

# CECL for Nonprofits

November 30, 2023

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# With You Today



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# Learning Objectives

At the end of this program, participants will be able to

- ▶ Describe key provisions of the new expected credit losses model
- ▶ Contrast the guidance with existing GAAP and identify the impact on operations and financial reporting for nonprofits
- ▶ Understand the adoption considerations your clients should be addressing

# Agenda for Today

1

Overview of Topic 326

2

Scope of Topic 326

3

Summary of Major Changes under CECL

4

CECL Examples

5

Discussions and Planning for Implementation

6

Recap

# Financial Instruments

Credit Losses (Topic 326) Overview



## FINANCIAL INSTRUMENTS

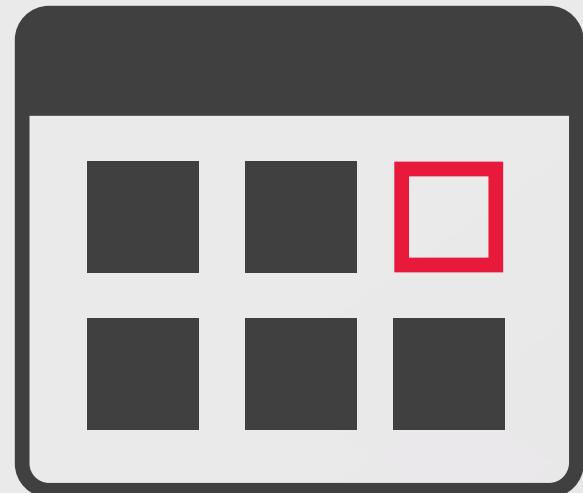
# Credit Losses (Topic 326)

- ▶ Issued to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by an entity.
- ▶ Changes the impairment model for most financial assets that are measured at amortized cost and certain other instruments from an incurred loss model to an expected loss model.
- ▶ Entities will be required to estimate credit losses over the entire contractual term of an instrument.
- ▶ The ASU includes financial assets recorded at amortized cost basis such as loan receivables, trade and certain other receivables as well as certain off-balance sheet credit exposures such as loan commitments and financial guarantees.
- ▶ The ASU does not apply to financial assets measured at fair value, promises to give (pledges receivable) and loans and receivables between entities under common control.
- ▶ Subsequently, the FASB issued ASU 2018-19, ASU 2019-04, ASU 2019-05 and 2019-10, 2019-11, 2020-02 and 2022-02 to clarify and improve ASU 2016-13.



## Credit Losses (Topic 326)

- ▶ The ASU is effective for fiscal years beginning after December 15, 2022 for all nonprofit entities.
- ▶ Thus 12/31/23 year ends entities should have done this already as we will discuss the fact they need to calculate the effect of CECL at 1/1/23 and at 12/31/23.
- ▶ An entity must apply the amendments in the ASU through a cumulative-effect adjustment to net assets as of the beginning of the first reporting period in which the guidance is effective except for certain exclusions.
- ▶ Early adoption could have been selected for fiscal years beginning after December 15, 2018.

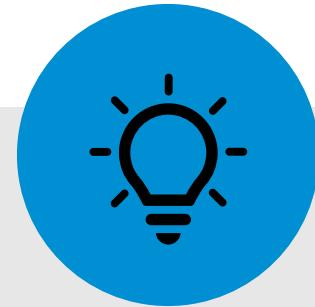


# Polling Question 1



## Fill in the Blanks

CECL applies to \_\_\_\_\_ and must be implemented for nonprofit organizations \_\_\_\_\_.



- A. Public companies only; never
- B. All entities; years beginning after December 15, 2022.
- C. All entities; years beginning after December 15, 2023

## Polling Question 1 - Answer



### Fill in the Blanks

CECL applies to \_\_\_\_\_ and must be implemented for nonprofit organizations \_\_\_\_\_.



- A. Public companies only; never
- B. All entities; years beginning after December 15, 2022.**
- C. All entities; years beginning after December 15, 2023

# Scope of Topic 326



# NFP CECL In Scope/Out of Scope Instruments

## GENERALLY

Loans and debt instruments not measured at fair value through net income

Trade receivables and contract assets recognized under ASC 606

Certain lease receivables

Financial guarantee contracts and loan commitments

Tuition Receivables



## Not in Scope

Contributions receivable (pledges), most grants receivable (if following the contribution model)

