Preparation: The Key to Enhancing Distressed Debt Recovery Opportunities*

By Scott A. Lessne and Vincenzo Paparo

There is no better time to plan a distressed debt workout strategy than at the earliest stages of the workout.

This article is the first of two intended as a refresher for commercial lenders who want to be proactive when faced with a credit exhibiting signs of financial distress. These two articles assume that it is just a matter of when and not if the next down cycle will occur. With that assumption in mind, the theme of this article is *to be prepared.*

Over the last several years, the financial markets have been awash with cash. A multitude of new players in the debt portion of the capital structure have aggressively sought new and creative ways to deploy this excess cash. When coupled with historically low interest rates, traditional lenders such as commercial banks and even commercial finance companies have been forced to compete with more risk-tolerant lenders in most commercial lending markets (with the possible exception of small business lending). As a result of this highly competitive market, traditional senior lenders have been forced to venture into lending structures that severely test their risk tolerance. With the gradual but continuous rise in interest rates over the past 12 to 24 months and with corporate profits under pressure from a slowing economy, a new down cycle is all but assured; the only questions are whether the down cycle will be general or industry specific, whether or not it will be prolonged and whether or not it will be severe. Only time will tell.

As the onset of the down cycle is still some time in the future, based upon the authors' collective experience, there is no better time than now to reestablish prudent procedures and strategies for dealing with weak or distressed borrowers.

Know the Facts

Most lenders routinely conduct portfolio reviews with an eye toward identifying credits that may need extra attention. At many financial institutions, portfolios range in credit quality from investment-grade corporate credits to traditional asset-based lending portfolios, and reaching a consensus for determining when a credit is in workout or restructuring is tricky at best. Setting aside the influence of internal institutional policies and politics on the decision of when to engage the institution's workout team, there are some universal warning signs that should be on every lender's radar screen, regardless of the nature of the credit and where the credit is managed within the institution. Those warning signs, which may also be described as credit weaknesses, can range from a general downturn in the borrower's industry to unexpected management changes, resignation of the borrowers' outside auditors, key covenant defaults, gradual degradation in the payables aging, unexplained inventory increases, loss of key contracts, vendor implementation of cash-on-delivery requirements or a dramatic

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The authors thank Susan Aufiero, an associate in the Corporate Department and Finance Group of Proskauer Rose LLP, for her assistance with this article.

revelation that a fraud has occurred. Each of these events, either by themselves or in combination with other signs of a credit problem, should trigger in a lender the desire to make the time to take stock of the developing situation.

Ultimately, the events that trigger the beginning of a workout will vary significantly depending upon the size and nature of the credit. We strongly believe, however, that regardless of when an institution formally transfers a credit to the workout experts, the best time to begin preparing for the workout is when credit weaknesses are first identified. There are a handful of relatively simple steps that lenders can take when credit weaknesses are first identified. All of these steps can be accomplished without the need to involve the borrower and can give the lender a leg-up in formulating the workout strategy. More than one workout strategy has been derailed at a crucial juncture when counsel for the borrower or a bankruptcy trustee advises the lender that a fact, long held to be true, is in reality not true. Nobody likes to be surprised.

The best time to begin preparing for the workout is when credit weaknesses are first identified.

Review the Credit File

The credit file normally contains all the information compiled about the credit and any information maintained in the lender's computer database. The credit file review is, therefore, a two-part process: a business review and a legal review. The information stored in the credit file will generally be able to tell the history of the loan from the initial contact with the borrower through the relationship developed while negotiating a term sheet or commitment letter, then on to the closing and finally ending up in the hands of the portfolio officer assigned to administer the day-to-day activity of the loan. The credit file may contain appraisals, environmental assessments, letters, memos, credit write-ups/approval documents and portfolio review summaries, as well as other written material that may be peculiar to a lender's loan origination, closing and administration process. Obviously, the organization and the component parts of the credit file will vary by institution but for our purposes will not include a complete set of the loan documents.

