

Just in Time

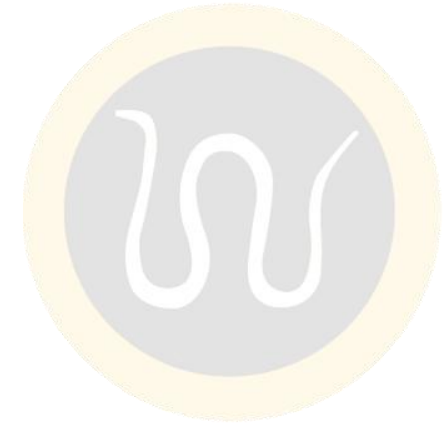
Revised Supervisory Guidance on Model Risk Management

June 2026

Executive Summary

The guidance ⁽¹⁾ provides **an updated supervisory framework for model risk management (MRM)** applicable primarily to banking organizations with over \$30 billion in assets. It replaces earlier guidance (SR 11-7 and SR 21-8) and reflects advancements in modeling practices and supervisory experience.

The revised guidance reflects the growing **complexity, scope and strategic importance of models** in the banking sector. Financial institutions increasingly rely on quantitative models to enhance decision-making, risk management, operational efficiency and profitability. This trend is driven by technological advancements, competitive pressures and the expansion of data-driven methodologies.



⁽¹⁾ [Federal Reserve, FDIC, OCC “Supervisory Guidance on Model Risk Management” \(SR 26-2\), April 2026.](#)

At a Glance

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Keywords: Model Risk Management, Model Lifecycle, Third-Party Risk



01

Introduction

Overview



Introduction

Overview

The guidance underscores that **model usage inherently introduces risk** (“**model risk**”), which may manifest in:



Financial losses



Misstatements in financial reporting



Poor or flawed strategic and risk decisions



Model risk arises from **limitations in model design, assumptions, data or misuse**, and therefore requires **active and structured management**.



A key principle introduced is that **model risk is context-dependent**. Its relevance and magnitude depend on:

- The **nature and scale of model usage**
- The **business context in which models operate**
- The **specific risk profile of the institution**



It emphasizes that:

- There is **no one-size-fits-all framework**
- Model risk management practices must be **tailored to each institution**



The guidance is explicitly **principles-based rather than prescriptive**, meaning:

- It does **not impose enforceable regulatory requirements**
- Non-compliance does not automatically trigger supervisory criticism
- However, **unsafe or unsound practices arising from poor model risk management may still result in supervisory action**



Furthermore, the document highlights that:

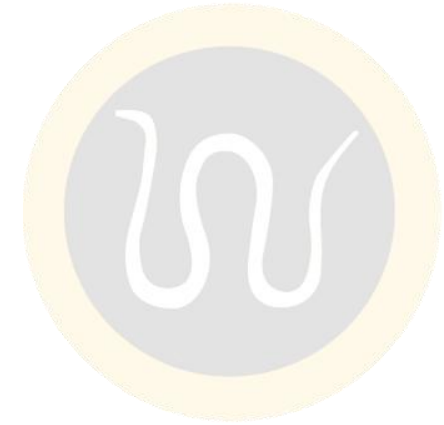
- Model risk management practices may differ significantly across institutions
- Even similar models can present **different risks depending on usage and context**

The scope of the guidance prioritizes **models supporting significant business activities**, recognizing that not all models carry equal importance.

02

Purpose and Scope

Scope of Applicability and Definition of “Model”



Purpose and Scope

Scope of Applicability and Definition of “Model”

The revised guidance aims to:

- **Clarify existing principles** established under SR 11-7
- Incorporate **supervisory experience and industry feedback** from the past 15 years
- Reflect **technological advancements in modeling techniques**



A central innovation is the introduction of a **risk-based approach**, requiring model risk management frameworks to be:

- **Proportionate to model risk**
- **Aligned with institutional size, complexity and operations**

Scope of Applicability



The guidance is primarily intended for:

- Banking organizations with **total assets exceeding \$30 billion**



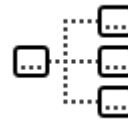
However:

- Smaller institutions may still fall within scope if they exhibit:
 - **High model complexity**
 - **Significant model dependency**
 - **Non-traditional banking activities**

Definition of “Model”

The document provides a **refined definition of a model**:

- ✓ *A complex quantitative method applying statistical, economic or financial theories to transform input data into estimates.*



- ✗ **Explicit exclusions:**
 - Simple arithmetic calculations
 - Deterministic rule-based systems
 - Non-theoretical tools



This reflects a **tailored supervisory approach**, avoiding unnecessary burden on smaller institutions while ensuring adequate oversight where risk is elevated.



