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2023 AICPA Conference on Banks & Savings Institutions

Takeaways and hot topics from our specialists

October 2023

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Conference overview

The 48th annual American Institute of Certified Public Accountants (AICPA) National Conference on Banks and Savings Institutions was held Sept. 11 through 13, 2023, in National Harbor, Maryland. The conference included remarks from leaders at the Securities and Exchange Commission (SEC), the Federal Deposit Insurance Corp. (FDIC), the Federal Reserve Board of Governors (Fed), and the Office of the Comptroller of the Currency (OCC), all of whom provided insight into the evolving regulatory landscape. The conference also provided current updates from the Financial Accounting Standards Board (FASB) and Public Company Accounting Oversight Board (PCAOB).

Conference speakers placed significant emphasis on cybersecurity and the amount of risk that financial institutions currently face. Artificial intelligence (AI) and automation were common themes throughout the conference, with specific focus on how technology already has impacted the banking industry and will continue to affect banks going forward. Industry hot topics such as environmental, social, and governance (ESG) issues; cryptocurrency and digital assets; and current expected credit losses (CECL) continue to be focal points of the conference, as they have been in recent years.

The conference included multiple keynote sessions. On Monday, Scott Klososky from Future Point of View presented a session titled "The AI Evolution of Banking." Last year Klososky talked to participants about Humalogy, the integration of humanity and technology in banking. This year he extended the Humalogy concept by explaining how intelligent systems will merge with the human side of financial services to deliver elite results. Later that afternoon, Dr. Romie Mushtaq postulated that modern leaders and employees are stuck in an iterative "stress – success cycle," where individuals work too hard, stress, obsess, and worry on the way to achieving goals – only to go right back into the cycle again after achieving these goals. Mushtaq dove into the neuropsychology and mental health syndromes affecting cognitive performance and emotional control.

On Tuesday, Dr. Marci Rossell delivered an economic update. Drawing on history, theory, and her ringside seat to Wall Street, Rossell delivered an insider's perspective on the most important economic events of our time and discussed the impact of key factors like inflation, supply chain disruptions, labor shortages, and the possibility of a recession. Among other things, Rossell said she believes that current conditions are symptomatic of a larger trend: that businesses today face a variety of seismic surprises, including cyberterrorism, environmental disasters, and swings in the regulatory regime. Later, Thomas Vartanian delivered a keynote address entitled "Banking on the Future: New Concepts of Money, Regulation, and Technology." Vartanian challenged participants to become more effective in their current roles by better understanding the complex future of banking.

On Wednesday, Scott Hildenbrand, Piper Sandler managing director, discussed in his annual presentation certain balance sheet management and interest-rate risk strategies. Hildenbrand emphasized the importance of transparent communication between management and boards when developing new strategies.

The 2024 conference is slated for Sept. 9 through 11, 2024, online and on-site, again at the Gaylord National Hotel and Convention Center in National Harbor.

We hope you find this summary useful.

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Economic updates

State of the economy
On the second day of the conference, Marci Rossell, former CNBC chief economist, provided an update on the overall state of the economy. Specifically, she offered thoughts on the interest-rate environment, the changing face of the global workforce, and how these circumstances are driving different outcomes than were experienced in prior high-inflation environments. On Wednesday, Doug Duncan, chief economist at the Federal National Mortgage Association (Fannie Mae), provided an update on the overall macroeconomic outlook and the U.S. housing market.

Rossell discussed how an aging population has changed the global workplace as fewer workers are available. As such, Rossell expects unemployment rates to remain muted despite a rising-rate environment. Her prediction on the unemployment rate is different from previous high-rate periods, primarily because of the labor scarcity.

Rossell also discussed differences between the high-inflation environments of today and those of the 1970s and 1980s:

- The U.S. is now a net exporter of oil. In prior high-interest-rate cycles the U.S. was a net oil importer. Thus, high oil prices are not as detrimental to the economy as in the past.
- The elevated levels of unemployment in the 1970s can be partially attributed to a younger workforce than the current one. Both then and today, individuals earlier in their career face higher frictional unemployment, which is defined as unemployment resulting from the process of moving from one job to another. However, the smaller pool of younger workers in the current workforce reduces both the length and volume of frictional unemployment.
- Investors expect interest rates to be lower in the near to medium term. In prior periods of rising interest rates, investor expectation was that interest rates would remain elevated indefinitely.

Conference observation: A poll of the audience during Rossell's remarks indicated that participants were evenly split on whether the Federal Reserve Board would maintain or raise the federal funds target rate in the next two quarters.

In addition, Rossell discussed challenges in the global economy including rising tensions in Taiwan and the struggles that China faces by becoming an "old" country (that is, an aging population) before becoming a "rich" country, unlike the paths taken previously by other developed economies (such as Japan).

Both Rossell and Duncan expressed concerns about the state of federal deficit spending. Duncan noted that the historical macroeconomic relationship between low unemployment and government surpluses has moved even further apart with debt as a percent of gross domestic product (GDP) near World War II levels. Both economists agreed that while borrowing at near-zero interest rates (as the U.S. did for a number of years) has merits, future cuts will be needed to address the growing U.S. debt and the resulting debt service.

Conference observation: While some similarities are present with prior high-rate and high-inflation periods, Rossell and Duncan informed participants that they should not expect the same macroeconomic outcomes as seen in those periods.

