Banks get break they needed on loan workouts

By John Reosti
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Banks and credit unions are eager to take advantage of newfound flexibility for restructuring loans battered by the coronavirus outbreak.

Federal regulators and the Financial Accounting Standards board gave lenders a helping hand Sunday, agreeing that short-term loan modifications tied to the pandemic do not have to immediately count as troubled-debt restructurings. Normally, any concession made to a borrower would trigger classification as a TDR.

In the aftermath of the financial crisis, restructured loans at banks topped $140 billion at the end of 2011. Clearly, regulators are hoping to head off a similar surge due to the coronavirus outbreak.

The issue had also gained the attention of some lawmakers.

Rep. Blaine Luetkemeyer, R-Mo., in an interview Friday, identified TDRs as "stumbling block" that would "inhibit banks from doing what they need to do." Luetkemeyer said at the time that he was exploring ways to rescind or suspend the accounting for such restructurings.

A delay in recording TDRs should lessen any spike in problem loans in advance of first-quarter earnings and, by extension, "reduces the threat on declines to tangible book value per share," especially for publicly traded banks, said Chris Marinac, an analyst at Janney Mntgomery Scott.

Marinac had called on regulators to issue emergency guidance on how lenders should treat credits impaired by coronavirus turmoil.

“This is an unprecedented credit event for all banks, therefore it requires an emergency playbook,” Marinac wrote in a Thursday research note.

Many banks, including Howard, the $4.4 billion-asset Camden National in Maine, and the $6.7 billion-asset Tompkins Financial in Ithaca, N.Y., started approving temporary deferments and other loan modifications for hard-pressed clients well in advance of Sunday's statement.

"We've been emphasizing short-term relief, deferring payments for 90 days," said Renee Smyth, chief experience and marketing officer at Camden National.

"We want to help take some of the pressure off borrowers, but we don't want to have to classify the loans as TDRs," Smyth added. The regulatory intervention "helps us as a bank."

While some loans will require restructuring, having to deal with a wave of new TDRs "would become a bigger reporting issue," Smyth said.

Scully noted that the relief will take some strain off her staff. Absent the intervention, bankers would be scrambling to calculate cash flows and discounts to determine impairment.

"Which cash-flow stream are you going to discount to determine if there’s impairment?" Scully said. "What if they said you have to look at the cash flow at the time you made this decision? … The people who are at ground zero in this situation are the last people in the world you’d want to be doing a premature discounted cash-flow analysis on.”

A number of banks might also suffer from "gaps of institutional knowledge" for work outs since it has been a dozen years since the last economic downturn, Aite Group noted in a recent report.

While the Federal Deposit Insurance Corp., Office of the Comptroller of the Currency, Federal Reserve and the National Credit Union Administration issued a joint statement March 9 encouraging lenders “to work constructively with borrowers," Scully said that guidance was too general to give lenders enough confidence that current actions wouldn’t come back to bite them in the future.

“That sort of guidance was much too high-level, as well intentioned as it might have been,” Scully said. “We’ve been desperately pleading with people for more specific and tangible and actionable guidance. … This whole idea of how forbearance actions are going to be treated has been at the top of every list of priorities.”

The event that appears to have galvanized the new stance was a letter FDIC Chairman Jelena McWilliams wrote to FASB Thursday urging for a suspending of the Current Expected Credit Losses standard and adjustments to TDR accounting rules.

Three days later, the regulatory agencies stated that they “will not criticize institutions for working with borrowers and will not direct supervised institutions to automatically categorize all COVID-19 related loan modifications as troubled debt restructurings.”

The FASB issued a separate statement Sunday agreeing with the approach.

“This guidance was developed in consultation with the staff of the FASB who concur with this approach and stand ready to assist stakeholders with any questions they may have during this time,” FASB stated.

The statements are "useful” because they "help ward off what would otherwise be a regulatory problem," said Stephen Romaine, Tompkins' president and CEO.

“It prevents an additional wound from a regulator saying your TDRs have gone up because you went out of your way to help your clients by deferring payments," Romaine added. “They’ve made things abundantly clear. We greatly appreciate the fact the regulators have acknowledged the significance of this and why banks need to do this for their clients.”

For Scully, Sunday's announcement puts Howard and other banks in a better position to help their communities when recovery efforts begin.

Uncertainty surrounding TDRs “was creating a lot of angst about what it would do to your future ability to help the economy rebound when it’s time for that to happen,” Scully said.