

# **An Insight into the Commercial Foreclosure Process**

*Let's not kill all the lawyers just yet!*

Foreclosure attorneys today are frequently reminded of Shakespeare's famous quote from Henry VI. What debtors overlook, however, is that Dick the Butcher was not trying to achieve commercial stability by eliminating the lawyers. Rather, he and Jack Cade were seeking to promote anarchy and chaos as a means to achieve their own self-serving objectives.

Similarly, attorneys engaged by lenders to foreclose upon assets secured under a defaulted loan are not necessarily counterproductive toward economic recovery. On the contrary, an understanding of how a foreclosure attorney interacts with a lender and approaches distressed credit files can provide insight to help address troubled credit scenarios and potentially avoid defaults and foreclosures.

## **The Initial Consultation**

Most foreclosures begin when a lender has red-flagged a loan file, usually for non-payment, and contacts counsel for assistance. The file is delivered to counsel for an initial review and evaluation, and a chronological history of the loan relationship is prepared and analyzed to reveal any prior problems (or lack of problems) that may have existed during the relationship between the lender and debtor.

The attorney will thoroughly review all pertinent documents in the loan file. This includes not only the promissory note, but also the security agreements, mortgages, correspondence and other supporting documents to ascertain the collateral that has been pledged to secure the loan. Lien searches must be obtained for all real estate and personal property pledged as collateral to determine whether other lenders may potentially have a claim for the same collateral. All personal guarantees and co-signing instruments must be reviewed, together with all available financial information related to them.

After a review of the loan file, counsel typically provides the lender with an opinion whether any potential defenses exist that may permit the debtor or guarantors to avoid some or all of their obligations. Once this information is compiled and reviewed, the lender and counsel must interact to formulate a strategy for addressing the troubled loan. The lender must make several important decisions, including: 1.) whether the lender wants ownership or control of the collateral; 2.) whether the lender wants to maintain a continued relationship with the debtor; 3.) whether the lender is willing to give a discount off the total debt due; and 4.) whether the lender has concerns if the debtor files bankruptcy. The answers to these questions will enable the attorney to develop a plan for addressing the problematic loan.

## **The Default Notice**

After the initial review and analysis of the loan file, the lender or its attorney will deliver default notices to all of the debtors, co-signors and guarantors. This letter will typically contain information related to the default, and inform the debtor that formal proceedings will soon begin. At this point, the debtor should obtain legal counsel. There are as many competent and experienced attorneys in central Illinois who represent debtors as there are those who represent

lenders. By the time a default notice is delivered, the lender and its attorney have typically constructed a clear strategy for approaching the debtor, and the debtor should not attempt to navigate this process without assistance.

After receiving the default notice, the debtor must determine how to respond. No response at all will typically result in the lender quickly filing a lawsuit. In some instances, the debtor may file bankruptcy, resulting in an “automatic stay” that requires the lender to stop its collection efforts and pursue its rights in bankruptcy court. Sometimes the debtor will respond by requesting additional time to cure defaults or negotiate a new arrangement with the lender, otherwise known as a “workout.” The success of a workout often requires a strong commitment and a sincere level of cooperation between the lender, debtor and their attorneys.

### **Litigation and Other Alternatives**

Once the debtor’s position has been articulated, the lender must decide its next course of action. If a workout is possible and the debtor persuaded the lender to modify the loan terms or allow an opportunity to cure the defaults, then a written agreement is executed by both the lender and the debtor. This agreement should clearly explain the terms of the loan that have been changed, and the rights and obligations of all parties as a result of that change.

If no workout can be arranged, the next step usually involves formal collection proceedings. If the loan includes real estate, and the lender has decided to take the property, a complaint under the Illinois Mortgage Foreclosure Law is filed. A title company will prepare a document known as *Minutes of Foreclosure*, which dictates to the lender how clear title to the real estate can be acquired. Often there are liens previously filed against the property, and counsel must analyze these liens to determine if they are superior or inferior to the lender’s mortgage. Ultimately, the property is sold and the proceeds applied toward the debt. Debtors must take care, however, because under some circumstances they can be held accountable for the difference if the proceeds from the sale do not completely satisfy the debt.

If the loan collateral includes personal property and the lender has decided to take the property, Illinois Uniform Commercial Code Article 9 prescribes the method lenders must follow to foreclose and sell the property. Generally, lenders must provide notice to the debtor and are prohibited from “breaching the peace” when repossessing the collateral. Once again, it is possible that the debtor will remain obligated to the lender if the debt is not fully satisfied from the proceeds of the sale.

Finally, if the lender has determined that it does not want to take the property, a lawsuit can be filed for the amount due under the loan. This is an action for breach of contract, which encompasses all the rules of procedure, evidence and discovery that govern a lawsuit. Under this alternative, it is imperative that the debtor and guarantors seek their own legal counsel to protect their rights.

### **Conclusion**

Troubled loans can present complex situations for both lenders and debtors. Attorneys experienced in this process can help simplify and streamline the procedure for all parties involved, and hopefully avoid the chaos that can result from Shakespeare’s prophecy.