Spring 2020

FINANCIAL newsletter

Expertise
Common Sense
Integrity
Fairness
Hard Work

shared values. firm results.

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FAIR CREDIT REPORTING ACT COMPLIANCE

The Fair Credit Reporting Act ("FCRA") is a federal law enacted in 1970 to promote the accuracy, fairness, relevancy, and privacy of consumer information in the file of credit reporting agencies. Banks and other financial institutions are an important link in the consumer credit reporting chain, and in a variety of circumstances, they are subject to regulation under the FCRA. Failure to understand and comply with one's obligations under the FCRA can result in liability for statutory or actual damages, costly litigation, and potential attorney fee awards and sanctions. As with any regulation it is important to ensure compliance with the law and regulations to avoid violations and liability.

The FCRA prohibits financial institutions from furnishing information to consumer reporting agencies which the financial institution knows, or has reasonable cause to believe, is inaccurate.

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FAIR CREDIT REPORTING ACT COMPLIANCE

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Likewise, a financial institution shall not furnish information to a credit reporting agency where it has received notice that the specific information is inaccurate, and the information is, in fact, inaccurate. Whether this reporting is negligent or willful the financial institution will still be liable for damages, and if the customer is successful, attorney fees and costs. Depending on the nature of the misconduct, there may also be punitive damages.

On March 27, 2020, President Trump signed the Coronavirus Aid Relief and Economic Security Act ("CARES Act"). The CARES Act amends the FCRA to provide that when a lender makes an accommodation for one or more payments to a consumer borrower that is otherwise current on their loan the lender must continue to report the loan as current during the period of the accommodation. If the loan was delinquent prior to the accommodation, the loan may be reported as delinquent.

The information requested by or provided to credit reporting agencies can be complicated and involve both factual and legal information. Determining whether information is "inaccurate" under the FCRA may be a complex question. One potentially tricky area of reporting relates to the furnishing of information to consumer reporting agencies regarding debts which have been discharged in bankruptcy. If a financial institution's customer has received a bankruptcy discharge, they may be reviewing their credit reports and attempting to improve their credit rating. Information provided to the credit reporting agencies must accurately state the current status and payment information related to any debt discharged. Information which does not reflect the discharge, or which shows information which the consumer alleges is misleading or inaccurate in light of the discharge, could be claimed to be a violation of the FCRA.

Reporting secured debt post-discharge can present concerns for a financial institution. While the bankruptcy discharge releases a customer from personal liability, a mortgage lien or security interest may continue with respect to the secured asset. This creates tension both from a collection standpoint – a bank must be careful not to demand payment for a discharged debt – and from a reporting standpoint. All though case law varies somewhat depending on the jurisdiction and the factual background, courts have generally agreed that because the nature of a discharged mortgage is only as a lien enforceable against property, and not as a personal debt, reporting the secured debt as discharged with zero balance, with no payments made after the date of discharge is accurate, even if a consumer has made voluntary payments after discharge. This is because the consumer's credit report should only include information about debts owed by the consumer, which would no longer include the mortgage debt.

A financial institution may also be subject to regulation as a user of consumer credit reports. A consumer credit report may only be requested for certain, enumerated permissible reasons, and pulling a credit report without such a reason will also be a violation of the FCRA. A user must not only have an authorized use for the consumer report, but must also certify that authorized use prospectively, either generally or specifically. But a user's obligations do not stop there. If a user of a consumer credit report takes any adverse action based, in whole or in part, on any information contained within that consumer credit report, they must provide notice of the adverse action to the consumer. These notices must contain specific information regarding the adverse action, the report itself, and the consumer's right to obtain a report and dispute its accuracy.

As with many consumer protection statutes, violations can result in legal costs, liability, and attorney fee awards for the consumer's attorney. Even if the statute has not been violated, or if the potential damages which appear to result from the mistakenly reported information, a claim of violation may still result in significant expense for defense of the alleged claim. Therefore, to ensure all credit reporting is accurate and consistent in each particular instance, if there is any doubt as to what is being reported or a notice to be given, a complete and careful review should be undertaken. ■


Financial
Analysis
Credit Report
Profiling
Debts


FRANKLIN

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QUESTIONS AND ANSWERS: NAVIGATING THE LEGAL ISSUES YOU FACE FROM THE COVID-19 PANDEMIC

The COVID-19 pandemic has caused an unprecedented change to what "business as usual" looks like across America. The banking industry is certainly no exception, and many common questions have arisen regarding what the coming months will look like in the industry. On March 27, 2020, Gislason & Hunter held a free webinar to offer insight on some of these questions. This article summarizes the questions asked and answers given in that webinar (which can also be accessed through the firm's website at https://www.gislason.com/resources/).

