About the Firm

Shapiro Sher was founded in 1972 with the mission of providing outstanding legal counsel for businesses of all sizes. Based in Baltimore, the Firm is nationally recognized for its practices in business law, litigation, bankruptcy, banking, and creditors' rights.

Shapiro Sher's banking lawyers provide experienced counsel in connection with all aspects of commercial loans. Chaired by **Scott Foley**, the firm's **Banking & Financial Services Group** regularly represents regional and community banks, credit unions, finance companies, and other financial institutions in the Mid-Atlantic and in transactions throughout the country.

The banking group includes partner Pat Gill, who represents financial institutions in connection with re-documenting troubled loans and structuring, negotiating, documenting, and closing commercial finance transactions. Attorneys in the group also advise financial institutions regarding under-performing and distressed loans. The group routinely handles loan modifications, workouts, restructurings, short and long-term forbearance agreements, and bankruptcy litigation. Because the group has extensive experience in the origination of loans and in workout situations, it is prepared to provide efficient representation at every stage in the lending process.

With decades of experience in the banking industry, Mr. Foley and the firm's other seasoned banking attorneys appreciate the potential hazards facing clients in the commercial loan process, and strive to protect lenders' interests throughout the lifecycle of the loan.

COVID-19'S IMPLICATIONS FOR EXISTING COMMERCIAL CREDIT FACILITIES

AN UPTICK IN DEFAULTS IS COMING

By Wes Parker

The coronavirus (COVID-19) outbreak, which the World Health Organization recently designated as a pandemic, is imposing significant strains on the global economy. Many businesses have ground to a halt due to a myriad of factors, including disruptions of global manufacturing and supply chains, travel bans, mandatory or self-imposed quarantines, employee absences, event cancellations, and decreased consumer activity. Although there is wide-ranging speculation on the long-term economic effects of the pandemic, it is apparent that downward market pressures are likely to severely impact a wide range of businesses and increase the probability of defaults occurring under outstanding debt obligations in the near term.

Lenders should anticipate a potential uptick in:

- **Monetary/Payment Defaults** – Borrowers that are struggling with short-term cash flow and liquidity may be unable or unwilling to continue debt-service obligations.
- **Financial Covenant Defaults** – Loss of business income may negatively affect financial covenant compliance (e.g. debt-service and liquidity covenants).
- **Cross Defaults** – Even a borrower that is performing under your financing documents may be defaulting under its obligations to other creditors.
- **Business Interruption Defaults** – As certain businesses across the country begin to cease operations as a result of mandated or recommended "social distancing", an event of default could be triggered as a result of such closures.

The rapidly evolving economic landscape resulting from the pandemic will make it challenging for a lender to develop a coordinated response to potentially numerous anticipated defaults under its commercial credit facilities. Furthermore, reputational considerations resulting from a lender's response in a time of crisis are likely to play a significant role in the analysis of whether to call a default during these uncertain times. Continued >>

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From a practical standpoint, modifying certain payment and potentially other loan terms on a temporary basis may be a sensible approach for a significant segment of defaulting borrowers (or borrowers for which a default is anticipated). A short-term modification will also provide (i) the borrower with an opportunity to develop a response to the challenges in its business imposed by the pandemic and perhaps resolve the same with an improvement of market conditions, and (ii) the lender (and its borrower) with additional time to analyze the progression of the COVID-19 outbreak and any long-term ramifications thereof.

Although the pandemic is likely to place certain limitations on a lender's ability to document agreements addressing defaults, it is best practice for the modification of loan terms to be memorialized in writing, be executed by the parties, and expressly state the temporary nature of the modification, with all other loan terms and conditions remaining in full force and effect.

Given that lenders may need to streamline the process of addressing numerous defaulted loans via short-term loan modifications in a compressed time-frame, a few key provisions protecting the lender should be contained in the loan modification. These should include, among others, an acknowledgement as to the amount of the indebtedness due under the loan, that the modification shall not be deemed a novation or have an adverse effect on the validity and priority of liens, and that, in consideration of the lender's accommodations, the obligors should release and discharge the lender from all claims and causes of action. With respect to borrowers that are in default and may not be candidates for a loan modification, lenders should consider a forbearance agreement. Under any scenario, when contemplating a waiver of existing defaults, lenders should take caution to keep their options open during uncertain times and ensure their rights are reserved to take action in the future without needing to await further events of default.

For more information about this or other banking law matters, please do not hesitate to contact any of the attorneys in our Banking and Financial Services Group.

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