CECL MODEL VALIDATION WEBINAR

More than a checkmark

How credit unions and banks can prepare for a CECL validation and get more value from it.

ValuRisk Partners × Accolade Advisory

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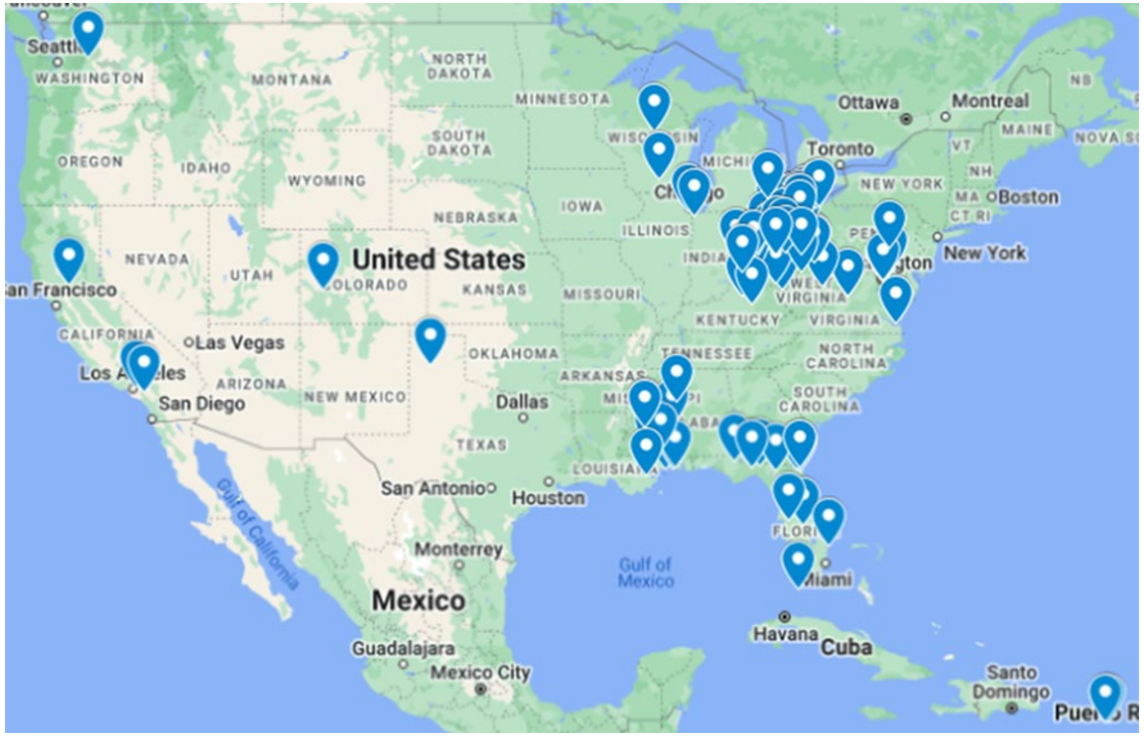
About Accolade

- A wholly-owned CUSO of Corporate One Federal Credit Union
- We provide:
  - Outsourced Chief Investment Officer
  - ALM reporting and consulting
  - Loan Analytics and CECL tools
  - Loan Pricing & Profitability consulting
- We've got your back, empowering credit union leaders to focus on what only they can do – serving their members and driving their mission forward.



ACCOLADE

About ValuRisk Partners

- Independent model validation and risk modeling firm serving banks and credit unions nationwide
- Deep, hands-on industry experience across model development, implementation, validation, and governance
- Specialized expertise in ALM/IRR, liquidity, CECL, credit and capital stress testing, and other key models
- Practical, risk-focused approach designed to meet regulatory expectations while providing actionable value beyond compliance
- Experienced across leading industry platforms and a wide range of institution sizes and model environments

25+
YEARS EXPERIENCE

100%
INDEPENDENT

Risk
ALIGNED

What we'll cover

What we see in validations, how to prepare, and how to get more from your CECL model.