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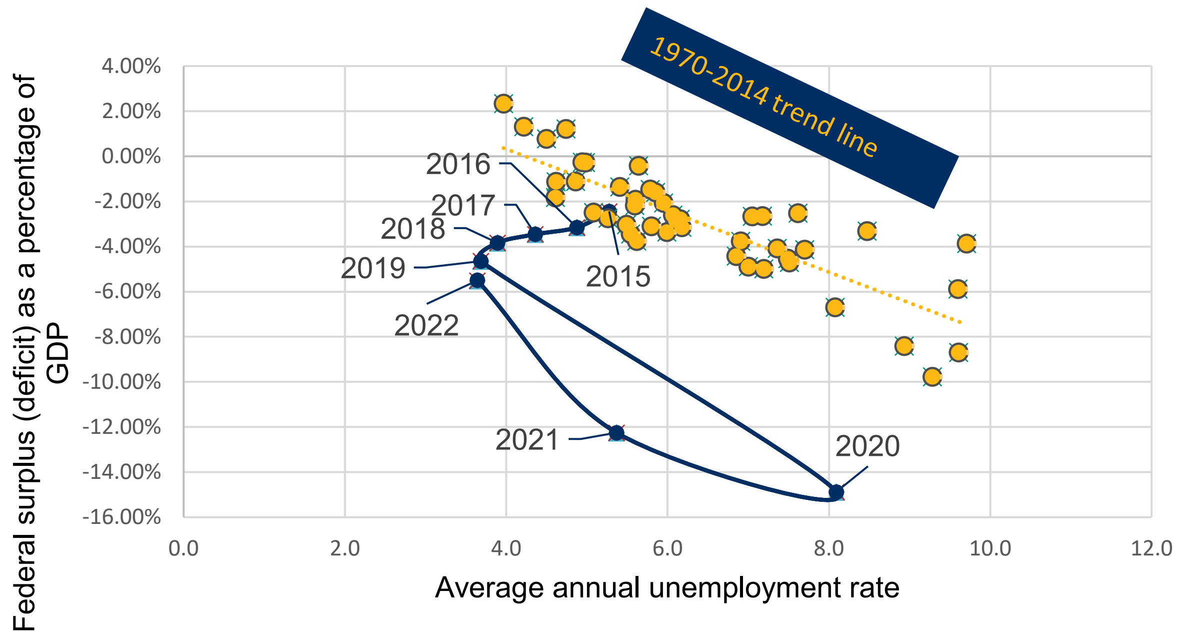

Source: https://fred.stlouisfed.org/

In Duncan's outlook, he said that Fannie Mae is forecasting a "mild recession" where the U.S. will see a slight increase in unemployment (while staying below 5%) and multiple quarters of negative GDP with an overall loss in growth of about half a percentage point. He also noted that delinquencies are rising in sectors such as automobile financing; however, the noted delinquency rates are still below historical averages.

Duncan discussed the impacts of tightening credit and lending conditions and whether it could trigger a recession. He noted that Fannie Mae's view is that tightening credit conditions in itself is not enough to trigger a recession. An audience poll indicated that more than two-thirds of participants concurred with this sentiment. In a nod to the current banking environment, Duncan noted that no empirical evidence exists to support a view that a limited number of large banks provide for a more stable economy than one made up of banks of all sizes. Furthermore, observable data sets show that larger banks do not engage in the level of commercial real estate (CRE) lending that currently is provided by community banks.

Lastly, Duncan noted that he does not believe that home buying activity by millennials has peaked; rather, millennials have shifted to purchasing newly constructed homes given the relative lack of home supply. He believes that when considering price-income ratios, current interest rates, and home supply, the housing market might begin to revert to normal levels in 2027-2028. The price-income ratio is expressed as a multiple of median existing home price divided by median household income. As seen in the following chart, Duncan noted that currently the price-income ratio is at its highest level since at least 1985, even with much lower rates. However, Duncan said that Fannie Mae expects this price-income ratio to begin reverting to the mean in 2024 and beyond.

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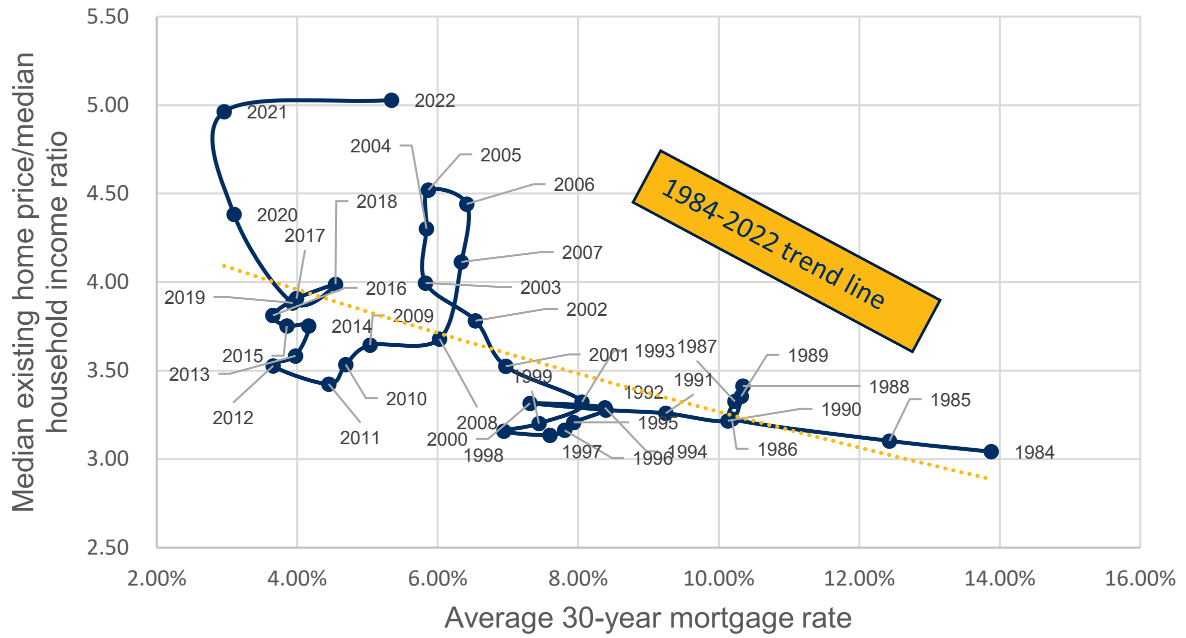

Source: https://fred.stlouisfed.org and https://www.dqydj.com

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CECL

Many conversations throughout the conference related to developments in FASB Topic 326, “Financial Instruments – Credit Losses.” Accounting Standards Update (ASU) 2022-02, “Troubled Debt Restructurings and Vintage Disclosures,” and the proposed ASU over purchased financial assets (PFA) drove many of the conversations.

