



## TOPICS:

Banking Systems

## SOURCE

European Central Bank

## ECB Publishes Revised Guide to Internal Models

- The **ECB Guide to Internal Models – July 2025** outlines the ECB's supervisory expectations regarding the use of internal models by significant institutions to calculate regulatory capital requirements for **credit, market, and counterparty credit risk**. The 2025 revision reflects recent regulatory developments, particularly the implementation of **CRR3** as of January 2025.
- Key updates include a new chapter on overarching principles for internal models, which consolidates expectations applicable to all risk types and **introduces** guidance on the use of **machine learning, data governance, and model risk management**.
- The **credit risk** section has been reorganized into three sub-chapters: general topics, definition of default, and estimation of risk parameters. Notable clarifications concern the criteria for days past due and unlikelihood to pay, as well as refinements to expectations around probability of default (PD) and loss given default (LGD), including calibration standards and data requirements aligned with CRR3.
- For **market risk**, the guide now includes separate chapters for CRR2 and CRR3 frameworks, reflecting the phased transition to Basel III's Fundamental Review of the Trading Book (FRTB). This dual structure accommodates institutions at different stages of adoption, as allowed under transitional EU measures.
- In **counterparty credit risk**, updates clarify treatment of margined exposures during the margin period of risk and incorporate changes to maturity treatment under CRR3.
- The guide also supports institutions in simplifying their Internal Ratings-Based (IRB) model landscapes, in line with CRR3 provisions that **enhance flexibility and reduce reliance on complex modelling for certain exposures**. While no formal public consultation preceded this revision, the ECB engaged with institutions through targeted roundtables in 2024.

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