1

What validations reveal

The most common findings and themes we see across CECL validations at credit unions and community banks.

2

Getting validation-ready

What to have in place before your validator or examiner starts asking questions.

3

Beyond the checkmark

How to use CECL to better understand your portfolio, identify key risk drivers, and support management decisions.

Takeaways: You'll leave knowing what validators look for, how to prepare, and how to get more value from CECL beyond calculating the allowance.

The bar has moved

CECL expectations have shifted from implementation to support and defensibility.

EARLY CECL YEARS

"Do you have a CECL model?"

→

TODAY

"Can you defend your modeling choices and assumptions."

Examiner focus

Support for key assumptions, governance, and evidence of effective challenge, not simply whether a model exists.

What gets tested

Your assumptions, configuration, and judgment - not just the vendor's calculations.

What a validation is

An independent challenge of the entire CECL process, from data and methodology through assumptions, results, and governance.

SR 26-2 and what it means for you

The latest evolution in model risk guidance reinforces several principles that matter for CECL validation.

1

Principles-based

Less reliance on prescriptive checklists and more emphasis on sound judgment, effective challenge, and a framework that fits your institution.

2

Proportionality

Expectations should scale with size, complexity, and risk. Smaller institutions don't need large-bank infrastructure, but they still need a defensible process.

3

Ongoing monitoring

Validation is not just a periodic exercise. Models should be monitored over time to ensure they continue to perform as intended and remain fit for purpose.

WHAT THIS MEANS FOR COMMUNITY BANKS AND CREDIT UNIONS

Model risk management isn't just a large-bank exercise. The expectation is a framework and validation process that is appropriate for your institution's size, complexity, and risk.

LIVE POLL

When was your CECL model last reviewed by someone outside your institution?

- **A** Never
- **B** At implementation, not since
- **C** Within the last two years
- **D** Annually, on a set cycle

PART 1

1

The findings that keep showing up

Recurring themes from our CECL validation work across credit unions and community banks.

Six common findings

The recurring issues we see when CECL methodologies are independently challenged.

1

Unsupported Q-factors

Adjustments may be reasonable, but the magnitude isn't supported. “We've always used 5 bps” isn't a methodology.

2

Segmentation that no longer fits

Pools no longer reflect meaningful differences in loss experience or risk characteristics.

3

Set-and-forget assumptions

Key assumptions were set at implementation and haven't been reassessed as the portfolio or environment changed.

4

Limited sensitivity analysis

Management knows the reserve but can't explain what drives it or how key assumptions matter.

5

Data quality issues

Key loan and loss data may be incomplete, inconsistent, or not flowing through the methodology as intended.

6

Limited back-testing

Prior estimates aren't consistently compared to actual losses, making it difficult to assess whether the methodology is performing as expected.

Give your Q-factors an anchor

The adjustment may make sense. But can you support the amount?

START WITH A STRESS ANCHOR

HISTORICAL STRESS LOSS RATE		CURRENT QUANTITATIVE RATE		AVAILABLE RANGE
1.25%	–	0.65%	=	60 bps
Highest relevant loss rate observed over the historical lookback.		Loss rate already produced by the CECL methodology.		Difference between the stress anchor and quantitative estimate.

WHAT IT REPLACES

"We use 5 bps for moderate and 10 bps for high."

Why anchoring works

- **It puts boundaries around judgment**
  Q-factor magnitude starts from an observable loss experience.
- **It helps prevent arbitrary scaling.**
  Management has a basis for why 5, 10, or 20 bps may be appropriate.
- **It preserves management flexibility.**
  The anchor gives you a starting point, not the answer.

The model certification is not your validation

Your vendor validated the calculation engine. Your validation needs to address how you've implemented it.

WHERE WE ACTUALLY FIND THE ISSUES

~90% institution-specific data, configuration, assumptions, documentation and governance

<10%

Based on recurring findings observed across our validation work.

The vendor's engine

Your vendor validated their calculation engine.

