American Bankers Association
Building Success. Together.

Michael L. Gullette
Senior Vice President – Tax and Accounting
202-663-4986
mgullette@aba.com

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Robert Storch, Chief Accountant
Federal Deposit Insurance Corporation
RStorch@fdic.gov

Sydney Menefee, Deputy Comptroller and Chief Accountant
Office of the Comptroller of the Currency
Sydney.Menefee@occ.treas.gov

Joanne Wakim, Deputy Associate Director and Chief Accountant
Federal Reserve Board
Joanne.Wakim@frb.gov

Via email

Re: CECL Delay, Guidance, and a Practical Expedient

Dear Bob, Sydney, and Joanne:

Upon the June 2016 issuance of Accounting Standards Update 2016-13 (also known as the CECL accounting standard) by the Financial Accounting Standards Board (FASB), it was generally accepted that, due to the significant changes to the data and analyses required under CECL, there would need to be a lengthy transition process. Earlier this month, a "FASB Staff Q&A," which states that the Weighted Average Remaining Maturity (WARM) credit loss estimation method "may be an acceptable method." A detailed example assists bankers on how to calculate a WARM credit loss estimate.

This is very disappointing. It has now been over 2 ½ years since FASB issued the standard and the only substantive written guidance that has been provided to community banks is to say that a specific calculation "may be acceptable." In reality, CECL implementation involves far more than a specific calculation. There has yet to be any real mention of the critical "Q factor" process or on how banks can prepare to credibly discuss CECL results in light of CECL's disclosure requirements. Worse, as noted in our attached Discussion Paper, is that WARM requires more work than other basic calculations, requires a knowledge of prepayment concepts that most community banks do not currently possess, and is conceptually questionable as an estimation method for certain key loan portfolios. In other words, for the community bank, WARM should not be used.

If there is one aspect of CECL that everyone agrees upon is that practice is likely to evolve. ABA believes that primary reliance on WARM calculations, however, can potentially set a bank back several years in their implementation, as a focus on WARM can severely limit the range of credit loss data a bank will maintain. It will have little capability to evolve.

In recent meetings with the ABA, significant concerns have been expressed by banking agency personnel and auditing firm representatives that many community banks have yet to begin substantive efforts toward implementing CECL. We believe this is because of the lack of comprehensive guidance they are receiving from their regulators or auditors. Unless substantive guidance is provided to these banks, it is foreseeable that arbitrary CECL provisions will often be recorded with management unable to address the most basic of questions from its board. With this in mind, we urge you to request a delay to the CECL effective date until such guidance is available.

While CECL is meant to be scalable to smaller institutions, measuring credit risk, unfortunately, is inherently complex. From the time CECL was initially proposed, ABA has insisted that CECL brings significant changes to banks of all sizes and we continue to be concerned about this. The heart of this concern is the need to set up processes that forecast economic conditions and their impact on credit losses throughout the contractual life of the loan portfolio. With this in mind, we believe that many banks should be allowed to merely record a credit loss allowance that represents a "through the cycle" (TTC) loss rate, one that takes into account both the highs and lows of a complete economic cycle. Such a rate can be easy to calculate (much easier than WARM), it will save significant time during an ongoing reporting process, and will also provide management and examiners with a generally understood metric of credit risk that well represents a lifetime loss expectation.

With this in mind, we believe a change to the CECL standard will be needed. If you are concerned about the costs to community banks, we urge you to recommend to FASB that a practical expedient be allowed to record and maintain such TTC rates. We envision that the banking agencies will provide guidance for banks to determine when use of the expedient would be appropriate and we see it applicable for many banks. There are various ways to address any perceived supervisory risks of using the TTC rate and we would be happy to work with you in evaluating them. ABA will submit this request to FASB if the agencies continue to ignore the operational realities of CECL.

Further, it is becoming apparent that many banks do not often have a sufficient amount of data to base reliable estimates of credit loss in their portfolio. This was anticipated by FASB with the expectation that external, or third-party, credit loss information be used. ABA believes that such data, which can be readily attainable for several key asset classes and based on various granular risk characteristics, will be used by investors and auditors and, perhaps, even your own examiners as benchmarks to evaluate a bank's provisions. With this in mind, we recommend that the agencies acquire and provide such relevant information to individual community banks on a regular basis. In addition to improving examiner ability to assess credit loss expectations of the member banks, if shared with the industry, such data can be enormously helpful to small banks as they learn more about credit risk and evolve their CECL estimation processes in the future.

While ABA has historically opposed enactment of the CECL standard, we have been steadfast in working with banks to maximize the likelihood of success in implementation not only for the effective date, but also for years thereafter. Bank safety and soundness depends on it! With that

in mind, we believe these recommendations are vital to ensure that community banks can implement the standard successfully and in a cost-effective manner.

Thank you for your attention to these matters and for considering our views. Please feel free to contact me (mgullette@aba.com; 202-663-4986) if you would like to discuss our views.

Sincerely,

Michael L. Gullette