`

August 26, 2022

Federal Deposit Insurance Corporation
550 17th Street NW
Washington, DC 20429

Via Electronic Mail to comments@fdic.gov

RE: Assessments, Amendments to Incorporate Troubled Debt Restructuring Accounting Standards Update, RIN 3064–AF85

To whom it may concern,

The American Bankers Association and the Bank Policy Institute[1] (Associations) appreciate the opportunity to comment on the Federal Deposit Insurance Corporation's notice of proposed rulemaking to replace troubled debt restructurings (TDRs) in the assessments scorecards for banks larger than $10 billion in total assets (large banks).[2]

The proposal recognizes that Accounting Standards Update No. 2022–02 (ASU 2022–02)[3] eliminates recognition and measurement guidance for TDRs for institutions that have adopted the Current Expected Credit Losses (CECL) methodology[4] and introduces new disclosure requirements for "modifications to borrowers experiencing financial difficulty" (MBEFD). The proposal would make two changes in the assessments scorecards for large and highly complex banks:[5] it would replace TDRs[6] with MBEFD in the underperforming assets ratio and change the criterion for a refinance of a consumer or commercial loan to classify as "higher-risk" based on whether the refinance is a MBEFD.

---

1 More information about the Associations is provided in the Appendix.

2 FDIC, "Assessments, Amendments to Incorporate Troubled Debt Restructuring Accounting Standards Update," 87 *Federal Register* 45023 (July 27, 2022), available at www.govinfo.gov/content/pkg/FR-2022-07-27/pdf/2022-15763.pdf

3 Financial Accounting Standards Board, Accounting Standards Update No. 2022–02, "Financial Instruments—Credit Losses (Topic 326): Troubled Debt Restructurings and Vintage Disclosures,'' March 31, 2022, available at www.fasb.org/page/getarticle?uid=fasb_Media_Advisory_03-31-22.

4 Prior to CECL, a TDR needed to be separated because it had a different credit loss recognition measurement than other loans. However, under CECL all loans are measured under a lifetime loss recognition model and therefore TDR accounting is no longer needed.

5 Per 12 CFR 327.8(f) and (g), for deposit insurance assessment purposes, a large bank is one with $10 billion or more in total assets; a highly complex bank is one with $50 billion or more in total assets and controlled by a parent holding company with $500 billion or more in total assets, or a processing bank or trust company.

6 As reported in Call Report Schedule RC–C, Part I, Memorandum items 1.a. through 1.g, "Loans restructured in troubled debt restructurings that are in compliance with their modified terms" less the portion reported on Schedule RC–O, Memorandum item 16, "Portion of loans restructured in troubled debt restructurings that are in compliance with their modified terms and are guaranteed or insured by the U.S. government."

ASU 2022–02 is effective for fiscal years beginning after December 15, 2022 for entities that have adopted CECL.[7] The Financial Accounting Standard Board required filers to adopt CECL beginning in January 2020, excluding smaller reporting companies as defined by the U.S. Securities and Exchange Commission. Most others are required to adopt CECL beginning in January 2023. Accordingly, the proposed changes would go into effect for assessments beginning with first quarter 2023.

Because ASU 2022-02 eliminates recognition and measurement guidance of TDRs, the Associations support removal of TDRs from the large bank assessment scorecards. We appreciate the FDIC's intent to replace TDRs in the assessments scorecards with something based on U.S. Generally Accepted Accounting Principles (GAAP) as revised for ASU 2022-02. The alternative of continuing to require large banks to report TDRs in the Call Report, or else report something not disclosed in their financial statements, solely for purposes of calculating deposit insurance assessments would impose significant burdens whose costs would not justify the benefits, as recognized in the proposal.[8] We further appreciate the FDIC for moving ahead to allow the large banks time to prepare for changes in their assessments, recognizing that all will have adopted CECL by first quarter 2023 and therefore no longer disclose TDRs in their financial statements.

