



Effectively documenting your CECL transition: Insights on implementation controls and documentation needs

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Learning objectives

1

Recognize effective methods for documenting the CECL implementation.

2

Identify critical control points in the CECL estimation process.

3

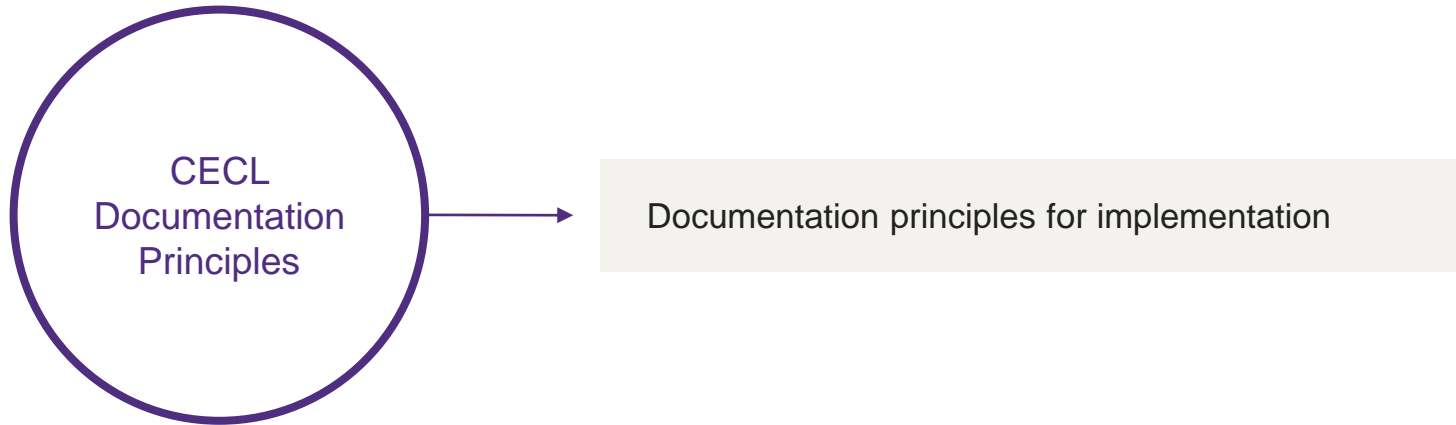
Assess sufficiency of implementation documentation.

Agenda

- Implementation
- Documentation Principles
- Implementation Framework: Organizing Controls
- Implementation Framework: Documentation Needs

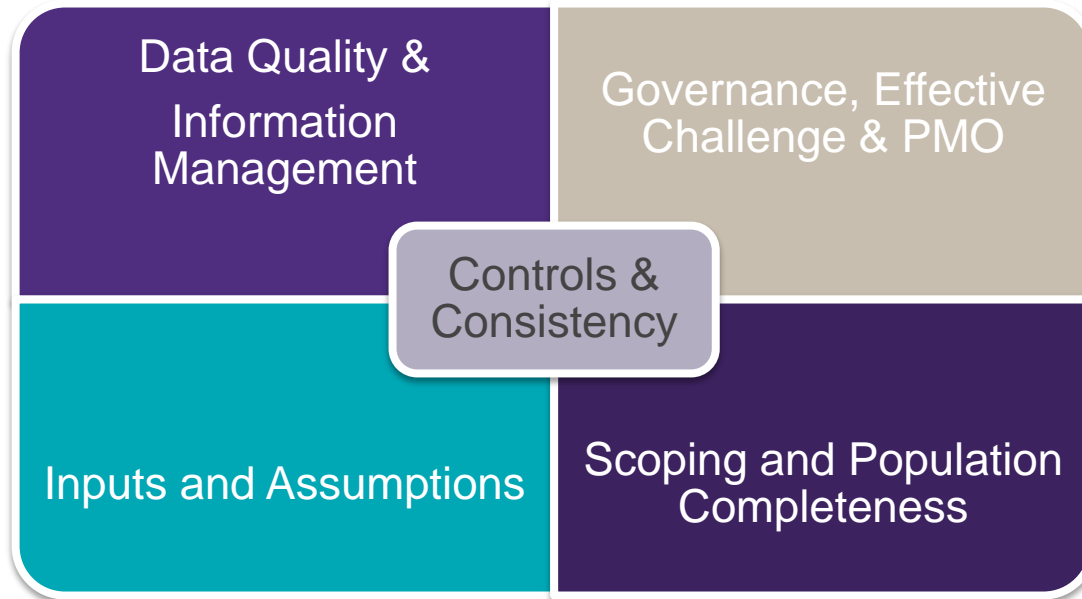
CECL Documentation Principles

CECL Documentation Principles



Documenting CECL Implementation

Guiding Principles for Documentation



Documenting CECL Implementation

Control Documentation – Tying it all together consistently



What are the risks for insufficient documentation?

