



Financial Services & Products ADVISORY ■

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It's Not Over Yet: FFIEC Issues Guidance for Additional Loan Accommodations

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On August 3, 2020, the Federal Financial Institutions Examination Council (FFIEC) members issued a [Joint Statement on Additional Loan Accommodations](#) Related to COVID-19 that discussed risk management principles relevant to institutions that work with their borrowers as loans near the end of initial loan accommodation periods related to the COVID-19 pandemic.

Generally, banking regulators have encouraged banks to consider prudent accommodations to borrowers in light of COVID-19. The Coronavirus Aid, Relief, and Economic Security (CARES) Act provides several forms of relief to businesses, including as described in our advisory [here](#). States and local governments have also provided for certain relief. In response to COVID-19, several regulators issued a [Revised Interagency Statement on Loan Modifications by Financial Institutions Working with Customers Affected by the Coronavirus](#) (discussed in our advisory [here](#)), which clarified the interaction between the [previous interagency statement](#) issued on March 22, 2020 (discussed in our advisory [here](#)) and the CARES Act. The Joint Statement now supplements and expands that previous guidance. We recommend carefully considering the Joint Statement as it applies to your individual institution and borrowers and continuing to monitor published guidance moving forward.

Prudent Risk Management Practices

For purposes of the Joint Statement, an “accommodation includes any agreement to defer one or more payments, make a partial payment, forbear any delinquent amounts, modify a loan or contract, or provide other assistance or relief to a borrower who is experiencing a financial challenge... ‘Additional accommodation options’ refer to the options a financial institution may provide to the borrower after the initial accommodation, which may include an additional accommodation, an agreement to repay any amounts deferred as a result of the initial accommodation, or an agreement to change the terms of the loan agreement to improve the long-term sustainability and affordability of the loan.”

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The Joint Statement emphasizes the need for institutions to monitor the credit risks of loans that receive accommodations and the terms of accommodations such as payment changes, interest rate changes, and modified amortization terms to spot and address deterioration in a timely manner. Following an accommodation, an institution should also reassess “risk ratings for each loan based on a borrower’s current debt level, current financial condition, repayment ability, and collateral.” However, the agencies note that an accommodation does not necessarily result in an adverse risk rating solely because of a decline in collateral value when the borrower has the ability to perform under the modified terms.

Further, the FFIEC members emphasize the importance of management information systems and reporting in monitoring accommodations or additional accommodations, specifically including:

- The scope of loans that received an accommodation.
- The types of initial and any additional accommodations provided.
- When the accommodation periods end.
- The credit risk of potential “higher-risk” segments of the portfolios, which may include segmenting by product types, post-relief payment characteristics (such as balloon payments, payment changes, and maturity extension), or borrower characteristics (such as unemployed or underemployed borrowers, credit score bands, industry, businesses in full or partial operation, or credit risk rating).

Finally, the FFIEC members emphasize the importance of clarity and timeliness of communication of options and contact protocols to borrowers and guarantors.

Well-Structured and Sustainable Accommodations

In encouraging banks to consider prudent additional accommodations, the agencies emphasize “a comprehensive review” of the borrower’s condition to improve effectiveness of the accommodation, while focusing on “fundamental risk characteristics affecting the collectability of that particular credit.” The agencies also recognize that because the COVID-19 pandemic creates uncertain long-term impacts on a borrower’s future earnings, institutions may need to rely more heavily than normal on projected financial information for both commercial and retail borrowers in making underwriting decisions.

Consumer Protection

The agencies encourage financial institutions to provide consumers with options for repaying any missed payments at the end of their accommodation and (where appropriate) for changing terms to support sustainable payments for the long term. The Joint Statement includes the following list of effective approaches:

- Providing additional accommodation options to borrowers that are affordable and sustainable.
- Providing clear, conspicuous, and accurate communications and disclosures to inform the borrowers of the available options.

