

The Inoculation and The Cure Are Both Remedies for Poor Credits

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Sometimes, there is little that can be done. A lender makes a loan to a person of questionable character who then defaults on the loan and claims that there are no funds to repay the credit. The bank sees the defaulted borrower living in a large home (or two), driving expensive vehicles, and otherwise living a very comfortable life, so it simply cannot be that the borrower has no income. The bank engages in legal proceedings to sue the borrower in order to become whole. However, the lender learns that the defaulted borrower has no income in his name personally—his homes are in his wife’s name (she is not liable on the debt)—and his businesses are all in LLCs that are owned by a trust in which his wife is the sole beneficiary. What is a lender to do?

This type of situation is all too common, but it can be addressed at the time of the credit as well as after the lending relationship has gone south.

Before the Loan

At the time that a lending decision is being considered, lenders should look at more than just the collateral even if the credit is collateral-based. Real estate fluctuates in value and different appraisers can reach vastly different opinions of value on the exact same piece of property. For example, court cases exist where one appraiser gives an opinion of value of \$450,000 and the other giving an opinion of value at \$900,000 for the exact same property. An opinion of value is just that—an opinion. Errors and omissions insurance for appraisers exists for a reason.

The ability of the borrower to repay the credit regardless of the collateral, even if it is a collateral loan, should be examined. Is the debtor someone who has tried to make himself “judgment proof”? Are all of the debtor’s assets in LLCs, her spouse’s name, or in a trust that she controls but benefits someone else? If the only thing that the debtor is risking with the loan is the collateral itself, lenders need to ask themselves if that is the character of a borrower with whom they wish to engage in a business relationship.

After the Loan

Once the horse has left the barn, there is little that can be done other than to chase it or let it go. The problem with a debtor with no assets in his name is that the creditor becoming whole becomes quite difficult. These borrowers put assets into other people’s names or into companies generally for the purpose of shielding them from creditors. Creditors can, however, prevail in actions to recover the loans from such borrowers, but it takes time and effort. Assets transferred out of the debtor’s name to avoid creditors can sometimes be recovered; LLCs that pay income to the debtor’s spouse but not to the debtor can sometimes have their assets used to satisfy the creditor’s judgment against the debtor. The downside to such proceedings is that they take both time and money to achieve. The wheel of litigation spins quite slowly at times and savvy debtors do everything they can to delay payment in the hopes of avoiding it. Attorneys are also expensive. Attorneys that are not adept at how to get at assets of debtors of questionable character are even more expensive as they may spend unnecessary time engaged in proceedings that will be of little assistance in the recovery of the amounts owed to the lender.

The good news is that lenders can recover from even the most uncooperative debtors, but lenders must be willing to spend the time and effort needed for a positive outcome. If the will to proceed until the end exists, creditors can prevail at the end.

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