CAN THE CALL REPORT BE USED ALONE TO GENERATE CECL?

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CECL COUNTDOWN SERIES

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CECL AND CALL REPORTS

The Financial Accounting Standards Board (FASB) issued the Current Expected Credit Losses methodology (CECL), a new accounting standard for estimating allowances for credit losses. This new accounting standard applies to all banks, credit unions, and savings associations that file regulatory reports, which conform to the Generally Accepted Accounting Principles (GAAP) of the US. The FASB introduced CECL so that financial institutions are better equipped to tackle any situation similar to the global financial crisis. CECL replaces the incurred loss methodology and instead relies on estimating expected credit losses using various methods. These methods need historical and other data to process CECL estimates so that banks can maintain enough allowance to account for any expected credit losses. The data that is required for CECL can come from the one maintained by banks internally and also through call reports.

What are call reports?

A call report is a regulatory document that American banks are required to submit to the Federal Deposit Insurance Corporation (FDIC) on a quarterly basis. By comparing several call reports, it is possible to gather information about the health of the US banking system. A call report comprises information about the bank's financial health.

- Call reports are quarterly financial condition reports sent to the FDIC by the US banks.
- The bank's management must approve and verify the report's contents.
- The size of the bank, and the capital standards applicable to it, decide its specific reporting requirements.

The call report contains several data, which are an indicator of the reporting bank’s viability. Items within the call report include:

- Bank's income statement
- Loan information
- Deposit information
- Balance sheet investment information
- Asset sale information
- Changes in the bank's capital

Call report submission

Financial institutions file their call reports with the Federal Financial Institutions Examination Council (FFIEC). The public can access these reports on the Federal Insurance Deposit Commission website. Call reports are used by the banking industry to find out loss information for historical periods. Future expected credit losses are then predicted using this information.

Call report limitations

But is the data contained in the call report sufficient to arrive at accurate CECL results? Several other factors influence CECL calculations that institutions need to consider to arrive at precise CECL results. These aspects are as under:

1. Historical pattern in lifetime losses derived from call reports is not sufficient to arrive at accurate CECL results. We need the right economic indicator data to predict CECL allowances.

2. As compared to public data sources such as call reports, the vintage or year of origination is an important data source for calculating credit losses. This vintage information, which is part of a bank's internal data, is used as part of the Vintage Analysis Methodology to estimate losses.

3. The Weighted-Average Remaining Maturity Method (WARM) calculates an average quarterly loss rate while estimating reserves under CECL. The WARM method uses the average quarterly loss rate to calculate the lifetime loss rate. Institutions that choose the WARM method should also use their internal data to subdivide portfolios by riskiness. This will help them come up with more accurate CECL results.

4. While call report data may be an important source for benchmark information, the calculation of historical loss rates should involve systematic analytical capabilities that compare various approaches. This result is then considered against qualitative adjustments and economic factors to estimate future reserve levels.

5. Besides historical information, CECL should consider reasonable forecasts of future events and current information along with prepayment estimates. Institutions can use various methods for estimating CECL, including probability of default/loss given default, historical loss rates, discounted cash flows, and roll-rates.

6. The analysis of how historical data measures against peer experiences and industry benchmarks is important and should be given due diligence in CECL.

7. Banks and other financial institutions should know the duration of their loans. They should factor in the categorization of these loans to estimate CECL and try not to be too dependent on call report data alone.

8. The vintage loss rate methodology for calculating CECL allowance has to ensure that the vintage pool must reflect the risk profile of loans in the pool. This is something that call reports do not address. We will have to resort to another methodology in the middle of a CECL reporting if we do not have a vintage pool to use anymore.

9. While using the WARM method, the portfolio has to be split based on riskiness. This is done so that we do not average away the risk and granularity that is supposed to be captured. Institutions, in their haste to arrive at quick and affordable CECL results, will end up using call report data, which fails to acknowledge portfolio-related factors such as granularity and riskiness. The inaccuracy of such CECL results will have severe and far-reaching consequences on institutional health.

