BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D.C. 20551

DIVISION OF BANKING
SUPERVISION AND REGULATION

SR 16-12

June 17, 2016

TO THE OFFICER IN CHARGE OF SUPERVISION AT EACH FEDERAL RESERVE BANK

SUBJECT: Interagency Guidance on the New Accounting Standard on Financial Instruments – Credit Losses

Applicability: This guidance applies to all Federal Reserve supervised financial institutions, including those with $10 billion or less in consolidated assets, that file regulatory reports prepared in accordance with generally accepted accounting principles (GAAP).

The Federal Reserve, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Office of the Comptroller of the Currency (agencies) are issuing the attached joint statement to provide supervised institutions[1] with initial information and supervisory views on the new accounting standard for credit losses recently issued by the Financial Accounting Standards Board (FASB). The new accounting standard, Accounting Standards Update No. 2016-13, *Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments*, replaces the existing incurred losses methodology for estimating allowances with a current expected credit losses methodology (CECL). It also allows a financial institution to leverage its current internal credit risk systems as a framework for estimating expected credit losses. The new standard will not be effective until 2020 for institutions that are required to file financial statements with the U.S. Securities and Exchange Commission or the appropriate federal financial institution regulatory agency under the federal securities laws, and 2021 for all other institutions (with early adoption allowed in 2019). The agencies encourage financial institutions to begin planning for implementation and ensure that appropriate staff work closely with their senior management and board of directors during the transition.

While the standard applies to institutions of all asset sizes, the agencies believe the new accounting standard can be implemented in a manner appropriate to an institution's asset size and complexity. Similar to the existing incurred losses model, the new accounting standard does not prescribe the use of specific estimation methods. The new standard allows institutions to apply judgment in developing estimation methods that are appropriate and practical for their

[1] For the Federal Reserve, this includes state member banks, bank and savings and loan holding companies, Edge and agreement corporations, and U.S. branches and agencies of foreign banking organizations.

circumstances. The agencies do not expect that smaller and less complex institutions will need to implement complex modeling techniques.

Until the effective date of the new accounting standard, institutions should continue using the incurred losses model to estimate allowances as required by current accounting standards.[2] That said, the change to an institution's expected losses methodology may impact its retained earnings and, thus, regulatory capital. Therefore, institutions are encouraged to plan for the potential impact on capital in advance of the new standard's effective date.

Reserve Banks are asked to distribute this letter to the supervised organizations in their districts and to appropriate supervisory staff. Questions regarding this letter should be directed to Shuchi Satwah, Senior Accounting Policy Analyst, at (202) 912-4620 in the Division of Banking Supervision and Regulation. In addition, institutions may send questions via the Board's public website.[3]

Michael S. Gibson
Director

Attachment:

- *Joint Statement on the New Accounting Standard on Financial Instruments – Credit Losses*

Cross Reference to:

- SR 13-19, "Guidance on Managing Outsourcing Risk"

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[2] Please refer to the table and discussion in the joint statement for details on the effective dates for the new standard.

[3] See http://www.federalreserve.gov/apps/contactus/feedback.aspx.