- **Implementation Control Risks**

- ❑ **Accounting/Audit Risk:** Lack of scoping assessment → potential non-GAAP interpretation
- ❑ **Audit/Regulatory Risk:** No project plan, approval authorities, PMO → implementation delays, no supporting evidence for auditor/regulator reviews
- ❑ **Modeling Risk:** Estimation uncertainty, increased F/S volatility, inability to communicate results and activities ("attribution analysis")
- ❑ **Process Risk:** Processes not documented may be overlooked for controls → increased reporting/disclosure risk, potential for control deficiencies, material weaknesses, auditor/regulator findings

"If it's not documented, it's not done"

Documenting CECL Implementation

Data Quality and Information Management



Key Principles:

- **Data Sources/Uses**
 - Bank's Data → Use internal whenever possible (e.g. loss experience, forecasts, risk data (LTV/FICO, etc.))
 - External data → How does it reflect our portfolio/expectations? Document similarities and why appropriate
 - Capture data lineage within the CECL process
- **Data Storage/Transfer**
 - Identify completeness & accuracy processes
 - Reconciliations, system controls, edit checks for data transfer
 - Data owners/stewards → who is responsible and who can modify?
- **Data Cleansing/Control**
 - Error correction processes
 - Data management control processes

Documenting CECL Implementation

Governance, Effective Challenge, & PMO



Key Principles:

- **Evidence approvals of major implementation decisions**
 - **Implementation:** Buy/build decisions, vendor selection, scoping impact
 - **Modeling/Accounting:** Forecasting methods, determination of expected life/reversion
- **Document all possibilities → why are selected approaches most appropriate?**
 - **Alternative theories/approaches:** modeling methods, vendor platforms
 - **Forecasting/modeling:** reviews/challenges to inputs/assumptions, criteria considered and selected
- **Evidence effective challenge**
 - Effective challenge by those charged with governance (CECL Steer Council)
 - Implementation and process
 - Challenges to selected approach/approval

Documenting CECL Implementation

Supporting Inputs and Assumptions



Key Principles:

- **Inputs and their alignment to credit risk** → why is it appropriate to capture your credit risk?
 - **Assumptions and their selection** → why are they appropriate for your institution?
 - Ex: portfolio life, reversion methods/techniques, forecasting approaches
 - **Tell the story of inputs/assumptions development**
 - Include alternative approaches/theories
 - Document what did and did not work → rationalize selected inputs
 - If it worked? If it didn't, why not?
- Key ICFR Point for Disclosures and Reporting
- **Reporting the output** → **attribution analysis**
 - Document process to understand how inputs drive estimate
 - Attribute inputs/assumptions to movement within the model results/output
 - Capture processes for reporting outcomes → ensure they align in procedures/controls for reporting