While there are rational business reasons for maintaining most of the documents normally found in a credit file, credit files can also be a ticking time bomb. Why? Because most, if not all, material contained in a credit file, with the possible exception of correspondence and memos between counsel and the lender, will be discoverable in a litigation or bankruptcy proceeding. There is not much that can be done with written material prepared in the ordinary course of administering the loan to immunize such material from the probing eyes of borrower's counsel or a bankruptcy trustee during the discovery process. There is much that can be said, however, about how to write intelligent and accurate memos, correspondence and reports; that topic, however, is for another day. The point that should be kept in mind is that a review of the credit file at an early stage will identify both strengths and weaknesses that may affect the lender's workout strategy. Limiting the world of uncertainty and surprise as early as possible adds significant value to the lender's position in a workout or bankruptcy.

The business review should first focus on financial trends based upon information received (or just as important) not received from the borrower pursuant to the credit agreement. During the normal loan administration process, many lenders tend to focus on current covenant testing but fail to step back and look at trends in the financial information, including information provided on borrowing base certificates. The legal review of the credit file that should occur in conjunction with a review of the loan documents will focus on legal issues based upon either noncompliance with the loan documents or legal issues arising outside of the loan documents during the ongoing interaction between the borrower and the lender.

For example, look for trends specifically relating to collateral; a slow but steady growth in inventory; a gradual but steady growth in ineligible receivables; a growth in receivables concentrations with specific key customers; or the nonrenewal of key customer contracts. Other trends of interest may be a steady growth in the over–90-day payables bucket; the nonrenewal of key vendor contracts; or, if the collateral is primarily rental real estate, a gradual but steady loss of tenants without evidence of releasing at comparable rental rates within a reasonable period of time.

It goes without saying that if there are gaps in the credit file where required financial information should reside, the lender should immediately make inquiry of the borrower and, if applicable, any guarantor and request that the information be provided. If a significant amount of time has passed since the due date of the required information and the lender has failed to act, arguments can be made that the requirement has been waived. Any response from the borrower other than providing the information should be viewed with a certain degree of concern, and the item should be added to the list of borrower deliverables in the next amendment or forbearance agreement.

Another trend of particular interest may be a gradual but steady decrease in the net worth of an individual guarantor over an extended period of time. In many instances, individual guarantor asset transfers are not prohibited. Don't be surprised to find that not long after credit is extended, a savvy individual guarantor has started to slowly move assets off his or her balance sheet into protected investments such as retirement accounts, offshore investments or investments protected by state law homestead exemptions. After closing, some individual guarantors may grant a mortgage on otherwise unencumbered real estate in a less than arm's-length transaction for no other reason than to gain negotiating leverage with the lender faced with protracted and costly fraudulent conveyance litigation to gain access to the value locked up in the real estate. Knowing and evaluating the impact of this data point at the beginning stages of the workout will leave the lender with a greater range of options as opposed to learning of this problem at the time the guarantor's assets become a necessary part of the recovery equation.

Finally, as part of the credit file review, do not overlook the electronic loan management system and the mountain of information contained therein. The data on this system is fertile ground for discovery and surprises, especially in light of the December 1, 2006, effective date of the new federal electronic discovery rules. Data entry mistakes happen; interest rates are not adjusted on a timely basis; interest rate swaps expire with no notice to the borrower; or collections are inadvertently misapplied. Carefully review the loan payment history for accuracy and compliance with any internal policies relating to loan data management or other requirements that may be contained in the loan documents. This is one area where surprise can be devastating.

Review the Lender's Legal File

For our purposes, the legal file contains the contractual agreements that govern the relationship between the lender and the borrower. The file should also contain information regarding legal relationships between the lender and certain other creditors of the borrower, information regarding initial and ongoing legal due diligence and information regarding the perfection of liens granted to the lender. For reasons that will be addressed below, a lawyer's review of the legal file should always also include a review of the credit file.

