

1 WHAT IS CECL?

In the wake of the financial crisis of 2008-2009, the FASB reassessed its current impairment model to address stakeholder concerns regarding the delayed recognition of credit losses attributable to the incurred loss model. The long-awaited revised standard was issued on June 16, 2016 as Topic 326 Financial Instruments—Credit Losses, or more affectionately known as CECL (the Current Expected Credit Loss) model.

2 CORE CHANGES

The application of CECL may be the biggest fundamental change ever made to financial institution accounting. For the last four decades, U.S. GAAP has applied the incurred loss model for recognizing credit losses on loans, receivables and debt securities. Under the incurred loss model, a loss is not recognized until it is probable that the loss-causing event has already occurred. **CECL replaces the current incurred loss model with a forward-looking expected credit loss model** that requires an estimate of the expected credit losses over the life of the instrument.

3 MEASUREMENT

The new standard increases the volume of information to be considered when establishing the Allowance for Loan & Lease Losses and recognizing credit losses. Below is what the new estimate of expected credit losses should and should not include:

INCLUDE	
<ul style="list-style-type: none"> Past loss experience Current conditions Supportable forecasts of future events 	<ul style="list-style-type: none"> Estimates of prepayments Allowance for expected credit losses at each reporting date
DON'T INCLUDE	
<ul style="list-style-type: none"> Forecast losses beyond the reasonable/supportable forecast periods 	

Favorable and unfavorable changes in expected credit losses are recognized in current period income. The allowance is presented separately on the balance sheet as a reduction to the amortized cost basis of the related assets. Credit losses are measured on a pool basis when similar risk characteristics exist.



SIMPLIFYING THE ACCOUNTING

OLD GAAP

- ASC 320-10 Investments-Debt/Equity Securities
- ASC 310-10 Receivables-Individually Impaired
- ASC 325-40 Investments-Beneficial Interests
- ASC 310-30 Receivables-PCI Assets
- ASC 450-20 Contingencies-Losses

NEW GAAP

- ASC 326 Financial Instruments - Credit Losses

AFS DEBT SECURITIES (Impairment Approach Revised)

- No change to credit loss measurement
- Under CECL, impairment recognized through an allowance (consistent with the application of CECL to other assets)
- New standard permits immediate reversals of credit losses through income upon improvement*
- Credit loss limited to the difference between the amortized cost basis and fair value and cannot be written down below its fair value
- No longer consider the length of time that FV below AC
- Continue to calculate impairment at the security level

**There may be potential differences between recoveries of pre-existing impairments and post-adoption incremental improvements of forecasted expected cash flows.*

