CECL Solutions with FSA Partners, LLC

GET STARTED RIGHT AWAY

The new current expected credit loss (CECL) impairment model, which is codified in Accounting Standards Codification (ASC) 326-20, requires significant changes in how entities will measure credit losses for financial instruments that are not measured at fair value. The CECL accounting change to measuring credit losses is a significant shift from an incurred loss model to an expected lifetime credit loss model. CECL affects many departments throughout the organization including credit, finance, accounting, risk management and IT.

Successful implementation of CECL is more than meeting compliance requirements. Management should begin to think through changes that may be required to current processes, systems and controls in order to implement the CECL standard. Management should also consider the evidence and documentation that a robust governance and internal control framework should produce to support their lifetime loss estimates.

FSAP is here to assist your organization throughout the entire CECL life cycle, beginning with assessing and designing an entity-wide approach to planning, vendor selection, implementation, validation, transition and ongoing compliance.

PLANNING AND ASSESSMENT

<u>Assemble a CECL project team</u>
Identify a strong internal candidate or an external third-party advisor with experience in such areas as credit risk or accounting to lead the project team. Other team members should include senior management, lending, credit underwriting, risk management, accounting, information technology and independent auditor.

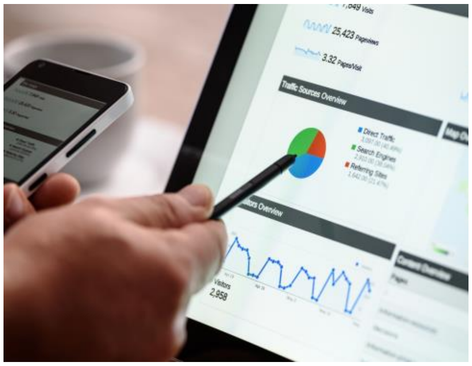
<u>Create a Project Plan</u>
Project plans should include key milestones, manage system and policy changes, identification of data requirements, provide training and communication, and account for contingencies.

<u>Readiness Assessment</u>
Identify potential gaps around technical accounting, business, operations, systems, data, modeling and other issues that may exist with implementing CECL. Communicate the changes necessary to close identified gaps based on the CECL requirements relative to the current organizational structure, systems, data, inputs and assumptions.

<u>Educate</u>
Educate client personnel including management, key stakeholders and the board of directors regarding CECL implications.

About FSA Partners, LLC

FSA Partners, LLC has been delivering value added solutions to the banking industry since 2008. We provide credit risk management solutions to community and regional banks through the enhancement and development of allowance for loan and lease loss (ALLL) methodology, including support for quantitative and qualitative loss factors, migration analysis, ALLL stress testing and ALLL memorandums. We also provide validation of ALLL process and methodology. We are currently providing solutions for implementing and complying with the FASB's new current expected credit loss (CECL) standard ASC 326-20. Post implementation, we help banks ensure compliance with regulatory guidance on model risk management standards identified in FRB SR Letter 11-7 and OCC 2011-12.



DESIGN AND KEY DECISION POINTS

<u>CECL Methodology</u>
CECL offers a great deal of flexibility in determining which modeling methodology to use. Institutions may apply different estimation methods to different groups of financial assets which gives you the power to choose a methodology that best suits your portfolio and business.

<u>Portfolio Segmentation</u>
Identify the portfolio segmentation needed to implement the proposed CECL model, such as grouping assets with similar risk characteristics. This can be done in various ways by product type, geographic, risk rating, etc.

<u>Vendor Selection</u>
Most community and regional banks have concluded to utilize a third-party vendor after performing a build-or-buy analysis to determine whether an internal build or an external vendor application is a better for their organization. Third-party solutions can be used to support the current ALLL calculations and then transitioned to the lifetime loss calculations under CECL. In addition, most third-party vendor applications also include a commercial real estate stress testing module and a capital stress testing module. Request for Proposals (RFPs) should be sent to multiple vendors and properly vetted prior to engagement.

Contact Us

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FINANCIAL SERVICES ADVISORY PARTNERS, LLC

VALIDATION AND TESTING

<u>Validate Methodology</u>
Ensure chosen methodologies meet all CECL requirements and provides the most accurate reserve estimates. The former will indicate your institution's compliance readiness; the latter helps quantify and minimize the financial impact from CECL.

<u>Run Parallel</u>
Calculate and compare both the current ALLL incurred loss model and the newly devised CECL model through the transition period, to help with budget decisions in preparation for CECL's effective date.

<u>Estimate Financial Statement Impact</u>
There is a general consensus that institutions will see an increase in reserves, therefore, a critical component in the adoption of CECL is to estimate the potential impact to capital, ratios and earnings. There is a need to assess whether the institution has sufficient capital to meet regulatory requirements and other debt covenants at the time CECL is adopted.

<u>Approval and Sign-off</u>
Prior to implementation, the final CECL process, methodology, model and conclusions should be reviewed and approved by senior management and the Board of Directors. Additionally, the CECL methodologies selected are subject to independent auditor sign-off and regulatory approval.

IMPLEMENTATION TIMELINES

Proposed Project Timeline – SEC Filers Excluding Small Reporting Companies

2017
- Assessment
- Planning

2018
- Design and Decision
- Vendor Selection
- Validation/Testing
- Implementation

2019
- Parallel Processing
- Transition
- Monitoring

2020
- Adoption
- Monitoring

Proposed Project Timeline – All Other Companies Including Small Reporting Companies (SRC) (1)

2017
- Assessment
- Planning

2018
- Planning
- Design and Decsion
- Vendor Selection

2019 - 2020
- Validation/Testing
- Implementation

2021 and 2022
- Parallel Processing
- Transition
- Monitoring

2023
- Adoption
- Monitoring

(1) SRC is defined in Part 230.405 of the SEC's general rules and regulations, Securities Act of 1933.