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M|J|B BANKING LAW TODAY

WE DECIDED NOT TO RENEW – SO NOW WHAT?

The Initial Steps Ag Bankers Should Take After Deciding to Non-Renew a Borrower

After a gut-wrenching renewal evaluation process, it is very likely that at least some borrowers will be non-renewed in 2020. After that decision is made, often a type of paralysis and confusion sets in among Ag bankers. After all, many Ag bankers have gone years or even decades without non-renewing a customer. "What do I do now?" is a very common question that I receive from my Ag banking clients after the initial non-renewal decision has been made. This article seeks to provide an answer to that question as well as a sound, coherent process for tackling this very emotional and challenging situation.

Step 1: Make Sure the Loan File is in Order.

Before the bank does anything else, it needs a concrete sense of the state of the loan file. Have all documents been properly executed? Have the UCC Financing Statements been filed against all proper parties and properly continued? Have the mortgages (with a correct legal description and all applicable mortgagors) been filed in all applicable counties? Have the CNS Financing Statements been filed against all proper parties and properly continued? Have all out-of-state commodity buyers been properly notified of the bank's security interest in agricultural commodities? Has the bank accounted for all commodities, commodities proceeds and equipment?

Very frequently I find that the answer to at least one of the above questions is "no." If that is the case, now is the time to fix the issue (if possible) given that correcting errors will become exponentially more difficult after the credit has gone into liquidation.

Step 2: Consider Whether an External Refinance is Possible.

Despite the agricultural economic downturn, there are a number of lenders and financing companies – both traditional banks and alternate financiers/funds – that are still actively looking to get deeper into the agricultural space. Some of these companies may be willing to do a straight refinance, and some may be willing to purchase the papers at an agreed upon price.

While a bank should never risk a lender liability claim – or risk putting customers into an ill-fitting financing relationship – by forcing a customer over to a new lender, it is a good idea to evaluate a variety of external refinance options before formally non-renewing a borrower. By doing so, the bank can have potential resources at the ready and can be seen more as helping borrowers find a new home rather than as delivering a deathblow that ends the borrower's farming operations.

In the event that your bank is looking for such resources, feel free to reach out to me, as I have a variety of contacts of all financier types who are actively looking for new agricultural deals.

Step 3: Assess Voluntary Liquidation Options.

If external refinance is not an option, or does not make economic sense for the bank, the next step is generally to discuss with the borrowers the prospect of an orderly, voluntary liquidation. While farming is a way of life and liquidation discussions can get very emotional, many borrowers can still be persuaded to take the sensible option and agree to a voluntary

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liquidation that likely leaves them with either additional money in their pocket or forgiveness of any deficiency balances.

That being said, you should be aware going into this discussion that farmers tend to be far less amenable to a voluntary liquidation than owners of other types of businesses. As such, do not be surprised if voluntary liquidation talks fail spectacularly even when there is no logical reason for this to occur.

And, be aware that a borrower's "cooperation" may really be a scheme to lead the bank down the primrose path, so the borrower can buy more time. Consequently, any voluntary liquidation should be tightly documented and should have firm dates and milestones that must be strictly observed.

Step 4: Find the Correct Attorney for the Liquidation.

If all of the above steps fail, then I recommend finding the correct attorney to help manage the liquidation process. Bankers need to be aware that agricultural liquidation is a very nuanced and technical area of the law, and the vast majority of attorneys have little to no real experience in the space. And, even for those attorneys who are able to "figure it out" such that they do not make a mistake that invalidates the liquidation (e.g. they fail to give Farmer-Lender notices or a right of first refusal), it is often the case that such an attorney leaves hundreds of thousands of dollars on the table because they do not realize that certain avenues of recovery are viable options (e.g. suits against commodities buyers for failing to observe CNS Financing Statements and fraudulent transfer claims against creditors that received fraudulently diverted loan proceeds).

Below is a list of questions I believe every banker should ask a prospective attorney before engaging him/her in an agricultural liquidation.

1. Have you been through the Farmer-Lender Mediation process before? Can you give me an overview of the process?
2. Have you been through the liquidation process with FSA guaranteed loans? Can you give me an overview of the additional timelines and requirements associated with this process?
3. Have you successfully litigated or recovered money from a commodity buyer who ignored a CNS Financing Statement?
4. Have you successfully litigated against or recovered money from a creditor who was the recipient of fraudulently diverted loan proceeds?
5. Have you successfully litigated fraudulent transfer claims in circumstances where one generation of farmer attempts to fraudulently shift assets and commodities to the next generation free of the bank's liens?
6. Have you been through a Chapter 12 Bankruptcy before? How about a Chapter 7 involving an agricultural debtor? Can you give me an overview of the processes for each Chapter?
7. Have you dealt with statutory agricultural liens and improper offsets? Can you given me an overview of the different types of agricultural liens?

If the prospective attorney answers that they do not have experience with a number of the above items, or if they give evasive answers that do not inspire much confidence, then the bank should strongly consider finding different legal counsel. Competence and experience are fundamental and very likely will directly affect the net recovery the bank sees in the liquidation.

Conclusion

The first steps that any Ag bank takes after deciding to non-renew a customer are generally the most critical. It is very important to have a checklist of steps and procedures for bankers to follow in these difficult circumstances. While the above list is not necessarily all encompassing, it does provide a solid analytical process for banks to employ after non-renewing a credit.

The fact remains that even if a bank does everything perfectly, it is not guaranteed that it will realize great recoveries or that it will maintain great relationships with the borrower after the non-renewal. However, taking the proper steps does at the very least maximize the chances that the bank will put itself in the best possible position from both a recovery and reputation standpoint.

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THE ENLIGHTENING ROUND

Q: Are Internal Bank Emails, Text Messages and Reports Regarding Troubled Borrowers Subject to Discovery in Litigation?

A: The answer here is "it depends." But, to be safe, banks should treat such communications/documents as if they are discoverable. With this in mind, harsh as it may seem, you should treat each document and written communication as if it will possibly end up as an exhibit in a lawsuit. The reason why – it is possible!

Some of the most devastating and humiliating moments of a banker's career can come when a snarky, disparaging or off-color email regarding a borrower takes center stage in a public trial. The fact that the banker may have been "just joking" is generally no real consolation or excuse in these challenging circumstances.

All that being said, intra-bank communications may be privileged and not subject to discovery if: (1) an attorney was copied on the communication and his/her legal opinion was being sought; or (2) the writing was created at the direction of an attorney in anticipation of litigation. The latter exception, known as "attorney work product" can be fairly broad, particularly if an attorney was actually consulted before the communication was made. And, it is notable that the mere act of cc'ing an attorney, even if no direct advice is sought, does at least give banks the argument that the communication is privileged (even if it is subsequently overturned by the Court after an "in-camera review").

In light of the foregoing, the general rules and guidelines that should be observed are: (1) if you are going to tell a joke or say something disparaging about a borrower or situation, do so orally or preferably not at all; (2) do not put harmful or damaging admissions or observations in an email to others within the bank, discuss the matter orally; (3) if you do reduce problematic situations to writing, do so in an email to legal counsel, explicitly seek legal advice regarding the situation, and note that the email is "privileged and confidential" in either the subject or body of the email; (4) if you wish to start discussing a problematic scenario in writing, first contact an attorney and request that he/she provide a written directive for the bank to discuss the situation; (5) if you engage in sensitive communications, cc an attorney – this is not infallible, but it will provide some protection; and (6) if you are concerned about damaging communications that have already been made, consult an attorney immediately to see if there are any actions the bank can now take to mitigate the potential harm of the communications.

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