

CECL – An Update & Bank Trends Demonstration

IBA 2019 Management Conference



WEALTH ADVISORY | OUTSOURCING | AUDIT, TAX, AND CONSULTING

Investment advisory services are offered through CliftonLarsonAllen Wealth Advisors, LLC, an SEC-registered investment advisor



Create Opportunities

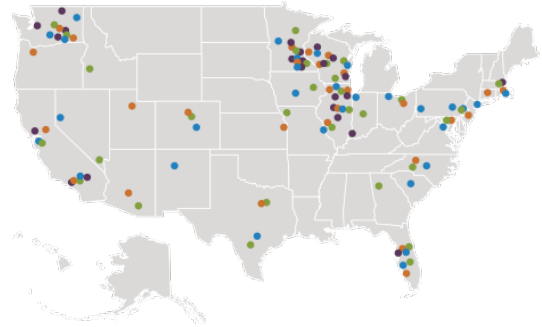
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About CliftonLarsonAllen

- A professional services firm with three distinct business lines
 - Wealth Advisory
 - Outsourcing
 - Audit, Tax, and Consulting
- More than 6,100 employees
- Offices coast to coast
- Serve 1,500+ financial institutions



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About Spotlight Financial

- Software development company that serves banks, credit unions, and their advisors
- Dashboard reports help streamline financial analysis
- Work with 400+ FIs across the country
- Wholly-owned subsidiary of Informa Financial



Speaker Introductions

- Liz Rider, Principal, CLA
- Michael Stinson, CEO, Spotlight Financial
- Reid TenKley, President, Spotlight Financial





Overview

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Effective Date

- SEC filers – annual reporting periods beginning after 12/15/19 including interim periods (Q1 2020)
- PBE – Annual reporting periods beginning after 12/15/20, including interim periods (Q1 2021)
- Non PBE – Year end of annual reporting periods beginning after 12/15/20

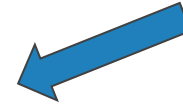
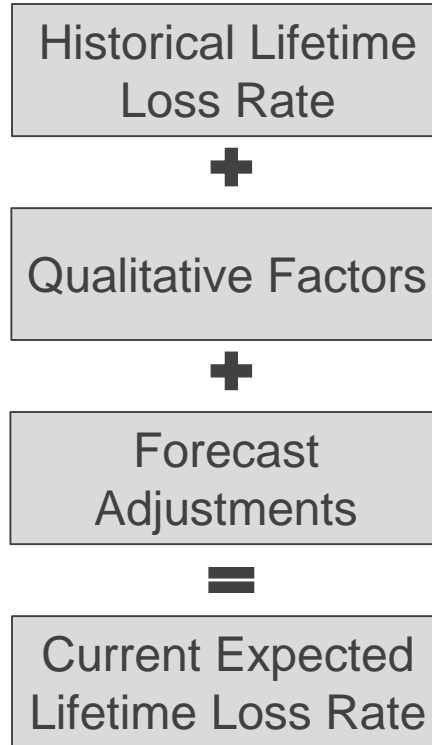


Current Expected Credit Loss Rate

Step 1: What methodology are you going to use to calculate the number?

