

# Single Rulebook Q&A

<b>Question ID</b>	2021_5712
<b>Status</b>	Final Q&A
<b>Legal act</b>	Regulation (EU) No 575/2013 (CRR)
<b>Topic</b>	Credit risk
<b>Article</b>	152
<b>Paragraph</b>	4
<b>Subparagraph</b>	-
<b>COM Delegated or Implementing Acts/RTS/ITS/GLs/Recommendations</b>	Not applicable
<b>Article/Paragraph</b>	N/A
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<b>Disclose name of institution / entity</b>	No
<b>Type of submitter</b>	Credit institution
<b>Subject matter</b>	Look-through application under IRB approach
<b>Question</b>	When an institution applies the look-through approach to units or shares of Collective Investment Undertaking (CIU) under the IRB approach and where the institution is allowed to use IRB advanced approach for the underlying credit exposures of the CIU in accordance with Article 148 CRR, can the institution still use the standard approach for those underlying exposures of which obligors are not internally rated and/or for which the information required for own LGD estimation are not available to the institution?
<b>Background on the question</b>	Revised Article 152(4) CRR dealing with the look-through treatment of exposures in the form of units or shares of CIU under the IRB approach requires institutions to apply the standardised approach to the underlying credit exposures when the conditions for permanent partial use are met for these exposures or when the conditions of Chapter 3 CRR are not met. For a given underlying credit exposure, institutions may be authorized to use the IRB advanced approach as if they were directly held by the institution, in accordance with Chapter 3 CRR. When this exposure is effectively booked on its balance sheet, the institution should thereby be in possession of all the information and data that are used in the PD/LGD homologated models as well as the relevant information and data required for the back-testing of

these models. When looking-through CIU units or shares, the underlying obligor may not be internally rated since not part of the institution's credit portfolio. Moreover, because the turnover of the fund's assets is generally high, the details of the underlying portfolio is generally known after the reporting cut-off date and the timing for the application of the look-through at each reporting date may not be compatible with an internal rating validation process. Then, even if the institution has been able to rate the obligor or if the obligor was already rated, the data and information related to such an exposure and required to estimate and back-test own LGDs of the applicable model may not always be exhaustively available to the institution. In particular, the realised losses given default if any will be observed by the CIU and not be necessarily communicated to the institution. Moreover, it is rather likely that funds will sell the exposure before its default (for instance, following a credit deterioration) and thus observe very few defaults and realized LGD. It thus seems that it may not always be possible for institutions to meet all the conditions for using the model relevant to a given underlying exposure in accordance with the Article 181 CRR and EBA (Guidelines on PD estimation, LGD estimation and treatment of defaulted exposures, e.g. Article 107) requirements for the purpose of own LGD estimation through this model. It is noteworthy that a CRDTG Q&A (question 173) already addressed a similar questioning under the Basel II environment for the application of CRDII Article 87.11) that allowed for the look-through approach on CIU units or shares when certain criteria were met. It was stated that "under the look through approach risk weights must be calculated according to the underlying exposures. Effectively, this means treating the underlying exposures as direct exposures of the institution. If underlying exposures belong to a type of exposures for which the institution has approval to apply the IRB approach by using an internal rating system, the first part of Article 87(11) requires the application of the internal rating system for those underlying exposures. Underlying exposures that belong to the type of exposures for which the institution, as part of its approved IRB approach, is allowed to use the Standardised approach (according to Article 85 'roll out' and 89 'partial use') are risk-weighted according to the Standardised approach. However, it should be noted that in such situations, these underlying exposures must also be taken into account when assessing compliance with the 'partial use' and/or 'roll out' limits. If underlying exposures are not treated under any partial use or roll out exemption, but the institution is unable to assign an internal rating to the exposure because the conditions to use the internal rating system are not met (for example due to a lack of information on the relevant risk drivers of the underlying exposures) Article 87(11), second sub-paragraph shall apply."

**Final answer**

Article 152 of Regulation (EU) 575/2013, as amended by Regulation (EU) 2019/876 (CRR), describes how institutions applying the IRB Approach shall treat exposures in the form of units or shares in CIUs.

According to paragraph 2 of this Article, where exposures in the form of

units or shares in CIUs meet the conditions set out in Article 132(3) of Regulation (EU) 575/2013 as amended by Regulation (EU) 2019/876 (CRR) and the institution has sufficient information about individual underlying exposures of the CIU to either apply the IRB Approach or any of the approaches referred to in points (a) to (c) of Article 152(4) CRR to those underlying exposures, it shall look through to those underlying exposures in order to calculate their risk-weighted exposure amounts and, where applicable, their expected loss amounts.

If all or part of the exposures that would fall into the range of application of a rating system for which an institution is permitted to apply for the IRB Approach and the available information on the underlying exposures is sufficient to apply those rating systems to the underlying exposures an institution shall apply the methods set out in Chapter 3, Title II, Part Three of the CRR to calculate risk weighted exposure amounts and expected loss amounts. Where such information is not sufficient to apply the respective rating system and therefore not all risk parameters required for the calculation of own funds requirements in accordance with the IRB Approach can be determined for certain underlying exposures of a CIU, the risk-weighted exposure amounts for those underlying exposures shall be calculated based on the applicable approach in accordance with Article 152(4) CRR.

According to Article 152(4) CRR, risk-weighted exposure amounts and expected loss amounts shall be calculated in accordance with the treatment prescribed:

- in point (a) of Article 152(4) CRR in case of exposures assigned to the equity exposure class referred to in point (e) of Article 147(2);
- in point (b) of Article 152(4) CRR in case of exposures assigned to the items representing securitisation positions referred to in point (f) of Article 147(2) CRR;
- in point (c) of Article 152(4) CRR in case of other underlying exposures.

As such:

- for underlying exposures assigned to the equity exposure class referred to in point (e) of Article 147(2) CRR, institutions using the look-through approach cannot use the Standardised Approach and shall apply the simple risk-weight approach set out in Article 155(2) CRR.
- Likewise, for underlying exposures assigned to the items representing securitisation positions referred to in point (f) of Article 147(2), institutions using the look-through approach may not use the Standardised Approach and shall instead apply the treatment set out in Article 254 CRR.
- By contrast, for all other underlying exposures to which the IRB

	Approach cannot be applied, institutions using the look-through approach shall apply the Standardised Approach laid down in Chapter 2, Title II, Part Three of Regulation (EU) 575/2013.
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