Documenting CECL Implementation

Scoping and Population Completeness

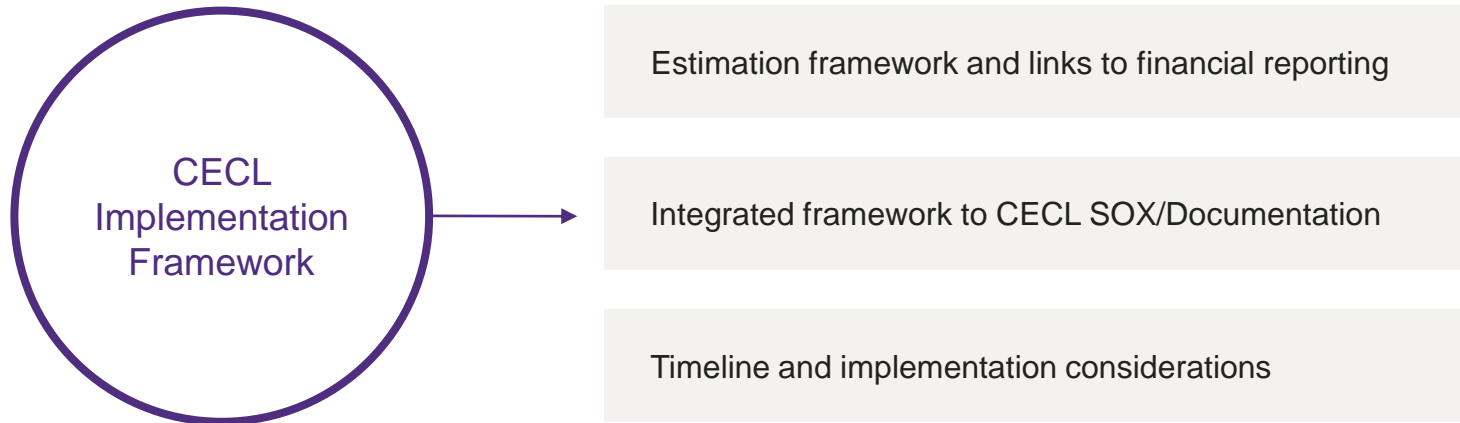


Key Principles:

- **Scoping application → determining impact of the standard**
 - Prepare scoping document/memo → complete portfolio application **not just loans** (e.g. off-balance sheet, non-loan receivables, securities)
 - **Items scoped out:** Document why and any other applicable guidance
- **Population completeness**
 - Procedures to capture population completeness for estimation
 - Data transfers, reconciliations between systems, accuracy of output reporting
 - Processes and controls (e.g. system to system, system to modeling platform, modeling platform to G/L)
 - Final validation/mathematical validation → implementation/pre-launch and ongoing model risk management
 - Ensure all in scope loan types are captured
 - Completeness of model documentation

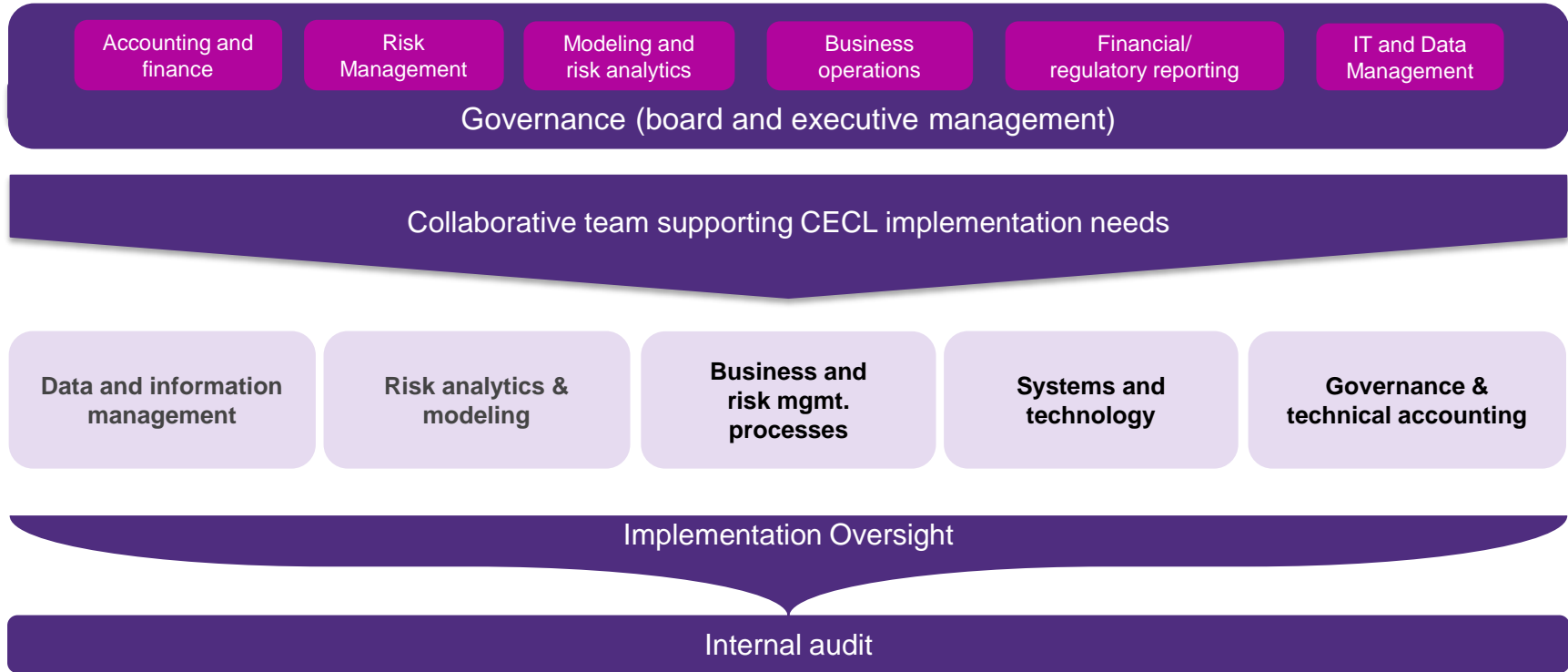
CECL Implementation Framework: Organizing Controls

