



Template for comments

Public consultation on the ECB guide to internal models - General topics chapter

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General comments

A public consultation is most welcome about any ECB guide to internal models, whereby consistency among supervisory teams should be ensured towards all those supervised banks

Likewise, most appreciated is the ECB's decision to seek public comments on the general topics chapter since it sets out in which way the ECB will approach those non-model-specific topics, in particular for IRB

:As general remarks, UniCredit believes as follows

Though some room for improvement does still exist, it is most appreciated the improvement of the Supervisory Expectations' current -
;version as compared with the previous release

The ECB's intended purpose underpinning such a consultation will be met as long as the final document resulting from this consultation -
;process is published within a reasonable period of time

When reference is made to key concepts (e.g. monitoring of compliance), a more precise definition of the concept itself should be -
provided in order to better perimeter whatever required action is asked to the bank and so to avoid unintended and undue burdensome
.activities

.More detailed views on the General topics chapter are set out in dedicate spreadsheet

ID	Section	Paragraph	Page	Type of comment	Detailed comment	Concise statement as to why your comment should be incorporated
1	Overarching principles for internal models	Guidelines at consolidated and subsidiary levels	5	Clarification	We would like to ask for a clarification regarding the sentence "The group-level policies should clearly define under which circumstances deviations from the group-wide principles would be accepted". In particular, we would like to understand whether the expectation is that of having a detailed and formalized list of circumstances supposed to be known in advance where a deviation from Group standards is admitted. Because in some cases this might be possible but needs for deviation can come up afterwards in case situation changes (thus a bottom up from the subsidiaries might be beneficial also in order to ensure a source of potential enhancement of the standards within their ordinary maintenance process, and this would be in line with the following sentence reported in the same paragraph "The parent entity should be informed about such deviations" which entails somehow a bottom up informative flow from subsidiaries). Rather than a closed list of deviation we would suggest to require to define a process to manage them.	The clarification would be beneficial in order to address properly the Supervisory Expectations
2	Overarching principles for internal models	Implementation of a model risk management framework	6	Clarification	We would like to ask for clarification regarding footnote 10. The assessment of capital adequacy entails an evaluation on Pillar 2 side, although there are areas of interconnections with Pillar 1 measure (as the Margin of Conservatism that effectively is also a Model Risk Management measure). Might it be possible to have better clarification and guidance if the measure of capital adequacy related to model risk should be exclusively related to Pillar 2 or they might be also on Pillar 1?	The clarification would be beneficial to foster a proper harmonisation across the industry on a very sensitive topic, also in consideration that some Model Risk Management measures are already covered (and in overlap) with Pillar metrics (i.e. margin of conservatism for model inefficiency).
3	Roll-out and permanent partial use	Governance of the roll-out plan for the IRB Approach	13	Deletion	Item d) of section 38 should be erased because the topic is already mentioned somewhere	This point should be moved in the sections/paragraphs related to the Internal validation (Chapter 5) and Internal Audit functions (Chapter 6), as those are the functions who should assess the compliance with the roll-out plan
4	Roll-out and permanent partial use	Monitoring of compliance with permanent partial use provisions	14	Amendment	In UniCredit Group's view the scope of the monitoring should be better defined. For instance, if a portfolio is tagged as "to be discontinued", the monitoring shall be performed only by assessing whether such strategy has not changed over time (independently of the materiality); or if the request of the materiality in terms of EAD at consolidated level only indicator will be subject to monitoring (and not the RWA or the number of counterparties), and so on.	In our view in order to avoid excessively burdensome activities, the monitoring should be ensured only with the aim to assess on a continuous basis the compliance with reference to the criteria for which the PPU was requested in the first place.
5	Internal validation	Validation level	22	Clarification	We would like to ask for clarification on the type of rating systems and situations intended to fall under item 66. b); in our understanding, the point is about models for non-wholesale customer rolled-out on more than one legal entity.	If not properly described, the requirement would end up being too broad in its interpretation to bring about also unintended consequences
6	Internal validation	Validation level	22	Amendment	Point b) of article 66 should be modified as follows: "If the institution has approval for a rating system on a consolidated basis as well as on a sub-consolidated and/or individual basis, the validation of that rating system should be performed at the consolidated level and, in case a robust and representative sample is available, sub-consolidated and/or individual levels. However, the results of the validation at the sub-consolidated and/or individual levels should be taken into account only complementing the result at consolidated level, where appropriate."	Additional analysis on a single institution level might rely on very small sample for some legal entities. Therefore we deem important that any detailed analysis has to be requested only in case of a robust sample is available. The article is not completely clear when stating "...should be taken into account for consistency reasons in the validation performed at consolidated level". We believe that it should be reworded in order to clarify that any analysis performed at individual level cannot be weighted as much as the one at consolidated level instead the former should be instrumental to the latter.
7	Internal validation	Content and frequency of tasks of the validation function	26	Clarification	When it is written at the last bullet of item vii: "For the annual validation of rating systems, the validation function shall also perform analyses of the representativeness performed by the CRCU" it is not clear to what extent validation function can rely on the analysis performed by CRCU.	As long as clear tasks are identified, execution of those instructions would end up being misaligned with the supervisor's expectation
8	Internal validation	Content and frequency of tasks of the validation function	26	Clarification	It is not clear which kind of checks have to be carried out by internal validation in order to assess the "use of the models and their correct application in practice": does this refer to processes and policies documentation checks or single case checks?	As long as clear tasks are identified, execution of those instructions would end up being misaligned with the supervisor's expectation
9	Model use	Risk management, credit approval and decision-making process	36	Amendment	We deem the wording of the requirement in par. 89-d-ii) as too strict and not fully in line with the premise in par. 89 regarding the internal use where the internal credit risk parameters should be "taken into accounts". Indeed the LGD models to be adopted for ELBE quantification are typically developed based on a risk drivers selection process in order to define the most relevant ones for risk differentiation purposes, with the aim to be accurate on grades or pools of homogeneous exposures in terms of risk. Thus, in a context of an individual LLP assessment it is somehow expected that the peculiarities of the single credit file might not be fully caught by the model (that's why, and this is the typical practice on large tickets, an individual assessment is performed and it is also the reason why, within EBA GL on PD and LGD, par. 187, the specific credit risk adjustment can be adopted for an override of the ELBE - "187. Where specific credit risk adjustments are assessed individually for a single exposure or a single obligor, institutions may override the ELBE estimates based on specific credit risk adjustments, where they are able to prove that this would improve the accuracy of the ELBE estimates and that the specific credit risk adjustments reflect or are adjusted to the requirements set in section 6.3.1 on the calculation of economic loss."). However, we deem that the use test requirement with regard to specific provisioning can be ensured by making available the ELBE estimates as a further element to the Analyst for the individual LLP quantification (which would also allow to structure an override process based on the individual credit risk adjustment calculation). Therefore, we suggest the following wording amendments "(i) With regard to specific provisioning, the information on the internal IRB parameters (ELBE) should be an important information available for the expert judgement outcomes definition, and the entire individual LLP quantification should be properly documented."	Higher consistency with the requirement of "taking into account" the parameters as for the wording included in par. 89 and possibility to set up a structure override process as envisaged by par. 157 of EBA GL on PD/LGD. The current proposal in the TRIM Guidelines forces the expert individual LLP calculation to be in line with ELBE (thus effectively not allowing to consider, on the other way round, individual LLP as a basis for overriding the ELBE estimates purely coming from the model)