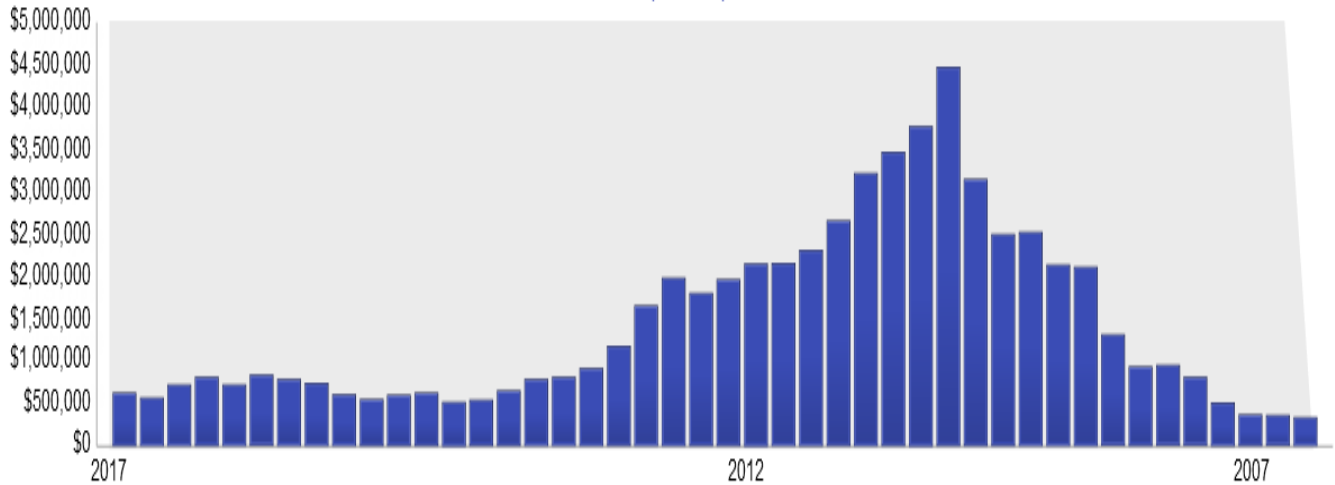
Step 2: How are we going to adjust our qualitative factors and narratives to the new standard?

Step 3: What is our forecast period and how are we going to adjust our history?

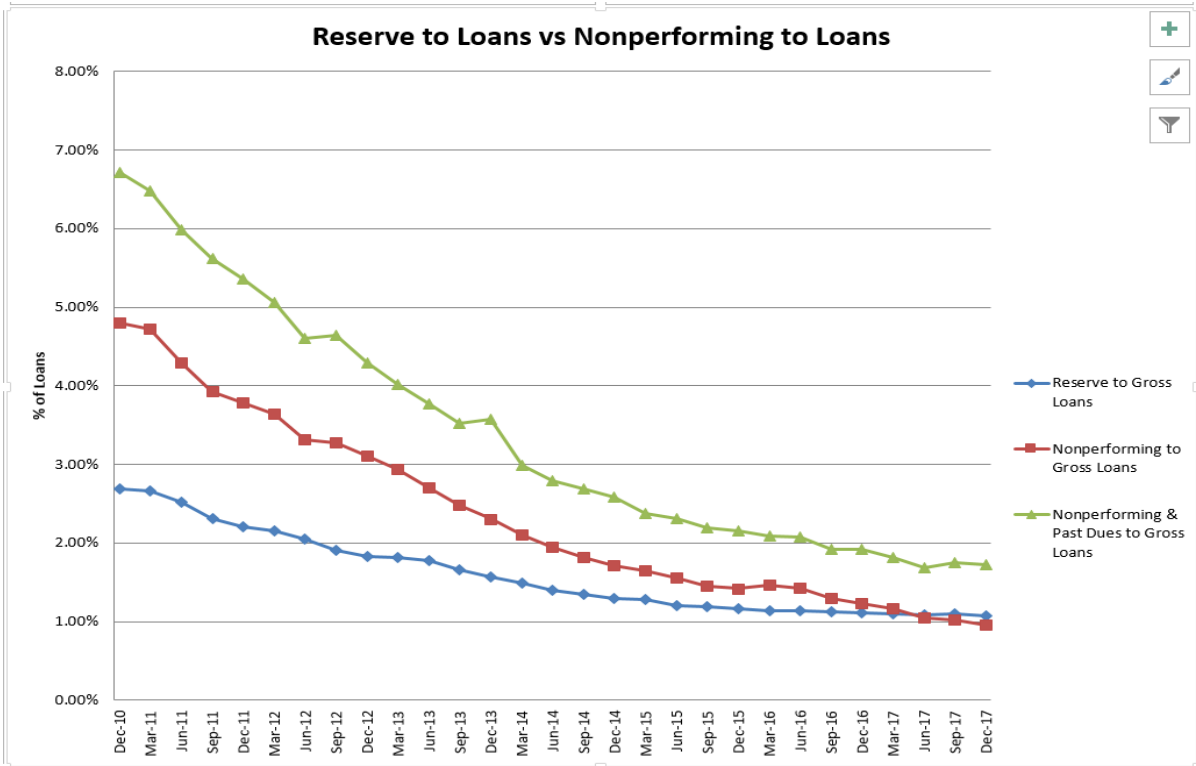


We have to start here, until we can compute our historic lifetime losses, we cannot start adjusting them to current expectations

