TO: Chief Executive Officers of National Banks, Department and Division Heads, and All Examining Personnel

PURPOSE

On June 12, 2000 the Federal Financial Institutions Examination Council published in the Federal Register a final notice that revised the Uniform Retail Credit Classification and Account Management Policy originally published in the Federal Register on February 10, 1999. The Office of the Comptroller of the Currency is adopting the revised policy and will apply it to all national banks and their operating subsidiaries. OCC Bulletin 99-13 is hereby rescinded.

POLICY

The policy establishes standards for classification and account management of retail credit in banks and thrifts. It generally requires that closed-end loans be charged off when 120 days past due and that open-end credit be charged off when 180 days past due. Other important provisions of the policy include:

- Criteria for classifying delinquent residential mortgage and home equity loans;
- Charge-off criteria for bankrupt obligors, deceased obligors, and fraud;
- Limits and criteria for re-aging open-end credit; and
- Guidance for controlling the use of extensions, deferrals, renewals, and rewrites of closed-end loans.

The final policy contains revisions adopted in response to comments and requests for clarification from the banking industry and consumer groups. The final policy:

- Requires banks to establish explicit standards that control the use of extensions, deferrals, renewals, and rewrites for closed-end loans;
- Allows an additional re-age of open-end credits in formal workout or debt management programs that meet all other re-aging requirements; and
- Extends the charge-off time frame for open-end and closed-end retail loans secured by one- to four-family residential real estate to 180 days past due.
The policy allows examiners to classify retail credits that exhibit signs of weakness regardless of their delinquency status, and to classify entire retail portfolios where underwriting standards are weak and present unreasonable credit risk.

**IMPLEMENTATION**

The policy should be fully implemented for the reporting period ending December 31, 2000.

Re-aging of open-end loans that occur prior to implementation do not count toward the once-in-twelve months/twice-in-five years limitation. However, examiners should review a bank’s record of re-aging accounts to ensure that the use of this practice was not excessive prior to the implementation date.

For further information contact the Credit Risk Division, (202) 874-5170.

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David D. Gibbons
Deputy Comptroller for Credit Risk

Attachment -- 65 FR 36903 (June 12, 2000)
AGENCY: Federal Financial Institutions Examination Council.

ACTION: Final notice.

SUMMARY: The Federal Financial Institutions Examination Council (FFIEC), on behalf of the Board of Governors of the Federal Reserve System (FRB), the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), and the Office of Thrift Supervision (OTS), collectively referred to as the Agencies, is publishing revisions to the Uniform Retail Credit Classification and Account Management Policy, to clarify certain provisions, especially regarding the re-aging of open-end accounts and extensions, deferrals, renewals, and rewrites of closed-end loans. The National Credit Union Administration (NCUA), also a member of FFIEC, does not plan to adopt the Uniform Policy at this time. This Policy is a supervisory policy used by the Agencies for uniform classification and treatment of retail credit loans in financial institutions.

DATES: Any changes to an institution's policies and procedures as a result of the Uniform Retail Credit Classification and Account
Management Policy issued on February 10, 1999, as modified by these revisions, should be implemented for reporting in the December 31, 2000, Call Report or Thrift Financial Report, as appropriate.

FOR FURTHER INFORMATION CONTACT:


SUPPLEMENTARY INFORMATION:

Background Information

On June 30, 1980, the FRB, FDIC, and OCC adopted the Uniform Policy for Classification of Consumer Installment Credit Based on Delinquency Status (1980 policy). The Federal Home Loan Bank Board, the predecessor of the OTS, adopted the 1980 policy in 1987. The 1980 policy established uniform guidelines for the classification of retail
installment credit based on delinquency status and provided charge-off time frames for open-end and closed-end credit.