- Providing such communications and disclosures in a timely manner, before the end of the accommodation period, to allow adequate time for the borrower and financial institution to consider next steps, which may include payment deferral, loan modification, or loan extension, among other options (noting certain RESPA timing requirements for mortgages).
- Basing eligibility and payment terms on consistent analyses of borrowers' (and, if applicable, guarantors') financial condition and reasonable capacity to repay.
- Ensuring policies and procedures reflect accommodation options offered by the financial institution and promote consistency with applicable laws and regulations, including fair lending laws.
- Providing appropriate training to employees and other persons responsible for compliance and operational procedures related to any additional accommodation options, including customer service personnel.
- Ensuring that risk monitoring, audit, and consumer complaint systems are adequate to evaluate compliance with applicable laws, regulations, policies, and procedures.
- Providing complete and accurate information to borrowers and subsequent servicers during loan transfers and ensuring post-transfer servicing is consistent with the agreement with the borrower and the borrower's status at the time of transfer (noting certain RESPA requirements and recent CFPB guidance on mortgage servicing transfers).

Accounting and Regulatory Reporting

For additional accommodations that are loan modifications under generally accepted accounting principles (GAAP) and call report instructions, the Joint Statement directs institutions to follow the applicable accounting requirements (including maintenance of appropriate allowances for loan and lease losses (ALLL) or allowances for credit losses (ACL)) and regulatory reporting requirements for loan modifications under Section 4013 of the CARES Act and the Revised Interagency Statement. Additional points emphasized by the Joint Statement include:

- ALLL and ACL methodologies should consider all relevant and available information when assessing the collectability of cash flows, including changes in borrower financial condition, collateral values, lending practices, and economic conditions due to the COVID-19 pandemic.
- Under GAAP, loans should be segmented into a separate portfolio when they share similar risk characteristics for the purposes of estimating credit losses, unless they are evaluated individually.
- The COVID-19 event may impact the timing of determinations of ability to repay and the valuation of collateral; therefore, institutions should consider these impacts on their ALLL or ACL estimation methodologies to ensure continued compliance with GAAP and call report requirements.
- The Joint Statement remains consistent with the accounting and reporting considerations issued in the Revised Interagency Statement for loan modifications. If a financial institution elects to account for a loan modification under Section 4013, an additional loan modification could also be eligible under Section 4013.

- If a financial institution does not elect to account for a loan modification under Section 4013 or a loan modification is not eligible under Section 4013, additional modifications should be viewed cumulatively in determining whether the additional modification is a troubled debt restructuring (TDR). Financial institutions can refer to the Revised Interagency Statement for additional information when making the determination.
- For all other subsequent loan modifications, a financial institution can evaluate the subsequent modifications by referring to applicable regulatory reporting instructions and internal accounting policies to determine whether such modifications are accounted for as TDRs under ASC Subtopic 310-40.
- Past due status should be determined by reference to the revised contract terms of the loan.
- Accrual status should be determined by reference to call report instructions and internal accounting policies.

Internal Control Systems

The Joint Statement provides that prudent testing by internal control functions (quality assurance, credit risk review, operational risk management, compliance risk management, and internal audit, commensurate with the size and complexity of the institution) typically confirm the following:

- Accommodation terms are extended with appropriate approval.
- Additional accommodation options offered to borrowers are presented and processed fairly and consistently and comply with applicable laws and regulations, including fair lending laws.
- Servicing systems accurately consolidate balances, calculate required payments, and process billing statements for the full range of potential repayment terms that exist once the accommodation periods end.
- Staff, including problem loan and collections personnel, are qualified and can efficiently handle expected workloads.
- Borrower and guarantor communications and legal documentation are clear, accurate, and timely and in accordance with contractual terms, policy guidelines, and federal and state laws and regulatory requirements.
- Risk rating assessments are timely and appropriately supported.

Note that federal and state regulators are issuing additional law and guidance as the COVID-19 situation evolves. If you encounter any specific issues that are not addressed in the regulatory guidance, please feel free to contact us.

Alston & Bird has formed a multidisciplinary [response and relief team](#) to advise clients on the business and legal implications of the coronavirus (COVID-19). You can [view all our work](#) on the coronavirus across industries and [subscribe](#) to our future webinars and advisories.

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