Current Expected Credit Losses (CECL)  
ASU 2016-13

EEI and AGA Corporate Accounting and Accounting Standards Committees  
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Overview of Guidance

**Effective Date**
- Fiscal years beginning after December 15, 2019 (for public business entities that are SEC filers)
- Fiscal years beginning after December 15, 2020 (for other public business entities)
- Fiscal years beginning after December 15, 2021 (for all other entities)

Objective is to increase transparency and improve financial reporting by requiring earlier recognition of credit losses for financial assets measured at amortized cost, net investment in leases recognized by a lessor, contract assets and certain off-balance sheet commitments.

**CECL Impairment Model:**
- Replaces the “incurred loss” impairment approach with an “expected loss” impairment approach to recognize credit losses.
- Requires entities to reflect the current estimate of expected credit losses using the life of the asset and eliminates the “probable” threshold for recognition.
- Historical write-offs may be used as a starting point for determining expected credit losses. However, entities must assess how conditions that existed during the historical write-off period may differ from current conditions and forecasted expectations.
- Does not prescribe a specific methodology to develop a reasonable & supportable forecast, the duration of the period losses that can be forecasted or the precision required.
- Any impact resulting from the adoption of CECL should be recognized through a cumulative effect adjustment to retained earnings.
Overview of Guidance (continued)

- **Available-for-Sale (AFS) Debt Securities Impairment Model:**
  - Replaces the concept of "other-than-temporary" impairment for AFS debt securities with the expected credit loss model which focuses on whether an impairment is the result of a credit loss (P&L) or other factors (OCI).
  - Limits credit losses to the amount that the fair value is less than the amortized cost basis.
  - Recoveries of impairment losses should be recognized immediately as a reduction to the allowance and credit loss expense.
  - Does not consider the length of time the fair value has been less than the amortized cost basis.
  - Requires credit losses to be recognized through an allowance account rather than as a reduction of the amortized cost basis.
Trade Accounts Receivable

Assessment of Current Allowance Approach

- Considerations:
  - Historical information
  - Current conditions
  - Reasonable & Supportable Forecasts

- Economic Downturns and Protracted Recessions
  - How did the 2008 – 2009 global financial crisis impact P&U companies’ write-offs?

- Potential Macroeconomic Factors to Consider:
  - Unemployment rate and claims
  - Personal disposable income
  - Housing price index

Unbilled Receivables

- Entities generally do not record reserves until receivables begin aging. However, under CECL, reserves are required to be recorded at the time unbilled revenue is recognized.

ASC 980

- Regulatory recovery considerations
Polling Question #1

- Does your company expect to significantly change its loss reserve methodology for customer accounts receivable with the implementation of ASU 2016-13?
  - Yes
  - No
  - Undecided
### Other Considerations

#### Regulatory Assets
- Regulatory assets are not financial assets. P&U companies should continue to apply the impairment models prescribed by ASC 980.

#### Net Investment in Leases
- CECL requires entities to estimate a loss allowance on the entire net investment in leases, including the unguaranteed residual value.

#### Contract Assets
- The impact of switching to an expected loss model from an incurred loss model may not be significant given the short-term duration of contract assets.

#### Zero Loss Expectation Exception
- Entities are generally required to estimate expected credit losses, even when the risk of loss is remote. However, the CECL model provides an exception when the expectation of nonpayment is zero.
- **Factors to Consider:**
  - Does the counterparty have a history of no credit losses (including during a recession or financial crisis)?
  - Does the counterparty have consistently high credit ratings?
  - Is the financial asset secured by collateral?
  - Are securities issued or guaranteed by a governmental agency?
Other Considerations *(continued)*

Off-Balance Sheet Credit Exposure
- Off-Balance Sheet Credit Exposure includes financial guarantees, loan commitments, standby letters of credit, surety bonds and other similar instruments.
- Financial Guarantees
  - Non-contingent aspect is in scope of ASC 460
  - Contingent aspect is in scope of ASC 326

Unconditionally Cancellable
- An entity is required to estimate expected credit losses for off-balance sheet credit exposures if there is a present contractual obligation to extend credit unless the obligation is unconditionally cancellable.
- Factors to Consider:
  - What are the sales contract terms?
  - Do any moratorium periods exist?

AFS Debt Securities
- Credit loss estimates should be recognized through an allowance account and are limited to the amount that fair value is less than the amortized cost basis.
An entity is required to separately present the allowance for credit losses on the Balance Sheet.

<table>
<thead>
<tr>
<th>Description</th>
<th>At December 31, 20X1</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Assets</strong></td>
<td></td>
</tr>
<tr>
<td>Cash and due from banks</td>
<td>$ 38</td>
</tr>
<tr>
<td>Deposits with banks</td>
<td>22</td>
</tr>
<tr>
<td>Fed funds sold and securities purchased under resale agreements</td>
<td>134</td>
</tr>
<tr>
<td>Securities borrowed</td>
<td>75</td>
</tr>
<tr>
<td>Trading debt securities</td>
<td>115</td>
</tr>
<tr>
<td>Debt securities available-for-sale (net of allowance for credit losses of $3)</td>
<td>75</td>
</tr>
<tr>
<td>Debt securities held-to-maturity</td>
<td>$ 34</td>
</tr>
<tr>
<td>Allowance for credit losses on held-to-maturity debt securities</td>
<td>32</td>
</tr>
<tr>
<td>Loans and lease receivables ($150 at fair value)</td>
<td>$560</td>
</tr>
<tr>
<td>Allowance for credit losses on loan and lease receivables</td>
<td>(10)</td>
</tr>
<tr>
<td>Loans and lease receivables, net of allowance for credit losses</td>
<td>550</td>
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<tr>
<td>Derivatives</td>
<td>60</td>
</tr>
<tr>
<td>Equity investments</td>
<td>125</td>
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<tr>
<td>Premises and equipment</td>
<td>10</td>
</tr>
<tr>
<td>Other assets</td>
<td>20</td>
</tr>
<tr>
<td><strong>Total assets</strong></td>
<td>$1,256</td>
</tr>
</tbody>
</table>
ASU 2016-13 requires additional financial statement disclosures related to an entity’s methodology and policy to develop the allowance for credit losses estimate.

Additional disclosure requirements include the following:

- Credit quality of a portfolio (not required for trade receivables due in one year or less)
- Management’s process for estimating the allowance for credit losses
- Changes in the allowance for credit losses estimate from the prior period
- Additionally, an entity is required to present a rollforward of the allowance for credit losses for each reporting period.
Polling Question #2

- Does your company expect a significant impact of adopting ASU 2016-13 in areas other than trade accounts receivable?
  - Yes
  - No
  - Undecided