

BANKRUPTCY

Most credit unions are accounting for bankrupt loans properly. However, a number of questions have arisen concerning the reporting of bankruptcies. Consistency in the industry is important. In addition, valuing the asset appropriately is essential. The primary question is will the credit union be paid.

Accounting Guidelines for Chapter 13 Bankruptcies

- A. Within 30 days of receipt of the court ordered payment plan, the loan must be written down to the maximum amount designated by the court. Regardless of whether or not the loan is re-aged, the principal balance in excess of the plan should be charged off at that time.
- B. The loan may be re-aged after three (3) consecutive months of compliance with the bankruptcy plan. Re-aging can only be applied to those loans receiving payments (generally secured loans).
- C. If the borrower is dismissed from the plan, the loan will revert to the original contract for the purposes of delinquency reporting.

Borrowers that have filed for bankruptcy are obligated to pay loans that the credit union can not possibly value as highly as loans that have been willingly and capably repaid. Not until a bankrupt loan has at least a small history of repayment should a credit union even consider restoring the asset to a status of those loans paid as agreed.

Accounting Guidelines for Chapter 7 Bankruptcies

- A. Within 30 days of receipt of the closing notice, Chapter 7 loans not reaffirmed (or not in the reaffirmation process) must be charged off.
- B. Chapter 7 loans may be reaffirmed whether the loan is paid current or is in a delinquent status at the time of reaffirmation. No minimum number of payments is required prior to the reaffirmation of a loan involved in a Chapter 7 Bankruptcy.
- C. If the member fails to adhere to the terms of the reaffirmation, the delinquency status is to revert to the original contract.

Key to the re-aging and reaffirmation process is the tracking and appropriate valuation of these loans. The value must be reflected through the funding of the Allowance for Loan and Lease Loss Account.

If you have further questions regarding the reporting of bankrupt loans, please contact your examiner.