# Items in the Scope of CECL

## ALL ENTITIES

Item	Nature
Loan Receivables/Notes Receivable	Financial assets measured at amortized cost
Held-to-maturity debt securities	Financial assets measured at amortized cost
Trade receivables and contract assets that result from revenue transactions or other income	Financial assets measured at amortized cost
Receivables that relate to repurchase agreements and securities lending agreements	Financial assets measured at amortized cost
Loans to officers and employees	Financial assets measured at amortized cost
Cash equivalents	Financial assets measured at amortized cost
Receivables arising from time-sharing activities	Financial assets measured at amortized cost
Receivables resulting from sales-type or direct financing leases	Net investments in leases recognized by a lessor
Loan commitments, standby letters of credit, financial guarantees, and other similar instruments	Off-balance-sheet credit exposures not accounted for as insurance or derivatives
All reinsurance recoverables, regardless of the measurement basis of those recoverables	Reinsurance recoverables

# Out of Scope Items under CECL

## ALL ENTITIES

Financial assets  
where fair value  
option elected  
(ASC 820)

Operating lease  
receivables (ASC  
842, ASU 2018-19  
clarified)

Equity securities  
(ASC 321)

Equity method  
investments  
(ASC 323)

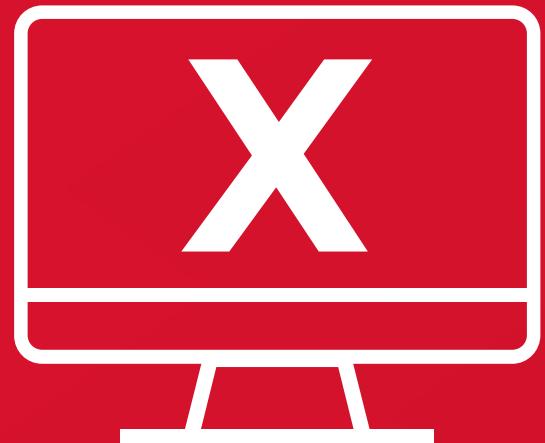
Derivatives  
(ASC 815)

Loans made to  
participants by  
defined contribution  
employee benefit  
plans (ASC 962)

Policy loan  
receivables of an  
insurance entity  
(ASC 944)

Related party loans  
and receivables  
between entities  
under common  
control

Pledge receivables  
of a not-for-profit  
entity



# Summary of Major Changes under CECL



# Objective

Reduce amortized cost to amount expected to be collected via valuation account

Expected credit losses shall be measured over

- ▶ Contractual term, considering estimated payments
- ▶ Contractual term shall not be extended for
  - Expected extensions and renewals

No minimums or triggering events

Not required to record a loss when the risk of nonpayment is zero



# Primary Changes in the New CECL Model

The Current Expected Credit Loss (“CECL”) Model creates three significant shifts from the current incurred loss model:

## FORWARD LOOKING ANALYSIS

Which requires the utilization of future information, and supportable forecasts to estimate allowance for loan and lease losses (“ALLL”) levels

## REMOVES “PROBABLE” THRESHOLD

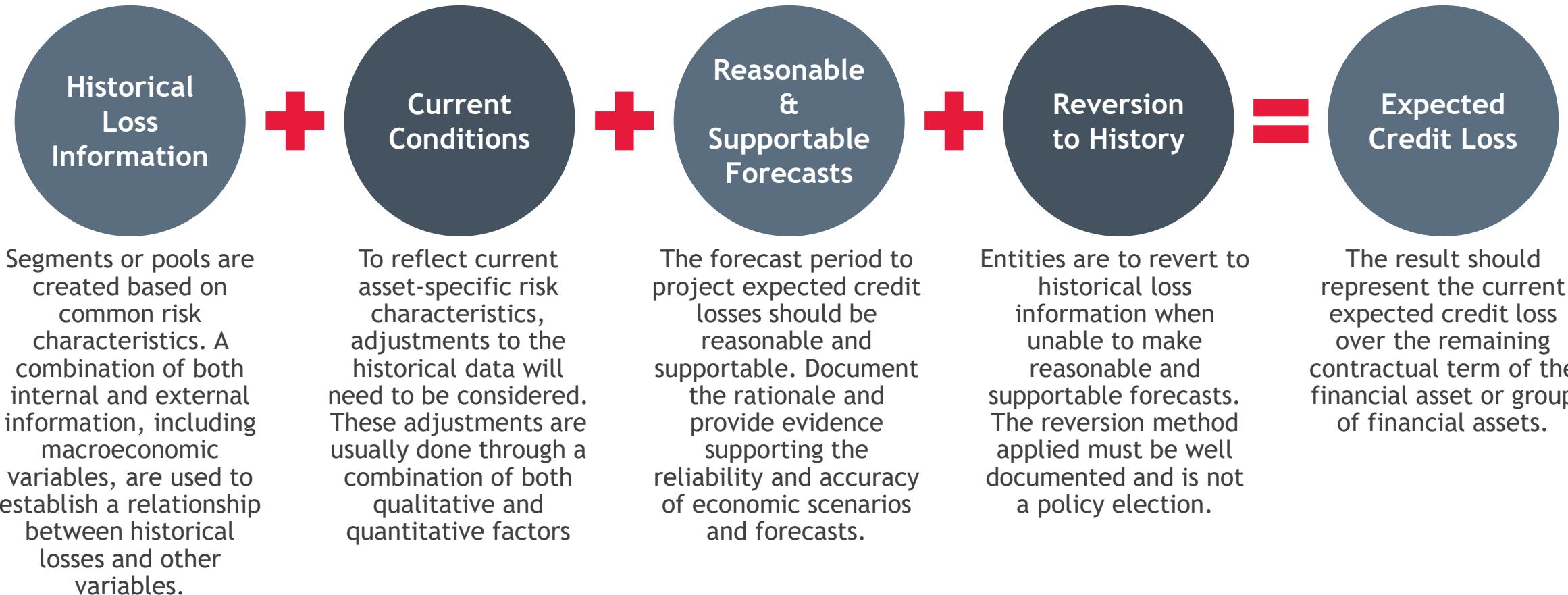
Which requires you to forego worst-case and best-case scenario and evaluate the possibility that a loss exists or does not exist