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Who should conduct the legal review? The answer varies by institution. Some lenders have a hard-and-fast rule that the legal review is the official start of the workout and regardless of whether an internal transfer has been made to the workout professionals, the lawyer reviewing the file not only should have an expertise in workout and bankruptcy but also should be at a law firm other than the firm that documented the transaction. Some institutions take a middle approach and do not transfer the matter to a new law firm but require that the file be reviewed by a lawyer with workout and bankruptcy expertise other than the lawyer who documented the transaction. A minority of institutions will not address this issue and will have the lawyer who documented the transaction conduct the legal review.

Engaging a lawyer with workout and bankruptcy expertise to conduct a legal review is a commonsense decision. Shifting the file to a lawyer and possibly a firm that is not part of the current deal team makes sense for the following two reasons. First, workouts are as much psychological warfare as they are legal and business engagements. Borrowers and their advisors develop a relationship with the lender and its advisors during the life of a loan. When signs of distress emerge, new counsel and possibly a new lender team will bring a renewed sense of objectivity to the matter at hand that will be less likely to be present with the existing deal team. Borrowers will often view the people on the existing deal team as their advocates within the lending institution. While a new team may also advocate on behalf of the borrower, a new deal team also creates a perception that until the weaknesses are corrected or the loan is repaid, it is no longer business as usual.

Second, new workout and bankruptcy counsel will review the legal and credit files not with an eye toward negotiating a deal satisfactory to both parties but with an eye toward creating a strategy that will allow either for the rehabilitation of the loan or a full recovery. This will include an objective assessment of both strengths and weaknesses of the lender's positions that will factor into both short- and long-term strategies. Numerous institutions have taken the position that in order to obtain true objectivity, a completely new law firm should be retained. The reasons are obvious: The closing law firm may be too close to the matter and, therefore, may make assumptions about issues that should require closer analysis; and, to be perfectly frank, few law firms will want to be in a position where they must admit a documentation mistake.

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Once workout counsel has been selected, the entirety of the lender's legal and credit files should be sent to counsel. It is best not to make assumptions about documents counsel may or may not want to review. Documents that may not appear to be relevant to a legal review from the lender's perspective may be of significance to counsel.

At minimum, counsel should focus on the following areas/issues when conducting the review:

- Discrepancies among the credit approval, the loan documents and the lender's perceptions of the credit
- Collateral perfection deficiencies
- Existing events of default
- Course-of-conduct issues (a/k/a what have I waived)
- Lender liability issues
- Intercreditor issues
- Other documentation weaknesses or inconsistencies

Counsel should provide to the lender a privileged and confidential memorandum setting forth the legal analysis addressing these areas/issues. The memorandum may also include a preliminary outline of the workout strategy from counsel's perspective.

Discrepancies Between the Credit Approval, the Loan Documents and the Lender's Perceptions of the Credit

The focus here is to align the lender's expectations with reality. Credit approval documents usually are not written by counsel; thus, the role of initial deal counsel is to translate the requirements of the credit approval document into the legal contract between the lender and the borrower. In the vast majority of cases, the loan documents accurately reflect the major substantive points of the credit approval. But as negotiations drag on, secondary points may be compromised and those compromises may not be readily apparent to the businessperson assigned merely upon a review of the approval documents. Those compromises may also affect the workout strategy. On more than one occasion, lenders have been unequivocal in stating their understanding of the agreement between the borrower and the lender and have operated on the assumption that their understanding is correct, yet when the specific contract language is reviewed by experienced counsel, the language is ambiguous at best. It then becomes the role of reviewing counsel to objectively advise the lender of the current state of affairs regardless of whether counsel agrees with the lender's perception of the current reality. Understanding these issues at an early stage will help guide the workout strategy.