The Agencies undertook a review of the 1980 policy as part of their review of all written policies mandated by Section 303(a) of the Riegle Community Development and Regulatory Improvement Act of 1994. As a result of this review, on February 10, 1999 (64 FR 6655), the Agencies issued the Uniform Retail Credit Classification and Account Management Policy (Uniform Policy). In general, the Uniform Policy:

- Established a charge-off policy for open-end credit at 180 days delinquency and closed-end credit at 120 days delinquency.
- Provided guidance for loans affected by bankruptcy, fraud, and death.
- Established guidelines for re-aging, extending, deferring, or rewriting past due accounts.
- Provided for classification of certain delinquent residential mortgage and home equity loans.
- Provided an alternative method of recognizing partial payments.

As issued on February 10, 1999, the Uniform Policy was effective for manual adjustments to an institution's policies and procedures as of the June 30, 1999, Call Report or Thrift Financial Report, as appropriate. In addition, the Uniform Policy allowed institutions until the December 31, 2000, Reports to make changes involving computer programming resources. In a modification issued on November 23, 1999 (64 FR 65712), the implementation date for manual changes was extended to the December 31, 2000, Reports.

Following the issuance of the Uniform Policy, the Agencies received numerous inquiries for clarifications of the standards contained in the Policy, especially with respect to the re-aging of open-end accounts and extensions, deferrals, renewals, or rewrites of closed-end loans. In response to these inquiries for clarification, the Agencies have decided to publish this revised Uniform Policy. In addition to various editorial changes, the Agencies have changed the Uniform Policy to clarify various items in the Uniform Policy with respect to (1) the re-aging of open-end accounts; (2) extensions, deferrals, renewals, and rewrites of closed-end loans; (3) examiner considerations; and (4) the treatment of specific categories of retail loans.

1. Re-aging of open-end accounts. The Uniform Policy provided that open-end accounts should not be re-aged more than once within any
twelve-month period and no more than twice within any five-year period. The Agencies have decided to clarify the Uniform Policy by stating that institutions may adopt a more conservative re-aging standard (e.g., some institutions allow only one re-aging in the lifetime of an open-end account). In addition, this modification of the Uniform Policy recognizes the importance of formal workout programs and provides guidance on the handling of open-end accounts that enter into this type of program.

Specifically, the Agencies have modified the Uniform Policy to provide that institutions may re-age an account after it enters a workout program, including internal and third-party debt counseling services, but only after receipt of at least three consecutive minimum monthly payments or the equivalent cumulative amount. Re-aging for workout program purposes is limited to once in a five-year period and is in addition to the once-in-twelve-months/twice-in-five-years limitation. The term "re-age" is defined in the document (in footnote 3) to mean "returning a delinquent, open-end account to current status without collecting the total amount of principal, interest, and fees that are contractually due." In the Agencies' view, management information systems should track the principal reductions and charge-off history of loans in workout programs by type of program.

2. Extensions, deferrals, renewals, and rewrites of closed-end loans. The Agencies have modified the Uniform Policy to provide that institutions should adopt and adhere to explicit standards that control the use of extensions, deferrals, renewals, and rewrites of closed-end loans. Such standards would be based on the borrower's willingness and ability to repay the loan and would limit number and frequency of such treatment of closed-end loans. The Agencies have also defined the terms "extension," "deferral," "renewal," and "rewrite."

This modification of the Uniform Policy states that institutions should adopt standards that prohibit additional advances that finance the unpaid interest and fees. The Agencies have added guidance that comprehensive and effective risk management, reporting, and internal controls be established and maintained to support the collection process and to ensure timely recognition of losses.

3. Examination considerations. The Agencies have added guidance
that an examiner may classify retail portfolios, or segments thereof, where underwriting standards are weak and present unreasonable credit risk and may criticize account management practices that are deficient.

Adoption of the Uniform Policy may affect an institution's timing and measurement of probable loan losses that have been incurred. As a result of changes the Uniform Policy made to the 1980 policy, an institution may need to adjust its loan loss allowance to reflect any shortening in its time frame for recording charge-offs. Moreover, a larger allowance may be necessary if an institution's charge-off practices are different than the new guidelines for accounts of deceased persons and accounts of borrowers in bankruptcy.