The certification covers the underlying calculations, code, and model mechanics.

You configured the model.

Segmentation, historical periods, forecasts, reversion, prepayments, Q-factors and other assumptions are institution-specific.

That's what your validation tests.

Whether your data, configuration, assumptions, and judgments are appropriate, and whether management can support them.

PART 2

2

Getting Validation Ready

What to have ready before your validation begins, or your examiner starts asking questions.

LIVE POLL

Have you ever compared your CECL forecast against actual losses?

- **A** Yes, formally, and it is documented
- **B** Informally, nothing documented
- **C** No
- **D** Not sure

B is the most common answer. B is also the one an examiner treats as C.

Five things to have ready

What to have in place before your validation begins.

1	**Documentation package**	Methodology documentation, key assumptions, data sources, and recent changes - all organized and current.
2	**Know your own settings**	Pull your configuration report and understand the key inputs and settings. If CECL runs in Excel, know the workbook.
3	**Q-factor support**	Document what changed, why an adjustment is warranted, how the magnitude was determined, and who reviewed it.
4	**Evidence of challenge**	Be able to show that someone reviewed and challenged the results, not simply approved the final reserve.
5	**Run your own back-test**	Compare prior estimates to actual losses. Understand where the methodology has been high, low, and why.

PART 3

Beyond the checkmark

3

Using CECL to better understand your portfolio, identify key risk drivers, and support better decisions.

All models are wrong,
but some are useful.

— George E. P. Box, statistician

Your CECL model doesn't need to be perfect to be useful. The question is what you're learning from it beyond the reserve.

Your CECL model is already telling you something

You don't need a sophisticated model to learn more about your portfolio.

1

Historical loss experience

Which segments have produced the most losses, and has that changed over time?

WHERE HAS THE RISK BEEN?

2

Reserve composition

Which segments, assumptions, or Q-factors are contributing disproportionately to the ACL?

WHERE DOES THE MODEL SEE RISK NOW?

3

Sensitivity

Change a key assumption and see what moves. Even a simple WARM model in Excel can do this.

WHERE ARE WE VULNERABLE?

The opportunity: Understand the story behind the reserve, not just the number you need to book.

Putting CECL insights to work

Once you understand what drives the reserve, the same information can support decisions beyond CECL.

Risk-based pricing

CECL gives you a view of expected loss across your loan segments. That loss information can help inform whether pricing adequately compensates you for credit risk.

Portfolio strategy

Segment-level loss experience can show where risk is concentrated and where it is changing. That can inform growth, concentration and underwriting decisions, not just the reserve.

Capital planning

Understanding how the allowance responds to adverse assumptions gives management another input into capital planning and stress testing.

The more you understand your loss experience at the segment level, the more useful CECL becomes beyond the reserve.

Three questions your CECL results can help answer

A few examples of how CECL can provide insight beyond calculating the allowance.

1

Where is the reserve concentrated?

Which segments are contributing more, or less, than their share of the portfolio?

2

What changed - and why?

What actually drove the movement in the reserve this quarter?