CECL Implementation Framework: Organizing Controls



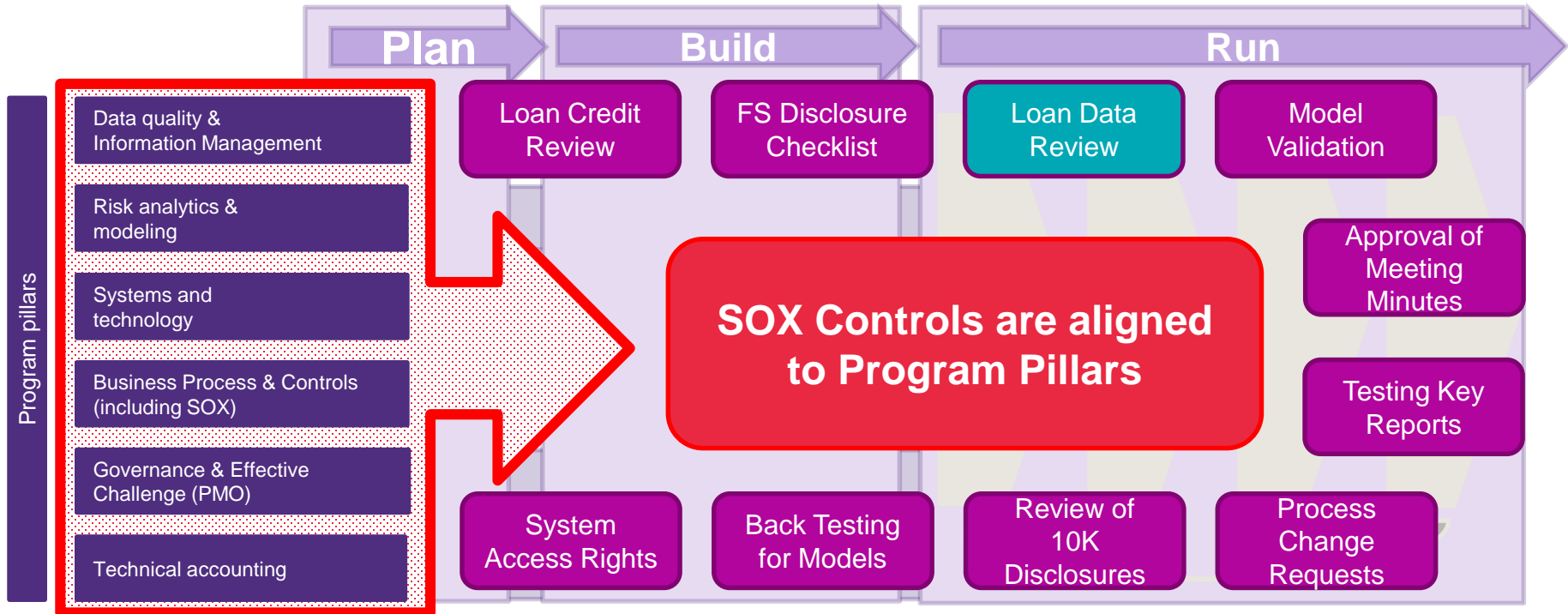
Implementation requires an integrated approach