## LOSS HORIZON CHANGES

From the current 12 to 18-month horizon to the lifetime of the asset. This is broadly expected to expand the horizon used for estimating the ALLL.

# Implementation of CECL

## THE NEW CECL MODEL



## Information to Consider

CECL requires estimates of expected credit losses based on internally and externally available information

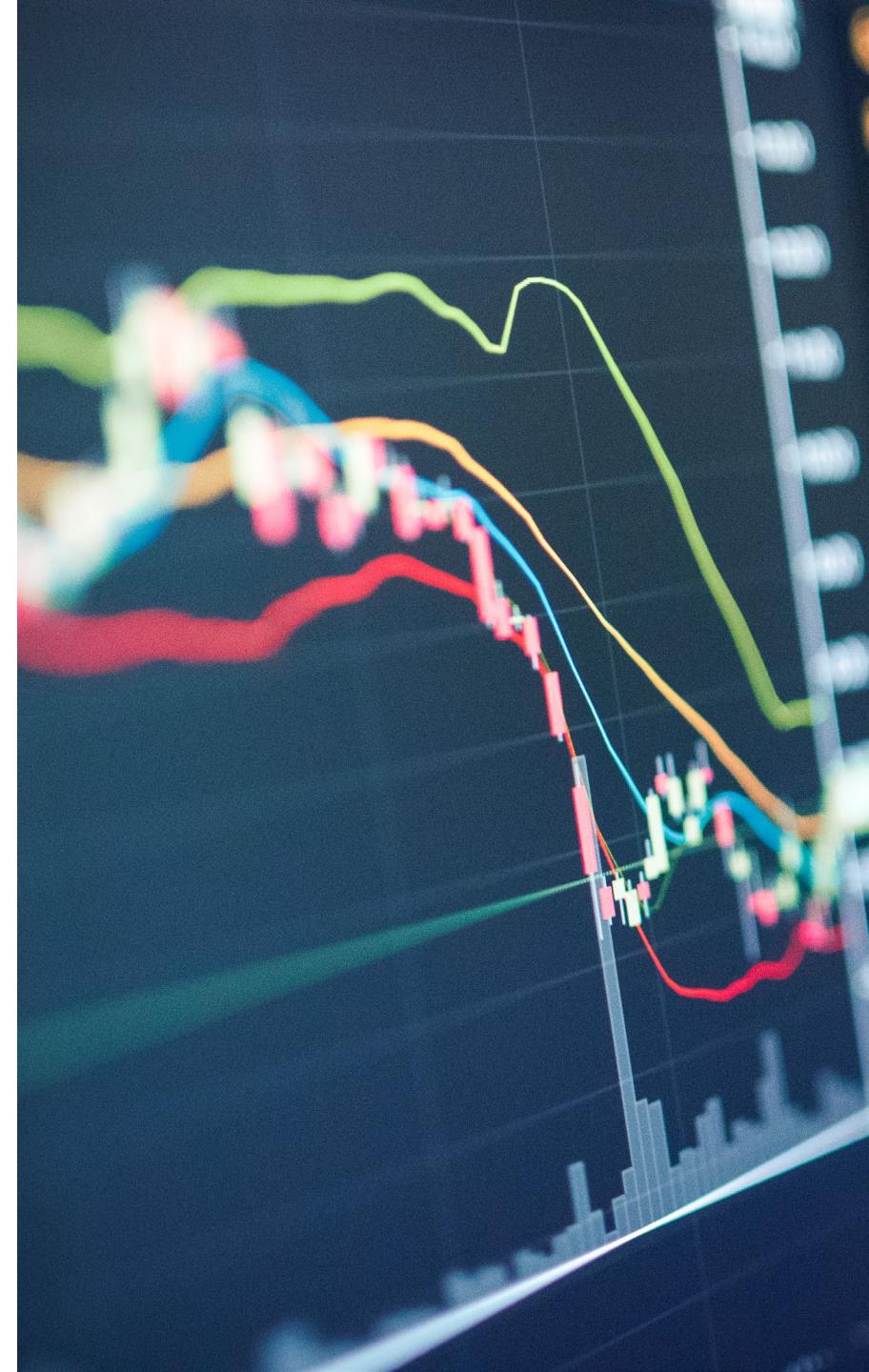
- ▶ Past events
- ▶ Current conditions
- ▶ Reasonable and supportable forecasts - cannot solely rely on past events
  - Qualitative and quantitative factors specific to borrowers and the economy
- ▶ Reversion - beyond reasonable and supportable period revert to historical loss experience