Generative AI and agentic AI models are excluded from scope, although institutions are expected to apply governance principles analogously where appropriate

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Overview of Model Risk and Model Risk Management

Key Dimensions and Principles of Model Risk

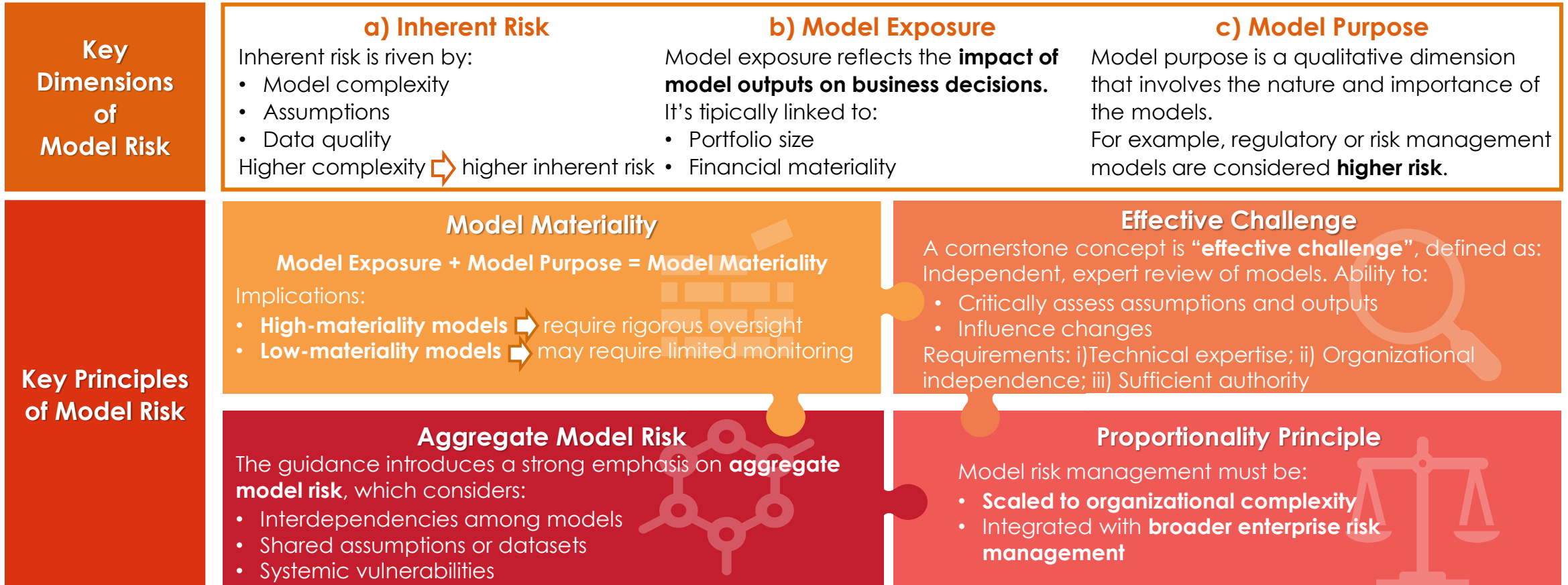


Overview of Model Risk and Model Risk Management

Key Dimensions and Principles of Model Risk

The guidance defines **model risk** as:

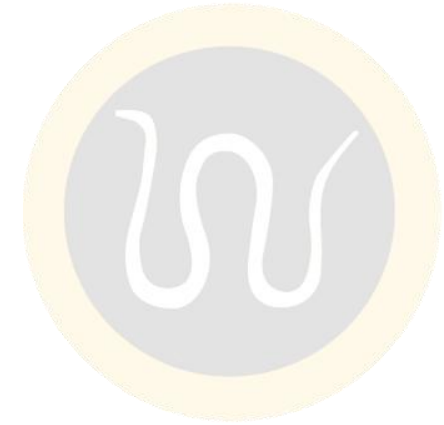
“The potential for adverse consequences arising from decisions based on model outputs.”