General comments

Representatives from the federal banking regulators commented on adoption of CECL by institutions in 2023. Chief accountants Amanda Freedle from the OCC and Lara Lylozian from the Fed noted that while it is early in the exam cycle, examination teams have observed that transition to CECL has been smooth, with most questions raised by examination teams being related to recordkeeping rather than methodology. Federal banking representatives also emphasized as they have in prior years that their expectation of banks relative to the adoption of CECL is good faith efforts rather than perfection.

The FASB continues its post-implementation review (PIR) of CECL, noting that feedback from smaller institutions in 2022 highlighted concerns about the resources needed to implement CECL and data requirements. FASB staff at the conference noted that CECL was intentionally designed to be flexible and scalable, with no requirement to use an econometric model if the data derived from a model would not yield relevant results. At a breakout session led by C-suite leaders from various community banks, panelists emphasized the importance of ongoing model backtesting.

Modifications made to borrowers experiencing financial difficulty

Various panels at the conference discussed banks’ adoption of ASU 2022-02. In a Tuesday afternoon panel, Crowe specialists J.P. Shelly and Patrick Vernon cautioned conference participants that although the accounting in ASU 2022-02 related to modifications made to troubled borrowers is more objective than the “concession”-based guidance in legacy troubled debt restructuring guidance, the objective reporting requirements in ASU 2022-02 require many changes to policy and procedure and also require tracking of different data points, many of which might have to be tracked outside of core accounting systems.

Conference observation: In prepared remarks, FDIC Chief Accountant Shannon Beattie clarified that ASU 2022-02 requires disclosure of loans to borrowers experiencing financial difficulty prospectively, thus institutions should no longer be reporting legacy TDRs on the Call Report.

The panelists emphasized the following concepts from ASU 2022-02:

- The only modifications required to be disclosed under the guidance in ASU 2022-02 are those that directly affect contractual cash flows, whereas modifications addressed in legacy TDR accounting would have included modifications considered to be concessions, including modifications such as covenant waivers, collateral substitutions, or changes in guarantors.

- ASU 2022-02 reintroduces a decision of whether a modification under ASU 2022-02 suggests that the modification represents the continuation of an existing loan or a new loan for modifications made to troubled borrowers. Under legacy TDR guidance, a concession granted to a troubled borrower was, by definition, a continuation of the existing loan. If the modification suggests that the instrument’s modified contractual terms are indicative of a new loan, the institution must recognize unamortized fees or costs from the original loan and any prepayment penalties in interest income when the new loan is granted.

Crowe takeaway: In June 2023, Crowe published a FAQ resource, “Goodbye TDRs, Hello Loan Mods and Vintage Disclosures.”

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In addition, specific to call report disclosures, FDIC Chief Accountant Shannon Beattie instructed institutions with questions on the presentation of loan modifications made to troubled borrowers on the call reports to reference the Federal Financial Institutions Examinations Council (FFIEC) supplemental instructions for reporting guidance. She observed that a common question the FDIC has received relates to the notion of a "clean slate"; Beattie clarified that ASU 2022-02 requires disclosure of loans to borrowers experiencing financial difficulty prospectively; thus, institutions should no longer be reporting legacy TDRs on the call report.

Purchased financial assets

Under existing GAAP, entities that acquire financial assets within the scope of Topic 326 must classify the assets as either purchased credit deteriorated (PCD) assets or non-PCD assets, depending on the level of credit deterioration that a PFA has experienced since its origination. While this distinction does not affect how expected credit losses are measured, it does affect how the allowance for credit losses (ACL) is initially recognized, which ultimately affects the effective yield recognized on the acquired assets. Under current GAAP, non-PCD assets are recorded at fair value, with the entire difference between par value and fair value recorded as a premium or discount; subsequently, the entity must record an ACL on the amortized cost basis through credit loss expense. Fair value includes a credit loss component, thus recording the full fair value premium or discount as an adjustment to amortized cost of the financial asset and recording an ACL on the same asset results in presentation of the acquired asset on the balance sheet at an amount that is lower than amount expected amount to be collected. As part of its CECL PIR, the FASB received feedback that the requirement to classify PFAs as either PCD assets or non-PCD assets is complex, requires significant judgment, and has led to reduced comparability among entities. Stakeholders also have asserted the requirement to recognize the allowance for non-PCD assets through a charge to earnings is unintuitive.

The proposed ASU expands concepts in current PCD treatment to all "seasoned" purchased assets. Under the proposal, the ACL for PFAs that are considered "seasoned" would be established by adjusting the initial carrying amount of the PFA, which has the result of allocating the credit component of the purchase price directly to the ACL. For all other PFAs, the ACL would be established through a charge to earnings. A PFA would be considered seasoned when either of the following two conditions are met: 1) the PFA is part of a business that was acquired in a business combination accounted for in accordance with Topic 805, "Business Combinations"; or 2) the PFA was acquired more than 90 days after origination and the entity did not have involvement with the origination of the PFA.

Entities would be required to adopt the proposed ASU using a modified retrospective transition approach. Under that approach, the proposed guidance would be applied retrospectively to all PFAs occurring since the first reporting period in which an entity adopted ASU 2016-13, "Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments."

The FASB's comment period on the proposed ASU on PFA has expired, and the FASB staff currently is reviewing comments. The FASB staff's comments at the conference on PFA primarily surrounded clarification of the ASU and preliminary stakeholder feedback.

No prevailing consensus in favor of or against the adoption of the proposal existed; rather, multiple panelists acknowledged pros and cons for various concepts addressed in the proposal.

Crowe takeaway: In June 2023, Crowe published a Take Into Account article related to the FASB's proposed ASU over purchased financial assets, "FASB Proposes Acquired Financial Asset Reporting Changes."

