

## **Letter 40: Nonaccrual of Interest**

The purpose of this letter is to advise banks of the accrual accounting procedures to be applied to loans in the event the borrower fails to make required principal or interest payments.

Loans and lease financing receivables are to be reported as being in nonaccrual status if: (1) they are maintained on a cash basis because of deterioration in the financial position of the borrower, (2) payment in full of interest or principal is not expected, or (3) principal or interest has been in default for a period of 90 days or more.

For the purpose of applying the third test for nonaccrual status listed above, the date on which a loan reaches nonaccrual status is determined by its contractual terms. If the principal or interest on a loan becomes due and unpaid for 90 days or more on a date that falls between call report dates, the loan should be placed in nonaccrual status as of the date it becomes 90 days past due and it should remain in nonaccrual status until it meets the criteria for restoration to accrual status described below.

The reversal of previously accrued but uncollected interest applicable to any asset placed in nonaccrual status and the treatment of subsequent payments as either principal or interest should be handled in accordance with generally accepted account principles. Acceptable accounting treatment includes a reversal of all previously accrued but uncollected interest applicable to assets placed in a nonaccrual status against appropriate income and balance sheet accounts.

In the following situations, a loan need not be placed on nonaccrual status: Loans fully secured to cover principal and interest by U.S. government securities, securities of agencies of the U.S. government, marketable securities, bank deposits, verified cash surrender value of insurance policies, and those loans or portions thereof which are guaranteed as to principal and interest by a government agency.

A nonaccrual loan may be restored to accrual status when (1) none of its principal and interest is due and unpaid, and the bank expects repayment of the remaining contractual principal and interest, (2) the loan has been formally restructured and qualifies for accrual status, or (3) the borrower has resumed paying the full amount of the scheduled contractual interest and principal payments on the loan that is past due and in nonaccrual status, even though the loan has not been brought fully current, and certain repayment criteria are met. Criteria to be evaluated must include consideration that the borrower has resumed making payments over a sustained period, generally a minimum of six months, in accordance with the contracted terms.

Bkg. Ltr. #40, May 8, 1985, Commissioner Galecki  
Reissued, May 10, 2012, Michael J. Mach, Administrator