04

Model Development and Model Use

Core Principles for Model Development and Model Use



Model Development and Model Use

Core Principles for Model Development and Model Use

The guidance defines key principles for Model Development and Model Use:

Model Development

Model development is framed as:

- A **multidisciplinary and judgment-driven process**
- Not purely technical

Core Principles

Clear Statement of Purpose: Ensures alignment between design and intended use

Developer Judgment:

Influences: {

- Model structure
- Assumptions
- Data selection

Stakeholder Engagement: Input from business users enhances:

- Practical relevance
- Model robustness

Model Testing

Testing is a **critical component**, including:

- Out-of-sample testing
- Sensitivity analysis
- Alternative methodology comparison
- Data quality assessment

Testing rigor must be:

Proportional to model complexity and materiality

Model Use

a) Effective use

Effective use requires:

- Understanding **model limitations**
- Avoiding misuse or **application beyond intended purpose**

b) Extending model usage

When extending model usage:

- Additional analysis is required
- Controls must be reassessed

c) User feedback

User feedback is emphasized as a key mechanism for:

- Continuous improvement
- Enhanced model understanding

05

Model Validation and Monitoring

Key Objectives and Core Components

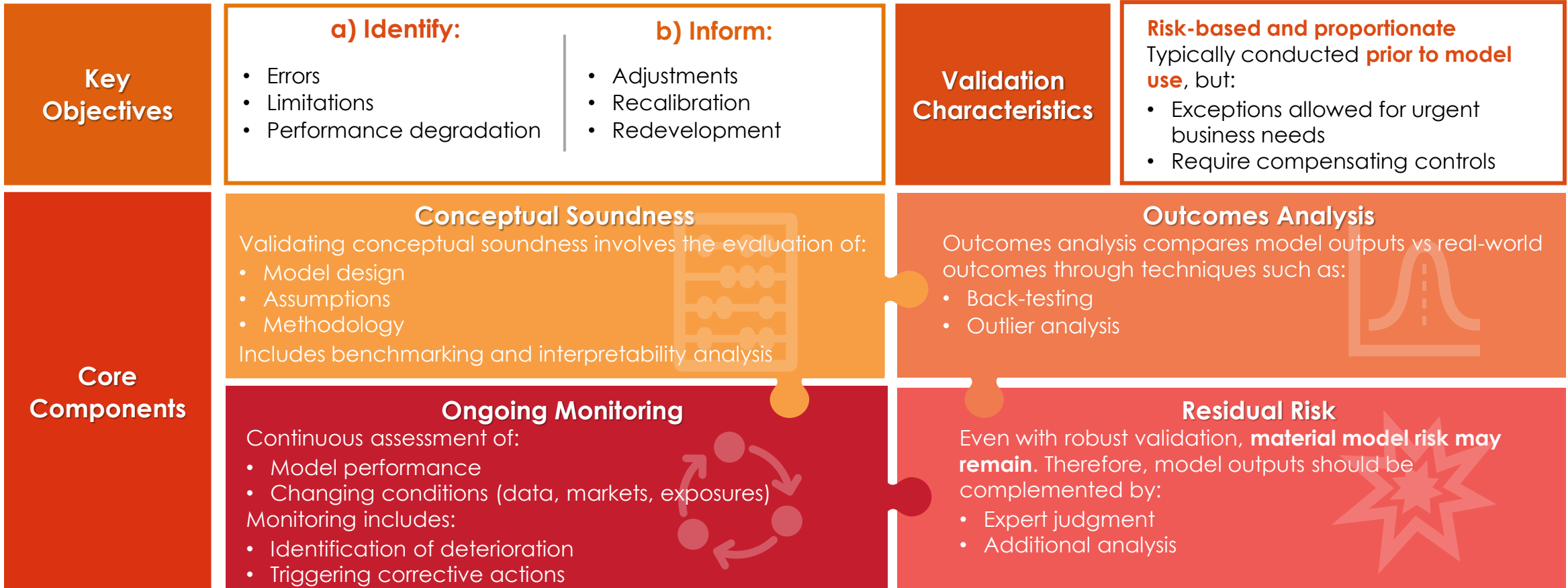


Model Validation and Monitoring

Key Objectives and Core Components

Model validation is defined as:

“A process to **assess model performance, reliability, and limitations**”.