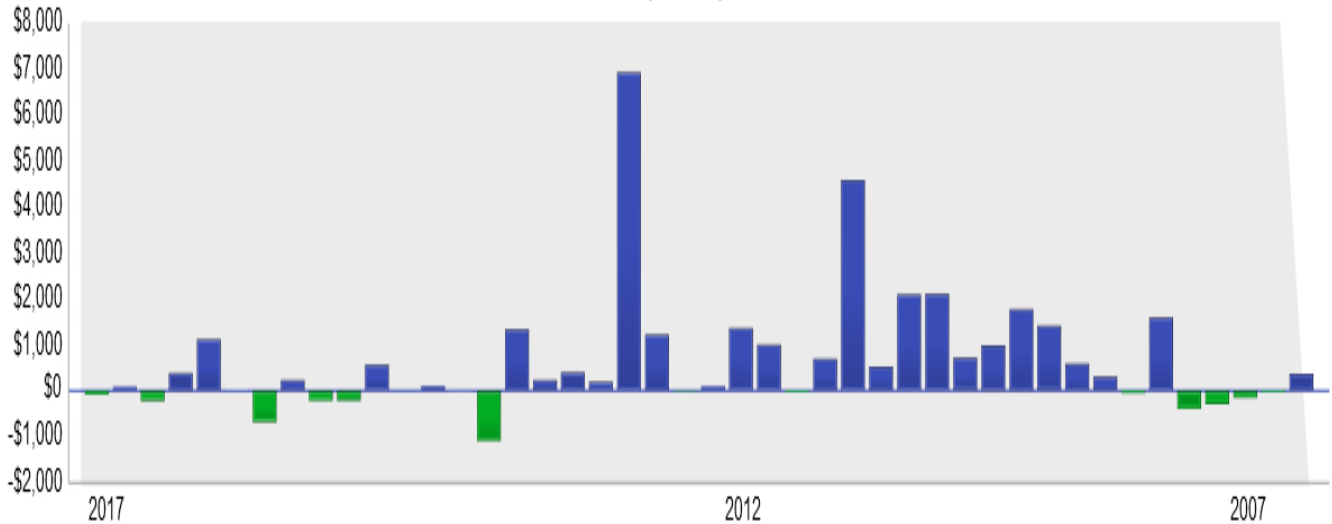
Large Institution Charge-Off Curve



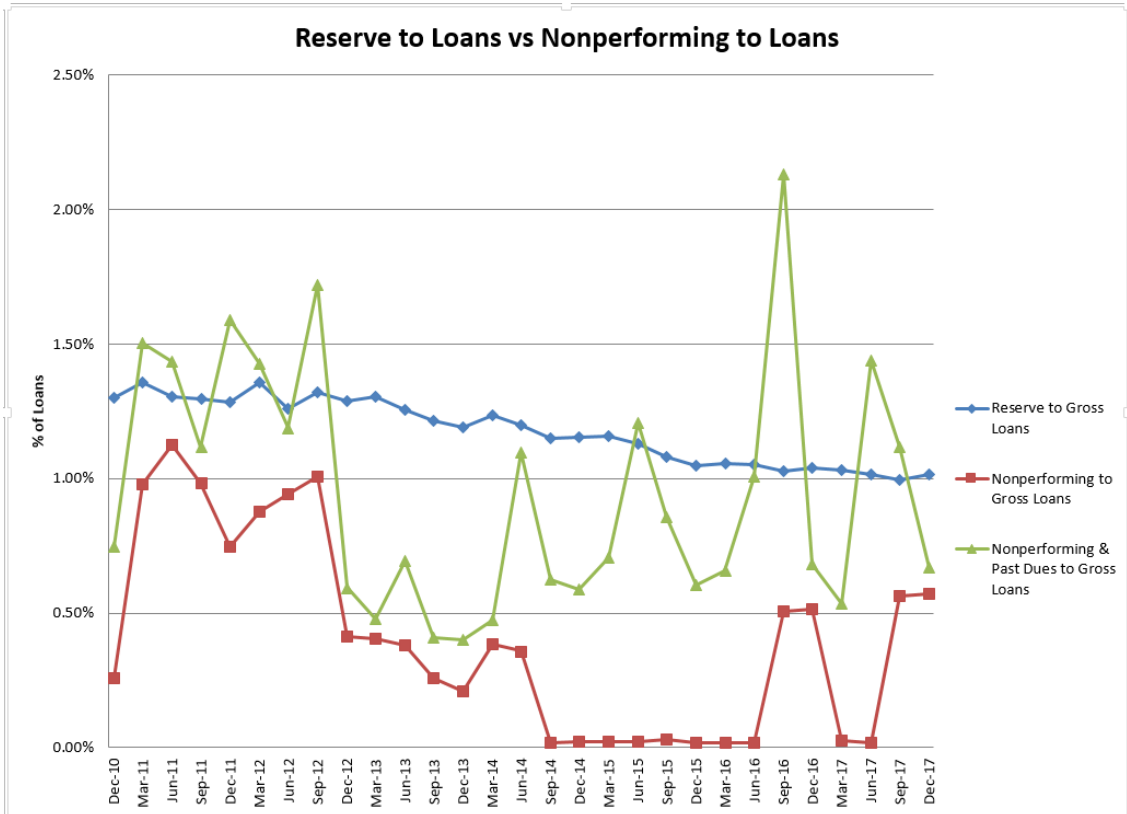
Large Institution Trend Analysis



Community Institution Charge-Off Curve



Community Institution Trend Analysis





Remaining Maturity Method

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CECL Methodologies

Any reasonable approach or approaches may be used – guidance is not prescriptive such as

- Remaining maturity analysis (Demo today)
- Loss-rate methods
- Probability of default and loss given default
- Snapshot analysis
- Migration analysis
- Vintage analysis
- Discounted cash flow analysis



Weighted Average Remaining Maturity Method

FASB Staff Q&A issued January, 2019

Q: “Is the WARM method an acceptable method to estimate allowances for credit losses..?”

A: “...may be an acceptable method to estimate expected credit losses....(it) considers an estimate of expected credit losses over the remaining life of the financial assets (that is, losses occurring through the end of the contractual term.”

Frequent mention of “flexibility to best report their expectations”, “complexity of the portfolio”



Weighted Average Remaining Maturity Method

FASB Staff Q&A issued January, 2019

Q: “What factors should an entity consider when determining whether to use the WARM method?”

A: “if an entity is using a loss rate-based method today, that entity may be able to continue with a comparable method, including the WARM method....assumptions and inputs will need to change to arrive at an estimate for expected credit losses that contemplates the contractual term of the financial assets adjusted for prepayments as well as reasonable and supportable forecasts.”

“scaled to the size and complexity”



