NCUA LETTER TO CREDIT UNIONS

NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA 22314

DATE: **September 2009** **LETTER NO.: 09-CU-19**

TO: **Federally Insured Credit Unions**

SUBJ: **Evaluating Residential Real Estate Mortgage Loan Modification Programs**

ENCL: **Supervisory Letter – Evaluating Residential Real Estate Mortgage Loan Modification Programs**

Dear Board of Directors:

In response to unprecedented levels of mortgage loan defaults and foreclosures credit unions are initiating mortgage loan modification programs or other workout strategies to alleviate or minimize losses. Credit unions must take action to identify and potentially assist borrowers whose financial stress may lead to future impairment in mortgage loan performance. By proactively identifying "at risk" loans, credit unions can measure the potential impact of borrower default on net worth, assess internal liquidity available to help borrowers through loan modifications, and closely monitor the performance of these loans. Further, identifying and assisting "at risk" members before delinquency occurs may improve chances for a successful modification and reduce potential losses.

NCUA examiners were recently provided guidance in evaluating the safety and soundness of residential mortgage loan modification programs. This letter provides all federally insured credit unions with the same guidance via the enclosed Supervisory Letter.

The Supervisory Letter discusses the objectives of a loan modification program and provides NCUA field staff with guidance for evaluating whether management has made a realistic assessment of risk and exercised the proper due diligence in developing, implementing, and monitoring these inherently higher risk programs. Some of the key points addressed in the Supervisory Letter include:

- Loan modification programs will vary in sophistication depending on the size and complexity of the loan portfolio and the level of risk.

- The objectives of a residential real estate loan modification are to help members who are struggling financially to maintain ownership of their homes and to minimize the credit union's default and foreclosure costs.

- Studies suggest that lowering the monthly payment sufficiently to make it affordable in the long term, and reducing the principal balance to create greater borrower equity, may result in a more sustainable loan modification.

- Credit union management should be able to quantify how much of the mortgage loan portfolio is at risk of default and have a prudent strategy for managing or reducing the risk.

- Full and fair financial disclosure warrants separate analysis in the allowance for loan and lease losses (ALLL) for loan modifications as the risk of default is very high, even when policies and procedures are sound.

NCUA has issued several letters encouraging credit unions to work constructively with residential mortgage borrowers who may be unable to meet their contractual payment obligations. These letters, and the enclosed Supervisory Letter, provide sound practices for managing the risk associated with residential mortgage loan portfolios, including distressed mortgages.

Sincerely,

/s/

Deborah Matz
Chairman

Enclosure