Nonetheless, the Associations do not see MBEFD as a suitable replacement for TDRs in the large bank assessment scorecards, as explained below. Seeing no other fitting substitute, we recommend that TDRs be removed without replacement. If the FDIC is determined to seek a TDR replacement, at a minimum, TDRs should be removed on an interim basis and the proposal reissued for public comment once ASU 2022-02 has been fully implemented via the Call Report. We request that the comment period be reopened once the Call Report and instructions are revised to incorporate ASU 2022-02 to allow bankers to fully comprehend and comment on the proposed changes.

The balance of "modifications to borrowers experiencing financial difficulty" is not an appropriate replacement for the TDRs balance in the large bank scorecards.

MBEFD are neither equivalent to TDRs nor a measure of asset quality. Similarly, the MBEFD balance is not functionally equivalent to the other items included in the large bank assessments scorecards as underperforming assets: loans 30 days or more past due, restructured loans, nonaccrual loans, and other real estate owned. Therefore MBEFD are not a fitting substitute for TDRs in these scorecards.

MBEFD are not analogous to TDRs for a few reasons. First, MBEFD under ASU 2022-02 serve as a disclosure mechanism that also includes modified assets that did not involve a concession given to the borrower and thus would not be classified as a TDR. Second, the aggregate balance of MBEFD, unlike that for TDRs (which is cumulative), is an activity and volume measure over a set period of time, whereas TDRs are a portfolio balance at a given point in time. More

---

7 Entities that adopt CECL earlier than year-end 2022 are permitted to implement ASU 2022-02 earlier.

8 Proposal, page 45027.

specifically, the MBEFD balance represents modification activity during the reporting period and subsequent performance of modifications on a 12-month trailing period. It is meant to capture how a bank manages its loan portfolio in the reporting period, not to communicate a risk profile for the loan portfolio. Under CECL the credit risk is captured and reported in the ACL. Third, the TDRs currently included in the large bank assessment scorecards include restructurings only for performing loans, whereas MBEFD include modifications for both performing and non-performing loans. (MBEFD include restructurings that are 30-plus days past due or in nonaccrual status, so use of MBEFD would introduce double-counting of underperforming assets.)

Banks conduct loan modifications to suit the needs of their customers and the banks' operations. Thus, MBEFD could vary dramatically between institutions, as it is a direct function of how individual banks execute loss mitigation efforts. A bank may disclose a higher modifications balance simply because its policies provide flexibility in working with borrowers. In consequence, the volume of modifications does not provide a fair relative measure of loan quality between different banks.

Because of this, a troubling effect of replacing TDRs with MBEFD would be to impose higher assessments on banks that actively work with customers through loan modifications. Penalizing banks for being proactive with modifications and disincentivizing this type of risk mitigation and customer assistance would seem to be at odds with the intent of the recent proposal from the FDIC, along with the Office of the Comptroller of the Currency and National Credit Union Administration, of a policy statement for prudent commercial real estate loan accommodations and workouts,[9] on the value of working prudently and constructively with creditworthy customers.

Moreover, banks will surely initiate more "modifications to borrowers experiencing financial difficulty" in times of broad financial difficulty in the economy. Therefore, inserting this measure into places in the large bank assessments scorecards would inevitably make large banks' assessments more procyclical – an undesirable effect.[10]

Elimination of TDRs with no replacement is preferred, subject to reconsideration after large banks have substantially implemented ASU 2022-02 to provide time for meaningful analysis and comment.

As an alternative to replacing TDRs with MBEFD in the large bank assessment scorecards, the proposal considers removal of TDRs without replacement – but argues that this alternative would ignore the information provided by MBEFD.[11] The Associations urge the FDIC to reconsider this

[9] FDIC, Office of the Comptroller of the Currency and National Credit Union Administration, "Policy Statement on Prudent Commercial Real Estate Loan Accommodations and Workouts," 87 *Federal Register* 47273 (August 2, 2022), available at www.govinfo.gov/content/pkg/FR-2022-08-02/pdf/2022-16471.pdf.

[10] A recent FDIC working paper "provides … large-scale evidence on the procyclical effects of deposit insurance premiums while also highlighting the importance of countercyclical deposit insurance policy." See Ryan Hess and Jennifer S. Rhee, "The Procyclicality of FDIC Deposit Insurance Premiums," FDIC Working Paper FDIC CFR WP 2022-10, August 2022, available at www.fdic.gov/analysis/cfr/working-papers/2022/cfr-wp2022-10.pdf.