4. Treatment of specific categories of retail loans. These modifications to the Uniform Policy clarified the Policy's treatment of various categories of retail loans:

- Regarding retail loans that are due to be charged off, in lieu of charging off the entire loan balance, loans with non-real estate collateral may be written down to the value of the collateral, less cost to sell, if repossession of collateral is assured and in process.

- For open- and closed-end loans secured by one-to four-family residential real estate, a current assessment of value should be made no later than 180 days past due, and any outstanding loan balance in excess of the value of the property, less cost to sell, should be charged off. The Agencies removed the condition in the Uniform Policy that such assessment would be required when a residential or home equity loan is 120 days past due.

- Loans in bankruptcy with collateral may be written down to the value of the collateral, less cost to sell.

As modified, the Uniform Policy now reads as follows:

Uniform Retail Credit Classification and Account Management Policy

\1\ The agencies’ classifications used for retail credit are Substandard, Doubtful, and Loss. These are defined as follows:

Substandard: An asset classified Substandard is protected
inadequately by the current net worth and paying capacity of the obligor, or by the collateral pledged, if any. Assets so classified must have a well-defined weakness or weaknesses that jeopardize the liquidation of the debt. They are characterized by the distinct possibility that the institution will sustain some loss if the deficiencies are not corrected. Doubtful: An asset classified Doubtful has all the weaknesses inherent in one classified Substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, conditions, and values, highly questionable and improbable. Loss: An asset, or portion thereof, classified Loss is considered uncollectible, and of such little value that its continuance on the books is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value; rather, it is not practical or desirable to defer writing off an essentially worthless asset (or portion thereof), even though partial recovery may occur in the future.

Although the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, and Office of Thrift Supervision do not require institutions to adopt identical classification definitions, institutions should classify their assets using a system that can be easily reconciled with the regulatory classification system.

The Uniform Retail Credit Classification and Account Management Policy establishes standards for the classification and treatment of retail credit in financial institutions. Retail credit consists of open- and closed-end credit extended to individuals for household, family, and other personal expenditures, and includes consumer loans and credit cards. For purposes of this policy, retail credit also includes loans to individuals secured by their personal residence, including first mortgage, home equity, and home improvement loans. Because a retail credit portfolio generally consists of a large number of relatively small-balance loans, evaluating the quality of the retail credit portfolio on a loan-by-loan basis is inefficient and burdensome for the institution being examined and for examiners.
Actual credit losses on individual retail credits should be recorded when the institution becomes aware of the loss, but in no case should the charge-off exceed the time frames stated in this policy. This policy does not preclude an institution from adopting a more conservative internal policy. Based on collection experience, when a portfolio's history reflects high losses and low recoveries, more conservative standards are appropriate and necessary.

The quality of retail credit is best indicated by the repayment performance of individual borrowers. Therefore, in general, retail credit should be classified based on the following criteria:

- Open- and closed-end retail loans past due 90 cumulative days from the contractual due date should be classified Substandard.
- Closed-end retail loans that become past due 120 cumulative days and open-end retail loans that become past due 180 cumulative days from the contractual due date should be classified Loss and charged off. In lieu of charging off the entire loan balance, loans with non-real estate collateral may be written down to the value of the collateral, less cost to sell, if repossession of collateral is assured and in process.

\[\text{OTS regulation 12 CFR 560.160(b) allows savings institutions to establish adequate (specific) valuation allowances for assets classified Loss in lieu of charge-offs.}\]

- Open-end retail accounts that are placed on a fixed repayment schedule should follow the charge-off time frame for closed-end loans.