3

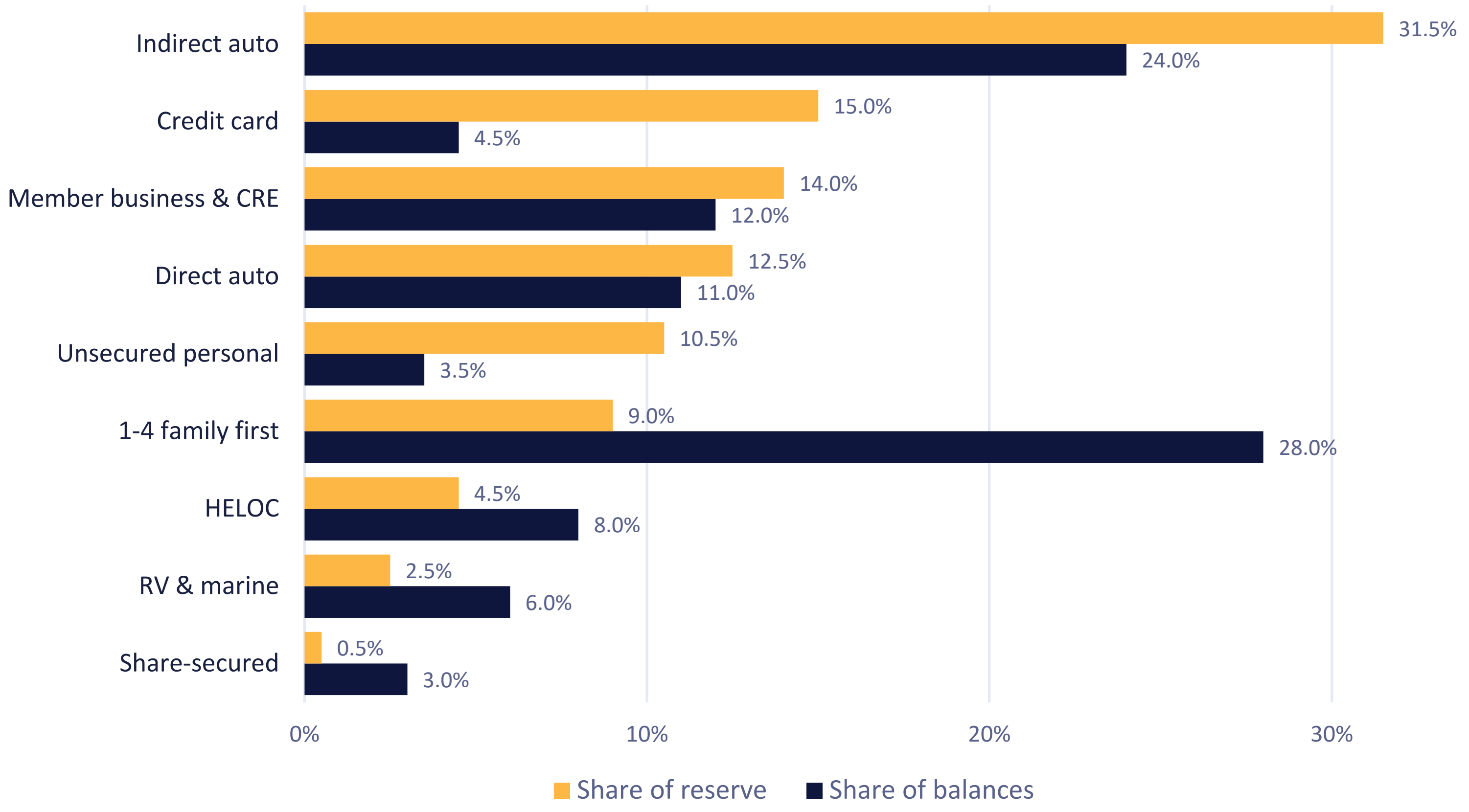
How much is management judgment?

How much comes from the quantitative methodology versus Q-factors and overlays?

These are just examples. The goal is to start asking what the CECL process is telling you about the portfolio - not just what to book.

Where is the reserve concentrated?

Compare each segment's share of the portfolio with its share of the ACL. The gaps show where to look closer.



Gold beyond navy = higher relative loss exposure

Indirect auto is 24% of the book and 31.5% of the reserve. Credit card is 4.5% of the book and 15% of reserve.