[11] Ibid.

alternative. As above, we question the appropriateness of MBEFD as a TDR replacement and are concerned that the former would be an inconsistent measure between banks and make large bank assessments more procyclical. On the other hand, elimination of TDRs would apply uniformly to all large banks, as noted in the proposal.[12]

With ASU 2022-02 implementation in process, large banks need more time to be prepared to provide full feedback on the proposed changes. The Associations recommend that TDRs be eliminated from terms in the assessments scorecards without replacement, at least until large banks can better assess changes to and recalibration in the scorecards.

Clarity is needed as to how MBEFD's are to be reported in the Call Report. To the extent any potential changes to the assessment scorecards may involve MBEFDs as a replacement for TDRs, the comment period for this proposal should be reopened once modifications to the Call Report instructions have been made.

At the very least, the Associations request that the comment period be extended to allow large banks to better understand how MBEFD will be reported in the Call Report.

The FFIEC released Supplemental Instructions for June 2022 Call Reports that require "all loans modified since adoption of the new standard for borrowers experiencing financial difficulty as defined by ASU 2022-02 that are performing in accordance with their modified terms to be reported on Schedule RC-C, Part I, Memorandum items 1.a. through 1.g. If a loan is not performing in accordance with its modified terms, it would be reported on Schedule RC-N, Memorandum items 1.a through 1.g."[13]

These instructions are unclear as to whether the intent is for disclosure of the performance of modified loans to borrowers experiencing financial difficulty in the 12 months period following the modification, or instead if the disclosure is to be cumulative balances following the old "once a TDR, always a TDR" requirement for modified loans to borrowers experiencing financial difficulty. If it is the latter, this would be contrary to the FDIC's intention to eliminate dual processes, a departure from U.S. GAAP, and a significant operational burden for banks.

Large banks are in early stages of implementing ASU 2022-02, so the effects of the proposed changes and the alternatives cannot be appraised properly, as the proposal recognizes.[14] We understand that the FDIC, along with fellow members of the Federal Financial Institutions Examination Council, are working on the range of modifications to the Call Report and its instructions in light of ASU 2022-02. With sufficient progress on that front, the comment period for the proposal should be reopened after these changes are in place, to allow sufficient time for bankers to evaluate them and then the changes can be implemented in time for first quarter 2023 reporting. We hope and expect that a comment deadline early in the fourth quarter of this year would provide the time needed.

---

[12] Ibid.

[13] Federal Financial Institutions Examination Council, "Supplemental Instructions – June 2022," available at www.ffiec.gov/pdf/FFIEC_forms/FFIEC031_FFIEC041_FFIEC051_suppinst_202206.pdf.

[14] Proposal, page 45025.

However, the Associations note that it will be difficult to evaluate the impact of the proposed change even once a revised Call Report and instructions are in place. At that point, large banks will be able to produce measures for MBEFD, but for one or a few quarters. As the proposal notes, the values are likely to be lower initially compared to TDR values but could be lower or higher over time. There is already ample historical data on how the large bank assessments scorecards would perform without replacement for TDRs. Thus, the FDIC could recalibrate these scorecards with this data.

* * *

The Associations appreciate your consideration of the views expressed in this letter. If you have any questions, please contact the undersigned.

Respectfully submitted,

Robert W. Strand

Robert W. Strand
Vice President and Senior Economist
American Bankers Association

Gregg Rozansky

Gregg Rozansky
Senior Vice President and Senior Associate General Counsel
The Bank Policy Institute

Appendix

The American Bankers Association is the voice of the nation's $24 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard nearly $19.9 trillion in deposits and extend $11.4 trillion in loans.

The Bank Policy Institute is a nonpartisan public policy, research and advocacy group, representing the nation's leading banks and their customers. Our members include universal banks, regional banks and the major foreign banks doing business in the United States. Collectively, they employ almost 2 million Americans, make nearly half of the nation's small business loans and are an engine for financial innovation and economic growth.