Collateral Perfection Deficiencies

The discovery of collateral perfection deficiencies is dreaded by both the lender and its closing counsel. Keep in mind, however, that there are several possible causes of documentation deficiencies to consider when addressing the problem. Some deficiencies are a result of legal miscues while others may relate to borrower bad acts. Over the course of a borrowing relationship, it is not unusual for the borrower to change certain aspects of its business or be subject to certain third-party forces that may require the lender to take certain actions to protect its lien position or reevaluate its lending parameters. Borrower changes may involve opening new locations, acquiring or creating new product lines, creating new banking relationships to service new locations or changing its name. Third parties may have been granted purchase money liens, judgments may have been filed by unpaid vendors or other third-party claimants, and the Internal Revenue Service (IRS), the Pension Benefit Guaranty Corporation (PBGC) or local taxing authorities may have filed or may be threatening to file a lien. The existence of any these facts will materially affect the development of a lender's workout strategy as the strategy may need to incorporate a plan to repair a problem or deal with a problem that is beyond repair.

Consider conducting searches on borrower and guarantor assets not currently the subject of the lender's lien.

Accordingly, a complete collateral evaluation cannot occur without obtaining an up-to-date lien search with respect to both collateral types, personal property (including intellectual property) and real property, as applicable to the transaction. Also consider conducting searches on borrower and guarantor assets not currently the subject of the lender's lien to determine the availability of other assets to bolster deficiencies in existing collateral. New search results taken together with any searches conducted in connection with the closing and with subsequent periodic searches should confirm the priority position of the lender's lien and should identify other liens of record. With respect to Uniform Commercial Code (UCC) filings, pay particular attention to the name of the borrower set forth in the debtor box on the form. Make sure that counsel determines that the name is absolutely the borrower's correct name as required under Article 9 of the UCC. There is little room for error. Your priority position is at stake. Real estate lenders may be a little less fanatical about searches if they received a satisfactory lender's title policy at closing from a reputable title insurance company.

If the lender is making revolving loan advances, note that the IRS does not need to follow the Article 9 rules when it comes to filing a federal tax lien. The IRS has the option of filing a lien in locations authorized by the Internal Revenue Code and those locations may not be the same of the locations required by Article 9 for the filing of a financing statement. Further, recent case law has upheld the IRS's ability to file under a borrower name that may not be an exact match with the borrower's legal name. It is the borrower's legal name that is required by Article 9 for a financing statement and any lender who deviates from that name will suffer the consequences. Not so for the IRS. A search of the legal name even in the correct locations may not uncover the IRS lien. If the lender does not have a copy of the borrower's federal tax returns, it would be prudent to obtain a copy as soon as possible to determine if the IRS may be using a variation of the legal name or a trade name in the event it were to file a lien. Then adjust your lien searches accordingly.

Existing Events of Default

A clear understanding of the current factual scenario will allow counsel to the lender to apply the existing facts to the loan documents to facilitate the identification of all events of default. The type and severity of the defaults can usually be ranked in decreasing order of materiality. Grace or cure periods are likely to exist for many nonpayment events of default. Lenders and their counsel, therefore, should note those periods in their document review to avoid unnecessary costs and possibly lender liability claims from disgruntled borrowers if the lender has acted prior to the expiration of a grace or cure period.

- **Payment.** A missed payment of principal, interest and/or fees often entitles the lender immediately to accelerate the debt and, if necessary, exercise any and all enforcement rights available to the lender under the loan documents and at law. Typically, commercial borrowers do not have a right to cure the missed payment(s). After acceleration of the loan, any payments received as a proportional cure payment (the full outstanding balance of the loan is due upon acceleration) may be accepted by the lender but should be followed immediately with a letter indicating that acceptance of the partial payment does not cure the default nor does it waive any rights the lender may have to continue to enforce the accelerated obligation. Should the lender desire to reach an agreement with the borrower, the lender can always reinstate the loan or enter into a forbearance agreement.
- **Financial covenants.** Particular attention should be paid by lender's counsel to whether borrowers have defaulted on financial covenants on prior occasions without lender response in the form of a waiver, amendment or reservation-of-rights letter. Counsel to the lender should then (given the circumstances) advise as to whether the failure to acknowledge and respond to prior covenant violations will limit the enforcement options.
- **Other defaults.** A thorough review of the facts may also reveal additional nonpayment defaults that may give the lender additional leverage during discussions with the borrower and indicate deficiencies that will need to be addressed as part of the workout plan.