Sustainable CECL solutions integrate all stakeholders through the process



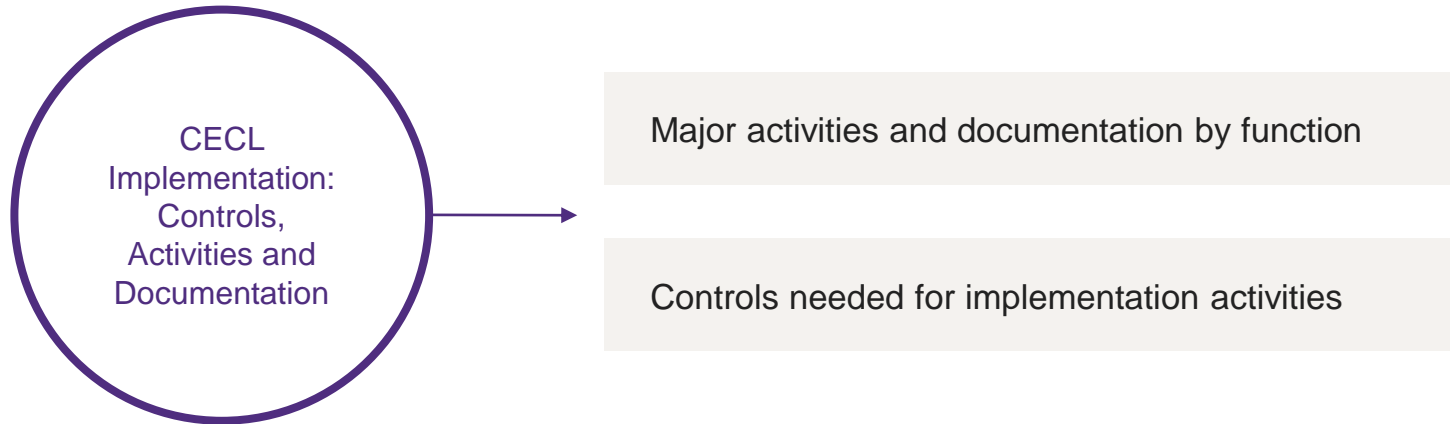
Using a comprehensive framework to implement

Sustainable CECL solutions integrate all stakeholders through the process and address early challenges faced by many institutions



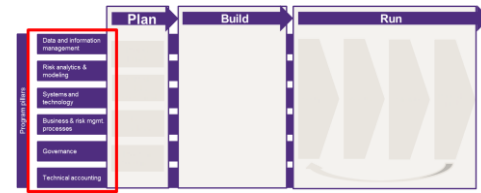
CECL Implementation: Controls, Activities, and Documentation

CECL Implementation: Controls, Activities and Documentation



Documenting Implementation

Documentation Needs by Major Functional Pillar

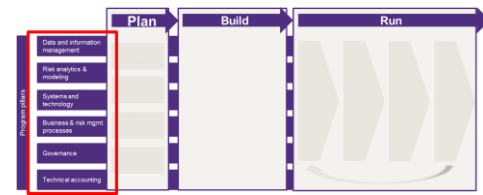


Governance and Effective Challenge

- **Steering Committee/Project Committee**
 - Project charter and work streams/working groups structure
 - Designated approval authorities for key decisions (e.g. RACI matrix)
 - Reporting back to the BOD and Those Charged with Governance on activities and key decisions
- **Project Plan**
 - Approved project roadmap/plan for implementation activities
- **Ongoing Implementation Oversight**
 - Evidence approvals over key decisions → buy/build, model/vendor selection
 - Demonstrate progress reporting to BOD/TCWG → implementation progress, parallel run/testing
 - Effective challenge over initial estimates and project output → model inputs/approach, SAB 74 disclosures, initial reporting output, etc.

