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CECL implementation: Survey shows where peers are as 2023 nears
By Mary Ellen Biery, Abrigo

With just weeks left to complete CECL implementation, how are banks doing?

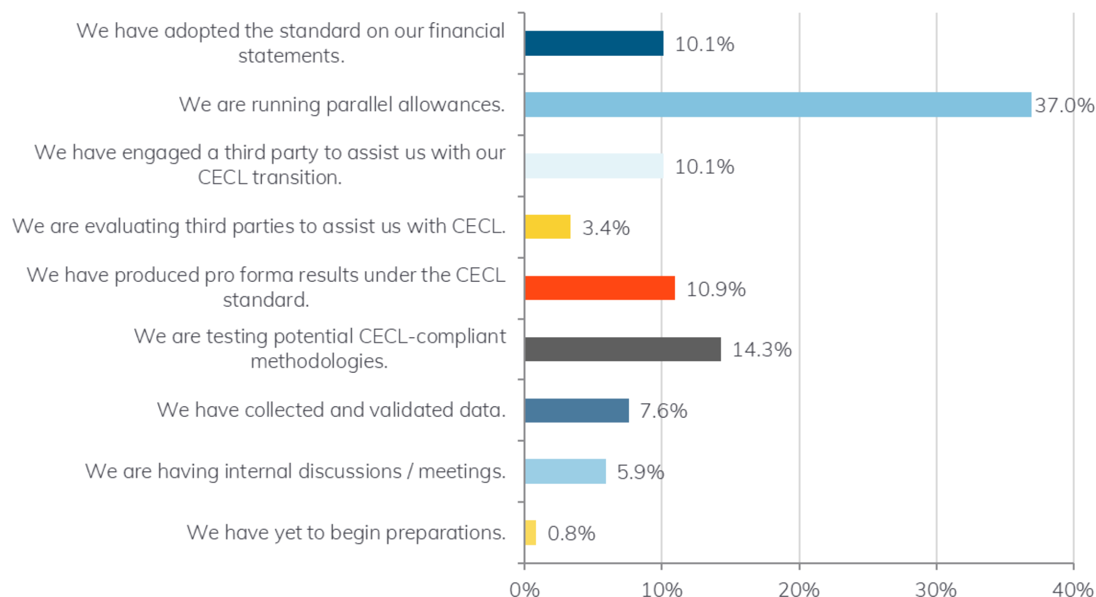
What are their biggest challenges with the current expected credit loss model? How has CECL implementation impacted their operations and reserves for credit losses?

The Q1 2023 compliance date is near for smaller SEC-reporting financial institutions and private or not-for-profit banks and credit unions, and progress is decidedly mixed, according to the Abrigo 2022 CECL Survey. Many institutions have made the most of the extra time the Financial Accounting Standards Board (FASB) provided when it delayed implementation. Others are still getting plans off the ground, Abrigo's CECL implementation survey found.

CECL implementation survey finds 8% still in early stages

In many cases, financial institutions adopting CECL for the 2023 deadline are tracking ahead of where SEC registrants were as they faced a 2020 deadline. The 2022 CECL implementation survey is the fourth such analysis since 2017 by Abrigo, which has worked with hundreds of financial institutions on CECL implementation.

One in every 10 bankers surveyed this year has adopted the standard on financial statements. Another 37% said they are running parallel allowances.



Compare this to Abrigo's 2019 CECL Survey responses, when no banks or credit unions had completed adoption, and less than 7% of all institutions were running parallel allowances.

Most bankers (86%) indicated they've moved beyond data collection in 2022, even if they haven't yet adopted the standard (i.e., they are testing methodologies, have produced pro forma results, are running parallel calculations, or are evaluating/have engaged a third party to assist).

However, some banks and credit unions (8%) remain at the CECL starting line. Their institutions are either having internal discussions and meetings or, in the case of 1% of respondents, have yet to begin preparations.

"Many institutions are well on their way to being ready, but others are still working through the process," said Garver Moore, Managing Director of Abrigo's Advisory Services.

