Resuming CECL Compliance Planning

regulatory CECL

Summary: CECL is not far away with a January 1, 2023 start date. Many bankers have put CECL on the back burner during COVID, but it is time to focus on CECL again. To get you started, we share six steps for completing CECL: form a team, create a timeline, look for third-party expertise, evaluate ALM and stress test, review lessons learned, and utilize resources.

We found some dishes take hours to make such as beef stew, French bouillabaisse, and slow-roasted pork belly from the Philippines. While on the back burner, these dishes become flavorful and crowd-pleasing. But, putting other things on the back burner could be anything but crowd-pleasing.

Community financial institutions (CFIs) that put current expected credit loss standard (CECL) work on the back burner during the pandemic are finding they need to once again bring it to the front burner and begin planning and implementation steps.

As many bankers are discovering, CECL can be more than a straightforward change in accounting methods. It has the potential to create material changes in the capital and reserve amounts needed to backstop expected credit losses.

The new CECL rules require institutions to be more forward-looking and utilize predictive forecasting models to estimate potential losses. Although CFIs have enjoyed a longer grace period compared to the large banks that have already implemented CECL, there are steps that need to be taken now to prepare for the January 1, 2023 start date.

Understanding key differences

It is easy to get stuck in the weeds in the details of CECL. From a high-level view, CECL has some key differences as compared to incurred loss. Dun & Bradstreet groups these differences into three important changes for bankers to recognize.

- Focus on forward-looking data versus past performance
- Group or cluster HTM securities and loans by risk profiles
- Provide consistent assumptions for losses for monitoring, auditing, and for all other forward-looking solutions

Tips to get started with CECL

The focal point of CECL is developing and validating a forecasting model, which will need to take into account the size and complexity of a CFI’s credit and security portfolios. Those models need to be transparent and defendable.

Another important piece will be managing the data inputs for those models. CFIs need to start gathering data internally, as well as determine what external or third-party data sources they need to access.

Additionally, you need to think about how you are going to manage, store, and update data. Below are six simple steps to help you resume your CECL compliance preparedness.

1. **Form a CECL preparedness team.** There will be a lot of heavy lifting ahead in preparing and implementing this new strategy. Include a good cross-section of disciplines, perspectives, and expertise to make sure all issues are addressed, such as credit (loans), accounting (reserves & securities), technology (data & new tools), and compliance (audit and regulatory expectations). This is a key component in ensuring your implementation goes smoothly. Don't forget to include Board training.
2. **Create a realistic timeline.** The American Institute of CPAs (AICPA) recommends running one year in parallel. To accomplish this, you'll need to have your model configured by the end of this year.
3. **Look for third-party expertise.** This type of project can be daunting and time-consuming, even with the best-laid plans. Consider working with third-party experts that can help put you on a path to success. Consultants can bring expertise and resources that can help to create a more efficient transition to CECL compliance.
4. **Evaluate ALM and stress test.** Although often more applicable to large banks, a Loan & Capital Stress Test also can be a valuable tool to assess CECL readiness for CFIs. Such tests help account for different potential loss rate scenarios. Additionally, you'll need to review the assumptions in your asset liability management (ALM) solution and other solutions using similar forward-looking assumptions, to ensure that these are consistent and defendable throughout your institution.
5. **Review lessons learned.** CFIs can gain some insight into the process and impact of CECL from the big banks, specifically the public disclosures, earnings calls, and reports from publicly traded companies. The AICPA is another resource that is tracking known CECL issues. Currently, that list includes more than 40 topics that range from appropriate considerations for a forecast period to how to account for troubled debt restructurings.
6. **Utilize available resources.** There are a variety of resources for CFIs ranging from FAQs to webinars and audio presentations. Besides the AICPA website, you might want to check out our CECL Resource Library.

CECL is coming and it is important to be prepared. The steps above will get you on the right path. But, if you find you need extra help, we are here to assist you. Our Advisory Team can share insights or walk you through our CECL solution, to help with your success.

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We know that not every banker has the same needs. So CECL FIT gives you options to custom fit your portfolio. Start with a small package and you can still upgrade as you grow. Learn more about our CECL solution.

ECONOMY & RATES

Rates As Of: 05/12/2021 06:38AM (GMT-0700)

Treasury	Yields	MTD Chg	YTD Chg
3M	0.01	0.00	-0.08
6M	0.04	0.01	-0.05
1Y	0.05	0.00	-0.05
2Y	0.18	0.02	0.06
5Y	0.87	0.02	0.51
10Y	1.68	0.04	0.76
30Y	2.36	0.07	0.72

FF Market	FF Disc	IORB
0.06	0.25	0.10
SOFR	**Prime**	**OBFR**
0.01	3.25	0.05