Credit Union National Association
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December 16, 2019

Mr. Gerard Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

Re: Interagency Policy Statement on Allowances for Credit Losses; RIN 3133–AF05

Dear Mr. Poliquin:

On behalf of America's credit unions, I am writing the National Credit Union Administration (NCUA) regarding the proposed interagency policy statement on allowances for credit losses (Proposed Statement). The Credit Union National Association (CUNA) represents America's credit unions and their 115 million members.

Proposed Statement on Allowances for Credit Losses

The NCUA, Office of the Comptroller of the Currency, Federal Reserve Board, and Federal Deposit Insurance Corporate (the agencies) have issued a Proposed Statement in response to changes to U.S. generally accepted accounting principles (GAAP) as promulgated by the Financial Accounting Standards Board (FASB) in Accounting Standards Update 2016–13, *Financial Instruments—Credit Losses* (Topic 326), which includes the current expected credit loss (CECL) methodology. Specifically, the Proposed Statement addresses:

- Supervisory expectations for designing, documenting, and validating expected credit loss estimation processes;
- Maintenance of appropriate allowances for credit losses (ACLs);
- Responsibilities of boards of directors and management; and
- Examiner reviews of ACLs.

In addition, the Proposed Statement would incorporate relevant aspects of existing guidance, which would then be rescinded.

Request for Comment

In general, the Proposed Statement appears reasonable and seems to comport with the requirements of Topic 326, including CECL. We also appreciate the flexibility provided in the Proposed Statement.

In addition to answering the following questions asked by the agencies, we provide additional comments below.

Does the Proposed Statement clearly describe the measurement of expected credit losses under CECL?

> We generally believe the Proposed Statement clearly describes the measurement of expected credit losses under CECL. However, as noted below, there are a few areas where credit unions could benefit from additional clarity.
>
> *Measurement of ACLs for Loans, Leases, Held-to-Maturity Debt Securities, and Off-Balance-Sheet Credit Exposures:*
>
> We particularly appreciate that under *Reasonable and Supportable Forecasts,* the Proposed Statement clearly states that management is not required to "incur undue cost and effort to collect data for its forecasts."[1]
>
> As noted in the Proposed Statement, historical loss information generally provides a basis for an institution's assessment of expected credit losses. However, there appears to be some ambiguity in instances where there are no historical losses, no industry data, and/or no internal data, such as lower credit, higher loan-to-value or exceptions, or anything qualitative that would support recording a loss. Therefore, we ask the agencies to review this section to see how it can be further clarified in such instances.

Does the Proposed Statement clearly communicate supervisory expectations for designing, documenting, and validating expected credit loss estimation processes, internal controls over ACLs, and maintaining appropriate ACLs?

> Yes, we believe the Proposed Statement clearly communicates supervisory expectations for designing, documenting, and validating expected credit loss estimation processes, internal controls over ACLs, and maintaining appropriate ACLs.
>
> *Analyzing and Validating the Overall Measurement of ACLs:*
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> After analyzing ACLs, the Proposed Statement requires management to periodically validate the loss estimation process to confirm that the process remains appropriate for the institution's size, complexity, and risk profile. The Proposed Statement requires the review to be conducted by an independent party and provides flexibility on who is considered independent, such as someone from internal audit staff, a risk

[1] 84 Fed. Reg. 55,515 (Oct. 17, 2019).

management unit of the institution independent of management supervising these processes, or a contracted third-party. Further, one party would not necessarily need to perform the entire analysis as the validation may be divided among various independent parties.

We agree with the importance of utilizing an individual for review who is independent of the institution's credit approval and ACL estimation processes. Further, we appreciate the Proposed Statement's flexibility regarding the individual conducting the review, as long as the individual is independent of management overseeing the process. While this is easier for larger credit unions with more resources, segregation of duties may be more difficult for smaller credit unions. This could result in a smaller credit union being required to utilize an external third-party review, which could result in additional costs. Again, while we recognize the importance of independence, we ask the NCUA to consider flexibility as it relates to smaller credit unions that may have difficulty achieving such independence in-house.

Examiner Review of ACLs:

We support the Proposed Statement's acknowledgement that examiners' review of ACLs, including the depth of the examiner's assessment, be commensurate with the institution's size, complexity, and risk profile.[2] We believe this is a critical component given the variety of charter type, membership composition, geographical location, and asset size of credit unions, making it that much more important that examiner review be commensurate with the uniqueness of the credit union.

Further, we support the Proposed Statement's recognition that when assessing the appropriateness of ACLs, examiners should recognize that the process, loss estimation methods, and underlying assumptions an institution uses to calculate ACLs require the exercise of a substantial degree of management judgement.[3] We believe the importance of allowing significant judgement by management in determining ACLs cannot be understated. The process can be highly individualized and very unique to the reporting entity.

<u>Has the Proposed Statement appropriately included concepts and practices included in existing ALLL guidance that also are relevant under Topic 326?</u>

Yes, we believe the Proposed Statement appropriately includes concepts and practices included in existing ALLL guidance that also are relevant under Topic 326.

Specifically, upon adoption of the Proposed Statement, the following policy statements would be rescinded and therefore no longer effective:

[2] 84 Fed. Reg. 55,521.
[3] 84 Fed. Reg. 55,522.

- The agencies' December 2006 Interagency Policy Statement on the Allowance for Loan and Lease Losses;
- The banking agencies' July 2001 Policy Statement on Allowance for Loan and Lease Losses Methodologies and Documentation for Banks and Savings Institutions; and
- The NCUA's May 2002 Interpretive Ruling and Policy Statement (IRPS) 02–3, Allowance for Loan and Lease Losses Methodologies and Documentation for Federally Insured Credit Unions.

Again, we believe the Proposed Statement properly incorporates relevant aspects of the existing guidance, including NCUA's 2002 IRPS. We appreciate the agencies retaining the parts of the 2002 IRPS that continue to be applicable in light of Topic 326.

Additional Comments

We have concern that the Proposed Statement could unintentionally stray from pure GAAP and spill into the area of regulatory accounting principles (RAP). We recognize and appreciate the agencies' comment that the Proposed Statement conforms to GAAP and is wholly consistent with Topic 326.[4] While, in our review, we did not observe any departures from GAAP, we ask the NCUA and the other agencies to ensure the statement and any supplemental material remain GAAP and GAAP alone. Further, we suggest the agencies state explicitly in the preamble to the final statement that all aspects of the statement are grounded in GAAP.

In addition, we urge the NCUA to recognize that credit unions—in addition to other reporting entities—are in the very early stages of understanding what CECL means for them and how to implement changes necessary for compliance. Therefore, we request the NCUA continue to be proactive in its outreach to credit unions in terms of examinations and guidance. While credit unions will not be examined in the context of CECL for a few years, the agency has been seeking input from credit unions during examinations to understand where they are in the process and to determine any areas that may be particularly problematic as credit unions work to come into compliance. We urge the NCUA to continue such outreach as well as increase its focus on compliance resources specific to credit unions.

[4] "The agencies are maintaining conformance with GAAP and consistency with FASB ASC Topic 326 through their issuance of the proposed Interagency Policy Statement on Allowances for Credit Losses." 84 Fed. Reg. 55,512.

Conclusion

On behalf of America's credit unions and their 115 million members, thank you for the opportunity to share our comments on the Proposed Statement. If you have questions about our comments, please do not hesitate to contact me at (202) 508-6743.

Sincerely,

[redacted]

Luke Martone
Senior Director of Advocacy & Counsel