

BANKING RULE BR/29

**THE MANAGEMENT OF INTEREST RATE
RISK AND CREDIT SPREAD RISK ARISING
FROM NON-TRADING BOOK ACTIVITIES**

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REVISIONS LOG

VERSION	DATE ISSUED	DETAILS
1.00	June 2023	Implementation of the EBA Guidelines (EBA/GL/2022/14).

BANKING RULE ON THE MANAGEMENT OF INTEREST RATE RISK AND CREDIT SPREAD RISK ARISING FROM NON-TRADING BOOK ACTIVITIES

INTRODUCTION

1. In terms of article 4(6) of the Banking Act (Cap. 371 of the Laws of Malta) (the “Act”), the Malta Financial Services Authority (the “Authority”) as appointed under article 3(1) of the Malta Financial Services Authority Act (Cap. 330 of the Laws of Malta) is empowered to make Banking Rules as may be required for carrying out any of the provisions of the Act. The Authority may also amend or revoke such Banking Rules. The Banking Rules and any amendments or revocation thereof shall be officially communicated to credit institutions and the Authority shall make copies thereof available to the public.
2. In accordance with article 4(7) of the Act, the Authority may make, amend or revoke Banking Rules as may be required for the purpose of implementing any guidelines, recommendations, decisions, opinions or any other instrument issued by the European Banking Authority (the “EBA”).

SCOPE AND APPLICATION

3. The Rule applies to all credit institutions licensed under the Act and such credit institutions shall ensure compliance with the provisions of this Rule.
4. The purpose of this Rule is to implement the EBA Guidelines issued on the basis of Article 84(6) of Directive 2013/36/EU specifying criteria for the identification, evaluation, management and mitigation of the risks arising from potential changes in interest rates and of the assessment and monitoring of credit spread risk, of institutions’ non-trading book activities, published on 20 October 2022 ([EBA/GL/2022/14](#)).
5. The Rule must be read and shall be applied in conjunction with the aforementioned EBA Guidelines, as well as any reviews and/or updates that may be undertaken to such Guidelines from time to time.
6. This Rule shall not replace any other law by which credit institutions shall abide, such as the applicable provisions in the Act, any other European and national legislation, and the Regulations, particularly, the relevant provisions of the Banking Act (Supervisory Review) Regulations (S.L.371.16).

DEFINITIONS

7. Unless otherwise specified in the EBA Guidelines being implemented in this Rule, terms used and defined in the Act and regulations issued thereunder shall have the same meaning in this Rule.

OVERVIEW OF THE EBA GUIDELINES

8. The EBA Guidelines specify
 - a. the criteria for the evaluation, identification, management and mitigation by a credit institution of the interest rate risk of the institution's non-trading book activities (IRRBB);
 - b. the criteria for the identification, management and mitigation by institutions of the IRRBB, either if it implements internal systems, standardised approach or simplified standardised approach; and
 - c. the criteria for determining non-satisfactory IRRBB internal systems.

RISKS FROM CHANGES IN INTEREST RATE OF NON-TRADING BOOK ACTIVITIES (IRRBB)

9. Section 4.2 of the EBA Guidelines sets out several considerations that shall be made by credit institutions with regard to the identification and management of IRRBB, including, but not limited to:
 - a. All interest rate sensitive instruments in the banking book to be included in the assessment;
 - b. The overall level of capital for IRRBB shall be commensurate with the credit institution's measurements and risk appetite, and duly documented in the Internal Capital Adequacy Assessment Process (ICAAP);
 - c. The IRRBB strategy, including risk appetite and mitigation, shall be part of the overall strategy, as approved by the Board of Directors;
 - d. Credit institutions shall have proper internal governance arrangements, including a comprehensive IRRBB framework with clear lines of responsibilities;

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- e. Credit institutions shall have clearly defined risk appetite statements implemented through comprehensive risk appetite frameworks, and approved by the Board of Directors; and
 - f. Credit Institutions shall have clear IRRBB risk policies, processes and controls, as specified in section 4.2.6 of the EBA Guidelines.
10. Credit institutions shall implement robust internal measurement systems (IMs) that capture all components and sources of IRRBB which are relevant for the business model of the credit institution. The measurement of exposures to IRRBB shall be in terms of potential changes to both the economic value and net interest income measures plus market value changes. Section 4.3.2 of the Guidelines specifies methods that shall be considered by institutions to identify sub-components of IRRBB.
 11. Credit institutions shall, at least on a quarterly basis, measure IRRBB exposures under various interest rate shock scenarios. Results shall always feed into decision-making and into the reviews of policies and limits for IRRBB.
 12. IRRBB stress testing shall be considered in the ICAAP, including forward-looking stress testing, reverse stress testing and changes in behaviour of their customer base, and integrate it into the overall stress-testing framework. Regular stress testing shall be performed, at least annually, with a framework that is tailored for the needs and exigencies of the credit institution.
 13. When measuring IRRBB, credit institutions shall fully understand and document key behavioural and modelling assumptions, which shall be aligned with their business strategies and must be regularly tested. The determination of these assumptions shall be made in a proportionate manner and take into account the materiality thresholds as referred to in section 4.3.5 of the EBA Guidelines.
 14. As a minimum, satisfactory IRRBB internal systems shall be implemented in accordance with the EBA Guidelines taking into account the principle of proportionality. Section 4.4 of the EBA Guidelines provides that, the competent authorities may require the use of standardised methodology, if the internal systems implemented by credit institutions are not satisfactory. Section 4.4. provides a non-exhaustive list of cases where the internal systems would be considered as non-satisfactory.

CREDIT SPREAD RISK OF NON-TRADING BOOK ACTIVITIES (CSRBB)

15. CSRBB captures both 'market credit spread' and 'market liquidity spread' but does not include the effect of credit quality changes during the observation period and excludes non-performing exposures. Currency specific dimensions may be considered when assessing changes, and credit institutions shall not exclude any instrument in the banking book from the perimeter of CSRBB. Credit institutions shall include CSRBB risk appetite in the overall strategy, in terms of the impact of fluctuating credit spreads on different measures.
16. The Board of Directors shall ensure that the credit institution has a CSRBB management framework in place, and that processes for the assessment of CSRBB are comprehensive and proportionate to the nature, scale, and complexity of the risks inherent in the business model and the activities of the credit institution. For further information on how to ensure that the credit institution has the appropriate risk policies, processes and controls with respect to CSRBB, reference must be made to section 4.5.4 of the EBA Guidelines. Institutions shall have appropriate approval processes and the CSRBB related processes shall be reviewed by an independent auditing function on a regular basis.
17. Credit institutions shall implement robust IMSs that capture all components and sources of CSRBB that are relevant for the business model of the credit institution. Credit institution should also monitor their exposure to CSRBB in terms of potential changes to the different CSRBB measures. While credit institutions shall develop and use their own assumptions and calculation methods for the assessment of CSRBB, the choice of measurement methodology shall be adequate for the complexity of the credit institution.

DATE OF APPLICATION

18. All requirements emanating from these EBA Guidelines shall apply from 30 June 2023, except for the provisions laid down in sections 4.5 and 4.6 (in relation to the CSRBB references in paragraphs 15 to 17 of this Rule) of the EBA Guidelines which shall apply from 31 December 2023.

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