Question 1: What is the current state of the judicial system?

Answer: As of the date this article is written, Minnesota courts are still open and accepting filings, but you should expect delays in getting motions heard and obtaining orders and judgments. The courts have prioritized cases on the bases of "Super High," "High," "Medium," and "Low." No civil cases have "Super High" priority status. "High" priority cases include matters involving public safety, temporary restraining orders, and statutory deadlines, such as avoidance of farmer-lender mediation. "Medium" priority status is assigned to court trials, and "Low" priority status is assigned to various other matters, including foreclosures. Bankruptcy courts are open and address different matters on a case-by-case basis.

Question 2: Are farmer-lender mediations still being held?

Answer: Yes, with mediation sessions being conducted by telephone. However, some have expressed additional concerns over the effectiveness of telephonic sessions where creditors and debtors are not all physically located in the same room.

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QUESTIONS AND ANSWERS: NAVIGATING THE LEGAL ISSUES YOU FACE FROM THE COVID-19 PANDEMIC

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Question 3: Are electronic signatures and electronic loan documents enforceable?

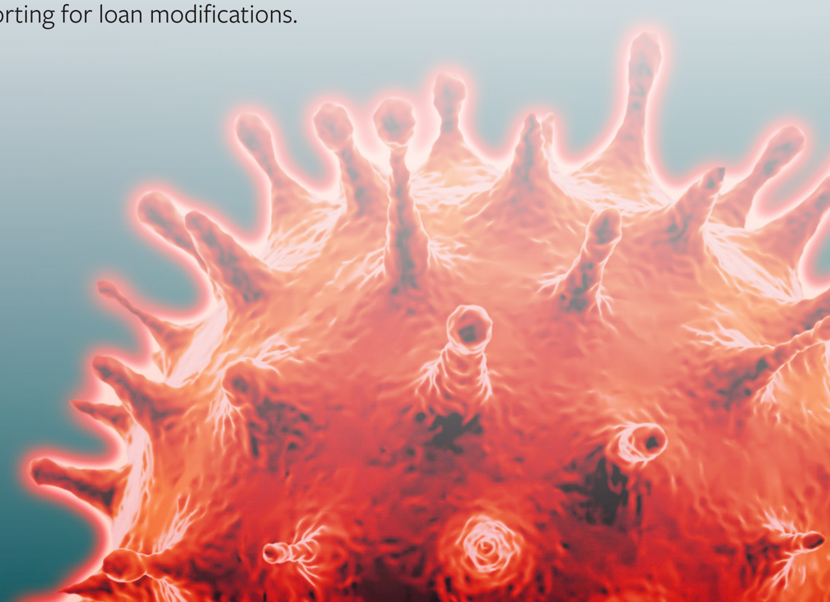
Answer: Generally, yes. Like most states, Minnesota has enacted the Uniform Electronic Transactions Act (the "UETA"), which provides that electronic copies of documents, and electronic signatures, are enforceable so long as certain basic requirements are met. There are some important exceptions, however, including real estate documents, promissory notes (if they are to be transferred), and documents that need to be notarized. Minnesota law does allow for remote, electronic notarizations, but in order for a notary public to conduct such notarizations, the notary public must have a special appointment to do so and adhere to specific requirements. Documents that are properly signed electronically and saved in an electronic medium will also generally be admissible in a court proceeding.

Question 4: How should financial institutions document loan modifications, deferrals of payments, etc.?

Answer: Documentation requirements for these situations have not changed. A loan modification or deferral should be documented with a new note or a modification/extension agreement, and such documentation should be signed by all borrowers and guarantors. A new note should refer to the prior note and state that it is a renewal, and not in repayment of, the old note. A modification/extension agreement should state the terms the parties are changing and should reiterate that all other original terms remain effective. Security agreements and mortgages should also be reviewed to determine if they are affected by an extension or modification and if they need to be modified as well.

Question 5: Have the FDIC, the OCC, or other agencies given any guidance or directives as to what banks can and cannot do in dealing with customers and loans to borrowers?

