

GUIDELINES

ON LOAN RESTRUCTURING FOR INDIVIDUALS

BANK OF ALBANIA

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I. INTRODUCTION

1.1. **Definitions**

“Loan restructuring”- means the facilities the bank or the financial institution provides to the borrowers due to their financial difficulties arising from either economical or legal reasons. These facilities shall not apply to other situations and in general shall include: facilities on lending terms & conditions by amending one or some contract terms (including product change and interest capitalisation), which mainly relate to the term to maturity, (principal) and interest rate, collateral execution or other assets for the partial payment on loan, replacement of the original borrower or involvement of an additional one.

“Creditor”- means banks, branches of foreign banks and non-bank financial institutions being granted a licence by the Bank of Albania.

“Borrower” (or co-borrower) means the individual who has received a loan by a bank or financial institution for personal purposes, for example house purchasing or renovation, car purchasing or other personal purposes.

“Loan contract / agreement for individuals” - means the agreement whereby a bank or financial institution grants or promises to grant to an individual an amount of money for *house purchasing or renovation, car purchasing, or personal consumption as the borrower deems fit.*

“Moratorium”- means the temporally interruption of legal actions against the other party.

1.2. Overview

The purpose of this document is to encourage a more active approach to loan restructuring for borrowers in a timely manner, through the introduction of principles and guidelines based on the best international practices, which should be implemented during the loan restructuring process. Overall, these principles provide guidelines on the rights and behaviour of parties during loan restructuring negotiations and serve as a tool for open communication between the borrower and the creditor. As such, this document aims to educate and provide guidance to borrowers regarding the restructuring process, and establishes the background for an open and collaborative relationship throughout the credit duration. The borrowers are encouraged to carefully assess the loan restructuring benefits and implement the principles laid down in this document.

These recommendations shall not affect the mandatory effects of legal standards (or their enforcement) or the mortgage credit agreements. Each creditor has in place the respective restructuring policy, based on the characteristics of the relevant consumers' portfolio and its strategy and is free to enter into loan restructuring negotiations in accordance with its policies.

1.3. Loan restructuring advantages

If the borrower fails to repay the loan in compliance with the credit agreement's terms and conditions, the creditor may request the liability repayment. If necessary, the creditor may initiate legal procedure and/or collateral execution. Nevertheless, recently a proper and timely restructuring of the credit agreement's terms and conditions, in collaboration with the borrower, has resulted more effective than initiating a legal process. Since loan restructuring is a swifter process and provides more benefits not only for the creditors and borrowers, but for the domestic economy as well. Nowadays, it is broadly accepted that loan restructuring:

- provides the borrower the possibility to successfully handle the financial difficulties and continue fulfilling its obligations;
- avoids the negative social and macroeconomic effects which might arise from the execution of a considerable number of properties pledged as collateral;
- reduces encumbered court procedures, by reducing the number of cases and the prolonged court sessions;
- is more effective than a legal process (the dispute is resolved more rapidly and provides for the recovering of a higher percentage of the debt);
- helps individuals gain confidence on the loan restructuring process, if it is objective and transparent.

II. PRINCIPLES AND COMMENTS

Principle 1 – Loan restructuring is a compromise not an obligation

All borrowers are obligated to repay their loans. Loan restructuring means a consent in borrower's interest and shall begin as a procedure only if the financial problems of the borrower are temporary in nature and can be solved so that the borrowers may succeed to repay their financial obligations within a reasonable period.

Comment:

All borrowers are obligated to repay their loans in accordance with the contractual terms and conditions of the consumer/mortgage credit. Hence, the borrowers should turn to their creditors and address their problems in a timely manner, rather than waiting until a payment default occurs.

Loan restructuring is a tool to work out the problems of a borrower that is facing financial difficulties, without pursuing collateral execution or legal process. One of the core loan restructuring principles is the voluntary act principle, which stipulates that individuals have the right to enter into legal relations with any party they choose and set forth conditions they want. Thus, whereas each party (borrower and creditor) might initiate loan restructuring negotiations, none might impose the other party to accept its conditions.

Restructuring of borrower's obligations by the creditor, shall not be considered as a right. On the contrary, it is a favour provided by the creditor. The restructuring should start when the creditor believes that a stable repayment schedule might be established and the borrower will be able to pay the restructured loan in accordance with the new terms and conditions.

Principle 2- Good faith

Negotiations between the creditor and borrower must take place in good faith with the objective of finding a constructive solution that is workable and acceptable to both parties.

Rights shall be exercised and obligations fulfilled in good faith, taking into account the other party's valid interests. The goal of the good faith principle is to facilitate loyalty, trust, and honesty between the creditor and borrower in a loan restructuring process in order to ensure that the rights of the parties are protected. It is crucial to note that loan restructuring is possible only if the borrower and creditor work together to achieve the same goal – for the benefit of all parties in the long term.

In any case, the creditor has the right to verify the accuracy of the data presented by the borrower and undertake the necessary legal steps in case the information provided by the borrower may lead to decisions that may damage the creditor.

Principle 3 - Negotiation between the borrower and creditor in the best interest of parties

It is in all parties' best interest the borrower contact the creditor as soon as possible when financial difficulties are identified, in order to start the discussions with respect to loan restructuring.