10	Management of changes to the IRB approach	Content of the change policy	43	Deletion	<p>Even though it seems theoretically reasonable to provide further details regarding the criteria used for the classification of model changes, the Group proposes to erase the following paragraph:</p> <p>- Par. 105 (v) regarding the criteria used to assess when a change in methodology is deemed fundamental according to Annex I, Part II, Section 1, Par. 2 (f);</p>	<p>The proposal is triggered by the fact that the Group believes that a change should be classified according to an holistic assessment based on the expert judgment of the competent functions which either propose the change or have to assess its proper classification. Units responsible for managing model changes should have the necessary expert basis and, in our opinion, it will be counter-productive to bind these experts with pre-defined criteria which can eventually avoid to assess comprehensively the model change under evaluation.</p> <p>In general, for the qualitative criteria (e.g. the concept of "fundamental change"), due to the fact that it was deemed not feasible to list all the possible cases within an internal regulation (considering the number of the models for all the LEs of the Group), the Group deems more appropriate to establish a strict classification process instead. Such process shall foresee the preparation of a specific document (so called "change report") by the proposing function of the change explaining the main features of the change, the impact analysis, the implementation date and the proposal for classification; the latter has to be confirmed by an independent functions (e.g. validation function) for all the changes related to IRB models. The main aim of such evaluation process will be to ensure an homogenous evaluation of the "fundamental" change concept throughout the Group. In the end the adoption of a process meeting the "four-eyes" principle as required in par. 109 is deemed appropriate to ensure a sound classification process.</p>
11	Management of changes to the IRB approach	Re-rating process	46	Amendment	<p>As for the item 118, we would propose following rewording: "Where competent authorities have provided their permission in relation to a material extension or change, Article 3(5) of Commission Delegated Regulation (EU) No 529/2014 requires institutions to calculate the own funds requirements on the basis of this approved extension or change from the date specified in the new permission or the closest implementation date (e.g. in case of technical implications)"</p>	<p>Rewording is suggested to make Supervisory Expectations effectively applicable</p>
12	Management of changes to the IRB approach	Re-rating process	47	Amendment	<p>We would propose following rewording of point 121(b): "To mitigate the risk of own underestimation of own funds requirements, in the event that a material change would lead to a material increase in the RW exposure amount (i.e. more than 10% on the range of application of the rating system subject to change), the institution should apply the RW exposure amount impact, simulated on the basis of the representative sample, to the part of the portfolio not re-rated within 12 months from the permission to adopt the new / updated / re-calibrated model. The impact thus produced is the positive difference between the simulated RW exposure amount after the material change and the RW exposure amount before the material change approved by the competent authority, to be computed on the relevant exposures not satisfying art 121.(a). This should be done at the first Common Reporting date after the 12 month allowed re-rating period and should stay until the completion of the re-rating process". Alternatively, "For the purpose of point (b) above, the ECB would consider the following approach as the most appropriate:</p> <ul style="list-style-type: none"> • apply the simulated RW exposure amount impact until all exposures within the range of application are rated using the changed model; • remove the simulated RW exposure amount impact linearly, i.e. 25% every quarter. <p>Unless the institution is able to update the impact to properly consider the underlying exposure evolution and re-rating carried out."</p>	<p>Models on which a massive re-rating is not applied are typically models with an important non automatic component and a non proportionally distributed re-rating process, furthermore the underlying exposures could vary over time. Thus, a massive simulation could lead to an outcome not fully reflecting the effect of actual re-rating process. For this reason we suggest to stick to the implementation timeline unless it exceeds the maximum timespan allowed (12 months)</p>