Preparation

- Communication with stakeholders
- Standard is designed to be scalable
- Methodology should fit the complexity of your loan portfolio and charge-off history

Mapping CECL to Current ALLL

- Remaining Maturity
 - Change how we are applying annual loss rate to the principal balance of the loans, i.e. applying the annual loss rate over the lifetime of the loan as opposed to at a point in time
- All Other Methods
 - Change how we calculate the loss rate (i.e. lifetime loss rate as opposed to annual loss rate) that we apply to the principal balance of the loans





Share Screen

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Other Items

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Benefits of Consulting

- Utilize tool for model validation if institution uses a more complex methodology
- Teach leaders in your institution how to use the CECL allowance calculator
- Help management or board members understand CECL concepts
- Evaluate CECL models, including data requirement identification and retention
- Access our CECL resources to help create a plan to meet the compliance requirements
- Assist in computation of inputs for various methodologies



Closing Thoughts

Overall impact on the industry

- Initial diversity in application of standard will result in hazy comparatives after implementation
- Expected diversities in practice
 - Reasonable and supportable periods
 - Methodologies for certain loan types
 - Examiner expectations and auditor expectations
 - Simplifying assumptions
- The standard is intended to be scalable, as the complexity of your models should reflect the complexity of your loan portfolio





Questions

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