Loan Workouts and Nonaccrual Policy, and Regulatory Reporting of Troubled Debt Restructured Loans

77 Fed. Reg. 4927 (Feb. 1, 2012)

Comments of

The National Consumer Law Center

on behalf of its low income clients

and

The National Association of Consumer Advocates

The National Consumer Law Center[1] (NCLC) submits these comments on behalf of its low-income clients and on behalf of the National Association of Consumer Advocates.[2]

We support the National Credit Union Administration's (NCUA) proposed rulemaking requiring federally insured credit unions (FICUs) to maintain written policies governing loan workouts. Requiring written loan workout policies is a sensible step that will promote the transparency and accountability of the credit unions.

We also applaud NCUA for moving to more commonsense reporting of troubled debt restructured loans (TDR loans) in the FICUs' Call Reports. Permitting modified loans to be reported as current when payments are made according to the modified terms is prudent and responsible. It reflects the economic realities better than the current reporting requirements. This more realistic reporting should encourage credit unions to perform more loan modifications. The result will be fewer foreclosures and more sustainable, performing loan modifications, improving the long-term safety and soundness of the federally insured credit unions.

The existing TDR reporting requirement discourages sustainable loan modifications. Permanent loan modifications result in better long-term outcomes for homeowners and creditors than do short-term modifications, because short-term modifications result in much higher rates of redefault.[3] But NCUA

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[1] The **National Consumer Law Center, Inc.** (NCLC) is a non-profit Massachusetts Corporation, founded in 1969, specializing in low-income consumer issues, with an emphasis on consumer credit. On a daily basis, NCLC provides legal and technical consulting and assistance on consumer law issues to legal services, government, and private attorneys representing low-income consumers across the country. NCLC publishes a series of eighteen practice treatises and annual supplements on consumer credit laws, including *Truth In Lending* (7th ed. 2010) and *Cost of Credit: Regulation, Preemption, and Industry Abuses* (4th ed. 2009) and *Foreclosures* (3d ed. 2010), as well as bimonthly newsletters on a range of topics related to consumer credit issues and low-income consumers. NCLC attorneys have written and advocated extensively on all aspects of consumer law affecting low-income people, conducted training for thousands of legal services and private attorneys on the law and litigation strategies to deal predatory lending and other consumer law problems, and provided extensive oral and written testimony to numerous Congressional committees on these topics. These comments were written by Diane E. Thompson, Of Counsel.

[2] The **National Association of Consumer Advocates** (NACA) is a non-profit corporation whose members are private and public sector attorneys, legal services attorneys, law professors, and law students, whose primary focus involves the protection and representation of consumers. NACA's mission is to promote justice for all consumers.

[3] *See, e.g.*, Zhiqin Huang et al., *Modified Current Loans Are Three Times as Likely to Default as Unmodified Current Loans*, MOODY'S RESILANDSCAPE 9, 11 (Feb. 1, 2011); Yan Zhang, Does Loan Renegotiation Differ by Securitization Status?

currently requires credit unions to report the delinquency status of permanently modified loans that qualify as TDRs based on the original contract terms, until the homeowner makes six consecutive payments under the modified loan terms.[4] This means that even if the homeowner is making all required payments, and indeed, even if the homeowner has never missed a payment, because the loan was modified before the homeowner fell into default, the credit union will have to show six months of delinquent payments on its books. Elevated delinquency numbers, of course, can lead to adverse consequences for the credit unions in a variety of ways. Faced with those adverse consequences, rational actors may well choose temporary modifications[5] because temporary modifications do not trigger the TDR delinquency reporting requirements.

The result of the current reporting scheme is that credit unions that offer permanent modifications have elevated delinquency numbers over credit unions that offer temporary modifications. Requiring modified but performing loans to be reported as delinquent unfairly penalizes credit unions that offer homeowners sustainable loan modifications and discourages sustainable modifications. Because the temporary modifications favored by the current rules are not sustainable, the current rules undermine the safety and soundness of the FICUs, as well as obscuring the reality that the loan is, in fact, performing as agreed.

Offering homeowners temporary agreements that are not sustainable does not promote the long-term safety and soundness of the federal credit unions. Allowing FICUs to report TDRs as current when payments are being made under the modified terms is, in itself, reasonable and promotes the long-term safety and soundness of the FICUs. We applaud NCUA's proposed changes to the delinquency reporting rules for TDRs.

An Empirical Study 29, 41 tbl.4 (Dec. 2010) (unpublished manuscript), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1773103 (follow "One-Click Download" hyperlink) (finding that temporary repayment agreements result in foreclosure nearly three times as often as permanent modifications).

[4] National Credit Union Administration, *Loan Workouts and Nonaccrual Policy, and Regulatory Reporting of Troubled Debt Restructured Loans*, 77 Fed. Reg. 4928-29 (Feb. 1, 2012).

[5] Manuel Adelino, Kristopher Gerardi, and Paul S. Willen, *Why Don't Lenders Renegotiate More Home Mortgages? Redefaults, Self-Cures, and Securitization* 23-24 (Fed. Reserve Bank of Boston Public Pol'y Paper No. 09-4, July 6, 2009), *available at* http://www.bos.frb.org/economic/ppdp/2009/ppdp0904.pdf.