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Governance and Controls

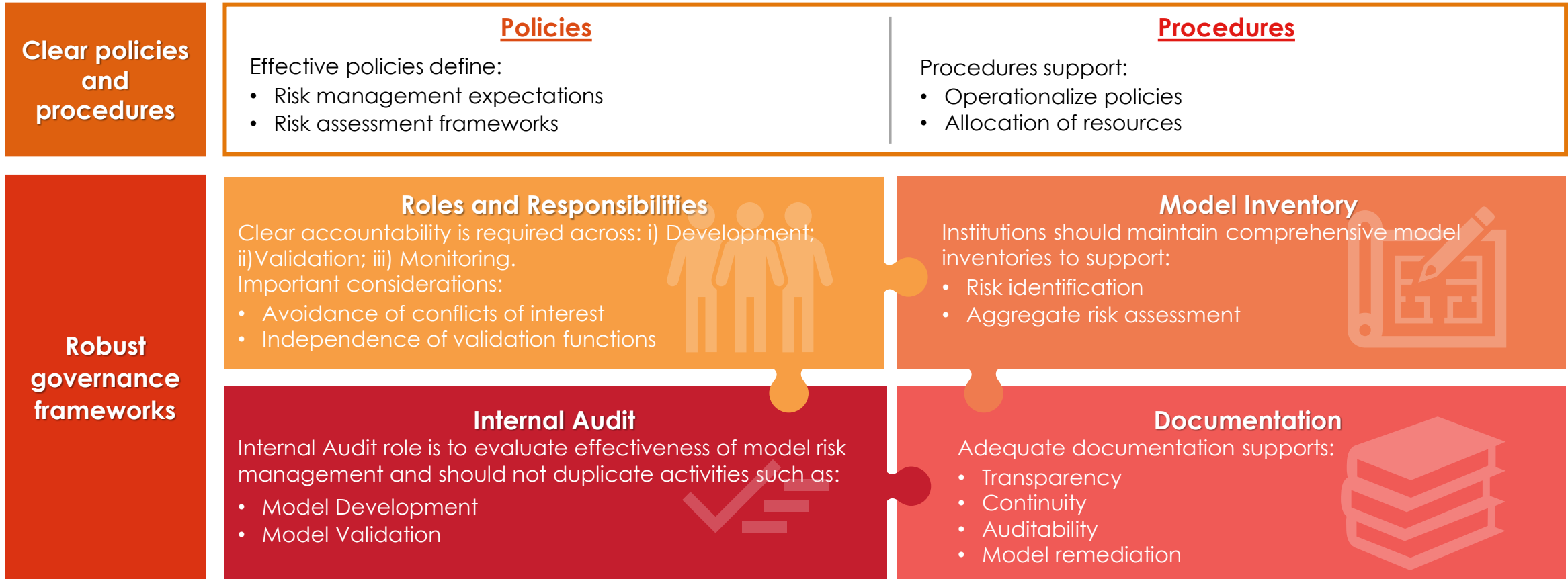
Key Elements for Governance and Controls



Governance and Controls

Key Elements for Governance and Controls

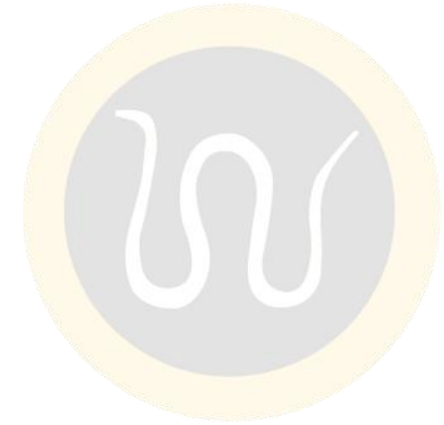
Effective model risk management requires: i) **Clear policies and procedures**; ii) **Robust governance frameworks**.



07

Vendor and Third-Party Models

Risks, Expectations and Requirements for the Use of Vendor and Third-Party Models



Vendor and Third-Party Models

Risks, Expectation and Requirements for the Use of Vendor and Third-Party Models

The use of external models introduces:

- **Additional validation challenges**
- Limited transparency due to proprietary constraints



08

Conclusions and Key Takeaways



Conclusions and Key Takeaways

a.

Strategic Principles: i) **Model risk is inherent and unavoidable**, requiring structured management; ii) **Risk-based proportionality** is the cornerstone of the revised framework; iii) **Principles-based approach** replaces prescriptive requirements.

b.

Model Risk Drivers: i) **Inherent risk, exposure and purpose** jointly determine materiality; ii) **Aggregate model risk** is critical and must be actively assessed

c.

Lifecycle Management: Model risk management must cover: i) **Development**; ii) **Use**; iii) **Validation**; iv) **Monitoring**

d.

Validation and Oversight:

- **Effective challenge** is essential and must be: i) Independent; ii) Expert-driven
- Validation must include: i) **Conceptual soundness**; ii) **Outcomes analysis**; iii) **Ongoing monitoring**

e.

Governance: Strong governance requires: i) **Clear roles and responsibilities**; ii) **Robust documentation**; iii) **Comprehensive model inventory**

f.

Third-Party Risk: Vendor models: i) Do not reduce accountability; ii) Require **equivalent validation rigor**

g.

Regulatory Positioning: The guidance: i) **Supersedes SR 11-7**; ii) Reflects **15 years of supervisory evolution**; iii) Emphasizes **flexibility and tailoring**

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