MORTGAGE BANKERS ASSOCIATION

November 19, 2018

The Hon. Steven T. Mnuchin
Chairman, Financial Stability Oversight Council
U.S. Department of the Treasury
1500 Pennsylvania Avenue, N.W.
Washington, D.C. 20220

**Re: Request for Delay of CECL Implementation Pending a Necessary Financial Stability Oversight Council (FSOC) Quantitative Study and Analysis of its Impact**

Dear Chairman Mnuchin:

The Mortgage Bankers Association (MBA)[1] is writing this letter to express concerns regarding the upcoming implementation of the "Current Expected Credit Loss" (CECL) accounting standard for the measurement of credit losses (Accounting Standards Update 2016-13) issued by Financial Accounting Standards Board (FASB). MBA believes that the requirements of the CECL standard, which is effective for SEC registrants in 2020, and for all other companies in 2021, will adversely impact the availability, structure and price of credit, with a larger proportion of such impact landing on longer-term loans, such as 30-year single-family residential mortgages, commercial and multifamily mortgages, student and business loans. CECL probably represents one of the most significant rewrites of U.S. GAAP in the past 40 years, and once implemented, will fundamentally change how banks and other financial companies recognize credit losses in their loan and held-to-maturity debt security portfolios. In contrast to the traditional U.S. GAAP approach, which required companies to establish a reserve when a loan loss is probable and reasonably estimable, CECL requires day-one upfront recognition of credit losses using long-term economic forecasts over the contractual life of the loan but does not allow a similar upfront recognition of corresponding future revenues associated with the loan.

MBA strongly recommends that the FSOC conduct a quantitative study on the overall impact of CECL implementation on the financial services industry, and pending the completion of such study, engage with FASB to request a delay in implementation. This

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets, to expand homeownership, and to extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,300 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies, and others in the mortgage lending field. For additional information, visit MBA's website: www.mba.org.

study is critical, as it will help the banking agencies as well as affected banks and non-banks understand the full impact, and all the unforeseen effects of the CECL standard, which creates new and challenging issues for financial companies specifically, and also for consumers and businesses in general.

While the goal of CECL was to establish an impairment model that would record credit loss reserves earlier and, therefore, reduce the level of pro-cyclicality[2] of the industry, the inherent unreliability of the long-term economic forecasting that is required by CECL will cause more harm than good, as it could actually cause more pro-cyclicality in the industry and increase the volatility of regulatory capital, necessitating increased capital at all times. A recent study[3] that demonstrates the pro-cyclicality of CECL indicates that the requirement of upfront charge to earnings for each loan originated will certainly have an adverse effect on the availability, structure and price of credit, thereby impacting lending activities. The spikes in allowances during times of economic stress caused by pro-cyclicality negatively impacts capital levels, which in turn adversely affects the cost and availability of credit. The result is that lenders will be less likely to make long-term loans or lend to borrowers with lower credit quality during stressed economic periods. Lenders will thus be under pressure to move away from longer-term individual or small-business lending (i.e., 30-year residential mortgages and commercial and multifamily mortgages), and focus more on structuring loans with shorter contractual terms.

For many MBA community bank members, more than 50% of their loan portfolios constitute residential mortgage products, and therefore, the unforeseen impact of CECL implementation on residential mortgage lending will have significant detrimental effects on these banks. In fact, according to a recent study on the impact of CECL on bank capital,[4] it was noted that many community banks may need to raise additional capital in order to maintain their "well capitalized" status and be in compliance under CECL on day one. This unforeseen impact of CECL, in addition to the fact that the heavy costs of implementation naturally hit smaller organizations the most, could result in costly and unintended adverse consequences for the community banking industry**.**

Despite a 2017 recommendation by the Treasury[5] for a study or analysis of CECL, we are not aware of any such formal study. It is very important for the U.S. economy that a study be conducted to analyze both the macroeconomic and public policy implications of CECL implementation, as well as to propose practical solutions to issues identified where

[2] See Financial Stability Forum, "Report of the Financial Stability Forum on Addressing Procyclicality in the Financial System" (April 2009); which states that "addressing procyclicality is an integral part of strengthening the macro prudential or systematic orientation of the regulatory and supervisory frameworks."
Available at http://www.fasb.org/wp-content/uploads/r_0904a.pdf

[3] Francisco Covas and William Nelson, "Current Expected Credit Loss: Lessons from 2007-2009," Bank Policy Institute, July 2018, *available at* https://bpi.com/wp-content/uploads/2018/07/CECL_WP-2.pdf (see Appendix A).

[4] See https://stonecastle.com/wp-content/uploads/2018/01/2017-12-18-CECL-and-Tier-2-Final.pdf

[5] Table of Recommendations (page 125) of the June 2017 U.S. Department of the Treasury report, "A Financial System That Creates Economic Opportunities – Banks and Credit Unions"

appropriate, well before the CECL implementation date. The study should not only focus on the overall potential impact of CECL – including potential reductions in economic activities and higher unemployment during economic downturns – but also assess how CECL would have affected regulatory capital leading up to and going through the recent recession. Given that the fundamental changes that are expected from CECL will impact financial companies, input from these stakeholders should be an essential part of this study.

The industry appreciates the fact that bank examiners will look to the "good faith" efforts of community banks in designing CECL systems, as well as efforts that have been made so far to understand the operational and capital challenges of implementing CECL. Nevertheless, many of the requirements of CECL pose very real and, in many cases, unidentified challenges and issues that could only be assessed and analyzed by a quantitative impact study initiative. We therefore strongly urge the FSOC to seek a delay in implementation pending the completion of a transparent quantitative impact study.

With a significant amount of input from the banking industry and other affected financial companies, the study should evaluate the impact of CECL on the stability of the financial services sector in general by analyzing how the requirements would affect the availability, accessibility, and affordability of credit throughout an economic cycle. Furthermore, the analysis should assess the capital and operational impact of the standard on smaller institutions, and especially how such impacts will affect their ability to compete and serve their communities. The study should propose solutions for identified negative or adverse impacts, and such solutions should be within existing liquidity, capital and accounting regulatory frameworks. Finally, the impacted industry (banks and other stakeholders) should be given an opportunity to review and react to the results and proposed solutions contained in the study before making the document final.

Thank you for your attention to this important matter**.** Please feel free to contact Fran Mordi at fmordi@mba.org or (202) 557-2860 if you have any questions, or require additional information on this issue.

Sincerely,

Robert D. Broeksmit, CMB
President and Chief Executive Officer
Mortgage Bankers Association