CECL does not mandate specific approaches or policy decisions to determine expected credit losses



## Information to Consider

- ▶ Credit losses should be evaluated on a pooled basis based on similar risk characteristics
- ▶ Financial assets without similar risk characteristics should be evaluated individually
- ▶ Cannot be included in both
- ▶ Need to reassess at each reporting period



# Recoveries

- ▶ Should include recoveries when estimating the allowance.
- ▶ Expected recoveries of previous amounts written off and expected to be written off
  - should be included in the reserve and
  - should not exceed the aggregate of amounts previously written off and expected to be written off by the entity
- ▶ Collateral dependent financial assets - an allowance for that is added to the amortized cost basis should not exceed amounts previously written off



# CECL Implementation Overview

## ASC 326-20 (CECL MODEL)

Under the CECL model, entities will estimate credit losses over the entire contractual term of the instrument (considering estimated prepayments, but not expected extensions or modifications unless the extension or renewal option are included in the original or modified contract terms and are not unconditionally cancellable) from the date of initial recognition of that instrument.

KEY CHANGES		
	EXISTING GUIDANCE	NEW CECL MODEL
WHEN TO RECOGNIZE CREDIT LOSSES	When probable that loss has been incurred, generally subsequent to initial recognition of the asset	When losses are expected, in almost all cases upon initial recognition of the asset
PERIOD TO CONSIDER	Not an explicit input to the incurred loss model	Contractual term
INFORMATION TO CONSIDER	Historical loss and current economic conditions	Historical loss, current economic conditions, reasonable and supportable forecasts about future conditions (with reversion to historical loss information for future periods beyond those that can be reasonably forecast)
UNIT OF ACCOUNT	Pooling generally not required, but permitted	Pooling required when assets share similar risk characteristics

## Polling Question 2



What are the elements of the CECL model that organizations must factor into their determination of the allowance for credit losses?

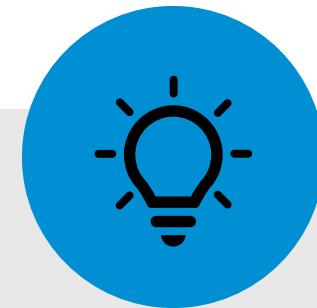


- A. Weighted average historical amounts and inflation
- B. The zero-loss model
- C. Historical loss information, current conditions, reasonable and supportable forecasts, and reversion to history (when applicable)

## Polling Question 2 - Answer



What are the elements of the CECL model that organizations must factor into their determination of the allowance for credit losses?



- A. Weighted average historical amounts and inflation
- B. The zero-loss model
- C. **Historical loss information, current conditions, reasonable and supportable forecasts, and reversion to history (when applicable)**

# Asset Segmentation

Asset segmentation is based on any one or a combination of the following risk characteristics

- ▶ Credit score or credit ratings
- ▶ Asset type
- ▶ Historical credit loss patterns
- ▶ Expected credit loss patterns
- ▶ Collateral type
- ▶ Size
- ▶ Effective interest rate
- ▶ Risk ratings or classification
- ▶ Borrower's industry
- ▶ Term
- ▶ Geographical location
- ▶ Reasonable and supportable forecast periods

(This list is not intended to be all inclusive)



## Zero Risk of Loss Vs. Remote Risk of Loss

Zero risk of loss - No reserve required when no history of loss and no expectation of nonpayment.

- ▶ U.S. Treasury securities
- ▶ Cannot assume zero loss if asset is secured by collateral and collateral value exceeds amortized cost basis. (Except for practical expedients)

An entity's estimate of expected credit losses should include a measure of the expected risk of credit loss **even if that risk is remote**, regardless of the method applied to estimate credit losses.

The FASB concluded that a 'bright-line' approach would be inappropriate for all facts and circumstances and decided not to provide explicit guidance on what specific assets are appropriate for zero credit losses.