The materiality of the default will have a significant effect upon the development of the lender's course of action during the restructuring. The lender should open communications with the borrower as soon as any event of default is identified. Lender's counsel should also be recommending that the lender send a reservation-of-rights letter or a demand to cure the default in order to preserve the lender's options for restructuring and enforcement.

Course-of-Conduct Issues (a/k/a What Have I Waived)

During the course of a relationship between a lender and a borrower, contractual agreements contained in the loan documents often may not have been strictly enforced. When a loan heads toward the workout phase, the lender, along with its counsel, will need to determine whether legitimate arguments can be sustained by the borrower that the lender (notwithstanding "No Waiver" provisions contained in the credit agreement) has effectively waived some of its rights under the loan documents. A waiver argument can be crafted when the lender either acts in a manner inconsistent with the requirements of the documents or consistently fails to enforce contractual requirements over an extended period of the time such that the borrower has come to rely on the lender's ongoing acts or failures to act.

The lender together with counsel should review the payment terms (including any grace periods) as set forth in the loan documents in comparison with the actual payments made by the borrower. For example, if the borrower has been making payments in violation of the terms of the loan documents and the payments have been regularly accepted by the lender, the borrower may argue that the lender, having continued to accept such payments without any objection, notice or other ramifications (that is, charging late fees, applying any default rate, *etc.*), is prohibited from charging late fees or calling a default with respect to such prior payments or any payments made in the future.

Be aware of third-party relationships that may have an impact on a workout strategy.

Counsel's review of the credit file will focus on identifying any course-of-dealing issues. Identification of these issues at the early stage of a workout is critical. Course-of-dealing issues may arise in any credit: large or small, secured or unsecured, syndicated or single lender. For example, on more than one occasion, a lender has failed to adjust interest rates properly during the administration of the credit resulting in either a credit due to the borrower or additional money owed by the borrower. Also common and equally problematic is lending based upon a borrowing-base certificate that does not accurately reflect the terms of the credit agreement or lending upon an accurately drafted borrowing-base certificate that is incorrectly completed by the borrower.

Typically, loan documents contain a provision limiting the effectiveness of waivers granted by the lender to waivers that are set forth in a writing signed by the lender. The lender can generally rely on the waiver provision in the loan document to rebut any presumption as to whether it has waived any of its rights thereunder. The nonwaiver provision, however, is not foolproof and is most effective when used in situations when the alleged waiver is the result of a singular event. In situations when there has been a recurring event and no lender reaction, reliance on the nonwaiver provision will most likely be unsuccessful; therefore, counsel should review the credit file to determine whether the lender's action or inaction has become repetitive so as to create such issues.

Course-of-conduct issues may be repaired. Identification of these issues early on in the restructuring will expand the time that the lender will have to make the repairs before the situation deteriorates.

Lender Liability Issues

A review of the legal and credit files should also focus on the possibility that the borrower may claim that the lender engaged in acts amounting to lender liability. Lender liability is not a single legal theory but rather a generic moniker for numerous legal theories under which lenders have been found liable to borrowers. Some lenders have had to compromise their loan amount to settle a lender liability claim, while others have recovered all or part of their debt but have then needed to pay to the borrower damages in excess of their debt owed. The possibility of lender liability claims by the borrower should always be considered when preparing to enter into a restructuring, but the risk of a successful prosecution of such a claim should be kept in perspective.

