Launching CECL With Your Board

regulatory CECL risk management

Summary: CECL is coming and bank management will need to answer questions from its board of directors as they prepare. Here are some questions to expect.

As a kid, everyone at one point or another probably looked at the stars in the sky and thought how amazing it might be to become an astronaut. Fast forward and SpaceX/Tesla founder Elon Musk says he will send the first manned mission to Mars in just 6Ys. That's right, we finally get to meet the Martians we have long heard about to see what makes them tick.*Note: I took out the last sentence of this paragraph before track changes...

Bankers too have to deal with the launch soon of new rules for calculating current expected credit losses (CECL). Community bank boards, accountants, regulators and others will all be keeping an eye on CECL preparation by management, since any lapse could be costly once the examiners show up.

So, what sorts of questions should the typical community bank board be asking?

Timing: When does CECL take effect for your bank and when will you have your preparations complete? CECL has staggered effective dates depending on the type of bank. Assuming a calendar year-end, public banks fall under the first adoption date of January 1, 2020. However, for non-SEC filers, your effective date is January 1, 2021. Be clear on the effective date and the target date needed for completion of your bank's implementation. Further, be prepared to give periodic updates on progress toward your goal and when you expect to have results to review with your board of directors.

Responsibility: Who exactly is in charge of CECL at your bank, how did you construct your team and who is on it? Ideally, the full CECL team should include the CFO, CCO, CIO and other critical staff. The new rule includes heavy use of data, credit, and the impact of rate movement over time, so make sure you have clearly designated responsibilities and lines of authority.

Data: Are you capturing the right data for CECL analysis, and is it clean and ready for use in calculations? You should be prepared to discuss the rationale for loan groupings, the average loan life for each group and how each was derived and applied in the calculation. This also requires data capturing the charge-off / recovery history for each loan group.

Reserves: Which modeling method(s) do you plan to use for your reserve calculations? Will you be using a method that requires more or fewer qualitative adjustments when economic and performance conditions change? The board will want to know which reserve methods you contemplate using and your reasoning for those selections. Be prepared to discuss scenarios you have evaluated and how reserves might change under each one. Boards may want to see a range of reserve rates. Finally, be prepared to discuss how changing conditions and/or assumptions might also impact your capital position.

Cost: How much is this going to cost the bank in terms of personnel and/or software/vendor expenses? Can the bank handle ongoing calculations in-house or will outside vendors be required? If external vendors are needed, how is the search and selection being handled, how do you review competency and what risks are you taking? You can even ask whether the vendors under consideration have a working model to review yet.

Preparing for board questions on CECL and responding to them can be a time-consuming process. But, it is an important thing to do. It will not only keep your board abreast of progress, but also help your team better prepare when the auditors and regulators start asking questions about your CECL compliance.

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CECL is one of the biggest challenges for community bankers these days. Our experts are ready to guide you every step of the way through this integration with no software to maintain. Learn more about our CECL Solution.