



Credit Risk Management During Uncertain Times

PRESENTED BY: JORGE OLAZAGASTI, MBA, DIRECTOR &
MELISSA CORREA, CRCM, MANAGER

AUGUST 27, 2020



How to Earn CPE Credits

To earn CPE Credit, each attendee must:

- Login individually to the session using your own link as provided to you via email.
- Successfully complete at least 3 of the 5 of the polling questions.
- Respond to polling questions within the allotted 90-120 seconds.

You will not earn CPE credit if you:

- Login using someone else's link.
- Join only the conference call.
- Fail to successfully complete 3 of the 5 polling questions.
- Fail to remain logged on to the session for a minimum of 50 minutes.
- Viewing a recording of this session (CPE is awarded only for live sessions).

Evaluation:

Upon completion of this program you will receive an event evaluation, you must complete it & send back to us via email at solutions@mercadien.com.

CPE Certificate:

Emailed to you within 2 weeks from the date of the webinar.

Agenda

- Safety & Soundness Examinations
- Lending Initiatives
- Forbearance
- Monitoring Delinquencies & Initiatives
- Troubled Debt Restructuring (TDR)
- Understand Your Loan Portfolio
- Internal Control Systems
- Independent Loan Review
- Board Reporting



Safety & Soundness Examinations

- Capital Adequacy
- Asset Quality
 - Classifications of Credits
 - Credit Risk Review
 - New Loans
 - Paycheck Protection Program
 - Credit Modifications
 - Nonaccrual
 - Allowance for Loan & Lease Losses
 - Obligations of Taxing Authorities
 - Real Estate Values
 - Appraisal & Evaluation Delays



Safety & Soundness Examinations (*cont'd.*)

- Management
 - Operational Risk
 - Independent RiskManagement & Audit
- Earnings
- Liquidity
- Sensitivity to Market Risk



Lending Initiatives

- Relaxing due dates for loan payments
- Extending grace periods
- Modifying terms on existing loans
- Easing credit card limits
- Extending new credit
- Waiving late fees and other fees
- Allowing customers to defer or skip payments
- Delaying the submission of delinquency notices to credit bureaus
- Fair lending laws - provide opportunity to all borrowers to benefit from these arrangements



Forbearance

- CARES Act provides protections for borrowers with federally-backed mortgages regardless of delinquency status
- Forbearance must be granted upon request & attestation to a financial hardship caused by the COVID-19
 - Attestation is exclusive requirement of CARES Act
- Period can last as long as two consecutive 180-day periods
 - Period can be shorter with customer's consent
 - No further attestation required

Forbearance *cont.*

- No additional interest, fees or penalties can be charged
- Payment deferral option - ability to repay their missed payments at the time the home is sold, refinanced or at maturity
- Refinance ability three months after forbearance ends and have made three consecutive payments under their repayment plan, or payment deferral option or loan modification.
- HUD multifamily program - up to 90-day forbearance

Loss Mitigation Guidance

- Consumer vs Commercial
- Foreclosure and eviction moratorium for single family homeowners thru August 31, 2020- federally-backed mortgages
 - New York
 - New Jersey



Loss Mitigation Guidance *(cont'd.)*

- New York

- No eviction or foreclosure of any tenant residential or commercial property for 90 days (June 20, 2020); extended to August 20 if owned by someone eligible for pandemic relief such as unemployment
- NY Supreme Court ruled that stay does not apply to sale of pledged interest governed by the UCC
- NYC administrative code amended to provide greater protections to tenants
- Free credit reports for NY consumers



Loss Mitigation Guidance *(cont'd.)*

- New Jersey
 - Consistent with safe & sound banking practices: relax due dates for loan payments (of all types, including mortgage, commercial, student & other consumer loans), extending grace periods, modifying terms on existing loans, easing credit card limits, extending new credit, waiving late fees and other fees, allowing customers to defer or skip payments & delaying the submission of delinquency notices to credit bureaus.



Monitoring of Delinquencies & Lending Initiatives

- Understand provisions of loan agreements
- Monitor terms of accommodations- payment changes, interest rate changes, modified amortization terms
- Reporting of volumes, \$ amounts, fees waived, extensions granted at portfolio level, but should be tracked at loan level as well



Initial Risk Management

- Provide additional accommodation options that are affordable & sustainable
- Provide clear, conspicuous & accurate communications & disclosures of available options
- Communications timely before the end of accommodation period
- Ensure consistent eligibility & payment terms, in line with laws & regulations
- Update to policies & procedures
- Employee Training
- Three lines of defense - risk monitoring by business line, compliance & audit

Troubled Debt Restructuring (TDR)

- CARES Act Section 4013 - option to temporarily suspend TDR treatment
 - Loan modification must be related to COVID-19
 - Loan was not more than 30 days past due as of 12/31/2019
 - Executed between 3/1-12/31/2020 or 60 days after termination of National Emergency declaration
 - Should maintain records of volume



Troubled Debt Restructuring (TDR)

(cont'd.)