IT WILL BE RARE TO HAVE  
ZERO RISK OF LOSS

# Disclosures

## Policy Disclosures

- ▶ Policy for charging off uncollectible debt instruments
- ▶ Changes to accounting policies or methodology from prior period
- ▶ Policy for accounting for nonaccrual financial assets

## Description of Estimate: How Expected Losses Are Developed

- ▶ Factors that influenced current estimate
- ▶ Changes in loss severity, portfolio composition, volume of assets
- ▶ Reasons for significant changes in amount of write-offs
- ▶ Collateral dependent - qualitative discussion of the type of collateral, extent to which collateral secures financial assets and any change that impacted how much collateral secures the asset

## Quantitative Disclosures

- ▶ Roll forward of the allowance for credit losses
- ▶ \*Disaggregation of class of financing receivable by vintage
- ▶ Reconciliation between purchase price and par value of Purchase Credit Deteriorated (PCD) assets

\* Disclosures apply to conduit bond obligors.

# CECL Examples

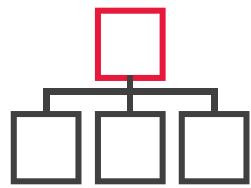


# Trade Receivables

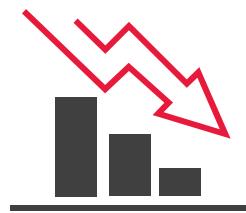


# Trade Receivables

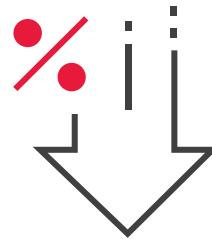
In general, the process for estimating life-of-trade receivables credit losses using an aging schedule can be summarized as follows:



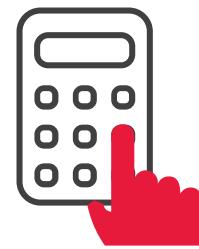
Pool receivables with similar risk characteristics



Consider whether historical loss rates need to be adjusted for asset specific characteristics



Adjust historical loss rates for current conditions and reasonable and supportable forecasts



Apply revised loss rates to the trade receivable balance to determine the CECL allowance

# Where Aggregation of Components Is Needed



CECL requires that trade receivables sharing similar risk characteristics be pooled.

Determine whether current segmentation practices for the aging analysis under the incurred loss model is consistent with the ASU's pooling requirement.

For instance, entity determines that it is appropriate to pool customers by geography (U.S., World), type (Corporate, Others) and Past Due Status (Aging Buckets).

Management could group the trade receivables similar to those in the following slides.

Apply the appropriate loss rate(s) determined under CECL to each of the pools/buckets to arrive at the allowance for credit losses.

# Trade Receivables



Entities typically apply an allowance for doubtful accounts based on historical losses by aging categories.

Under CECL, entities will have to consider whether such historical data requires adjustment, including upon recognition of the receivable.

Will likely result in recognition of allowance for credit losses for receivables that are not yet past due.

Individually significant balances with historical zero loss will most likely require a loss factor.

The standard applies to receivables that result from revenue transactions, even if a non-customer party will make the payment.

## TRADE RECEIVABLE EXAMPLE

### Using Aging Schedule

- ▶ Entity E provides services to their members. The members are homogenous and have the same risk characteristics. Members are provided with payment terms of 90 days.
- ▶ Entity E has tracked historical loss information for its trade receivables and compiled the following historical credit loss percentages
  - 0.3 percent for receivables that are current
  - 8 percent for receivables that are 1-30 days past due
  - 26 percent for receivables that are 31-60 days past due
  - 58 percent for receivables that are 61-90 days past due
  - 82 percent for receivables that are more than 90 days past due



## TRADE RECEIVABLE EXAMPLE

### Using Aging Schedule

- ▶ Entity E believes that this historical loss information is a reasonable basis to determine expected credit losses for trade receivables held at the reporting date because the risk characteristics of its members are similar and its credit practices have not changed significantly over time.
- ▶ However, Entity E has determined that the current and reasonable and supportable forecasted economic conditions have improved.
- ▶ Entity E has observed that unemployment has decreased as of the current reporting date, and Entity E expects there will be an additional decrease in unemployment over the next year.
- ▶ Entity E estimates the loss rate to decrease by approximately 10 percent in each age bucket.
- ▶ Entity E developed this estimate based on its knowledge of past experience for which there were similar improvements in the economy.



## TRADE RECEIVABLE EXAMPLE

### Using Aging Schedule

At the reporting date, Entity E develops the following aging schedule to estimate expected credit losses.