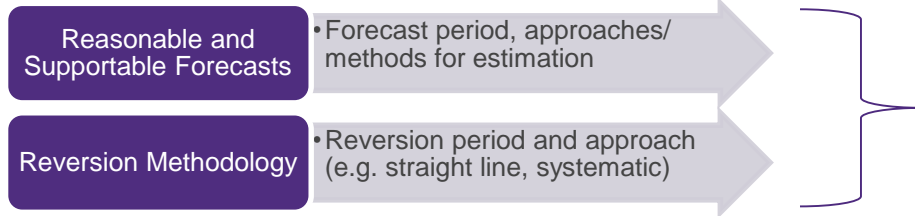
Documenting Implementation

Documentation Needs by Major Functional Pillar



Technical Accounting

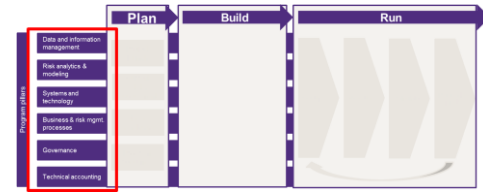
Documentation Needs	Content
CECL Scoping Impact/Memo	<ul style="list-style-type: none"> <u>In scope instruments</u>: approaches to scoping, methods to verify completeness and accuracy <u>Out of scope instruments</u>: supporting conclusions on scope application, alternative methods/standards in scope
CECL Accounting Policy Preparation	<ul style="list-style-type: none"> Treatment of all in-scope financial instruments → complete population Modeling approaches for each pool/asset class



Not accounting policy elections:
document within modeling
approaches w/ input from
accounting policy

Documenting Implementation

Documentation Needs by Major Functional Pillar

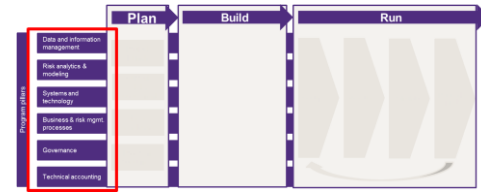


Business Process and Controls (incl. SOX)

Documentation Needs	Content
Process Flows for Implementation and ongoing Estimation	<ul style="list-style-type: none"> • CECL Process Flows for key activities <ul style="list-style-type: none"> ▪ Loss forecasting (inputs/assumptions, etc.) ▪ Model estimation ▪ Data Flows ▪ Reporting and Disclosure
Risk and Control Matrix for Implementation	<ul style="list-style-type: none"> • Identify key risks <ul style="list-style-type: none"> ▪ Modeling/forecasting ▪ Data flows/system integration ▪ Reporting and disclosure • Build controls to address key risks <ul style="list-style-type: none"> ▪ Gap assessment of new processes against risks

Documenting Implementation

Documentation Needs by Major Functional Pillar



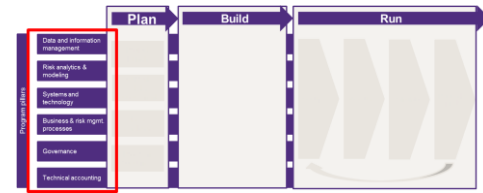
Data and Information Management

Documentation Needs	Content
Data sourcing approaches/methodologies	<p>Document internal and external data sourcing methodologies</p> <ul style="list-style-type: none"> • Data integrity thresholds for exceptions/inconsistencies • Document controls/procedures ensuring data accuracy
Data flowcharts for CECL estimation	<p>Document data flow within CECL estimation (systems, edits, completeness/accuracy, etc.)</p>
"Forecast data" development processes	<p>Document how data/inputs are <u>reasonable and supportable</u></p> <ul style="list-style-type: none"> • Reasonable – alignment with risk and relevance to portfolio, impact on losses • Supportable – documentation support outputs, directional consistency

*Document the integration with
enterprise wide data
management activities*

Documenting Implementation

Documentation Needs by Major Functional Pillar



Risk Analytics & Modeling

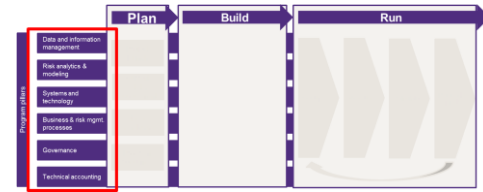
Documentation Needs	Content
Model Design Document	<ul style="list-style-type: none">• Model theory and design selection process• Selected modeling approaches and alternative approaches considered
Model Development Document	<ul style="list-style-type: none">• Interpretation of trial/dry runs of models/calculations• Model modifications as a result of dry runs
Model Process Documentation (future state)	<ul style="list-style-type: none">• Processes and controls (reconciliations, inputs development, etc.)