Lender liability claims are rarely successful and should be a cause of concern only in very specific instances. Occasionally, an unhappy borrower will threaten legal action against a lender in response to tighter lending requirements or requests for accelerated repayment. The question the lender and its counsel must ask when weighing the possibility of a lender liability claim is "Have I (lender) breached my agreement with the borrower or somehow damaged (that is, through control over all or merely certain aspects of the business, improperly refusing to fund, *etc.*) its business?" If the answer is no, the weight ascribed by the lender to the borrower's threats should be limited to nuisance value, that is, to litigation costs and time. It is important to note that a real lender liability claim can only arise from a discrete and limited list of legal concepts, namely, a breach of contract or a tort claim. If the action you take as a lender is within your contractual rights (declaring an event of default, ceasing advances after an event of default or demanding repayment), you have not breached your agreement with the borrower. If, however, you stop advancing money, set higher reserves, *etc.,* when such actions are not authorized under the credit agreement, and, the borrower is financially harmed as a result, there may be a real claim. To that end, courts are pretty consistent in upholding the rights of a lender to exercise its contractual rights and remedies even if the result appears to be harsh. On the other hand, keep in mind that a bankruptcy court operates under a different set of rules and is a court of equity. While contracts are generally enforced, bankruptcy judges at times have a way of surprising even the most seasoned workout professional.

A failure to fund absent an event of default or sharing information about the borrower with a competitor who also happens to be a borrower of the same lender are classic examples of actions taken by a lender that can lead to a lender liability claim and possibly a judgment. Even then, however, the question becomes, "To what extent did my breach or bad act really harm the borrower?" A significant part of the ensuing litigation will therefore revolve around the issue of damages, and the burden to prove same will be on the borrower.

As the potential for a lender liability claim always exists, early analysis of the facts and legal theories that might support a claim will determine if the lender must incorporate the prospect of such litigation into its restructuring strategy. For example, a claim with a real basis in law might be mitigated by attempting to achieve an early settlement to avoid litigation and possibly a judgment; while on the other hand, threats of a clearly frivolous claim may be set aside as the lender continues to pursue its enforcement remedies.

Other Due-Diligence Opportunities

There are a variety of other items of which the lender should take note in the preworkout period. It is important for a lender to understand the borrower's cash management structure. If the lender is the borrower's main cash management bank, reach out early and often to the internal cash management people assigned to the borrower. If the cash management structure is complex, work with the cash management unit to develop a schematic of the borrower's cash flow. Understand the borrower's cash collection cycles, its use of ACH transfers, zero balance and other special-purpose accounts. Learn where money is and where it is supposed to be. Significant variations in normal day-to-day patterns of cash moving through the system may be a sign that the borrower has opened accounts in another institution to avoid a lender's setoff rights. Be prepared to shut down ACH transactions so as not to be caught as an unsecured and unprepared lender in a bankruptcy. Know when the borrower's cash balances are high in the event a setoff of funds is required.

It is quite common for the lender who hesitates to see its workout options diminished.

Also explore the possibility that the borrower may have other business (credit card, securities accounts, *etc.*) and personal (friends with the CEO) relationships within the institution. In a distressed situation, the borrower will use all of the tools available to it to survive. You as the lender should know what these tools are before they are employed by the borrower to blunt any potential impact.

Be aware of third-party relationships that may have an impact on a workout strategy. First and foremost, determine if the borrower has any issues with the IRS, PBGC or any other third party that may have a claim to the borrower's assets. Pay particular attention to parties who may have legal rights to a lien on assets that may prime your own lien. There are some industry-specific and state law statutes that may come into play. Counsel should be asked to advise if these liens are applicable to the situation.

In addition, pay careful attention to landlords and utility companies, both of whom have the ability to impair the value of the collateral. Landlord waivers, if obtained at closing, should be reviewed to determine what if anything must be done to gain access and, if necessary, liquidate collateral on premises. If waivers were not obtained, other options should be explored with counsel to determine what legal course of action may be necessary to gain access to the collateral. If the borrower is responsible for paying the utilities, failure to pay may result in frozen (in the winter) or melted (in the summer) collateral.