Some banks "are behind" unless partnering on CECL

It's reasonable that financial institutions today are farther along than SEC registrants were, considering the challenges first adopters faced, Moore said. "As [institutions facing a 2020 deadline] were doing this, there was a lot more uncertainty around what they should be doing, a lack of confidence in certain approaches, and a general 'measure 70 times and cut once' trepidation from being the first to go," he said.

Today's CECL adopters benefit from earlier adopters' experiences, as well as from the extra time. As a result, Moore said, they "appear to be moving along in a more streamlined way with less risk."

"Taking advantage of the delay FASB gave to learn the best ways for CECL implementation to be done is certainly wise," he said. But given the short time left and presumably other responsibilities to take care of by CECL preparers, financial institutions that haven't begun preparations are behind the ball, he added.

CECL implementation is more straightforward for smaller financial institutions than larger ones, Moore noted. However, with only months until the deadline, not having started at this stage means "you're behind unless your plan is to partner with someone to pull you through this."

"Anyone you partner with probably has a lot of experience in getting this done and getting it done efficiently, so you may not be in that bad spot of trouble if you've literally done nothing," Moore said. "But even then, that window is closing."

In addition, as FASB officials have noted, internal and external resources become more stretched and valuable the closer the deadline.

CECL implementation took most FIs more than a year

Among the small share of CECL implementation survey respondents who finished implementing the standard in time for the survey's mid-year deadline, two-thirds said the process took more than a year from start to finish. Another 25% said they went from establishing a team to adopting the standard on financial statements in a year. The remaining 8% of respondents said CECL implementation took six months.

One option for banks to meet the CECL implementation date while ensuring the optimal use of crucial bank staff in the interim is to work with a CECL consulting team on an outsourced transition. Some CECL consultants can provide financial institutions with the model and initial allowance calculation, including documentation of the decision and backtesting. They can provide a transition to staff or ongoing delivery of the allowance calculation.

About 3% of bankers said their institutions are evaluating third parties to assist with CECL. Another 10% have already engaged a third party.

CECL's impact on operations

Bankers generally aren't planning to change how they pool or segment loans under CECL, with only about 1 in every four saying they would. However, among CECL adopters, half said adopting the standard caused a change in loan pooling or loan segmentation. Most cited a change that incorporated call codes or further granularity in pools.

However, one widespread change among banks and credit unions was the shift from manual, spreadsheet-based allowance estimates to automated functions. Many institutions are taking the opportunity to automate the allowance using CECL software as they transition to the expected-loss accounting standard.

More than half of respondents (including 75% representing institutions with less than $250 million in assets) use spreadsheets to estimate the allowance under the incurred loss model. However, only 16% of banks and credit unions plan to continue primarily using spreadsheets under CECL. Instead, 84% of bankers in Abrigo's CECL implementation survey expect to use a software solution for estimating the allowance under CECL.

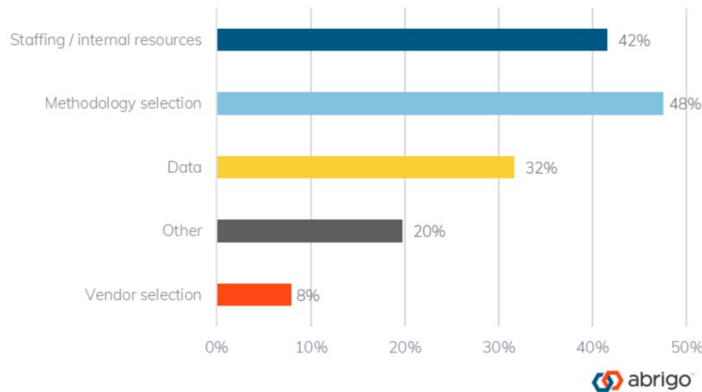
An even more significant shift to automation occurred among those that have already implemented CECL. Ninety percent of institutions that are across the CECL finish line are using software, compared to 33% of institutions that used software for the allowance for loan and lease losses (ALLL).

Top challenges during CECL implementation

The shift to digitalization is understandable, given the challenges respondents face and expect to face.