Model Validation Report

Prior to issuance, obtain an independent model validation report with an assessment of model's "fit for purpose" → should model development, governance, and mathematical accuracy

Documenting Implementation

Documentation Needs by Major Functional Pillar

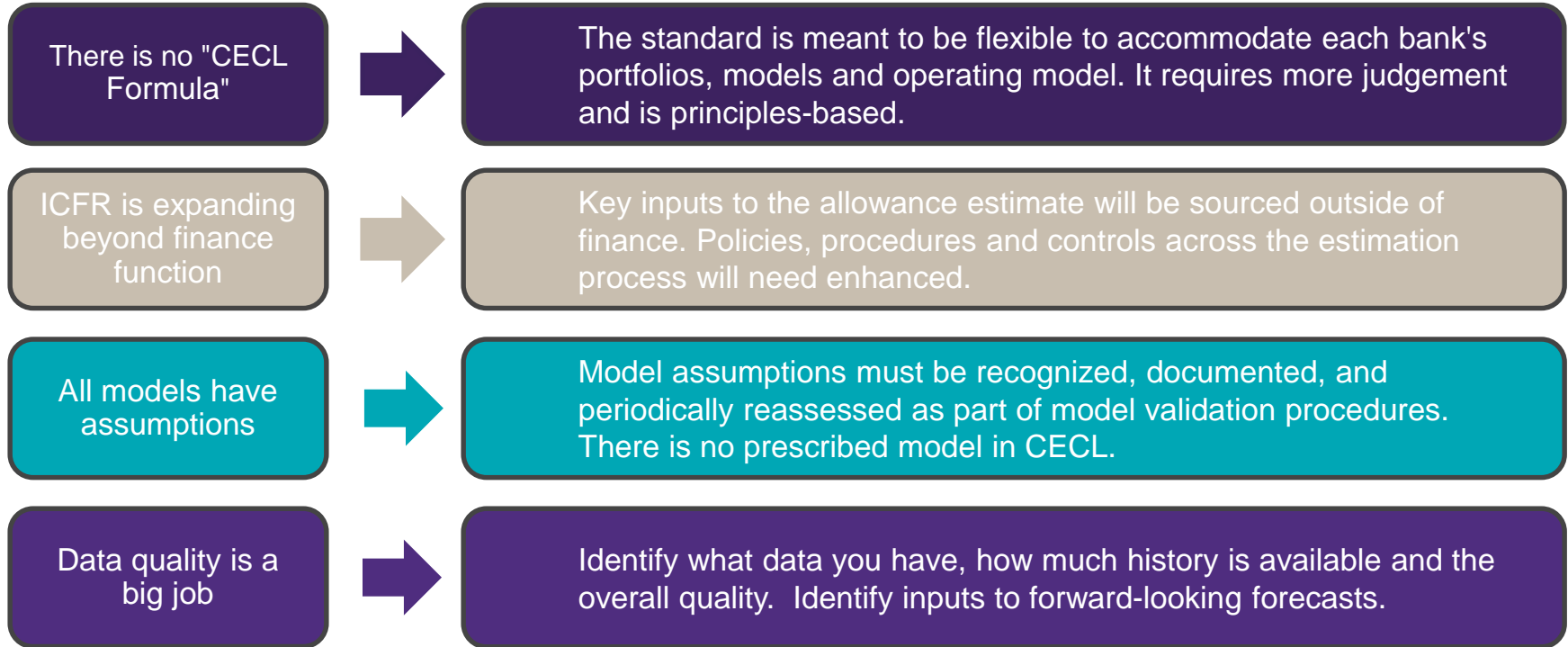


Systems and Technology

Documentation Needs	Content
Technology/System Selection Documentation	<ul style="list-style-type: none"> • Document process/methodology and selection criteria (e.g. scorecards) • Include process for data migration and validation of data → link to data management approaches • Process of testing key reports and data transfer → results of testing, including SSAE reports
Documentation of IT General Controls	<ul style="list-style-type: none"> • Document integration of system into enterprise IT environment • Controls over: <ul style="list-style-type: none"> ○ Access rights ○ Workflow for change requests (approvals) ○ Backups/data storage ○ Data migration and validation procedures • System flows for CECL processes → highlight key control points and link to SOX/Data Management processes

Key Takeaways

Operating principles of CECL program



Questions?



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