Measuring CECL allowance accurately is a challenge for most financial institutions, and this is especially true for smaller establishments. To estimate lifetime losses, a number of different factors need to be considered. Qualitative adjustments can be made by comparing related economic indicators with historical periods of loss data. Banks must use both external and internal data for their model-based approaches while calculating CECL.

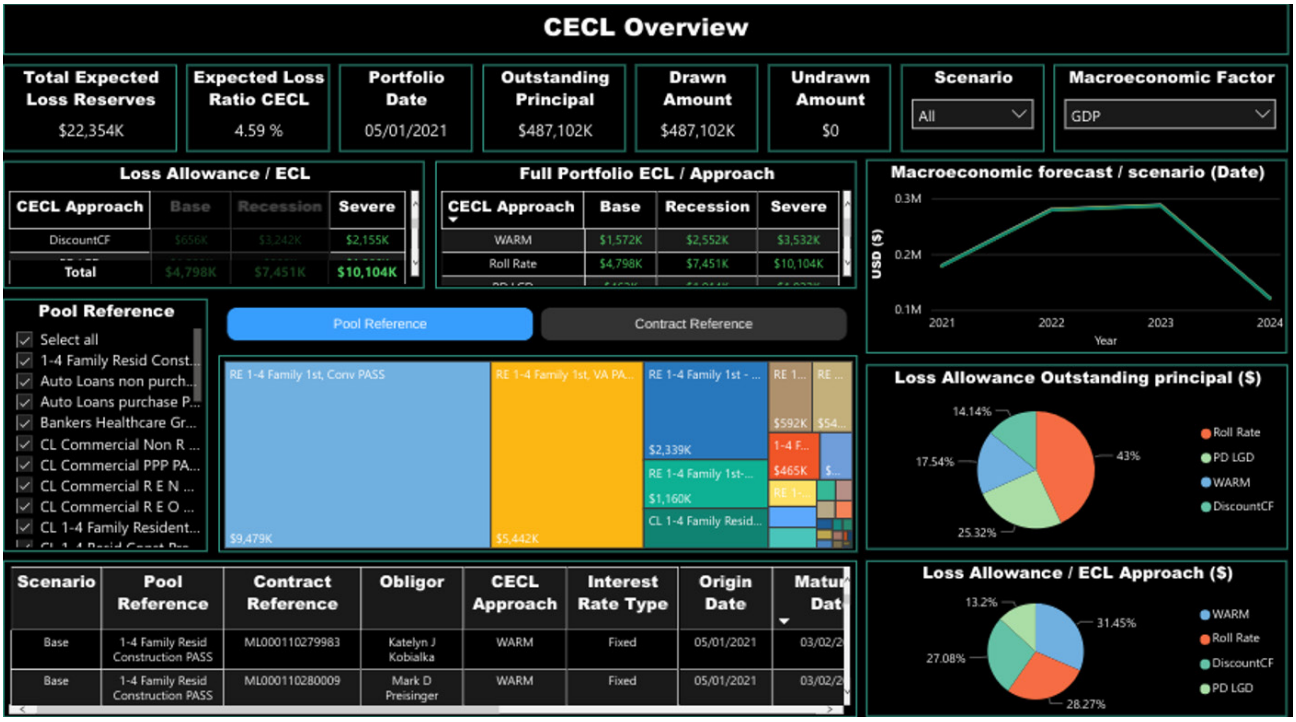
CECL Express can help...

CECL Express is a turnkey solution that fully satisfies all elements of the new CECL accounting standard. The system provides all non-loan data, including:

- Yield curves and Fed data
- Linked reports on losses from the FFIEC and NCUA
- PD and LGD curves
- Macroeconomic data

Banks and credit unions need to only provide the underlying loan details for the system to provide fully auditable ECL results for multiple calculation methods, including:

- Vintage
- Roll Rate
- Discounted Cashflow
- WARM
- PD/LGD



CECL Express provides more than valid ECL results. The system computes results for all methods and all loan pools, allowing the bank to optimize its CECL configuration and avoid the worst impacts of the new standard.

Visit ceclexpress.com for more information about the most efficient route to optimal CECL compliance.