- One- to four-family residential real estate loans and home equity loans that are past due 90 days or more with loan-to-value
ratios greater than 60 percent should be classified Substandard. Properly secured residential real estate loans with loan-to-value ratios equal to or less than 60 percent are generally not classified based solely on delinquency status. Home equity loans to the same borrower at the same institution as the senior mortgage loan with a combined loan-to-value ratio equal to or less than 60 percent need not be classified. However, home equity loans where the institution does not hold the senior mortgage, that are past due 90 days or more should be classified Substandard, even if the loan-to-value ratio is equal to, or less than, 60 percent.

For open- and closed-end loans secured by residential real estate, a current assessment of value should be made no later than 180 days past due. Any outstanding loan balance in excess of the value of the property, less cost to sell, should be classified Loss and charged off.

- Loans in bankruptcy should be classified Loss and charged off within 60 days of receipt of notification of filing from the bankruptcy court or within the time frames specified in this classification policy, whichever is shorter, unless the institution can clearly demonstrate and document that repayment is likely to occur. Loans with collateral may be written down to the value of the collateral, less cost to sell. Any loan balance not charged off should be classified Substandard until the borrower re-establishes the ability and willingness to repay for a period of at least six months.

- Fraudulent loans should be classified Loss and charged off no later than 90 days of discovery or within the time frames adopted in this classification policy, whichever is shorter.

- Loans of deceased persons should be classified Loss and charged off when the loss is determined or within the time frames adopted in this classification policy, whichever is shorter.

Other Considerations for Classification

If an institution can clearly document that a past due loan is well secured and in the process of collection, such that collection will occur regardless of delinquency status, then the loan need not be classified. A well-secured loan is collateralized by a perfected security interest in, or pledges of, real or personal property.
including securities with an estimable value, less cost to sell, sufficient to recover the recorded investment in the loan, as well as a reasonable return on that amount. In the process of collection means that either a collection effort or legal action is proceeding and is reasonably expected to result in recovery of the loan balance or its restoration to a current status, generally within the next 90 days.

Partial Payments on Open-and Closed-End Credit

Institutions should use one of two methods to recognize partial payments. A payment equivalent to 90 percent or more of the contractual payment may be considered a full payment in computing past due status. Alternatively, the institution may aggregate payments and give credit for any partial payment received. For example, if a regular installment payment is $300 and the borrower makes payments of only $150 per month for a six-month period, the loan would be $900 ($150 shortage times six payments), or three full months past due. An institution may use either or both methods in its portfolio, but may not use both methods simultaneously with a single loan.

Re-Aging, Extensions, Deferrals, Renewals, and Rewrites

\[3\] These terms are defined as follows. Reage: Returning a delinquent, open-end account to current status without collecting the total amount of principal, interest, and fees that are contractually due. Extension: Extending monthly payments on a closed-end loan and rolling back the maturity by the number of months extended. The account is shown current upon granting the extension. If extension fees are assessed, they should be collected at the time of the extension and not added to the balance of the loan. Deferral: Deferring a contractually due payment on a closed-end loan without affecting the other terms, including maturity, of the loan. The account is shown current upon granting the deferral. Renewal: Underwriting a matured, closed-end loan generally at its outstanding principal amount and on similar terms. Rewrite: Underwriting an existing loan by significantly changing its terms,
including payment amounts, interest rates, amortization schedules, or its final maturity.

Re-aging of open-end accounts, and extensions, deferrals, renewals, and rewrites of closed-end loans can be used to help borrowers overcome temporary financial difficulties, such as loss of job, medical emergency, or change in family circumstances like loss of a family member. A permissive policy on re-agings, extensions, deferrals, renewals, or rewrites can cloud the true performance and delinquency status of the portfolio. However, prudent use is acceptable when it is based on a renewed willingness and ability to repay the loan, and when it is structured and controlled in accordance with sound internal policies.