Past-Due Status	Amortized Cost Basis	Credit Loss Rate	Expected Credit Loss	
			Estimate	
Current	\$ 5,984,698	0.27%	\$ 16,159	
1–30 days past due	8,272	7.2%	596	
31–60 days past due	2,882	23.4%	674	
61–90 days past due	842	52.2%	440	
More than 90 days past due	1,100	73.8%	812	
	<u><u>\$ 5,997,794</u></u>		<u><u>\$ 18,681</u></u>	



## TRADE RECEIVABLE EXAMPLE

# Where Aggregation of Components Is Needed

Geography	Type	Current	1-30 days past due	31-60 days past due	61-90 days past due	>90 days past due
U.S.	Corporate	\$X	\$X	\$X	\$X	\$X
	Others	\$X1	\$X1	\$X1	\$X1	\$X1
World	Corporate	\$Y	\$Y	\$Y	\$Y	\$Y
	Others	\$Y1	\$Y1	\$Y1	\$Y1	\$Y1

## Polling Question 3



What are some examples of ways an organization might choose to pool financial assets measured at amortized cost?

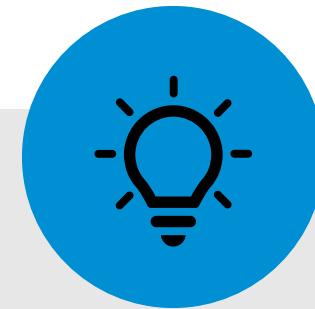


- A. Asset type, size, geographical location
- B. Pooling of financial assets measured at amortized cost is only required for public companies
- C. Pool all financial assets measured at amortized cost into a single pool

## Polling Question 3 - Answer



What are some examples of ways an organization might choose to pool financial assets measured at amortized cost?



- A. Asset type, size, geographical location**
- B. Pooling of financial assets measured at amortized cost is only required for public companies
- C. Pool all financial assets measured at amortized cost into a single pool

# Notes Receivable



## CONSIDERATIONS

### Notes Receivable

- ▶ Outside of a financial institution setting, entities may accept notes receivable as consideration for non-revenue transactions, such as the sale of assets
- ▶ Under the CECL model, a day-one allowance will be required
- ▶ Generally, cannot assume zero risk of loss



# Contract Assets



# Contract Assets

- ▶ Contract assets under ASC 606 represent an entity's conditional right to consideration for goods or services it has provided if that right is conditioned on something other than the passage of time.
  - E.g., Nonprofits may have unbilled receivables which are contract assets related to billed receivables.
- ▶ Need to assess for impairment under CECL and incorporate reasonable and supportable forecasts.



# Commitments to Lend



# Commitments to Lend

- ▶ Estimate losses over contractual period of the commitment
- ▶ Consider likelihood of funding



- ▶ If there is an unconditional ability to cancel the unfunded portion, no estimate of losses is required even if there is no history of canceling the commitment



# Financial Guarantees



# Financial Guarantees

## At inception of a guarantee

- ▶ Guarantor continues to recognize guarantee liability (non-contingent stand-ready obligations) at fair value\*, AND
- ▶ CECL will require recognition of a liability for the expected credit losses on the guarantee (contingent losses).

## Subsequent measurement of guarantee

- ▶ Guarantee liability is amortized into revenue as guarantor is released from risk from the guarantee
- ▶ CECL liability is independently assessed each reporting period for the life of the guarantee
  - Two aspects to consider - likelihood to fulfill obligation and estimate of expected losses on the obligation. Consider recourse to obligor.

**Guarantee premium and credit loss provision are presented separately on the statement of activities.**

\*The guidance for financial guarantees is different for related parties under common control.



# Lessor's Net Investment in Sales-Type and Direct Financing Leases



## CONSIDERATIONS

# Lessor's Net Investment in Sales-Type and Direct Financing Leases

ASU 2018-19 has clarified that operating lease receivables are outside the scope of Topic 326.

Topics 326 and 842 require a CECL reserve on net investments in sales-type and direct financing leases, including the unguaranteed residual value.

- ▶ Consider collateral value at end of lease term - Represents the cash flow expected
- ▶ Discounted Cash Flows (DCF) method - use same discount rate used to measure the lease receivable
- ▶ CECL estimated considering both credit risk and non-credit risk (unguaranteed residual asset)



# Discussions and Planning for Implementation



# Implementation of CECL

**The transition requirements for the adoption of ASC 326 are as follows:**

- ▶ A cumulative effect adjustment shall be recorded to net assets without donor restrictions as of the beginning of the year of adoption to reflect the impact on the estimate for expected credit losses as of the adoption date versus the legacy accounting treatment for credit losses.
- ▶ Accounting policy election to maintain pools of financial assets previously accounted for under Subtopic 310-30 on an ongoing basis.
- ▶ Allow for entities to elect to use the fair value option under Subtopic 825-10 on an instrument-by-instrument basis for assets that are eligible for fair value election under Subtopic 825-10 but also otherwise within the scope of ASC 326.
- ▶ Accounting policy election on accrued interest and whether to bifurcate it from the associated loans for separate estimation of expected credit losses.
- ▶ ASC 326 does not provide an option to adopt the standard using a retrospective transition method as the FASB determined that it would be impracticable for entities to apply in prior periods because the use of hindsight would be necessary in making estimates of expected credit losses.

