

COVID-19 FAQ 4: When is debt forbearance required?

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Authors: [Global Financial Services Regulatory Group](#)

This FAQ is intended to provide financial institutions with an overview of the requirements imposed on them by governmental authorities to provide relief to consumer and businesses affected by the COVID-19 pandemic.

In the space of a few months, across the US and EMEA, we have seen the roll out of debt forbearance measures aimed at easing the financial repercussions of the COVID-19 crisis on household and SME debt. Household and SME debt payments to service mortgages, credit cards and personal loans generally remain due and payable even during times of widespread economic distress. The purpose of debt forbearance measures is to alleviate some of the economic burden for financially vulnerable customers. Such measures may result in a permanent loss of income for the banks or lenders as interest payments, as well as late or missed payment fees, are irretrievably waived. A significant loss of such income from an “over-application” of forbearance could initiate a domino effect and have far-reaching consequences for the financial system.

Given the variables between short- and long-term loans, secured and unsecured loans and retail and wholesale debt markets—add to the fact that different classes of debt can be housed within different domestic legal frameworks—regulators have struggled to provide detailed guidance and have, with some exceptions, approached the issue by way of guidance rather than rule change. The challenge our clients are finding with a “one-size-fits-all” guidance or expectation setting is that they are left with a number of critical decisions to take in an uncertain legal context:

- To what extent do lenders need to perform normal affordability assessments, particularly where additional interest accumulates and/or the subsequent capital repayment profile will require higher periodic repayments? If affordability assessments are required, is regulatory guidance available as to shortcuts or assumptions that can be made?
- How does the expectation on firms fit within the normal rules applying to forbearance activities and are any waivers provided? In some jurisdictions, varying or modifying consumer agreements without following a particular process can render the loans unenforceable.
- Any forbearance will inevitably impact a lender’s own economic position, but this in itself may be set within a framework of funding conditions and securitization covenants that mean any forbearance outside of “business-as-usual” could trigger a series of other legal consequences.

As you will see from the below tracker table, there is a contrast between top-down mandated measures required by law (see US CARES ACT and Spain’s RDL 8/2020) and softer regulatory (perhaps even moral) pressure on banks and lenders to “do the right thing” (see the UK regulator’s response). We expect to see government and regulator responses rush to provide more detail as industry feedback reaches them. At the EU level, the European Banking Authority (“EBA”) has provided guidance to the effect that payment moratorium schemes should not be treated as forbearance, if the measures taken are “*based on applicable national law or on an industry or sector-wide private initiative agreed and applied broadly by the relevant lenders.*” Early reviewers suggest the EBA’s Guidelines do not go far enough in assisting banks and lenders with resolving the key questions of detail identified above.

Responses in specific jurisdictions

Jurisdiction	Debt forbearance considerations
United States	<ul style="list-style-type: none"> • Federal <ul style="list-style-type: none"> ○ Relief is available for homeowners with federally backed mortgage loans under various regulatory initiatives (see here and here) and the CARES Act. ○ Federal and state financial regulators have also released joint guidance (see, e.g., here and here) and a FAQ intended to provide supervisory flexibility, facilitate residential mortgage servicers’ ability to place consumers in short-term payment forbearance programs and help them comply with the CARES Act provisions. ○ Starting July 1, 2020, homeowners who are in COVID-19 related forbearance on their federally backed mortgages may take advantage of new repayment solutions, including payment deferral, reinstatement, repayment plan or loan modification options. Effective July 1, 2020, the Consumer Financial Protection Bureau also issued an interim final rule permitting mortgage servicers to offer loss mitigation options to borrowers affected by COVID-19. ○ The CARES Act provides temporary automatic suspension of principal and interest payments on federally held student loans. ○ Federal and state financial regulators issued an interagency statement (subsequently revised) encouraging financial institutions to offer payment accommodations to their customers affected by COVID-19, including by modifying terms on current loans, if consistent with safe and sound banking practices.