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Updates from the federal banking agencies

On Monday, Crowe partner Sydney Garmong hosted a “fireside chat” with the chief accountants of the federal banking agencies: Shannon Beattie (FDIC), Amanda Freedle (OCC), and Lara Lylozian (Fed). Many of the topics covered by the chief accountants appear elsewhere in this publication (see “CECL,” “Topics related to current events,” and “FDICIA Part 363 considerations”).

The speakers emphasized the importance of trust in the banking system. Per Freedle, trust is needed in standard-setters, auditors evaluating information, and regulators monitoring banks' health. Actions should align with words, and accountability is essential when something goes wrong. Panelists noted that change in the banking system can potentially lead to distrust, but it also creates opportunities for improvement. Navigating changes in the banking industry is crucial for success.

Lylozian commented that the Fed is engaged in climate risk management, conducting scenario analysis with the top six banks. Results from these activities are being evaluated, and the Fed plans to publish a public report aimed at informing the industry at large. Lylozian also remarked that robust disclosures are an important avenue to address climate-related risks. Regulators are continuing to enhance their education and understanding of ESG issues.

Beattie informed participants that the FFIEC will introduce changes to the call report in the third quarter, primarily related to changes in uninsured deposit reporting requirements. Amendments to the call report will also focus on transfers from available-for-sale (AFS) to held-to-maturity (HTM) classifications. Beattie emphasized that collateralized deposits are not FDIC-insured deposits.

Conference observation: FDIC Chief Accountant Shannon Beattie reminded participants that the federal banking agencies follow legislative and regulatory definitions for uninsured deposits. Banks and bank holding companies should read the FDIC’s Financial Institution Letter (FIL) 37-2023, “Estimated Uninsured Deposits Reporting Expectations,” for certain observations made by the FDIC in review of uninsured deposit reporting on call reports.

When asked what areas the federal banking agencies believe carry increased risk over the next year, the chief accountants listed general credit risk, ballooning credit card balances, new developments in technology like cryptocurrency and AI, and novel banking practices.

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FDICIA Part 363 considerations

In the Monday session with the chief accountants of the federal banking regulators, Beattie highlighted certain compliance requirements of Section 36 of the *Federal Deposit Insurance Act* (FDI Act) – which was added by Section 112 of the *Federal Deposit Insurance Corp. Improvement Act* (FDICIA) – and Part 363 of the FDIC's regulations. This section of the FDI Act affects insured depository institutions (IDI) with assets greater than $500 million. Eligible banks must submit an annual report to the FDIC, and any other appropriate banking agency, which includes the following:

- Annual financial statements prepared in accordance with GAAP
- A report signed by the CEO and CFO (or chief accounting officer) that contains:
  - A statement of the management's responsibilities for:
    - Preparing financial statements
    - Establishing and maintaining an adequate internal control structure and procedures for financial reporting
    - Complying with the laws and regulations relating to safety and soundness that are designated by the corporation and the appropriate federal banking agency
  - An assessment, as of the end of the institution's most recent fiscal year, of:
    - The effectiveness of such internal control structure and procedures
    - The institution's compliance with the laws and regulations relating to safety and soundness that are designated by the corporation and the appropriate federal banking agency
- An independent auditor's report on the financial statements
- For IDIs with greater than $1 billion in total assets, an independent auditor's report on the internal controls over financial reporting of the IDI, including controls over the preparation of applicable regulatory reports (e.g., call reports)

In certain circumstances, a company can use financial statements prepared on a consolidated basis to satisfy the IDI's reporting requirements under the FDI Act. Beattie emphasized that holding company-only financial statements (that is, regulatory reports that account for the IDI as an equity method investment) do not satisfy the requirements under Part 363.

Conference observation: FDIC Chief Accountant Shannon Beattie remarked that an independent auditor's report or management's assessment of internal control over financial reporting that references internal controls over financial reporting related to the preparation of a company's FR Y-9SP or FR Y-9LP regulatory report to satisfy reporting requirements under Section 36 of the FDI Act and Part 363 of the FDIC's regulations will no longer be accepted by the agency.

Crowe takeaway: In 2018, the Federal Reserve removed the requirement for bank holding companies (BHC) with less than $3 billion in consolidated financial assets to prepare the consolidated Form FR Y-9C on a quarterly basis; instead, the Fed requires BHCs with consolidated assets greater than $1 billion but less than $3 billion to file a parent-only regulatory report, Form FR Y-9SP, on a biannual basis. Certain institutions and auditors referred to Form FR Y-9SP in reports issued to the federal banking regulators to satisfy reporting requirements under the FDI Act. Beattie emphasized that holding company-only financial statements (that is, regulatory reports that account for the IDI as an equity method investment) do not satisfy the requirements under Part 363.

Crowe recommends contacting your external auditor if your institution 1) publishes external financial statements on a consolidated basis and does not report consolidated financial statements for regulatory reporting on Form FR Y-9C and 2) references Form FR Y-9SP on the management's assessment of internal control over financial reporting filed annually with the FDIC or OCC in satisfaction of Section 36 of the FDI Act and Part 363 of the FDIC's regulations.

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Beattie reminded banks of the requirement to retain an independent audit committee when subject to Part 363. For IDIs with total assets of $500 million but less than $1 billion, the majority of the audit committee's members (outside directors) should be independent of management.
IDIs with total assets of $1 billion or more should have audit committees comprising solely outside directors that are independent of management. When the IDI has total assets over $3 billion as of the beginning of its fiscal year, the audit committee should further include members with banking or related financial management expertise, should have access to its own outside counsel, and should not include any large customers.

Finally, Beattie reminded both preparers and auditors of the enhanced independence requirements for IDIs subject to Part 363. Audit committees should ensure that the independent public accountant is compliant with the independence standards of the AICPA, the SEC, and the PCAOB, regardless of whether the institution or its parent holding company is a public company. Also, the audit committee should ensure that engagement letters and any related agreements with the independent public accountant for audit services to be performed under Part 363 do not contain any limitation of liability provisions that 1) indemnify the independent public accountant against claims made by third parties; 2) hold harmless or release the independent public accountant from liability for claims or potential claims that might be asserted by the client institution, other than claims for punitive damages; or 3) limit the remedies available to the client institution.

