

The last serious economic downturn that gave rise to financial services litigation was back in 2008 – over 10 years ago. Lenders should recall that era and buckle up for a new wave of litigation as the COVID-19 downturn speeds upon us. This is true despite the fact that current legislation seeks to bring borrowers and lenders to the table to avoid conflict – these measures will not prevent wide-scale litigation over the coming years.

Let's start with a few basics. The Coronavirus Aid, Relief, and Economic Security Act (the "CARES Act") provides an avenue for, and in some instances requires lenders to exercise greater flexibility in, lending and restructuring during the COVID-19 crisis. The CARES Act is intended to – and should – foster a period of cooperation between lenders and borrowers during the crisis. At least with respect to regulated financial institutions. CMBS and alternative lenders are not addressed in the CARES Act.

So now – while everyone is focused on working together – is actually an excellent time for lenders to do some housekeeping so they are prepared to enforce their creditors' rights in litigation when and if it becomes necessary. Here are a few things to keep in mind.

Lenders should review the loan file for deficiencies, omissions or gaps. It will be much easier to clean up the loan file during the period of cooperation. Lenders should pay particular attention to the following:

- **Documents.**

- Review loan documents to confirm:
  - Complete copies and required originals of all documents are in the loan file.
  - Documents were fully and properly executed, including notarization where required.
  - Documents – required to be filed – were in fact filed in the appropriate location or jurisdiction and the loan file contains file stamped copies.
  - Post-closing deliverables, if any, were received and are in the loan file.
  - Lender's understanding of the loan terms was properly documented in the loan documents.

- **Collateral.**

- In a disrupted financial market with companies failing, loan collateral may be the primary source of repayment of the loan. With that in mind, Lender needs to determine whether it has the collateral it intended and should confirm:
  - Loan documents, including security agreements and UCC-1 financing statements, accurately and completely describe the collateral.

- Perfection of liens. Keep in mind that different types of collateral require different perfection methods. Also, certain perfection methods, such as UCC-1 financing statements, must be continued periodically.
- Priority of liens. Remember that an existing UCC-1 can be primed by a purchase money security interest, a tax lien or a judgment lien.
- Insurance. Lender should confirm that insurance policies naming Lender as an additional insured or lender loss payee, as applicable, are current and in full force and effect.
- If the collateral is tangible, Lender should consider a site visit to view and confirm the existence and status of the collateral. In the case of real property, Lender should consider obtaining an updated title and UCC search as well as an updated property appraisal and property condition report. Market studies may be useful for certain real estate collateral.

Early housekeeping by Lenders now will facilitate dealing with borrowers after default – whether in a workout situation or litigation – with the goal of minimizing risk and maximizing recovery. Please watch for our next client alert *Borrower in Default? Déjà Vu 2008 Financial Crisis* which discusses preventative measures Lenders should consider when dealing with distressed borrowers in default.

### Authors

**Michael S. Forshey**

Partner, Dallas  
T +1 214 758 3540  
E michael.forshey@squirepb.com

**John E. Thomas**

Partner, Washington DC  
T +1 202 457 7511  
E john.thomas@squirepb.com

**Patrick J. Burke**

Partner, Cleveland  
T +1 216 479 8297  
E patrick.burke@squirepb.com

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