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	<ul style="list-style-type: none"> ○ Similarly, the Consumer Financial Protection Bureau reminded regulated financial institutions, including providers of checking, savings or prepaid accounts, as well as credit card issuers and other open-end creditors, of their responsibility to assist consumers affected by COVID-19, such as by waiving fees, lowering minimum-balance requirements and implementing changes in account terms that benefit consumers. ● New York <ul style="list-style-type: none"> ○ A March 21, 2020, executive order temporarily amended New York Banking Law to provide that any bank subject to NYDFS jurisdiction that does not grant a 90-day forbearance to any person or business with a financial hardship due to the COVID-19 pandemic is deemed to have engaged in an unsafe and unsound business practice. NYDFS issued implementing regulations suggesting that this order, in practice, should only apply to requests for consumer mortgage forbearances. The executive order expired in late April 2020 and has not been extended. ○ NYDFS has issued guidance to state-regulated financial institutions encouraging them to support consumers negatively affected by COVID-19, and notably by reporting credit information regarding loan accommodations in ways that minimize negative impacts on consumers. ○ NYDFS has also taken steps to provide flexibility to state-regulated mortgage servicers and help them address COVID-19-related compliance challenges that may arise under New York law. ● California <ul style="list-style-type: none"> ○ State regulators have encouraged California banks and credit unions, as well as other regulated lenders, to provide loan accommodations to affected customers, such as restructuring debt, easing terms for new loans and making other payments modifications consistent with prudent banking practices. ○ Most large national banks, state-chartered banks, credit unions, and mortgage lenders and servicers agreed to provide relief to California homeowners impacted by COVID-19 (a list of participating financial institutions is available here). ○ Holders of commercially or privately held student loans in California who are impacted by COVID-19 are also eligible for relief, including temporary forbearance and other payment accommodations. Many private loan servicers participate in this initiative (a list of participating financial institutions is available here).

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European Union	<p>ECB has provided flexibility when implementing the ECB Guidance on non-performing loans. EBA clarified that offering/accepting terms of general moratoria do not lead to automatic reclassification as forborne exposures. See:</p> <p>ECB flexibility when implementing ECB Guidance on NPLs</p> <p>EBA statement on the application of the prudential framework in light of COVID-19 measures</p> <p>EBA Guidelines on legislative and non-legislative moratoria on loan repayments applied in the light of the COVID-19 crisis – Consolidated version updated on 2 December 2020</p>
United Kingdom	<p>The FCA has made it clear by way of guidance that accommodation is expected.</p> <p>See:</p> <p>FCA Draft Guidance: Consumer credit and Coronavirus: Additional Guidance for Firms (Update to previous guidance – published September 16, 2020)</p> <p>FCA Draft Guidance: Overdraft and Coronavirus: Additional Guidance for Firms (Update to previous guidance – published September 16, 2020)</p> <p>Mortgages and Coronavirus: Additional Guidance for Firms (Update to previous guidance – published September 14, 2020)</p> <p>FCA Final Guidance and Rules (Credit Cards) (firms)</p> <p>FCA Final Guidance and Rules (Overdrafts) (banks)</p> <p>FCA Final Guidance and Rules (Personal Loans) (lenders)</p> <p>FCA Guidance (Mortgages) (mortgage providers—updated June 16, 2020)</p> <p>FCA Guidance (Motor Finance) (motor finance providers – updated)</p> <p>FCA Guidance (RTO/BNPL/Pawnbrokers) (rent-to-own, BNPL and pawnbrokers)</p> <p>FCA Guidance (HCSTC Inc. Payday Loans) (high cost short-term credit providers)</p> <p>FCA Draft Guidance (Insurance and Premium Finance) (insurers, premium finance and debt collectors)</p>
France	<p>All penalty payments, penalty clauses or termination provisions that punish non-performance are neutralized as from March 12, 2020. These may only take effect at the end of a period of one month from the end of the state of health emergency if the debtor has not performed.</p> <p>This measure does not apply to financial obligations and related collaterals mentioned in Articles L. 211-36 <i>et seq.</i> of the Monetary and Financial Code (implementing Directive 2002/47/EC on financial collateral arrangements), as well as agreements entered into within the framework of a payment system and systems for the settlement and delivery of financial instruments mentioned in Article L. 330-1 of the same code.</p>
Germany	<p>Forbearance regarding retail loans (whether secured or not) based on a temporary rule change measure ended June 30, 2020.</p>
Italy	<p>Secured and unsecured debts of Italian SMEs and self-employed professionals are subject to a general payment moratorium ending on September 30, 2020.</p>

