

# Troubled Real Estate Loans: A Lender's Perspective

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# Introduction

- Commercial real estate loans not as troubled as residential loans
- Loans to borrowers in the housing industry are at serious risk
- Commercial property market not immune – sales volumes down, credit availability diminished, bank regulators are closely scrutinizing all real estate loans
- High-profile examples
  - Australian mall developer, Centro, unable to refinance \$3.4 billion debt
  - Las Vegas developer, Bruce Eichner defaulted on \$750,000,000 loan from Deutsche Bank
  - Other development projects on hold for lack of funding sources

# Warning Signs for Troubled Loans

The following are common examples of “warning signs” that Debtor’s business and its ability to meet its obligations under the loan documents may be in trouble:

- A. Missed or late payments of interest, principal or fees (especially if prior months’ payments made on time)
- B. Notice of tax liens
- C. Late and/or inaccurate financial reporting

# Warning Signs for Troubled Loans

- D. Overdrafts
- E. Notice of mechanic's liens
- F. Changes in senior management or the Board of Directors
- G. Changes of accounting firms
- H. Draws on letters of credit securing obligations

# Preparing to Respond to a Default

## A. Review Loan Documents

1. Confirm all documents properly prepared and executed
2. Analyze documents to understand events of default, rights and remedies
3. Notice requirements
4. Right to income (i.e., assignment of rents or right to receiver)

# Preparing to Respond to a Default

## B. Review Status of Collateral

1. UCC, tax lien, judgment and bankruptcy searches in Debtor's name and property name (if any)
2. Real Property Status
  - a. Title Evidence
  - b. Environmental Status
    - i. Past environmental reports
    - ii. Current environmental examinations (i.e., Phase I, etc.)
  - c. Valuation of Property

# Preparing to Respond to a Default

## C. Analyze Defenses

1. Document issues
2. Lender's conduct issues

# Options: Negotiate or Pursue Default Remedies

## A. Negotiated Approaches

1. Work-out/loan restructuring
2. Deed in lieu of foreclosure

## B. Pursue Remedies

1. Self-help
  - a. Set off
  - b. Notice of direct payment to account debtors/enforcement of security interests
  - c. Notice to tenants/enforcement of assignment of rents
  - d. Pursuit of other credit enhancements

# Options: Negotiate or Pursue Default Remedies

2. Foreclosure by advertisement
3. Foreclosure by action
4. Receivership
5. Action on guaranty or other credit enhancements
6. Timing issues regarding collateral
  - a. Usually easily obtained collateral first (i.e., cash, letters of credit, rents, receivables, etc.)
  - b. Tangible personal property next
  - c. Real property usually last

# Thoughts on Lender's Perspectives

- A. Do not want to own collateral – want to be paid
- B. Likely to negotiate if a reasonable possibility of payment
- C. New advances of cash unlikely – certainly need more collateral
- D. Negotiations will not continue if Borrower is not straightforward, honest, cooperative
- E. Current Strategies
  - sell loans at deep discount
  - sell collateral at deep discount