SCOPE OF CECL CHANGES

IN

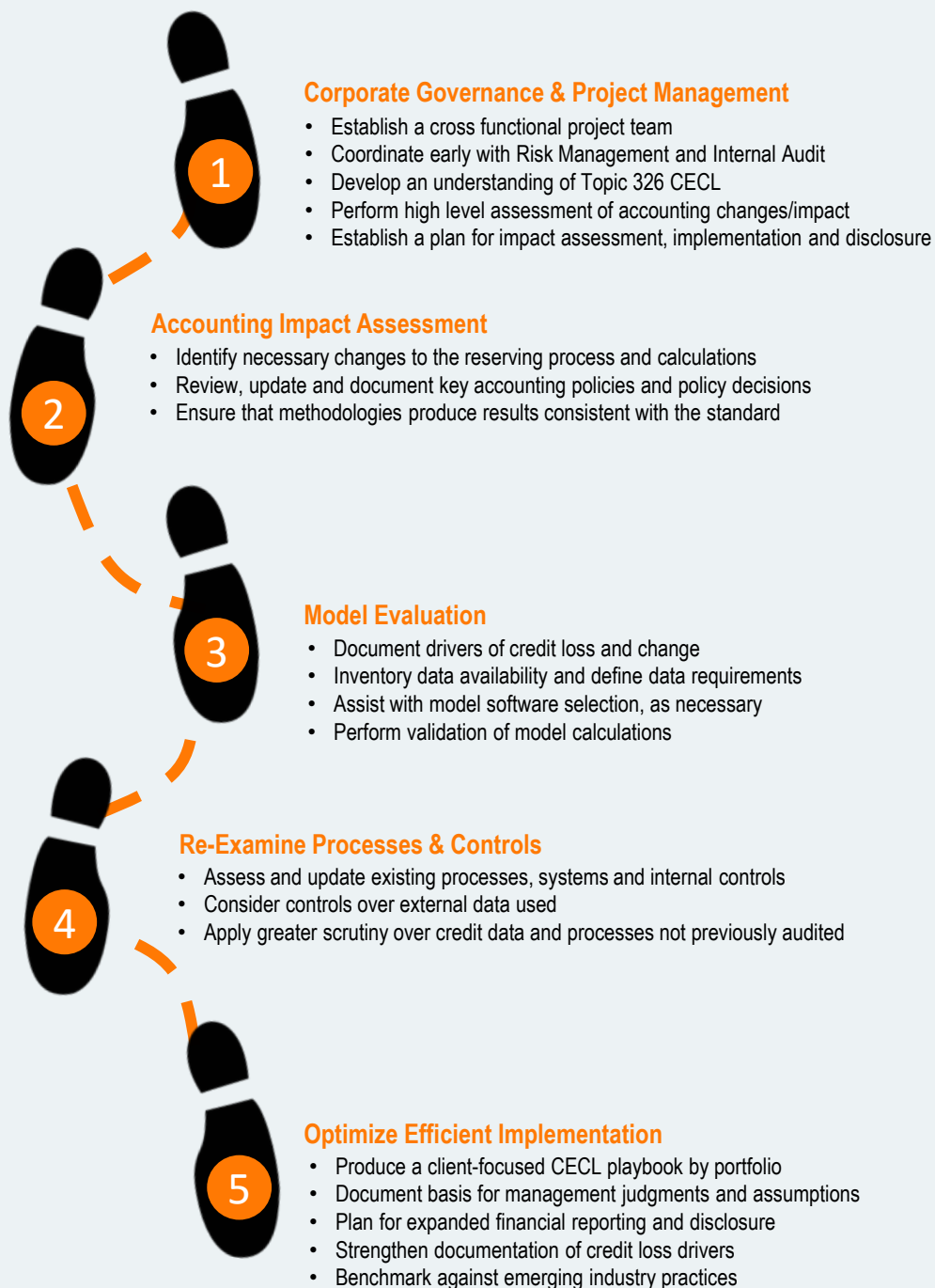
- Loans
- Trade receivables
- Debt securities classified as HTM
- Loan commitments
- Financial guarantee contracts that are not accounted for as insurance
- Net investment in leases recognized by a lessor
- Reinsurance receivables
- Purchased credit-deteriorated assets*

OUT

- Equity investments
- Debt securities classified as AFS
- Financial instruments measured at FV through net income
- Loans and receivables between entities under common control
- Financial guarantee contracts that are accounted for as insurance

**Record allowance at purchase and gross up asset basis to reflect the expected credit loss estimate. No income statement impact on day one.*

