



LOAN REVIEW: GROWING LOAN REVIEWERS

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INTRODUCTION: A FEW GOOD MEN AND WOMEN

In previous articles we have explored the objectives of a credit review system in general and the role of credit grading in particular. Let's move on to another element of credit review systems—loan reviewers.

Mark Twain remarked, "I never let my schooling interfere with my education." DiCOM's annual loan review survey has noted that schooling has not interfered with loan reviewers' education because loan review departments have not had much in training dollars to expend. Part of the reason may be the absence of any formal loan review training programs, so why don't we start thinking about what a loan review curriculum might look like?

LOAN REVIEW POLICIES CALL FOR A RENAISSANCE BANKER IN THE 21ST CENTURY?

Loan review policies are typically reviewed and approved at least annually by the board of directors. Policy guidelines usually include a written description of the overall credit grading process and establish responsibilities for the various loan review functions. The policy generally addresses the following items:

- Qualifications of loan review personnel;
- Independence of loan review personnel;
- Frequency of reviews;
- Scope of reviews;
- Depth of reviews;
- Review of findings and follow-up; and
- Workpaper and report distribution.

So what kind of qualifications should a loan reviewer have in order to meet the frequency, scope, and depth of reviews? What does a loan review need to have in order to review, evaluate, and follow up on findings? What kind of communication skills does a loan reviewer need in order to get those findings distributed and explained?

QUALIFICATIONS OF LOAN REVIEW PERSONNEL: JUNIOR LOAN REVIEWERS—NOT ENOUGH EXPERIENCE?

Robert Frost observed, "Education is hanging around until you've caught on." But if you're the new kid on the block, you haven't been there long enough to catch on. So, the conundrum is that loan reviewers are expected to meet some minimum combination of education, experience, and training. They should be knowledgeable of both sound lending practices and their own institution's specific lending guidelines. In addition, they should be familiar with pertinent laws and regulations affecting credit and lending activities. But what if the minimum expectations are set so high that it discourages wannabe loan reviewers?

There is a well-documented shortage of junior reviewers, which means loan review units need to recruit people short on education, training, and experience. Meanwhile more senior loan reviewers are generally not getting their fair share of intermediate and remedial training. These challenges really call for the development and implementation of some minimum but reasonable standard of education and training, so let's put some suggestions on the table.



JUNIOR LOAN REVIEWERS OUGHT TO HAVE BASIC CREDIT AND LENDING EXPERTISE

INCLUDING:

- credit analysis including evaluation of cash flow, collateral, and guarantors
- underwriting basics such as minimum debt service coverage ratios, maximum collateral loan-to-value ratios, guarantor strength as measured by adjusted net worth and personal income available to support borrower repayment, evaluation of financial statement projections, maximum loan terms and amortization
- commercial and commercial real estate loan documentation
- commercial loan operations for loan doc preparation, loan doc closing, booking, and funding
- basic compliance concepts such as spousal guarantees and real estate related requirements

Relevant prior experiences would be as credit analysts, lending assistants, and/or any role in supporting business lenders in client support, prospecting, credit requests for new and existing borrowers. These experiences help candidates understand the dynamics of commercial relationships and the interplay between lenders and the credit approval process. Some banks have enough critical mass to rotate junior teammates from credit analysis to workout to loan review for 6-month exposures to each of these areas before sending them on to lending assignments. The rotation assures them that they are not permanently assigned to any of these areas, but the exposure is long enough to give them some basic proficiencies.

Yet another educational focus should include some basic statistics in valid sampling techniques in order to understand how loan review frequency, scope, and depth interplay.

Besides basic compliance requirements for business borrowers such as appraisal requirements, junior reviewers also need to be aware of accounting issues affecting borrowers—revenue recognition, lease capitalization, current expected credit loss, troubled debt restructuring. Generally accepted accounting principles change over time, regulations get revised, so loan reviewers need to be cognizant that accounting rules and regulatory rules are not engraved on stone tablets but are prone to change, too.

The preceding is certainly not an exhaustive, complete list, but it is meant to get you readers thinking about what you would revise, add, or delete from the list. Like the weather, everyone talks about educational and experiential needs, but we need to move one step closer to actually implementing some basic curriculum. Keep in mind that the junior reviewer pool has been shallow because banks have generally preferred to recruit more experienced loan reviewers from other banks rather than try to build a junior layer to give senior loan reviewers more time to work on more challenging credit exposures.

A short list of training topics for **senior loan reviewers** might include:

- credit risk management and its role among the other enterprise risks
- merger and acquisition accounting given loan review's frequent deployment on due diligence teams
- basic forensic accounting techniques to identify fraud
- current expected credit loss processes and loan loss reserve calculations, including the role of the risk rating systems in estimating loss via obligor probability of default and transactional loss given default
- more advanced compliance issues and regulatory guidance

In addition, the regulatory agencies have concerns that have not been covered under formal guidance. It is the responsibility of the reviewer to understand the issues of concern and how to apply them to the examination process. A recent example of this is climate related financial risks.

As with the earlier list for junior loan reviewers, you are invited to offer your own topics to this senior loan reviewer training curriculum.



CLOSING: TIME TO GET SERIOUS ABOUT LOAN REVIEW TRAINING

Comedian Steven Wright complained, “When I was in school, the teachers told me practice makes perfect. Then they told me nobody’s perfect, so I stopped practicing.” Loan review management needs to scale back its expectations of pre-existing skills for new recruits and to take on more responsibility for training its own. That is not easy because of the dearth in training dollars, but senior loan reviewers should accept that if they want more support, they will have to shoulder more of a mentor responsibility. Loan review management needs to develop a basic loan review curriculum so that their senior loan reviewers are being given recruits acquainted with the basics.

Remember, this article is really aimed at getting you loan review managers thinking about what you want and need in education, training, and experience for your junior and senior loan reviewers. What do you think are essential topics for junior and senior loan reviewers? I invite you to use this matrix to help you focus on what you think junior and senior loan reviewers ought to have:

Topics	Junior loan reviewers	Senior loan reviewers
Credit analysis		
Loan underwriting		
Loan documentation		
Loan operations		
Credit administration		
Credit risk management		
Enterprise risk management		
Compliance risk		
Portfolio management		
Credit quality monitoring		
Risk ratings and estimate of loss		
Loan loss reserve and CECL		
Other topics		

Remember, we all start at the beginning. As inventor Tom Edison recalled, “I was at the foot of my class.” So, one foot at a time, please share your curriculum ideas with DiCOM and me.