Crowe takeaway: In 2020, Crowe published "5 Things Banks Should Do as They Approach $1 Billion in Assets."

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SEC updates

Representatives from the SEC’s Division of Corporation Finance (CorpFin) and the Office of the Chief Accountant (OCA) provided insight on emerging issues affecting SEC registrants and audits of publicly traded financial institutions. The discussion by Paul Munter, chief accountant, and Jonathan Wiggins, associate chief accountant, offered insights into various aspects of financial reporting, risk assessment, audit committees, standard-setting, and more. Later in the conference, Erik Gerding, director of CorpFin; Stephanie Sullivan, associate chief accountant; and Rachel Mincin, associate chief accountant, went into specific detail on activities of both CorpFin and OCA.

Opening remarks from the speakers reinforced the SEC’s emphasis on high-quality financial reporting. Munter told conference participants that financial reporting serves as a vital communication tool, conveying an organization’s economic activities transparently and consistently. Focusing on current risks, speakers noted that the current interest-rate environment is a source of concern for the SEC. It has led to a tightening of liquidity and declines in the fair values of securities, which affects both financial institutions and the broader banking system. Speakers reminded the audience that the SEC operates within a disclosure-based regime, where investors rely on material information provided by organizations to make informed decisions. Trust is fundamental to the capital markets, and organizations must assess whether rising risks could lead to material misstatements in their financial statements. Investors must be informed about how future financial performance might deviate from historical results, especially in volatile economic conditions.

Risk assessment

Munter reminded the audience of management’s responsibility to be alert to new or changing business risks that could impact the system of internal control or the ability to disclose necessary information in periodic filings. Munter also stressed to auditors the necessary role of risk assessment and professional skepticism in the audit practice.

Crowe takeaway: Readers should take a look at Paul Munter’s speech “The Importance of a Comprehensive Risk Assessment by Auditors and Management,” delivered on Aug. 25, 2023.

Entity-level controls

Munter noted that bank management should evaluate whether its organization has implemented processes and controls that can timely prevent or detect a material misstatement in financial statements. While an organization’s financial reporting objective might be separate from its operational or compliance objectives, the organization’s internal control system should be dynamic and expand beyond a singular focus on internal control over financial reporting (ICFR). Munter added that when evaluating control deficiencies identified outside of an organization’s financial reporting objective, both management and auditors should consider the root cause of the deficiency and whether it impacts the issuer’s ICFR conclusions. Even though not directly related to ICFR, identification of deficiencies in other nonfinancial reporting areas could impact the assessment of entity-level controls, particularly controls over risk assessment and monitoring activities.

Conference observation: SEC Chief Accountant Paul Munter remarked that when evaluating control deficiencies identified outside of an organization’s financial reporting objective, both management and auditors should consider the root cause of the deficiency and whether it impacts the issuer’s ICFR conclusions. Even though not directly related to ICFR, identification of deficiencies in other nonfinancial reporting areas could impact the assessment of entity-level controls, particularly controls over risk assessment and monitoring activities.

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Representatives from CorpFin discussed their current focus on regulatory activities and rulemaking objectives. They also highlighted recent final rules adopted by the SEC, including those related to stock buybacks, insider trading arrangements, clawbacks, and cybersecurity disclosures. Additionally, they mentioned several proposed rules, such as beneficial ownership reporting and conflicts of interest rules.

Presenters also emphasized CorpFin's focus on fostering one-to-many communication with the public, as evidenced by the issuance of "Dear Issuer" letters on various timely topics, including the war in Ukraine and China-related issues.

CorpFin highlighted areas of focus when reviewing corporate disclosures. CorpFin's comments and reviews have centered on various risk-related disclosures, which are categorized into specific areas:

- **Risk management disclosures.** CorpFin expects disclosures to go beyond boilerplate language and provide specific details regarding risk management processes. Examples include disclosing policies or controls related to internal controls over deposits, information on brokered deposits, and how particular risks manifest in the issuer's specific circumstances.
- **Interest rate risk (IRR) sensitivity analysis.** Banks are expected to disclose key inputs and assumptions related to deposits. The presentation emphasized the importance of regularly reassessing these inputs, particularly when derivatives are used for hedging deposit relationships.
- **Deposits (concentration).** CorpFin encourages banks to provide more detailed information about deposit types, including disaggregation of characteristics, estimated deposit duration, deposit beta, and qualitative and quantitative data on changes in deposit bases.
- **Credit risk concentration.** Focus on credit risk concentration is heightened, particularly in the context of CRE. CorpFin expects banks to provide information about risks associated with material concentrations and how these risks are being managed.
- **Liquidity disclosures.** Some banks have improved their disclosures on liquidity during interim periods. CorpFin has observed enhanced disclosures regarding sources of liquidity, their ability to access these sources, and potential material losses or consequences. This includes tabular disclosures on sources of liquidity, remaining capacity, and comparisons against total deposits. Banks are encouraged to discuss their liquidity policies and how they manage liquidity.
- **Non-GAAP disclosures – tangible common equity (TCE) disclosures.** Panelists emphasized that non-GAAP disclosures, particularly those related to TCE, should be appropriately labeled, described, and disclosed in accordance with regulatory guidance. They also mentioned that banks should provide disclosure on the calculation method and explanations for any adjustments made to non-GAAP measures.

OCA representatives discussed significant judgments in the accounting for certain financial instruments. Panelists highlighted the importance of recognizing unrealized losses in HTM securities and provided examples of when sales or transfers of HTM securities may occur without tainting the remaining portfolio. OCA representatives also discussed loans, emphasizing the immediate recognition of fair value losses when an organization's intent changes from holding loans for investment to holding loans for sale. Furthermore, OCA staff referred to Staff Accounting Bulletin (SAB) 119,[1] which provides guidance on developing governance and documentation of a systematic methodology for accounting practices related to the ACL.

[1] https://www.sec.gov/oca/staff-accounting-bulletin-119

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FASB updates

FASB technical director Hillary Salo, along with staff members Chase Hodges and Daniel Stuhlemmer, provided an update on the FASB's current standard-setting agenda and offered insight on the ongoing CECL PIR process.