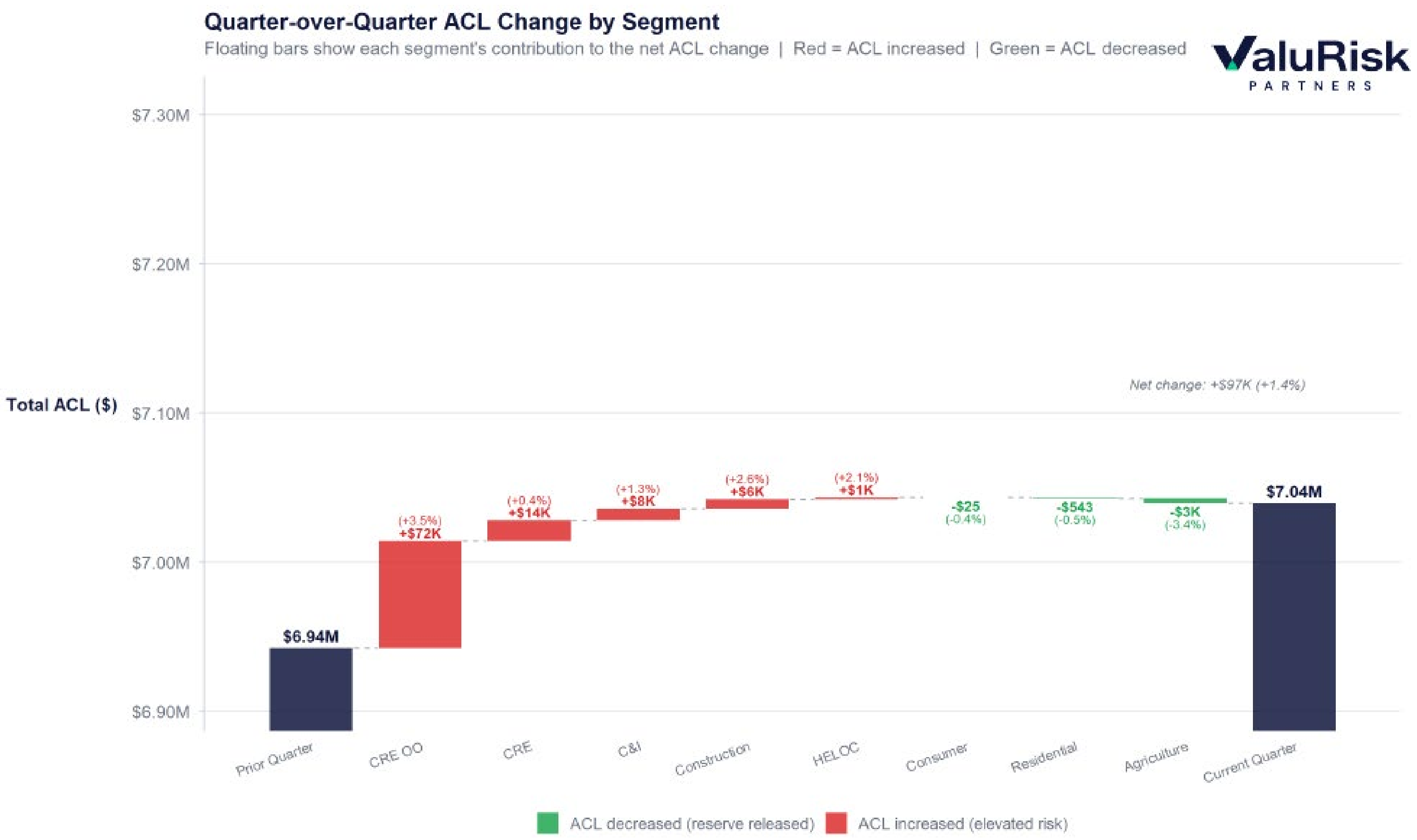
Ask why the gaps exist

Are higher-loss segments priced for that risk? Are concentrations growing? Has the relationship changed over time?

Illustrative credit union portfolio.