Answer: Yes. On March 19, 2020, the Federal Reserve, FDIC, and OCC issued a "Joint Statement on CRA Consideration for Activities in Response to COVID-19," which encourages fee waivers, payment deferral, and the like to affected individuals, small businesses, and small farms by indicating that such accommodations may be favorably considered for CRA credit. The FDIC has also released its "Frequently Asked Questions for Financial Institutions Affected by the Coronavirus Disease 2019 (Referred to as COVID-19)," which provides detailed guidance regarding working with borrowers affected by COVID-19, including guidance as to reporting and accounting. Finally, on March 22, 2020, the Federal Reserve, FDIC, NCUA, OCC, CFPB, and Conference of State Bank Supervisors issued an "Interagency Statement on Loan Modifications and Reporting for Financial Institutions Working with Customers Affected by the Coronavirus," which provides further broad and detailed guidance regarding accounting and reporting for loan modifications.



Question 6: How are existing SBA-guaranteed loans affected, has SBA said how financial institutions should handle SBA loans, and are there new SBA-related loan facilities available?

Answer: On March 10, 2020, the SBA issued an Information Notice to remind 7(a) Lenders, 504 program Certified Development Companies (CDCs), and Microloan Intermediaries of their unilateral authority to provide temporary relief in the form of deferred payments to existing borrowers under certain circumstances. Also, on March 20, 2020, Minnesota was designated as an Economic Injury Disaster Loan area, so such loans are available in Minnesota in connection with the COVID-19 pandemic. These loans can be up to $2 million at a 3.75% interest rate, can be used to pay fixed debts, payroll, accounts payable, and other bills, can have long-term repayment terms, and are applied for directly through the SBA.

Question 7: Can a financial institution stop advancing money on a line of credit?

Answer: It depends on what the governing loan documents provide with regard to conditions of advances and events of default. Some typical terms in loan documents allow a lender to refuse an advance in situations where the lender in good faith believes it is insecure, there is a material adverse change in the borrower's financial condition, the borrower ceases doing business, or the lender believes the prospect of payment or performance of the loan is impaired.

Question 8: Are there any moratoriums on collecting loans?

Answer: Governor Walz has issued various executive orders regarding evictions and collections in response to COVID-19. In Minnesota, there can be no evictions from residential premises, landlords cannot terminate residential leases (except where a tenant is seriously endangering the safety of others), and officers cannot execute writs of recovery of residential premises. There are no moratoriums on foreclosures, although financial institutions are "requested" (but not required) to implement a moratorium where a foreclosure results from a substantial decrease in income or increase in medical expenses caused by COVID-19. Financial institutions are also "strongly urged" (but not required) not to impose late fees or other penalties.

Question 9: What is the status of Minnesota's sheriff's offices with regard to foreclosure sales?

Answer: For the most part, sheriff's offices are conducting foreclosure sales, but sales may be delayed or difficult to schedule on a short-term basis. Regardless of sale logistics, statutory pre-sale service and publication requirements can still be completed to work towards a foreclosure sale. After completing those requirements, the foreclosing creditor can always postpone a scheduled sale if there are logistical issues with the sale as scheduled without having to replicate various pre-sale requirements.

New information on the COVID-19 pandemic continues to come out and evolve on a regular basis, and Gislason & Hunter continues to monitor and respond to changes in the legal landscape caused by the pandemic. If you have further questions on how current events affect your banking operations, please feel free to reach out to us, and stay tuned for follow-up webinars and publications addressing this evolving situation.

SAVE *the* DATE

Gislason Banking and Financial

WEBINAR

Tuesday, April 28 at 11:00 a.m.

The webinar will include the latest information on the banking and financial situation:

- **Update on COVID-19 impact on accessing the court system**
- **Executing loans remotely**

We want to hear from you.
What topics do you need more information on?

Send topics to:
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DIFFERENCES BETWEEN NOTE CO-MAKERS AND GUARANTORS

When a prospective borrower approaches a lender and requests financing for any consumer purpose or business operation, the lender must evaluate whether or not the borrower has sufficient capacity to repay the loan. Two options will often come to mind for most lenders. First, the lender may require more than one individual or entity to sign the same promissory note evidencing the loan. In this scenario, more than one borrower promises to repay the entire loan. Second, a non-borrower may be required to guarantee the repayment of the borrower's debt and/or pledge certain collateral to the lender, which can be collected by the lender if the borrower fails to re-pay the loan. This article will address some of the differences between these options.

The first option involves a situation where two or more people sign the same promissory note. This scenario is commonly referred to as two individuals "co-signing" the same note, but having multiple signers execute the same instrument may not always have the same legal effect. The scope of a "co-signer's" liability depends upon the specific language in the "co-signed" document. For example, one Minnesota case determined that two "co-signers" executing the same note resulted in only one "co-signer" being primarily liable for the debt evidenced by the underlying note. Therefore, the first option referenced above is more accurately described as having two "co-makers" of the same note.