Further, check the status of insurance coverage. If the information in the credit file is incomplete, start with contacting the borrower for updated information. If the borrower is not cooperative, go directly to the insurance agent or broker listed on the insurance documentation obtained at closing or thereafter. If you cannot ascertain if sufficient insurance is in place, do not hesitate to obtain and pay for coverage. While it is an additional expense that will be added to the borrower's obligations, it is the time when the lender chooses not to obtain coverage that the collateral will be destroyed or damaged. On more than one occasion a lender has been repaid *via* the proceeds of insurance obtained by the lender after the borrower's coverage had lapsed.

Finally, various entities, such as insurance companies, guarantors, bonding companies, bondholders, state and federal economic development agencies, *etc.*, will often have notice and subrogation rights. Knowing and understanding those rights will often be critical to the development of the restructuring plan.

The Rights of Junior Lenders and Participants

The financing structure of many borrowers today is not as simple as it once was, and any lender in a workout situation needs to be cognizant of the rights of various *pari passu* or subordinate lenders.

Clearly, a situation where the lender has violated the rights of a junior or mezzanine lender, co-lender or participant, or a surety will only further complicate the ability to restructure a distressed credit. The best way to avoid creating and then dealing with such a situation is clearly understanding the issues before taking any action.

Junior or mezzanine lenders (depending on the type of financing) will have a variety of negotiated rights and remedies. All of their rights and remedies will typically be contained in an intercreditor agreement that often contains notice provisions, buyout and takeout rights, standstill provisions for various types of default, additional financing prohibitions after an event of default, *etc.* Your best bet as a lender is to understand clearly those rights and duties and adhere to same without deviation. *In a workout scenario, the interests of holders of subordinated debt are not usually aligned with the interests of the senior lender, especially if the subordinated lending institution is of a different lender type; bank secured lender versus hedge fund, for example.* If on the part of the senior lender there have been deviations from the terms of the intercreditor agreement, it is best to know the nature and extent of the deviations as early as possible. Finally, when looking at your restructuring options, you will need to factor in the impact of all of the restrictions or limitations contained in your intercreditor agreement.

A lender will also want to understand its rights and duties *vis-à-vis* other lenders when acting as the agent for a syndicate or as a lead lender on a credit facility where there are participating lenders. The how, when and where in keeping the other lenders involved in the restructuring must be carefully orchestrated. Knowing when to seek approval for waivers or a proposed restructuring along with thoroughly understanding the voting and blocking rights of the lender group is essential to a successful multilender workout strategy. Developing a strategy around a faulty understanding of voting rights and other multilender provisions in the credit agreement will impair the agent or lead lender's ability to implement its strategy.

Finally, the buying and selling of debt, whether performing or distressed, is a daily fact of life for financial institutions. The identity of your fellow lenders and their particular business objectives will force you to identify and maintain acceptable common restructuring goals, especially when it affects various "sacred rights" such as payment schedules, interest rates, fees, release of collateral, debt forgiveness, *etc.*

Plan a Workout Strategy Early

There is no better time to plan a workout strategy than at the earliest stages of the workout. Time is not on the lender's side once the financial deterioration process has commenced. It is quite common for the lender who hesitates to see its workout options diminished because it is having to deal with issues on the fly. Early preliminary due diligence structured in a manner that is appropriate for the size and nature of the credit will significantly enhance the chances of increasing the lender's recovery.

The next article of this series will focus on the basics of enforcement and the options available to lenders when enforcement is the next step in the loan recovery strategy.

Endnotes

* This article is designed only to give general information on the topics actually covered. It is not intended to provide legal advice or render a legal opinion. The views expressed herein are those of the authors and do not necessarily reflect the views of Proskauer Rose LLP or of CapitalSource Finance LLC.