Technical agenda update

The technical agenda is being driven by the results of the agenda consultation that concluded in mid-2022.[2] Salo noted that the technical agenda[3] is smaller than in recent years, indicating that many ongoing projects are approaching completion.

In addition to the five ASUs that have been released in 2023 to date, the FASB anticipates issuing six additional ASUs prior to year-end. The following projects expected to be finalized in 2023 based on the FASB's technical agenda might be of interest to readers:

- Accounting for and disclosure of crypto assets
- Improvements to income tax disclosures
- Segment disclosures

The project on accounting for crypto assets is a major focus of the FASB, as investors want an accounting outcome that reflects the fair value of these assets; furthermore, investors desire more disclosures regarding the types of crypto assets held. Based on preliminary discussions by the FASB, crypto assets and related income and expense will be separated on the balance sheet and income statement as separate line item. In addition, required disclosures will include the number of units held and any restrictions on disposal. If adopted as currently discussed by the FASB, the standard will be eligible for early adoption and effective in 2025 for calendar year-end preparers.

With respect to income tax disclosures, the expected standard will require enhanced disclosures, including rate reconciliations and income taxes paid by jurisdiction. Segment reporting is another area of focus, aiming to provide more information about segment expenses and management approaches.

Crowe takeaway: For updates on current FASB projects, please visit our Take Into Account accounting and financial reporting hub.

Projects on the technical agenda that are not expected to be finalized in 2023 include the following:

- Accounting for and disclosure of software costs
- Accounting for environmental credit programs
- Credit losses: PFAs
- Hedge accounting improvements
- Disaggregation of income tax expenses

With respect to software costs, the project aims to improve the accounting for software costs, both internally developed and acquired. Salo indicated the current model does not reflect modern software development practices, and stakeholders have provided diverse feedback through mechanisms such as the agenda consultation. The FASB is considering a single model for software capitalization.

Notably, the PFA project has been exposed for public comment by the FASB and is expected to be finalized sometime in the first quarter of 2024. Please refer to the "CECL" section of this publication for further information on this project and on the broader CECL PIR process.

[2] https://www.fasb.org/page/PageContent?pageId=/projects/recentlycompleted/agenda-consultation.html

[3] https://www.fasb.org/technicalagenda

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The FASB's research agenda includes projects that are actively being worked on by FASB staff to identify emerging issues in financial reporting. The research agenda is determined by the chair. Items on the research agenda include:

- Accounting for and disclosure of intangibles
- Accounting for government grants
- Consolidation of business entities
- Definition of a derivative
- Financial key performance indicators for business entities

With respect to the project on the definition of a derivative, the FASB staff is considering a proposal to the board to make targeted improvements to hedge accounting to simplify the extant standard. As a part of this, the current research project is focused on addressing the definition of a derivative and related scope exceptions from hedge accounting. Stakeholder feedback suggests that the current bifurcation criteria in Topic 815 are unintuitive.

FASB staff members in attendance were explicit in their remarks to conference attendees that although a current research agenda project relates to the accounting for and disclosure of intangibles, no current plans or projects relate to the accounting for goodwill.

Finally, the FASB staff discussed two recently issued ASUs. Update 2022-06, "Reference Rate Reform (Topic 848): Deferral of the Sunset Date of Topic 848," defers the sunset date of Topic 848 from Dec. 31, 2022, to Dec. 31, 2024, to align with the U.K. Financial Conduct Authority's (FCA) decision to defer the cessation date of certain tenors of the London Interbank Offered Rate until June 30, 2023.

Please refer to the "CECL" section of this publication for a discussion of ASU 2022-02, "Financial Instruments – Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures."

Conference takeaway: FASB staff members in attendance were explicit in their prepared remarks to conference attendees that although a current research agenda project relates to the accounting for and disclosure of intangibles, no current plans or projects relate to the accounting for goodwill.

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PCAOB updates

Associate Chief Auditor Lisa Busedu provided an update on the PCAOB's standard-setting agenda. Glen Tempro, associate director, provided an update on the Division of Registration and Inspections.

While standard-setting remains a key focus of the PCAOB in the short and medium term, inspection results were a point of emphasis during this year's presentation. Given events that transpired during the year (that is, certain regional bank failures) the PCAOB has developed an inspection plan for audits of publicly traded banks and bank holding companies to address the perceived risks in the market and focus inspections on the audit areas sensitive to these risks. These risks include:

- Impact of inflation on the financial statements and related disclosures
- Exposure to interest-rate risk and related impact on the financial statements and disclosures
- Impact of remote and hybrid working environments from an operational and controls perspective

With respect to the 2022 inspection cycle the speakers said 157 audit firms were inspected, encapsulating 710 public company audits. For audits of banking companies, common areas of focus included loans, the ACL, investment securities, and derivatives, particularly related to auditing the valuation assertion. Tempro noted a significant increase in the number of engagements that received comments compared to audits reviewed in the 2021 inspection cycle. Common deficiencies were related to evaluation of the ACL, primarily the auditor's assessment of significant inputs and assumptions, as well as the presentation and disclosure of securities, and the evaluation of sensitivity of assumptions for complex estimates.

The Division of Registration and Inspections developed an inspection plan for the current year to address risks in the market, such as inflation, interest rates, and the impact of remote and hybrid work arrangements. As a result of the failure of certain banks in 2023, the PCAOB is placing added emphasis on audit areas sensitive to current risks present in the financial services sector.

Busedu provided an update on the PCAOB's short-term and midterm agendas. Certain projects on the short-term agenda include:

- Confirmations
- Noncompliance with laws and regulations (NOCLAR)
- The auditor's general responsibilities
- Going concern
- Firm and engagement performance metrics
- Substantive analytical procedures, and
- Amendments related to audit procedures involving technology-assisted analysis.

