Five Tips for Avoiding Lender Liability During a Workout

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While there seems to be light at the end of the tunnel with the COVID-19 pandemic, many parts of the economy are still hurting. For lenders, that means there will continue to be more credits being pushed into workouts or special assets.

And workouts normally involve intense negotiations, conversations and meeting with distressed borrowers. During these discussions, it is crucial for lenders to be careful to avoid any actions that could result in lender liability.

Here are 5 tips for avoiding bank liability during a workout.

1. Don't Make Any Promises.

Distressed borrowers are looking for assurances from the bank during these difficult times. However, the bank should not make any commitments, oral or in writing, without first completing its due diligence and analyzing its options. Once the bank determines a course of action, any commitments to a loan modification, forbearance agreement, or anything else should come from the lender's counsel, or a document from the lender drafted by the bank's counsel.

2. Be Professional.

This should go without saying. However, it bears repeating. In all communications with the borrower, make sure your tone and vocabulary choice reflect well on both you and the financial institution you represent. You could find yourself explaining poorly worded communications to a Judge or Jury.

3. Document Oral Communications.

Any time you talk with a borrower, make sure to document what was communicated in the conversation. This can be done by a simple email to the borrower summarizing what was discussed, and a reminder to the borrower that the bank reserves its rights and remedies. This is an effective way to avoid a "he said, she said" argument later in the process.

4. Don't Give Advice to the Borrower.

You are the lender, not a consultant or financial advisor to the borrower. Do not try to give advice to your borrower regarding how he/she could better run their business. Giving such advice to the borrower is fraught with potential liability if the borrower does not emerge from financial distress.

5. Follow Your Loan Documents.

These documents govern your relationship with the borrower. Lenders must review them and make sure the bank complies with all of its obligations in them. Failure to do so will undoubtedly come back to haunt the bank.

There are many potential pitfalls for lenders during loan workouts, but they will be made less likely by adhering to the tips above. If you have any questions regarding loan workouts or lender liability, please reach out to your Vorys attorney.