

## I NEED A LOAN....WHAT DO ALL THESE DOCUMENTS MEAN?

When a business wants to expand and grow, the need for capital is usually the first hurdle that needs to be overcome. While there are many ways to raise capital, including the owners of the business investing additional personal funds or initiating private or public securities offerings, the most common method is for the business to borrow the funds from a financial institution.

Documentation of business loans has always been complicated and somewhat frightening to the uneducated borrower. To further complicate matters, since many financial institutions are still feeling the sting of the lenient lending practices of the past, they are requiring loan documentation that is a minefield for even the most savvy borrower. While the interest rate and the length of amortization are commonly negotiated, many borrowers don't realize that many other provisions of the loan are negotiable.

A borrower and/or guarantor should read all loan documents carefully and understand what all the terms and conditions mean and their respective ramifications and how they affect the ability of the borrower to repay the loan. Many provisions are intended to protect the lender rather than the borrower and/or guarantor. It is advisable to hire an attorney to review the documents and to suggest revisions that better protect the borrower's and/or guarantor's interest. The following are only a few common examples of provisions and concepts buried within loan agreements, promissory notes and/or guaranties that can be negotiated to better protect the borrower and/or guarantors.

In general, loan documents contain agreements and promises by the borrower and/or guarantor to perform certain actions. While making timely payments is the first action that comes to mind, being in compliance with all provisions of the documents is important. The "events of default" section of the loan documents sets forth what is considered a "default" under the loan. A default is the borrower's and/or guarantor's failure to satisfy any requirement of the loan documents. When an event of default occurs, certain rights of the lender are triggered, which can include the acceleration of the loan and/or foreclosure.

It is important to understand how all the events of default relate to the provisions of the loan documents. An attorney can advise a borrower and/or guarantor how to negotiate the events of default to reduce the risk of being in default. An example of this is the right to "cure" an event of default. The right to cure generally requires the lender to give notice to the borrower and/or guarantor that an event of default has occurred and provides the borrower and/or guarantor a period of time to correct or "cure" such default. The cure period, notice requirements and which events of default are curable are only a few examples of what can be negotiated.

The Guaranty is another loan document that contains provisions that can be negotiated to reduce the guarantor(s) exposure. Generally, lenders utilize a unconditional continuing guaranty. This means the guarantor guaranties the entire loan for the entire period the loan is outstanding. However, there are ways to limit the exposure of the guarantor.

The type of guaranty directly determines the rights of the lender and the guarantor. An example of this is a guaranty of "payment" versus a guaranty of "collection." Guaranty of "payment" means the lender can demand payment from the guarantor immediately upon a default by the borrower. The lender is not obligated to first try to collect from the borrower or to foreclose against any collateral. Alternatively, a "collection" guaranty is very different. The lender first must repossess and sell any collateral, sue the borrower for the deficiency, and have the judgment returned partially unsatisfied before the lender can collect from the guarantor.

There are other provisions within the guaranty that can limit the guarantor's exposure. For example, limits can be placed on the dollar amount of the guaranty and/or the guaranty may have a

“sunset” provision where the amount of the guaranty reduces as the outstanding balance of the loan is repaid. If there are multiple guarantors, then each guaranty can be “pro-rata.”

This article is limited by space and can not discuss all the various provisions of a loan transaction; however, the importance of determining that the appropriate provisions are contained in the loan documents can not be stressed enough. Therefore, you should thoroughly discuss your loan transaction and how the specific provisions apply with your attorney.

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