Please refer to the "NOCLAR" section of this publication for a robust discussion of this proposed audit standard. With respect to the confirmations project, American Bankers Association representative Josh Stein highlighted concerns related to this proposed standard, specifically whether it aligns with modern cybersecurity messages to customers. As it concerns the going concern project, OCC Chief Accountant Amanda Freedle noted that the federal banking agencies are actively monitoring the status of project, particularly because of the unique characteristics of the banking industry.

Midterm projects on the PCAOB's standard-setting agenda include:

- Fraud
- Interim standards
- Use of a service organization

Finally, a project on data and technology is on the PCAOB's research agenda. Research projects focus on whether changes to PCAOB standards or other regulatory responses are needed. If standard-setting is deemed appropriate, the project will be added to the standard-setting agenda.

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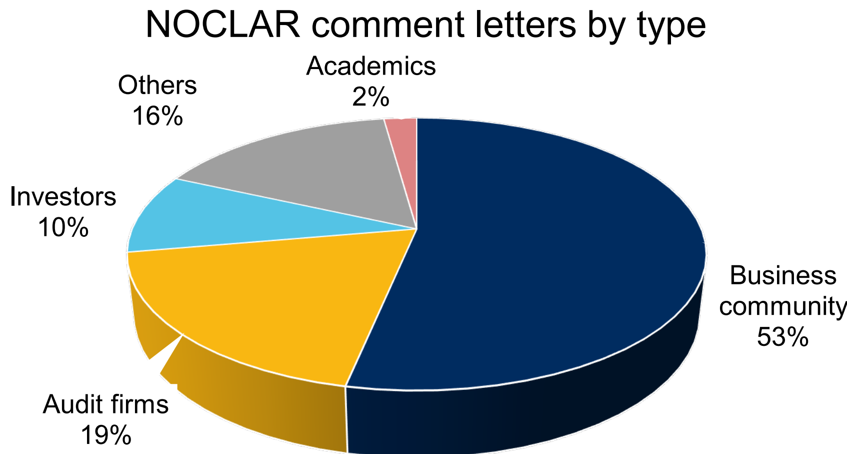
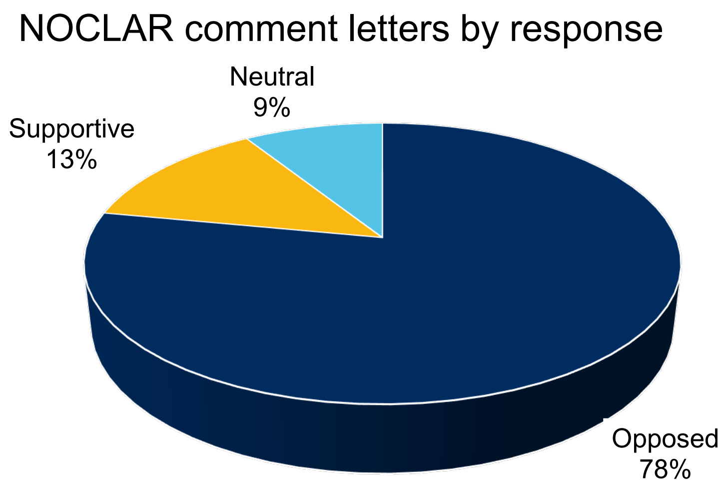
NOCLAR

A wide number of conference panelists discussed the PCAOB's recent proposed amendments to PCAOB Auditing Standards related to a Company's Noncompliance with Laws and Regulations (NOCLAR).

On June 6, 2023, the PCAOB proposed certain updates to existing audit standards related to an auditor's consideration of a company's NOCLAR. In proposing the updates, the PCAOB is "proposing to establish and strengthen requirements for (i) identifying, through inquiry and other procedures, laws and regulations with which noncompliance could reasonably have a material effect on the financial statements, (ii) assessing and responding to the risks of material misstatement arising from noncompliance with laws and regulations, (iii) identifying whether there is information indicating noncompliance has or may have occurred, and (iv) evaluating and communicating when the auditor identifies or otherwise becomes aware of information indicating that noncompliance with laws and regulations, including fraud, has or may have occurred."[4] The proposal was accepted by the board by a 3 to 2 vote. Notably, both CPAs on the board dissented from exposing the proposed audit standards to public comment. The comment period for the proposed updates closed on Aug. 7, 2023. Most of the respondents during the comment period opposed the proposed amendments as currently written.





Source: Remarks by PCAOB staff before the 2023 AICPA National Conference on Banks and Savings Institutions.

[4] https://assets.pcaobus.org/pcaob-dev/docs/default-source/rulemaking/docket-051/pcaob-release-no.-2023-003---noclar.pdf?sfvrsn=fe43e8a_4

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Crowe observation: As of the date of the conference, the PCAOB received 137 comment letters related to the proposed NOCLAR audit standard update. More than half of the comment letters did not agree with or support issuance of the audit standard as proposed; however, many commenters said that enhancement to the extant PCAOB standards covering NOCLAR is warranted.

In a panel featuring attorneys, auditors, and industry groups, concerns over the scope of the proposed rules and the expected effort needed to comply with the standard were discussed. Panelists argued that a significant increase in the reliance on specialists would be needed. Further, auditors could be required to make legal determinations on whether noncompliance with laws or regulations have occurred, which is not a core competency of auditors. Panelists also noted that the proposed standards would require that auditors perform procedures that extend beyond what is required of management under federal securities law and GAAP.

Amanda Freedle, chief accountant of the OCC, remarked that the federal banking agencies are aware of the discussion within the industry, and offered to frame her views in the context of bank supervision. Freedle does not believe that the proposed standard conflicts with existing supervision activities and believes that enhancing standards around NOCLAR would potentially allow for a more robust dialogue between various stakeholders.

Crowe takeaway: Crowe issued a comment letter on the NOCLAR proposal to the PCAOB, which was published on Aug. 7, 2023.

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Machine intelligence

Throughout the conference, a focal point was the impact of AI and machine learning on banking and the greater economy.

When polled, most conference participants indicated that they have not observed tangible examples of AI implementation that have directly contributed to productivity gains; however, presenters and panelists discussed ways that they envision or observed the impacts of AI.