Management should ensure that comprehensive and effective risk management and internal controls are established and maintained so that re-agings, extensions, deferrals, renewals, and rewrites can be adequately controlled and monitored by management and verified by examiners. The decision to re-age, extend, defer, renew, or rewrite a loan, like any other modification of contractual terms, should be supported in the institution's management information systems. Adequate management information systems usually identify and document any loan that is re-aged, extended, deferred, renewed, or rewritten, including the number of times such action has been taken. Documentation normally shows that the institution's personnel communicated with the borrower, the borrower agreed to pay the loan in full, and the borrower has the ability to repay the loan. To be effective, management information systems should also monitor and track the volume and performance of loans that have been re-aged, extended, deferred, renewed, or rewritten and/or placed in a workout program.

Open-End Accounts

Institutions that re-age open-end accounts should establish a reasonable written policy and adhere to it. To be considered for re-aging, an account should exhibit the following:

- The borrower has demonstrated a renewed willingness and
ability to repay the loan.

- The account has existed for at least nine months.
- The borrower has made at least three consecutive minimum monthly payments or the equivalent cumulative amount. Funds may not be advanced by the institution for this purpose.

Open-end accounts should not be re-aged more than once within any twelve-month period and no more than twice within any five-year period. Institutions may adopt a more conservative re-aging standard; for example, some institutions allow only one re-aging in the lifetime of an open-end account. Additionally, an over-limit account may be re-aged at its outstanding balance (including the over-limit balance, interest, and fees), provided that no new credit is extended to the borrower until the balance falls below the predelinquency credit limit.

Institutions may re-age an account after it enters a workout program, including internal and third-party debt counseling services, but only after receipt of at least three consecutive minimum monthly payments or the equivalent cumulative amount, as agreed upon under the workout or debt management program. Re-aging for workout purposes is limited to once in a five-year period and is in addition to the once in twelve-months/twice in five-year limitation described above. To be effective, management information systems should track the principal reductions and charge-off history of loans in workout programs by type of program.

Closed-End Loans

Institutions should adopt and adhere to explicit standards that control the use of extensions, deferrals, renewals, and rewrites of closed-end loans. The standards should exhibit the following:

- The borrower should show a renewed willingness and ability to repay the loan.
- The standards should limit the number and frequency of extensions, deferrals, renewals, and rewrites.
- Additional advances to finance unpaid interest and fees should be prohibited.

Management should ensure that comprehensive and effective risk management, reporting, and internal controls are established and
maintained to support the collection process and to ensure timely recognition of losses. To be effective, management information systems should track the subsequent principal reductions and charge-off history of loans that have been granted an extension, deferral, renewal, or rewrite.

Examination Considerations

Examiners should ensure that institutions adhere to this policy. Nevertheless, there may be instances that warrant exceptions to the general classification policy. Loans need not be classified if the institution can document clearly that repayment will occur irrespective of delinquency status. Examples might include loans well secured by marketable collateral and in the process of collection, loans for which claims are filed against solvent estates, and loans supported by valid insurance claims.

The Uniform Classification and Account Management policy does not preclude examiners from classifying individual retail credit loans that exhibit signs of credit weakness regardless of delinquency status. Similarly, an examiner may also classify retail portfolios, or segments thereof, where underwriting standards are weak and present unreasonable credit risk, and may criticize account management practices that are deficient.

In addition to reviewing loan classifications, the examiner should ensure that the institution's allowance for loan and lease losses provides adequate coverage for probable losses inherent in the portfolio. Sound risk and account management systems, including a prudent retail credit lending policy, measures to ensure and monitor adherence to stated policy, and detailed operating procedures, should also be implemented. Internal controls should be in place to ensure that the policy is followed. Institutions that lack sound policies or fail to implement or effectively adhere to established policies will be subject to criticism.

Implementation

This policy should be fully implemented for reporting in the
December 31, 2000 Call Report or Thrift Financial Report, as appropriate.

Dated: June 6, 2000.

Keith J. Todd,
Executive Secretary, Federal Financial Institutions Examination Council.

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