"A person is a comaker if the contract personally binds that person, jointly and severally, with a principal." See Trebelhorn v. Agrawal, 905 N.W.2d 237, 242 (Minn. App. 2017) (citation omitted). In this situation, all individuals who sign the same note evidencing a debt are 100% liable for repaying the entire debt. Consequently, if one borrower finds himself in dire financial straits, the lender can simply look to the other borrower who signed the same note to repay all the debt. Electing this first option can be beneficial for a lender in many situations. For example, financing one borrower (i.e. one co-maker) may be an acceptable risk even though that borrower's credit history is questionable because a second borrower who signed the same note (i.e. another co-maker) is financially capable of repaying the loan. So long as at least one of the co-makers is financially capable of repaying the debt, requiring one or more co-makers on a note may seem like a no-brainer. However, sometimes it's not possible to get more than one person to sign the same note. For example, if a young farmer with few assets requests financing from a lender, that lender will likely want that young farmer's parents to also promise to repay the young farmer's loan. But it's possible that the young farmer's parents may be near retirement age and reluctant to put their retirement at risk if their son's or daughter's new farming venture fails. In such a situation, the second option described below may enable the lender to provide the financing without requiring more than one borrower on the note.

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The second option involves a situation where a non-borrower "guarantees" some or all of the borrower's debts. The person or entity that guarantees the borrower's debt is called a "guarantor." A guarantor "is one whose promise 'is collateral to a primary or principal obligation on the part of another and which binds the obligor to performance in the event of nonperformance by such other, the latter being bound to perform primarily.'" Trebelhorn, 905 N.W.2d at 243 (citations omitted). Put another way, a guarantor will generally only pay for a borrower's debt if the borrower defaults. In the above-referenced hypothetical, the retirement-age parents of a young farmer may refuse to put their entire retirement on the line for their son's or daughter's start-up farming operation. However, the parents may be open to guaranteeing repayment of some or all of the young farmer's debt if the young farmer is unable to pay the debt. In this situation, the "primary" person responsible for repayment of the debt is the young farmer borrower, and generally the lender may only collect the debt from the guarantors if the borrower is in default. Consequently, it's generally less burdensome – or at least less time-consuming – to collect a debt from a co-maker than it is to collect a debt from a guarantor.

In addition, there are different types of guarantees that can further limit a lender's ability to collect a debt from a guarantor. For example, a guaranty may be limited or unlimited. As the name implies, a limited guaranty limits the amount of debt that a guarantor will repay in the event that the borrower defaults (e.g. a $500,000.00 guaranty from a guarantor in connection with a $750,000.00 loan to a borrower). An unlimited guaranty guarantees a borrower's entire debt. Further, a guaranty may be secured or unsecured. For example, often times a guaranty is secured by a mortgage on a guarantor's real estate that is equal to or in excess of the value of the guaranty. If a guaranty is unsecured, then it is not tied to any specific collateral owned by the guarantor.

In sum, lenders will often require more than one co-maker on a note or a guaranty of repayment from a non-borrower in connection with providing a loan to one or more borrowers. Indeed, requiring multiple borrowers to serve as co-makers on the same note is often the preferred method of providing financing, but that is not possible when a person who could serve as a guarantor refuses to serve as a co-maker. Nonetheless, a lender may still want to enter into a lending relationship with a new but undercollateralized borrower upon the condition that a non-borrower provide a guaranty to the lender to provide additional reassurance of repayment. These situations provide opportunities for lenders, borrowers, and guarantors. Of course, whether parties should select one or the other (or a combination of both) of the above-referenced options is a judgment call dependent upon the parties to the transaction and other facts and circumstances that may make either option more appropriate in a given situation.

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Banking Services

Gislason & Hunter represents numerous financial institutions and has a thorough familiarity with financial economic conditions, as well as an ever-evolving regulatory environment. We have extensive experience in the following banking areas:

- Management & shareholder issues
- Transfer of bank assets
- Bank litigation
- Business planning
- Real estate
- Property foreclosures and repossessions
- Loan and workout agreements
- Collateralizing and securing all forms of loans
- Loan and credit agreements
- Subordination and participation agreements

This publication is not intended to be responsive to any individual situation or concerns as the contents of this newsletter is intended for general informational purposes only. Readers are urged not to act upon the information contained in this publication without first consulting competent legal advice regarding implications of a particular factual situation. Questions and additional information can be submitted to your Gislason & Hunter Attorney.

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