# Implementation of CECL

- ▶ Clients need to develop memos that outline their adoption and all their estimates and assumptions
- ▶ This needs to be performed both at the beginning of the year being adopted and the end of the year
- ▶ We need to audit the analysis



## OPERATIONAL CONSIDERATIONS

# The Primary Challenge

New model inherently integrates assumptions that appear to be more open to interpretation, and therefore could create less consistency in the sector, and possibly a less “auditable” or “supportable” result

- ▶ “Utilization of future information”
- ▶ “Supportable Forecast”
- ▶ “Evaluate the Possibility”
- ▶ Overall, more judgment involved



## Polling Question 4



Which of the following financial statement items are NOT scoped in for CECL?



- A. Trade receivables
- B. Notes receivable
- C. Pledge/Contributions receivable

## Polling Question 4 - Answer



Which of the following financial statement items are NOT scoped in for CECL?

- A. Trade receivables
- B. Notes receivable
- C. **Pledge/Contributions receivable**



# Let's Recap



# Historical Information



Can an entity's process for determining expected credit losses consider only historical information?

No, an entity should not rely solely on past events to estimate expected credit losses. When an entity uses historical loss information to forecast expected credit losses, it should **consider the need to adjust historical loss information** to reflect the extent to which management expects current conditions and reasonable and supportable forecasts to differ from the conditions that existed for the period over which historical loss information was evaluated. The adjustments, if needed, to historical loss information may be **qualitative or quantitative in nature** and should reflect changes related to relevant data. In addition, an entity should **consider adjustments to historical loss information for differences in current asset-specific risk characteristics**, such as underwriting standards, portfolio mix, or asset term within a pool at the reporting date. An entity also should consider whether historical loss information used covers a sufficient time period such that it reflects the term of the financial asset or group of financial assets.

# Historical Information



How should an entity determine which historical loss information to use when estimating expected credit losses?

In determining what historical loss period information best represents the financial assets (or pools within those assets), an entity **may use historical loss information that is nonsequential** (such as historical loss percentages based for each year since origination as opposed to an average 5-year historical loss percentage). The appropriate **historical loss period can vary between loan portfolios, products, pools, and inputs**. An entity should consider both the appropriate historical period and the appropriate length of the period when **developing those estimates**. An entity should **use judgment** in determining which period or periods to consider when determining which historical loss information is most appropriate for estimating expected credit losses. An entity **does not have to use historical losses from the most recent periods**. An entity should use historical loss information that is more reflective of the remaining contractual term of the financial assets for periods beyond the reasonable and supportable forecast period.

# Reasonable and Supportable Forecast Period in Relation to Contractual Term



Does an entity need to include the full contractual period (adjusted for prepayments) in its estimate of the reasonable and supportable forecast period?

No, some entities may be able to apply reasonable and supportable forecasts over the estimated contractual term (that is, the contractual term adjusted for prepayments). However, **the guidance does not require an entity to develop forecasts over the contractual term (adjusted for prepayments) of the financial asset or group of financial assets (paragraph 326-20-30-9).**

# Reasonable and Supportable Forecasts



Does the application of the word forecasts infer computer-based modeling analysis is required?

No, developing forecasts **does not require** an entity to perform computer-based modeling. Topic 326 allows a **quantitative or a qualitative adjustment** to be made when assessing current conditions and reasonable and supportable forecasts.

# Reasonable and Supportable Forecasts



If an entity's actual credit losses differ from its estimate of expected credit losses, is it required to modify its forecasting methodology?

Credit losses often **will not predict with precision actual future events**. The objective is for entities to present their best estimate of the net amount expected to be collected on financial assets. The standard does not require a specific loss method; rather, **an entity is required to use judgment** in determining the relevant information and estimation methods that are appropriate in its circumstances. There generally is a **range of reasonable outcomes** and, therefore, it's reasonable to see differences between estimates of expected credit losses and actual credit losses. Ultimately, estimates of future losses and actual losses should converge to the same amount. **An entity should continue to refine future estimates** of expected credit losses based on actual experience.

# Reasonable and Supportable Forecasts



May the length of reasonable and supportable forecast periods vary between different portfolios, products, pools, and inputs?

Yes, the duration or length of the **reasonable and supportable forecast period** is a **judgment** that may vary based on the entity's ability to estimate economic conditions and expected losses. The **reasonable and supportable forecast may vary between portfolios, products, pools, and inputs**. However, specific inputs (such as unemployment rates) should be applied on a consistent basis between portfolios, products, and pools, to the extent that the same inputs are relevant across products and pools. **It also is acceptable to have a single reasonable and supportable period for all of an entity's products.**

# Reasonable and Supportable Forecasts



Should an entity reevaluate its reasonable and supportable forecast period each reporting period?