Rossell noted that she would expect large-language AI models to provide more scale in labor-intensive small businesses that do not currently have the scale to take on large projects.

In an example of how machine intelligence is currently impacting the banking industry, Chris Ackerlund, head of accounting policy at Bank of America, noted that implementation of robot-assisted evaluations of large and complex reconciliations allowed their team to focus only on the exception items as opposed to manually evaluating thousands of entries.

Scott Klososky, founding partner at Future Point of View, presented a keynote speech titled “The AI Evolution of Banking.” He referred to AI as “machine intelligence” since AI explicitly labels the intelligence as “not real.” Klososky said that the impacts of machine intelligence (and the related impact to the banking sector) will accelerate once access to quantum computing space becomes widely available.

In Klososky’s presentation, most participants indicated that while today they have done little in the way of AI, they cannot envision how the banking industry will be impacted by AI in 20 years. Participants also stated that AI will be critical to young professionals in their careers.

Klososky said he believes that humans must use AI to achieve optimal productivity levels. Transferring knowledge from human to human or from human to machine is slow and only a low percentage of knowledge is transferred. However, with AI, 100% of knowledge can be transferred quickly.

Stein noted that while AI will be transformative for certain areas, challenges will relate to explaining to regulators and stakeholders the use case of AI and how AI integrates into a banking organization. Stein also believes that finding skilled practitioners to help with the implementation of AI technology will be challenging.

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Other items of relevance for banks

Securities valuation and HTM/AFS transfers

In Wednesday's "Ask the Experts" large bank panel, representatives from banks including JP Morgan Chase, Wells Fargo, Bank of America, and Citi fielded an array of questions that arose over the course of the conference. In one session, panelists discussed the valuation assertion as the accounting issue of greatest concern in 2023.

One of the notable discussion points during the conference surrounded the decrease in market activity in certain bond markets, such as mortgage-backed securities, and how the decline in activity interacts with pricing services that banks rely on to value their securities portfolios. Conference speakers noted that many of these services rely on market activity to price securities. Given the variety of vintages, portfolios, and other data and assumptions that go into pricing, the speakers emphasized the importance of having a well-controlled process to evaluate the pricing of these securities, including whether more assets have moved to Level 3 in the fair value hierarchy.

Another conference topic that arose in numerous sessions was transfers of securities between AFS and HTM classifications. Speakers reminded the audience of the following:

- The rationale for the transfer, the specific securities to be transferred, and the date of the transfer must be documented.
- The impacts to accumulated other comprehensive income (AOCI) are not immediate; the AOCI adjustments are accreted over the remaining life.
- HTM securities must be evaluated for impairment under CECL.

Crowe takeaway: Topic 1 of the OCC Bank Accounting Advisory Series (BAAS) provides helpful examples related to AFS to HTM transfers.

Cybersecurity

The discussion of emerging technologies gave rise to cybersecurity questions. Klososky noted that although historically criminals have been faster to exploit weaknesses in information security systems, security professionals can catch up to the speed of criminals using AI.

Lance Noggle, vice president of operations and senior regulatory counsel at the Independent Community Bankers of America, noted that as AI and cloud computing become more prevalent, the challenges of achieving adequate staffing levels to support the information security infrastructure and regulatory requirements are also becoming more prevalent. This challenge was described as more acute for smaller banks that are struggling to keep up with emerging regulations and managing third-party risk where they might have less leverage than larger competitors.

Cash flow

Presenters reminded conference participants of the need to report items within a cash flow statement according to the correct classification, based on U.S. GAAP. In the SEC's presentation, Munter noted that, for banking organizations, the cash flow statement appears to receive less audit and ICFR focus than the balance sheet and income statement even though the cash flow is considered on par with those financial statements. Munter added that when a classification error arises, it is important to evaluate the error using a "reasonable investor lens" to determine if the error is material. These points were emphasized by the large-bank panel at the end of the last day of the conference.

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Environmental, social, and governance (ESG)

In the "Mid-size Bank Chief Accounting Officer Panel" Ryan Richards from Zions Bancorporation (Zions) discussed current ESG related efforts that the company undertaking. Richards noted that Zions expects, at a minimum, Scope 1 and Scope 2 disclosure requirements to eventually be implemented by the SEC and is increasing voluntary disclosures in anticipation of the rulemaking.

Panelists from large banks shared similar thoughts on that last day of the Conference, but the panelists also discussed the importance of consistent reporting across the entity and ensuring that reporting was complete and accurate. Panelists instructed participants to ask the following questions about ESG related data:

- How do you know the data you are using is valid?
- How do you validate the data?
- How do you control data integrity from capture through financial reporting?

Conference speakers emphasized data governance matters for both required and voluntary reporting as institutions must ensure data reported across the entity is consistent and that information included in management's discussion and analysis (MD&A) is not in conflict with other publicly available data.

Crowe observation: The California Senate recently passed two climate bills that create ESG reporting requirements for companies that do business in the state and have more than $500 million in revenue.

Crowe takeaway: While the SEC has not yet finalized the timeline for when ESG reporting will be required, other jurisdictions or regulatory bodies may have additional requirements that must also be considered.

Health of the accounting profession

Participants asked questions during the conference related to work from home policies and the overall health of the accounting profession.

Stein and others discussed in a panel focused on the current industry environment that the amount of pressure on accounting professionals is not only causing practitioners to leave the profession, but also discouraging others from entering it. In additional to addressing some of the items that are creating the pressures, the panel noted that practitioners can help build interest in the profession by advertising the positive aspects of the profession and the opportunities that a career in accounting can provide.

Related to work-from-home policies, the panel discussed strategies for successfully integrating entry-level employees in a hybrid or fully remote working environment. Key takeaways included:

- Go to the office "with intention." Employees should schedule time for meetings, collaboration, and so on when in person and use home days for "head-down" focused tasks.

- Be mindful about creating new opportunities for new hires to get integrated into the culture. While these opportunities can be both in person and virtual, employers must be intentional about creating a culture that employees want to be associated with.

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