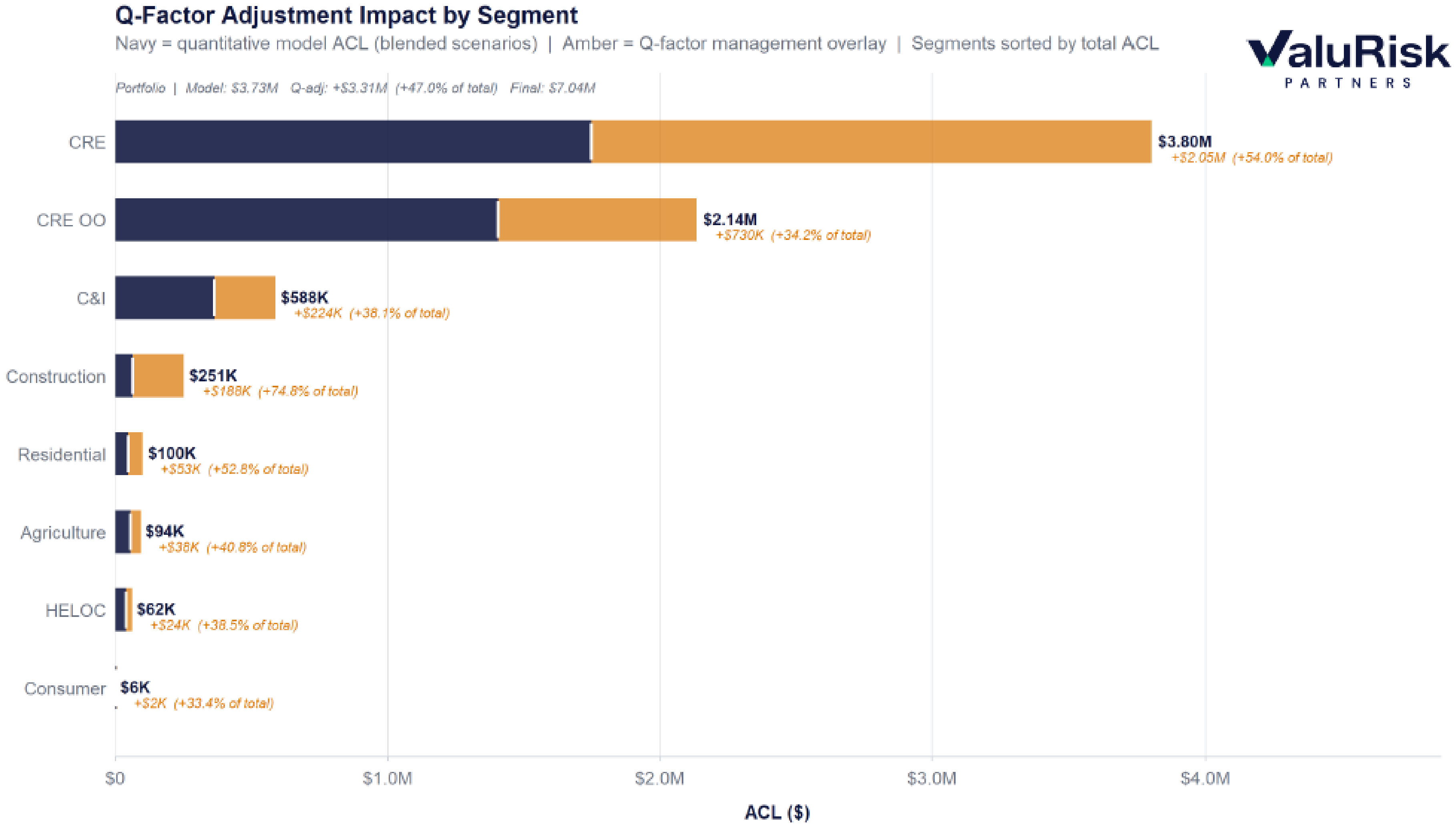
What changed and why?

Don’t just report the reserve. Explain what moved it.



How much is management judgment?

Separate the quantitative ACL from Q-factors and management overlays to see how much judgment is driving the reserve.



A reserve number tells you what to book.

A sound model gives you practical insight into what’s driving it.

Q&A

A good validation finds issues before your examiner does. A great one helps you get more value from the model you already have.

QUESTIONS WE OFTEN GET ASKED

- We implemented last year. Is it too early to validate?
- Our core provider says the model is already validated. Isn’t that enough?
- What is the difference between a model validation and an audit of our reserve levels?

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