5 STEPS TO A SUCCESSFUL CECL IMPLEMENTATION

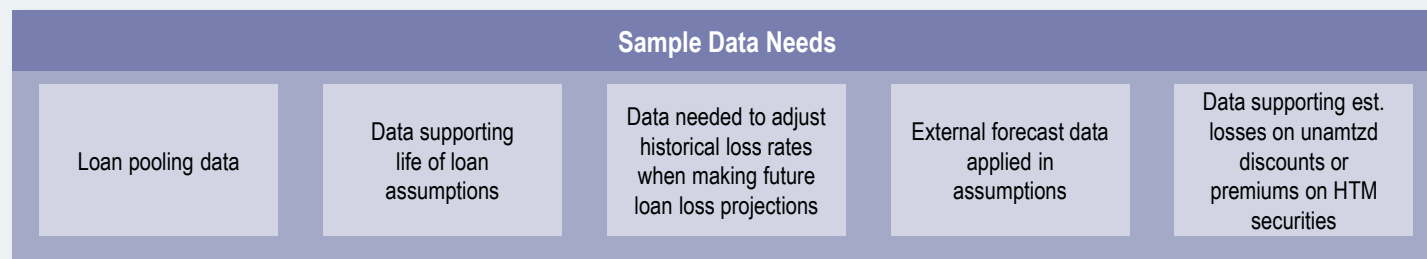


CECL DATA CONSIDERATIONS

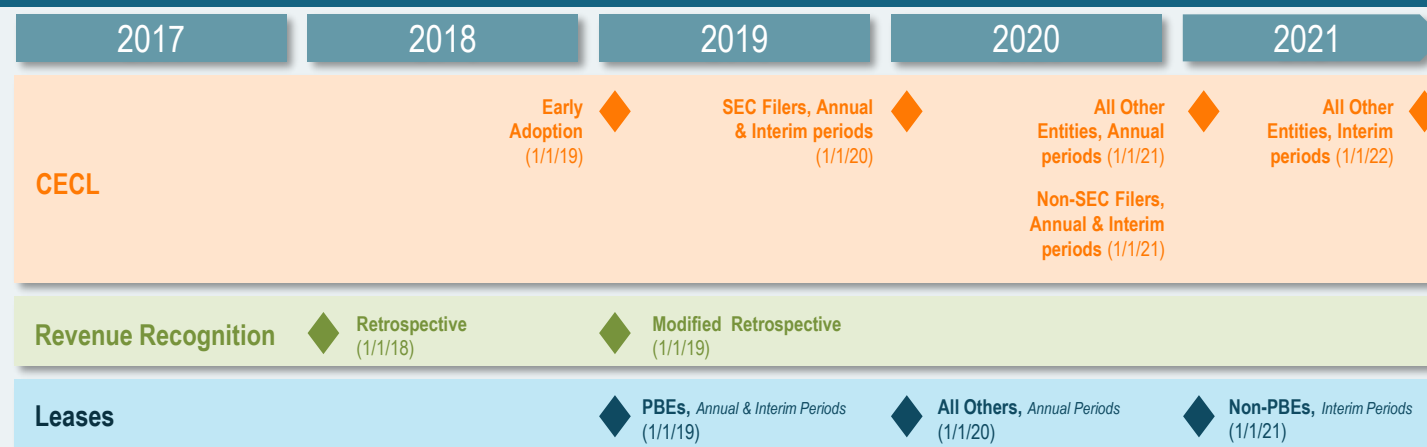
An organization's data needs will be impacted by their selected approach to implementing CECL, the complexity of the portfolio, the size of the entity, access to information and management of the portfolio. In addition, IT systems may need to be upgraded or modified to capture additional data to support the accounting and disclosure requirements.

Economic Forecasts	Data Needs	Data Culture	CECL Modeling
<ul style="list-style-type: none"> • Are your forecasts relevant to the location where loans are originated? • Do you have other locations that have an influence on loan performance? <p><small>This will increase the complexity of forecasting for multi-regional banks, or banks that have a multi-regional lending strategy.</small></p>	<ul style="list-style-type: none"> • Do you need to capture additional data? • Do you need to retain data longer than in the past? • What is the quality of the data? • Where is the data stored? • How will you get the external data? <p><small>The amount and quality of information will impact your ability to come up with a stronger, more supportable and manageable reserve figure</small></p>	<ul style="list-style-type: none"> • Can you rely on the data you have today? • Do you have access to data you'll need for compliance? • Will your data controls pass an accounting and regulatory audit? • Do you have the data governance, quality control, analytics, security and systems functionality you need to deal with CECL? 	<ul style="list-style-type: none"> • Model selection: Create in-house or buy third party solution? • Do you have the data management processes and the data availability to use an in-house solution? • Do you have the modelling expertise necessary to build and analyze an in-house solution? • Where do you want to be on the model cost vs sophistication spectrum?

THESE CONSIDERATIONS SHOULD BE EVALUATED NOW



STANDARDS IMPLEMENTATION TIMELINE



Major accounting changes headed your way, make time for CECL now!