CECL COUNTDOWN SERIES

ABOUT
CECL EXPRESS

- CECL Express is a turnkey, cloud-based solution, designed to provide banks and credit unions with optimized results and reporting that fully meet the 'Current Expected Credit Loss' accounting standards.
- CECL represents a major change in what is expected from financial institutions in their reporting of, and provisioning against potential credit losses.
- Smaller financial institutions are expected to implement forward-looking credit models to estimate losses they may experience.
- Selecting inappropriate 'Expected Credit Loss' (ECL) models will create a need to hold far more capital than is required, directly causing a loss of Profit and Loss (P&L). Data used within these models must also be reported for audit purposes.
- January 2023 will see the first official reporting period for the beginning of CECL. Banks and credit unions must have a framework in place, which is fully tested and reports results based on that data. In practice, this means selecting, implementing, and testing the system in the first half of 2022.
- For Finastra core systems, the integration has already been built. For customers with these systems, their CECL results are ready to be calculated and reported.

GreenPoint> Financial

ABOUT
GREENPOINT FINANCIAL

- GreenPoint Financial is a division of GreenPoint Global, which provides software-enabled services, content, process and technology services, to financial institutions and related industry segments.
- GreenPoint is partnering with Finastra across multiple technology and services platforms.
- Founded in 2006, GreenPoint has grown to over 500 employees with a global footprint. Our production and management teams are in the US, India, and Israel with access to subject matter experts.
- GreenPoint has a stable client base that ranges from small and medium-sized organizations to Fortune 1000 companies worldwide. We serve our clients through our deep resource pool of subject matter experts and process specialists across several domains.
- As an ISO certified company by TÜV Nord, GreenPoint rigorously complies with ISO 9001:2015, ISO 27001:2013, and ISO 27701:2019 standards.

Marcus Cree

MANAGING DIRECTOR AND
HEAD OF FINANCIAL TECHNOLOGY AND SERVICES

Marcus has spent 25 years in financial risk management, working on both the buy and sell side of the industry. He has also worked on risk management projects in over 50 countries, gaining a unique perspective on the nuances and differences across regulatory regimes around the world.

As Managing Director, Marcus heads GreenPoint Financial Technology and Services and has been central in the initial design of GreenPoint products in the loan book risk area, including CECL and sustainability risk. This follows his extensive experience in the Finastra Risk Practice and as US Head of Risk Solutions for FIS. Marcus has also been a prolific conference speaker and writer on risk management, principally market, credit and liquidity risk. More recently, he has written and published papers on sustainability and green finance.

Marcus graduated from Leicester University in the UK, after studying Pure Mathematics, Phycology and Astronomy. Since graduation, Marcus has continually gained risk specific qualifications including the FRM (GARP's Financial Risk Manager) and the SCR(GARP's Sustainability and Climate Risk). Marcus's latest academic initiative is creating and teaching a course on Green Finance and Risk Management at NYU Tandon School of Engineering.

Sanjay Sharma, PhD

FOUNDER AND CHAIRMAN

Sanjay provides strategic and tactical guidance to GreenPoint senior management and serves as client ombudsman. His career in the financial services industry spans three decades during which he has held investment banking and C-level risk management positions at Royal Bank of Canada (RBC) Goldman Sachs, Merrill Lynch, Citigroup, Moody's, and Natixis. Sanjay is the author of "Risk Transparency" (Risk Books, 2013), Data Privacy and GDPR Handbook (Wiley, 2019), and co-author of "The Fundamental Review of Trading Book (or FRTB) - Impact and Implementation" (Risk Books, 2018).

Sanjay was the Founding Director of the RBC/Hass Fellowship Program at the University of California at Berkeley and has served as an advisor and a member of the Board of Directors of UPS Capital (a Division of UPS). He has also served on the Global Board of Directors for Professional Risk International Association (PRMIA).

Sanjay holds a PhD in Finance and International Business from New York University and an MBA from the Wharton School of Business and has undergraduate degrees in Physics and Marine Engineering. As well as being a regular speaker at conferences, Sanjay actively teaches postgraduate level courses in business and quantitative finance at EDHEC (NICE, France), Fordham, and Columbia Universities.