Yes, an entity should consider the appropriateness of its reasonable and supportable forecast period, as well as other judgments applied in developing estimates of expected credit losses each reporting period. If the reasonable and supportable period does not cover the full expected contractual term (adjusted for prepayments), an entity should **consider the appropriateness of the duration of its reversion period** (that is, the periods beyond the reasonable and supportable period) and the **methodology applied** when reverting back to historical loss information.

# Reversion to Historical Loss Information



What should an entity do if it cannot forecast estimated credit losses over the entire contractual term (adjusted for prepayments)?

An entity is not required to develop forecasts over the entire contractual term (adjusted for prepayments) of the financial asset or group of financial assets. For periods beyond which the entity is able to make or obtain reasonable and supportable forecasts of expected credit losses, it is **required to revert to historical loss information** that reflects expected credit losses during the remainder of the contractual term (adjusted for prepayments) of the financial asset or group of financial assets. **Update 2016-13 does not require an entity to develop reasonable and supportable forecasts for the entire expected remaining life of a loan** (that is, contractual term adjusted for prepayments), such as a 30-year note receivable. The periods after the reasonable and supportable forecast periods are often referred to as the “reversion period” and “post-reversion period,” as applicable. When reverting to historical loss information, an entity should (1) **consider whether the historical loss information is still relevant to estimating expected credit losses** and (2) **not adjust historical loss information in the reversion period and post-reversion periods for existing economic conditions or expectations of future economic conditions.**

# Reversion to Historical Loss Information



Can an entity adjust the historical loss information used in the reversion period for existing economic conditions or expectations of future economic conditions when developing estimates of expected credit losses?

No, for periods beyond which an entity is able to make or obtain reasonable and supportable forecasts of expected credit losses, it **should revert to historical loss information** determined that reflects expected credit losses during the remainder of the contractual term (adjusted for prepayments) of the financial asset or group of financial assets. The entity **should not adjust historical loss information for existing economic conditions or expectations of future economic conditions** for periods that are beyond the reasonable and supportable period. However, this historical loss information **should be adjusted for differences in current asset-specific risk characteristics**. The reversion to an entity's historical loss information emphasizes the relevance of known loss experience that has occurred in the past on similar financial assets or groups of financial assets and addresses preparers' concerns about the reliability of estimating those credit losses in periods of declining precision.

# Reversion to Historical Loss Information



Is an entity required to revert to historical loss information on a straight-line basis?

No, although an entity is required to revert to historical loss information for periods that cannot be forecasted based on reasonable and supportable information, **there is no single methodology for reverting to historical loss information**. An entity may revert to historical loss information immediately on a straight-line basis or using another rational and systematic basis. In addition, the guidance permits an entity to apply different reversion methods for different inputs and asset classes. An entity should use judgment in determining which reversion technique is most appropriate at the reporting date. The reversion method is not a policy election but rather a component of the overall estimate of expected credit losses. Like other components used to measure expected credit losses, an entity should support the reversion methodology and period it uses to develop its estimates of expected credit losses. Additionally, reversion to historical loss information, whether immediately or on a straight-line basis or using another reasonable methodology, is required only for periods that cannot be forecasted based on reasonable and supportable information.

# Zero Risk of Loss vs. Remote Risk of Loss

## TREASURY SECURITIES

### Indicators for Zero Loss

- ▶ High credit rating by rating agencies
- ▶ Long history with no credit losses (adjusted for current conditions and reasonable and supportable forecasts)
- ▶ Explicitly fully guaranteed by a sovereign entity of high credit quality
- ▶ Widely recognized as a "risk-free rate"
- ▶ Can print its own currency which is routinely held by central banks, used in international commerce, and commonly viewed as a reserve currency

### Indicators for Loss > \$0

- ▶ Experience of a downgrade

# Resources



## CECL RESOURCES

### External

- ▶ [CECL for Non-Financial Institutions](#)
- ▶ [BDO Knows CECL: FASB Topic 326, Financial Instruments - Credit Losses](#)
- ▶ [BDO Knows CECL: Presentation and Disclosure](#)

These can be provided to clients for their use. There are other resources on [www.bdo.com](http://www.bdo.com) - just search “CECL” for all resources.



## About BDO USA

At BDO, our purpose is helping people thrive, every day. Together, we are focused on delivering exceptional and sustainable outcomes – for our people, our clients and our communities. Across the U.S., and in over 160 countries through our global organization, BDO professionals provide assurance, tax and advisory services for a diverse range of clients.

BDO is the brand name for the BDO network and for each of the BDO Member Firms. BDO USA, P.C., a Virginia professional corporation, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms.

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Material discussed is meant to provide general information and should not be acted on without professional advice tailored to your needs.

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