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	Payment holiday provisions were also introduced with respect to home mortgage loans, while a separate voluntary moratorium regime has been set out by the Italian association of banks.
Spain	New legislative debt forbearance initiative in connection with credits/loans (whether secured by a mortgage or not) extended to individuals in a vulnerable economic situation (as this is defined in article 9 of RDL 8/2020). The forbearance will apply to principal and interest and the term thereof will be of three months. See RDL 8/2020 (which has been amended by RDL 11/2020).
Belgium	The financial sector undertakes to grant a payment moratorium until October 31, 2020 to (i) viable non-financial companies, (ii) viable self-employed persons, and (iii) residential mortgage borrowers experiencing payment difficulties as a result of the COVID-19 crisis. Retail, wholesale, secured and unsecured loans are covered by the initiative. This undertaking is part of a public-private sector agreement in the context of the state guarantee for private sector loans. See Payment Moratorium (NL/FR)
Sweden	The Swedish regulator has issued a decision that allows banks and other providers of residential mortgages to grant forbearance on mortgage loans. More specifically, banks are allowed to waive the legal requirement for borrowers to amortize on mortgages. The exemption will apply until August 2021.
UAE	Targeted Economic Support Scheme (See TESS). The substance of TESS as it relates to lending to “private sector corporates, SMEs and individuals” is as follows: <ul style="list-style-type: none"> • Banks are directed to offer payment deferral relief for a period up to six months on installment of loans/financing (principal and/or interest/profit) to their respective private sector corporates, SMEs and individuals affected by COVID-19; and the maturity of these loans/financing may be extended by the period of the relief and repayment schedules to resume as normal following the expiration of the temporary relief period. The availability of the Zero Cost Facility of AED 50 billion available to banks and financial institutions in the UAE has been extended for an additional duration of six months, <i>i.e.</i>, until June 30, 2021. • CBUAE expects that the IFRS 9 staging and classification under CBUAE Circular 28/2010 of customers receiving relief under TESS shall normally remain unchanged during the period of the scheme, not downgraded. • There is a new requirement for all banks to apply a prudential filter to IFRS 9 expected loss provisions. The prudential filter aims to minimize the effect of IFRS 9 provisions on regulatory capital, in view of expected volatility due to the COVID-19 crisis.

Our FSR team has developed the [COVID-19 Regulatory and Legislative Dashboard](#) as a resource to help clients and affected institutions, companies, governments, other entities and individuals around the world navigate the complexities of the crisis and the policy response. Please refer to the Dashboard for our periodic updates and insights into the issues addressed in this FAQ.

Find out more about the business response to the Coronavirus outbreak: [Coronavirus: Managing business impact and legal risks](#).

AMERICAS

New York

Duane Wall

Partner of Counsel, New York

T +1 212 819 8453

E dwall@whitecase.com

EMEA

Berlin

Martin Weber

Local Partner, Berlin

T +49 30 880911 570

E martin.weber@whitecase.com

Brussels

Willem Van de Wiele

Counsel, Brussels

T +32 2 2392 575

E willem.vandewiele@whitecase.com

Dubai

Adrianus School

Local Partner, Dubai

T +971 4 381 6273

E adrianus.school@whitecase.com

Frankfurt

Carsten Loesing

Local Partner, Frankfurt

T +49 69 29994 1145

E carsten.loesing@whitecase.com

London

Jonathan Rogers

Partner, London

T +44 20 7532 2163

E jonathan.rogers@whitecase.com

Washington, DC

Prat Vallabhaneni

Partner, Washington, DC

T +1 202 626 3596

E pratin.vallabhaneni@whitecase.com

Madrid

Fernando Navarro

Partner, Madrid

T +34 91 787 6373

E fernando.navarro@whitecase.com

Milan

Angelo Messori

Associate, Milan

T +39 02 00688 366

E angelo.messori@whitecase.com

Paris

Emilie Rogey

Partner, Paris

T +33 1 55 04 16 22

E emilie.rogey@whitecase.com

Stockholm

Martin Järvengren

Partner, Stockholm

T +46 8 506 32 371

E martin.jarvengren@whitecase.com

White & Case LLP

1221 Avenue of the Americas

New York, New York 10020-1095

United States

T +1 212 819 8200

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