TROUBLED DEBT RESTRUCTURING (TDR) GUIDANCE

DANIEL F. MORRILL, CPA

In these difficult times, we understand that financial institutions are ready to do what is necessary to assist borrowers. The question that arises is whether or not modifications to assist borrowers need to be evaluated to determine if they are a troubled debt restructuring (TDR), even if it is a program offered to every borrower. The short answer is "yes." At this time, we are not aware of any expected guidance from standard setters or regulators that would grant relief from TDR accounting as a result of COVID-19. If that changes, we will certainly provide additional communication.

The following considerations are provided to assist you in assessing whether modifications qualify as a TDR.

A TDR occurs if the creditor for economic or legal reasons related to the borrower's financial difficulties grants a concession to the debtor that it would not otherwise consider.

Given the types of modifications that are being proposed (payment deferrals, interest only periods, reduction of rate for a period), there are two key steps to consider that should assist you in determining whether a modification is a TDR.

STEP 1: Does the modification result in an insignificant delay in payment?

If the modification results in an insignificant delay in payment, there is no concession, and it is not considered a TDR. Key considerations in this assessment are as follows:

- The significance of the delayed payments relative to the unpaid principal balance or collateral value of the loan
- The significance of the period of delay relative to any of the following
    - the frequency of payments
    - original contractual maturity
    - original expected duration

How we see it: The facts and circumstances of each modification program and individual modification will need to be assessed. However, a 3-6 month payment deferral or interest only period will most likely be considered an insignificant delay in payment on most commercial,

commercial real estate and residential real estate loans, unless the term or expected duration of the loan was extremely short upon origination.

If the modification is deemed to be only an insignificant delay in payment, Step 2 does not need to be performed as you do not have a TDR.

STEP 2: Is the borrower experiencing financial difficulty?

One key indicator that should be examined to determine if the borrower is experiencing financial difficulty is as follows:

- Is the borrower currently in payment default (i.e. past due) or **do you expect they would be in payment default in the foreseeable future without the modification?**

How we see it: If a borrower is already in payment default, any modification that is a concession will likely be a TDR.

However, for those borrowers that are current, the assessment of being in payment default in the foreseeable future is very judgmental and difficult. We believe that understanding the industry the borrower operates in will be critical to this assessment. A borrower that is current today that operates in an industry such as hospitality, may have a greater likelihood of being in default in the future without the modification than a borrower in an industry that isn't expected to be impacted as much.

DANIEL F. MORRILL, CPA
PRINCIPAL, AUDIT
413-726-6857
DMORRILL@WOLFANDCO.COM

WOLFANDCO.COM