Management's Role When Outsourcing CECL

CECL risk management

Summary: The AICPA provided tips on CECL through its practice guide. We break it down for you in the first of three articles. Check back next Wednesday for part two of the series.

A study by market research firm OnePoll finds 11% of people have never traveled outside of the state where they were born, and 13% say they have never flown in an airplane. In this day and age, that is pretty shocking. But, it also reminds us how interesting human behavior can be.

In like fashion, the humans at the AICPA made a CECL practice aid available the 2nd week of September. This 63-page document provides a lot of good information for banks, but it may be a bit overwhelming to read too. So, we thought we would highlight some of the important elements for you in a series of BID articles. This is the first one in a series of three.

Today, we discuss the role of management responsibility when outsourcing CECL.

Key Takeaway: You can't outsource your management's responsibility.

This point has been mentioned multiple times by the AICPA, so we were not surprised to see it again. The audit expectations are the same for management whether they develop their model in-house or outsource. While mid-size and even some smaller banks will likely be outsourcing some, if not all, of the CECL implementation, it is important to work closely with vendors to understand why the model and method(s) were chosen, how the model works with the bank's loan segments, show how to drill-down to the note level for full transparency, explain the inputs and why assumptions were chosen.

Solution: Ensure that management knows all the ins and outs of its CECL model.

The key is to have regular meetings with your CECL stakeholders, including finance, credit, IT and the vendor, to review the development, progress, any hiccups and the solutions to those issues. Challenge stakeholders to ensure that there are no biases used from previous loss estimates. Discuss what management controls are appropriate vs. vendor controls, so there is a clear understanding of this from the beginning.

Also, do an internal review with your team regularly. Has all the information been captured that is needed? Are all the internal controls in place? Some information may not have been needed under the current loan loss allowance process. If this is the case, your management team will need a thorough plan, including the ways this new data will be captured and the controls in place to validate it.

While vendors will validate the model and how the calculations work, you need to be sure you have pretty much everything else. This includes but is not limited to: whether all the data is complete, that the assumptions are consistent and defendable, and that you understand the model with its inputs and methodology. The AICPA notes that forecasting credit losses can be subjective with judgment calls on collectability. Yet, it is critical to put these judgments into a "systematic, disciplined, and consistently applied approach." As a bank ourselves--and one that only serves other community-based financial institutions--we are also directly subject to CECL, just like you (unlike other vendors). We have a model and process to help you, so give us a call to learn more.

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CECL is one of the biggest challenges for community bankers these days. CECL FIT gives you a powerful, web-based intuitive solution with experts available as little or as much needed. Learn more about our CECL solution