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## Exec: U.S. recovery program needs new category for loans

### GUEST COLUMN

ALTAMONTE SPRINGS - Geof Longstaff, chairman at Mercantile Commercial Capital LLC, recently said a small regulatory change could eliminate many of the problems that banks currently face with their loan portfolios.

"We need a new category to classify loans that are currently viewed as substandard but whose borrowers are still making payments," Longstaff said.

The problem now, put simply, is this: Among other criteria, banking regulators gauge a loan's merit against the value of the collateral pledged to secure the loan. If the collateral - an office building or retail center - declines in value, the loan can be considered "substandard" and subject to reserves.

"Regulators see banks that loaned \$1 million against \$1.5 million in collateral as sound," Longstaff, who has more than 37 years of experience as a banking executive, explained. "But if the asset value drops to \$900,000, regulators call that a non-performing asset - NPA - or substandard loan, and tell banks they can either post reserves to cover the collateral deficiency or demand additional money from the borrower," he said.

"We do this at a time when borrowers need to preserve liquidity to

handle volatility in their business.

Making these cash demands can cause businesses to fail and thus promotes job losses," Longstaff said.

Assets have been dropping in value all over the country, Longstaff said, and NPAs are a major challenge to the nation's economic recovery.

"If the bank takes the additional reserve, that increases the need for capital and subjects the bank to further capital impairment," Longstaff said.

But many borrowers have continued to make payments on loans even though their assets have been devalued. "They are confident the real estate market will come back and they know their asset value will improve," Longstaff said. "They are employing the sort of long-term investment strategy our economy has been built on," he said.

The solution, Longstaff said, is to create a new category for NPAs that are actually performing - whose borrowers are making their payments on time.

"We need a new category called a "performing under-margined loan" to describe a loan that is performing, but whose collateral assets have suffered a short-term devaluation as a result of the national economy," Longstaff explained.

Such classification would reduce demands on the bank's reserves without adding to the cost of recovery, Longstaff said.

"Bank regulators shouldn't require increased reserves against these loans when the borrower shows the ability to make the payments," he emphasized.



**Geof Longstaff**