Technology can ease pressure on staffing and internal resources, a category identified by 42% of respondents as one of their biggest challenges so far. Even after adoption, CECL will increase demand on internal resources, including staff, and increase the complexity of compliance, according to more than half of the respondents. Automating the allowance can eliminate data entry and spreadsheet calculations. It can also reduce the time spent on documenting decisions and report writing.

Methodology selection, another facet of CECL that can be streamlined with automation, was the biggest challenge for nearly half of the respondents.

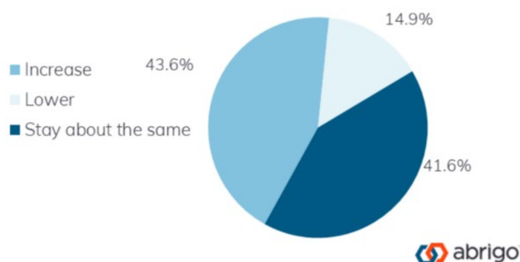


44% expect reserves to increase

CECL accounting experts agree that by itself, the accounting change doesn't necessitate an increase to reserves. Instead, economic conditions, the nature of the portfolio, and the institution's process for recoveries, among other factors, influence whether there's a change in an institution's reserve and the direction of any change.

The largest share of bankers (44%) expected reserves to increase under CECL, followed closely by 42% expecting reserves to stay about the same. Only 15% anticipated lower reserves.

"They're all three right," Moore said, adding that choices institutions make during implementation will affect whether the reserve stays the same, goes up, or goes down compared to their present allowance for loan and lease losses levels. "For community banks specifically, they're already reserving for a lifetime of credit losses," he said. "They're just doing it through the wrong mechanism. They're torturing incurred loss to make the outcome a number that would make sense under a CECL regime."



The CECL implementation survey found that reserves increased for two-thirds of the banks and credit unions that have completed CECL implementation. A quarter reported lower reserves, and 8% said they stayed the same. However, it's unclear how various portfolio compositions influenced the results. Differences in economic outlooks and recovery processes also couldn't be determined.

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None of the respondents whose institutions had finished implementing CECL said CECL substantially and negatively impacted profitability or led them to change the types of loans offered.

Conclusion

Making it across the 2023 deadline will be a major milestone for banking staff who have heard about CECL for more than seven years. CECL represents one of if not the most significant banking accounting changes ever, and financial institutions clearly are taking it seriously.

The 2022 Abrigo CECL Survey shows that financial institutions appear better prepared for CECL than in the past years. Nevertheless, given a chance to offer peers advice, respondents cautioned against delaying implementation.

Their other advice?

- "Make it as complex as it needs to be, but as simple as possible."
- "Prepare documentation—policies and procedures—as you go. We did it all at the end, which was time-consuming as we had to go back through our notes to document elections, etc."
- "Use a software tool [and] ensure your auditors and regulators are in the loop on progress."
- "Make sure your vendor has validations for their models."

This year's Abrigo CECL implementation survey shows that banks and credit unions are generally on track for implementation. However, some will race to cross the finish line, and all will look to auditors and examiners for information about where CECL practices should go from here.

Banks will undoubtedly need to update CECL models and operational aspects of allowance calculations as the lending, risk, and regulatory environments change. Understanding industry practices, as well as examiner and auditor expectations, will allow financial institutions to tackle that transition, too.

About the survey

The 2022 Abrigo CECL survey drew a wide array of staff from banks and credit unions, including Presidents, CEOs, CFOs, Chief Risk Officers, Controllers, Chief Credit Officers, Senior Vice Presidents, Vice Presidents of Finance/Accounting, Financial Analysts, and Allowance Managers.

Almost half (45%) of the 119 respondents represented institutions with $1 billion to $5 billion in assets, and 43% had less than $1 billion (Figure 1). Staff from institutions with more than $5 billion in assets made up only 12% of those surveyed.

Banks regulated by the Federal Reserve, the OCC, or the FDIC made up the bulk of institutions represented by survey-takers (73%). One-quarter were credit unions, and 2% were banks or cooperative institutions of the Farm Credit System. The online survey was conducted between June 14 and July 29, 2022.

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