CAPITAL

'Workout' may be solution for those facing potential loan default

With weakened cash flows, an increase in vacancies and a decrease in market value of their commercial properties, borrowers are finding it difficult to refinance or make their loan payments.

Many borrowers are looking for alternatives to defaulting.

A "workout" occurs when the lender and borrower of a failing commercial loan consent to alter the terms of the loan to benefit the borrower in an effort to prevent a default, says Brett L. Slobin, attorney in the Houston law firm of Slobin & Slobin PC.

"While not a cure-all, in the right situations, workouts can provide relief to borrowers and benefits to lenders, he says.

Below, Slobin answers some common questions about loan workouts:

Q *How should a borrower approach getting a loan workout?*

A Borrowers requesting a workout should establish a business plan that recognizes the borrower's current problems and addresses these problems with viable solutions. Providing this business plan to the lender in advance of a default will give the lender confidence that the borrower is being honest and realistic, and the plan will demonstrate to the lender that the borrower is somewhat in control of the situation.

Q *What would a typical workout agreement provide?*

A There are a myriad of actions and alterations of loan terms that lenders may take that would be considered a workout, including changing the interest rate, reducing the loan payments in exchange for either a longer loan term or a balloon-type payment in the future and reducing the borrower's capital requirements within the loan. Solutions could also include reducing the borrower's capital requirements within the loan or forgiveness of a portion of the debt outright — an option that is admittedly more rare than others — or adding any forgiveness of monthly payments to the balance of the loan and forgiving or forbearing default interest or late penalties.

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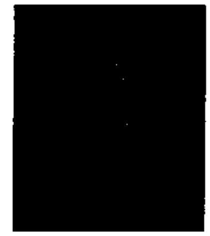
>
> **Brett L. Slobin**
> Slobin & Slobin PC



Q *It's obvious why a borrower would want a workout of a loan, but why would a lender participate in a workout?*

A First, most lenders do not want to have ownership of the property. Ownership carries with it risks that lenders normally are not prepared for and do not want to assume. Risks involved in the operation of a property could include payment of taxes and insurance premiums, the risk of loss from personal injury and property damage claims, as well as any shortfall in cash flow.

Most lenders are not in a position to operate a property, and problems causing the loan to be in jeopardy will not disappear simply because of a change in ownership. Since most properties today will not appraise for the same value as of the date the loan was made, the likelihood of a buyer, at a foreclosure sale, paying enough money to cover the debt is slim. Therefore, the lender will still have a deficiency on its books which it may or may not be able to collect.

Also, failure to strictly adhere to foreclosure laws (i.e., required notices of default and acceleration) may lead to expanded risk and liability for lenders. ■

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