- Modifications not eligible under Section 4013
 - Not automatic TDR treatment, if made in good faith in response to COVID-19, three assumptions
 - Short term (e.g. six months) modifications – payment deferrals, fee waivers, extensions of repayment terms, delays in payment that are insignificant
 - Borrower was current
 - Modification in response to National Emergency
 - Gov't mandated modifications or deferrals related to COVID would not be in scope for TDR evaluation.
- All other modifications - refer to applicable regulatory reporting inductions & accounting policies related to TDRs.

Understand Your Loan Portfolio

- Commercial & Industrial
- Commercial Real Estate
- Construction & Development
- Owner-Occupied/Income Producing Property
- Loan Approved with Policy Exceptions
- Others (Asset Based Lending, Participations, Shared National Credits)



Sources & Nature of Loan Repayment

- Rent roll based
- Asset conversion
- Services
- Industries served
- Timing & quality of updated financial information
- Accounts receivables
- Borrower's liquidity levels & timeliness of cash conversion

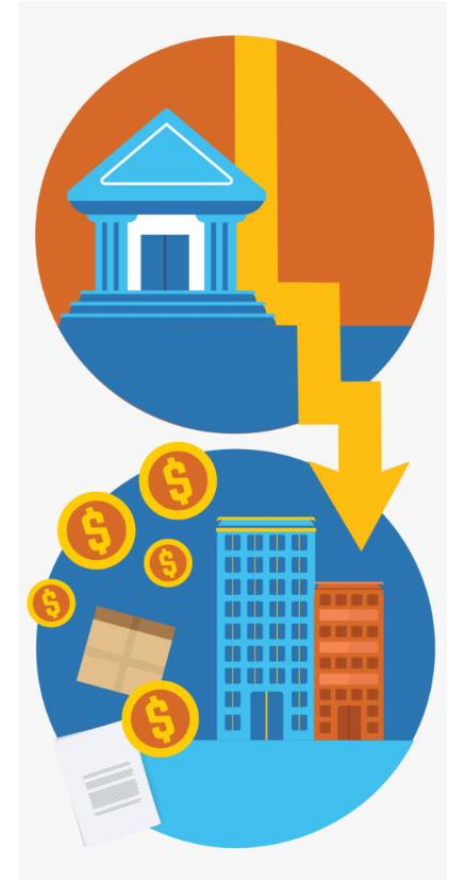
Loan Contractual Terms

- Common contractual terms
- Waivers
- Accommodations granted related to COVID-19
- Events of default



Business Relation with the Bank

- Deposit accounts
- Lines of credit
- Other lending products (consumer & commercial)
- Guarantors relations



Ongoing Repayment Ability

- Assessment of post COVID-19 accommodations
- Guarantors willingness & ability to financially support the business
- Collateral values



Identification of Potential Problem Loans

- Portfolio slicing & dicing
- Industries/borrowers more affected by COVID-19
- Scenarios for loan payment stress testing
- Contractual extensions & modifications
- Technical loan defaults



Internal Control Systems



- Approvals are documented & in accordance with loan policy
- Core systems accurately reflect balances, payments, collection status, risk ratings, etc.
- No apparent violations of laws or regulations occurred through the underwriting process
- Staff levels are appropriate to manage the loan volume
- Risk rating assessments & determination of accrual status are timely & appropriately documented
- Front end and back end collections
- Compliance with Government-Guaranteed lending programs

Independent Loan Review

- Timely identification of problem credits
- Identification of loans that should be charged off, placed in non-accrual status, recognized as covered transactions, or subject to workout management
- Identification of weaknesses in procedures which could expose the bank to losses
- Independent assessment of credit quality & process integrity
- Validation of grading activities by account managers, underwriters & workout specialists to ensure grades are accurate & reflective of risk in the bank's credit granting activities
- Monitoring of credit policy exceptions & reporting on levels of exceptions & trends therein

Board Reporting

- Enhanced reporting packages



Resource Guide

- **Interagency Statement on Loan Modifications & Reporting for Financial Institutions Working with Customers Affected by the Coronavirus (March 2020)**
 - Encourages financial institutions to work prudently with borrowers
 - Describes the agencies' interpretation of how current accounting rules
 - Applies certain COVID-19-related loan modifications
- **Interagency Examiner Guidance for Assessing Safety & Soundness Considering the Effect of the COVID-19 Pandemic on Institution (June 2020)**
 - Describes examiner guidance to outline the supervisory principles for assessing the safety & soundness of institution given the ongoing impact of the COVID-19 pandemic
- **Joint Statement on Additional Loan Accommodations Related to COVID-19 (August 2020)**
 - Provides prudent risk management protection principles for financial institutions to consider while working with borrowers as loans near the end of initial loan accommodation periods applicable during the Coronavirus Disease 2019 (COVID event).

Questions?



Contact Us



Jorge Olazagasti, MBA

Director

jolazagasti@Mercadien.com

609-689-2445



Melissa Correa, CRCM

Manager

mcorrea@Mercadien.com

609-689-2367

Disclaimer

- *DISCLAIMER: This advisory resource is for general information purposes only. It does not constitute business or tax advice, and may not be used and relied upon as a substitute for business or tax advice regarding a specific issue or problem. Advice should be obtained from a qualified accountant, tax practitioner or attorney licensed to practice in the jurisdiction where that advice is sought.*