

Practice Pointer: When Should You Send Default and Demand Letters?

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In a prior practice pointer, we discussed the importance of reservation of rights letters. However, there are times when a lender will want to start enforcing one or more rights or remedies. In all or almost all jurisdictions in the United States, a lender is required to provide a written notice of default to the borrower and guarantors, and to make a written demand for payment, before exercising any rights or remedies. In many jurisdictions, however, a borrower or a guarantor can waive these requirements in the loan documents, and many loan documents contain such waivers.

This begs the question of whether to send a default and demand letter.

Before answering that question, we recommend a review of the loan documents to determine what notice, if any, is required. Although many loan documents will waive all such notices, there are times when the loan documents require notice of default with an opportunity to cure. Reviewing the loan documents will disclose the minimum that needs to be done before exercising rights or remedies.

Even when the loan documents waive notice and the jurisdiction does not require it, we often recommend sending notice—not as a necessity, but rather as communication tool. Indeed, if the goal is to address and resolve an issue, or if it appears that the borrower should refinance, sending a notice letter will often get the conversation started. In those situations, you should consider adding a reservation of rights in the default and demand letter.

There are times, however, when a hard exit is needed, or remedies need to be enforced immediately. In those situations, we still typically recommend sending written notice before exercising remedies. Hard exits have an increased risk of litigation. Typically, courts will enforce loan documents as written, and will enforce remedies; but judges are people. More often than not, a judge prefers to see that a lender has given notice before seeking judicial relief. Indeed, some remedies, such as the appointment of a receiver, come with an element of judicial discretion. In those situations, it is even more important for the lender to appear as reasonable as possible.

Ultimately, whether and when to send a default and demand letter depends on the loan documents and the circumstances presented.

This e-alert is the third in a series of practice pointers relating to lending related issues, with a particular focus on distressed credits. If you have questions, or would like further information, please do not hesitate to call one of the authors or your favorite Miller Canfield attorney.