yet to be applied to :**

- Regulation power to amend conferred by [S.I. 2018/1115 Sch. Pt. 4 para. 148](#)
- Regulation power to modify conferred by [2023 c. 29 s. 3 Sch. 1 Pt. 13](#)
- Regulation revoked by [2023 c. 29 Sch. 1 Pt. 13](#)