Although creditors typically send reminders to the borrowers in case of a missing payment, *the borrower* is strongly advised to talk to the creditor before such an event occurs. The borrower, showing his responsibility and commitment to repayment, should contact the creditor as soon as possible to discuss payment difficulties. Early discussions provide both the borrower and the creditor an opportunity to reach a reasonable solution to avoid legal processes or the collateral execution.

The borrower and creditor must discuss the causes of the overdue payments, the borrower's financial position as well as any prospects for resuming payments (for

example, the parties may consider the temporary or long-term nature of causes for failure to make payments in a timely manner, as well as the capacity of the borrower to pay the arrears within a reasonable timeframe).

Principle 4 – Clear communication

Each party shall communicate and provide information to the other regarding any relevant aspects. Communication by each party shall be clear, honest, fair and reliable.

Upon the creditors' request, the borrower shall present the required documents to support the application for restructuring. If, based on the collected information, the creditor believes that the provided information is false, the creditor has the right to terminate the negotiations by informing the borrower in writing and implementing the necessary legal steps.

In the meantime, both parties are free to discuss the restructuring terms and conditions, the repayment schedule or any other condition of the agreement, which shall become effective upon the approval in writing by both parties.

Principle 5 – The creditor shall provide the borrower with a clear statement of the borrower's obligations based on the credit agreement

Once the discussions on restructuring begin, the creditor shall provide the borrower with detailed information, in writing, about the payment status of the credit(s), including at least the following information:

- a) total amount of the arrears, number of delayed dates for the oldest amount outstanding;
- b) outstanding balance of the loan, time remaining to fully repay the loan;

- c) detailed statement of all interests, including late-payment interest, and/or other penalties; and
- d) amount of interest, including penalty interest, late fees and/or other penalties, which accrue on daily basis.

Principle 6 - The borrower shall provide the creditor with all necessary information, in a timely and accurate manner

The borrower shall provide the creditor with all the required information within a time frame established by the creditor.

The information shall include, but not be limited to, the regular income and other financial sources, savings accounts, investments, current conditions of employment, individual income sources, employment prospects, etc, to ensure a proper assessment of the borrower's financial situation. The borrower must inform the creditor about any other loan or financial obligation.

Principle 7 - Moratorium period

Throughout the negotiations for restructuring, the creditor shall not initiate a collateral execution procedure. When it has started this procedure, the creditor shall interrupt it. The borrower shall not take any action, which may affect negatively the solvency or relations with the creditor.

This principle derives from the basic premises of this guideline - that the process is approved by both parties on a private contractual relationship, based on which, the creditor is willing to assist the borrower for long-term benefits. In this regard, if the creditor believes that it will benefit the borrower to restructure the loan, then the creditor should provide the necessary conditions to the borrower to negotiate a restructuring plan, allowing a short-term moratorium period on the legal or collateral execution

procedures. Depending on the situation's complexity, the moratorium shall not exceed 45 to 90 days, from the date of the written approval of the creditor on the initiation of restructuring negotiations.

The borrower should recognise that in exchange of granting the moratorium period, the borrower should promise not to undertake actions that might affect negatively its ability to restructure the loan and re-affirm the commitment to provide all the required information, in an accurate and timely manner.

Principle 8 - The creditor shall provide a prompt response to the borrower's proposal for loan restructuring

The creditor shall provide a response to the borrower within the time frame of 10 business days, from the day of receiving the borrower's request (in writing) for the loan restructuring. During the negotiating period, both parties must provide a prompt response to each other in order to finalise the negotiations within the moratorium term.

Principle 9 - The borrower shall have sufficient time to provide the requested information and consider the proposal on restructuring

The creditor should allow the borrower reasonable time, in general up to 20 days, to providing the information and consider the formal loan restructuring proposals by the creditor . The parties are free to discuss the review of the conditions, if the borrower is willing to formally be engaged for the restructuring, if the restructuring conditions are clearly presented in writing, so that the borrower understands and assesses the implications of the proposal.

Principle 10 - Restructuring shall be reasonable and achievable

The loan restructuring proposal shall be based on a viable and reasonable payment schedule, in accordance with the restructuring method agreed with the borrower and based on the applicable internal standards of the lending institution.

Principle 11 – Confidentiality

The creditor shall ensure the confidentiality of the information received from the borrower and shall not disclose any details or information about the borrower's status to a third party unless agreed upon in writing with the borrower, except for cases required by the laws in force.

III. Example - Decision tree for the restructuring process of mortgage loans

Understanding the problem		
Causes of arrears	Borrower's financial capacity	Value of mortgaged assets

Examining the problem		
Confirming the causes of arrears and finding out the borrower's intentions	Financial statements, accounts' situations, credits	Assessment of current situation, deficiencies

Solving the problem		
There is good will, but there is no capacity	There is good will and some capacity	There is no good will although there is capacity
<u>Standard solution:</u> Voluntary sale Mandatory execution	<u>Standard solution:</u> Rescheduling, changes, capitalisation, Voluntary sale Mandatory execution	<u>Standard solution:</u> Mandatory execution