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How to Prepare for a Real Estate Enforcement in Europe, Part 4 – Challenges

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In this mini-series on European real estate enforcements and restructurings, we have covered how to prepare for an enforcement in Part 1, emphasised the importance of valuation evidence in Part 2 and highlighted key enforcement implementation considerations in Part 3. In this final installment, we will cover how lenders can best position themselves to face challenges from stakeholders looking to stop an enforcement process.

Challenges by Stakeholders

It is impossible to predict with exact certainty the types of challenges that stakeholders may launch against a creditor leading an enforcement process. That said, lenders may be faced with the following:

1. Uncooperative Directors

Firstly, directors or shareholders of the debtor company may actively resist the enforcement. A common strategy used by opposing stakeholders is to directly attack the conduct of the lenders through an onslaught of correspondence. This strategy could be enough to "muddy the waters" and complicate a lenders' enforcement strategy, or cause the lenders to become nervous and reluctant to undertake their planned enforcement action.

2. Applications to Court

There is a risk (however remote) that a stakeholder could apply to Court on an urgent, expedited basis seeking to stop the enforcement. For example, the company may seek an injunction to stop a lender exercising its power of sale in relation to the secured property or a declaration that the lender's actions are not permitted (such as raising technical challenges on the enforcement documentation).

Theoretically, there is a risk that disgruntled stakeholders (such as directors, shareholders or junior creditors) could even apply to Court without first giving notice to the senior lenders of their application. In this situation, the applicants would need to establish that there was an exceptional urgency, and an imminent risk that the real estate asset would be materially impacted by the enforcement strategy proposed by the lenders. It is, however, an onerous task to show urgency, and the directors would need to successfully justify why they did not inform the lenders of their Court application. For these reasons, the risk of challenging directors taking this unilateral action without notification to the lenders is remote.

Risk Mitigation and Defensive Steps for Lenders

So, in a situation where a lender is faced with a board of directors who are being difficult and opposing their proposed enforcement plan, what defensive steps can a lender take?

- Firstly, as emphasised throughout this mini-series – *and particularly in **Part 2*** – valuation evidence is **critical**. Robust valuation evidence should always be obtained. In enforcement situations where there is a risk of challenge, this becomes even more important. Robust valuation evidence can be an effective "shield" against litigation risk.
- As part of good practice lenders should ensure accurate files are kept. In particular, detailed, contemporaneous file notes of discussions with the borrower can be an important record for lenders when defending their actions.
- Next, a robust letter to the board reminding the directors of their legal duties can be a sensible step. The letter should stress the duties of a director of a financially distressed company, and, in particular, the duty of directors to consider the interests of creditors. If the lenders are concerned that the opposing directors may make an application to the Court, this letter may also act as an opportunity to put the company on notice that if any such application were to be made, the directors will be liable for any adverse costs incurred by the lenders in defending the action.
- A more fulsome option for the lenders when dealing with difficult management would be to exercise their voting rights under the security documents. Typically, an English law share pledge will provide that following an event of default a lender can exercise the member's voting rights in the company which would allow the lenders to change the board. Lenders could seek to replace the directors and appoint their own preferred (suitably qualified) company directors in order to manage the company with the interests of creditors in mind. It is worth considering the fact that the replacement directors must be willing to immediately accept the appointment, which may come with a degree of challenge, particularly if the company operates in a highly specialised or regulated area of business.
- Alternatively, the lenders could seek to appoint administrators over the holding company. The administrator would then be granted the power to change the board (removing the opposing directors). However, any move to appoint administrators should be carefully considered and taken in line with legal and financial advice.

Enforcement Checklist

In summary of our four-part mini-series, the below checklist sets out the key considerations for lenders actioning a real estate enforcement.

1. Structure	What is the structure of the company? It is critical to get the structure right when the deal is negotiated, as this can aid enforcement later down the line. Understanding weaknesses in structure and security provisions is essential.
2. Events of Default	What Event of Default has occurred? It will always be preferable to enforce on the basis of a clear, objective Event of Default.
3. Waivers and Amendments	Use these requests as an opportunity to tighten permissions, obtain more information, and to engage advisers to aid in the enforcement preparation stages. Preparation is key!
4. Security	Have you engaged lawyers to conduct a security review? Knowing how security can be enforced and how long an enforcement might take is crucial. Enforcement procedures may differ considerably across Europe, particularly as not all jurisdictions on the Continent are as "creditor-friendly" as the UK (and local law advice should always be obtained).
5. Valuation	Expert valuation evidence is key! Have you engaged an independent expert with experience in valuing the specific type of target real estate asset? This will be important for secured creditors to assess if the sale proceeds can repay their debt.
6. Stakeholders	Are you the only creditor? If more than one creditor is involved, it is essential to quickly understand their strategy and start working on an agreement as to how the enforcement should be implemented. Do you need management support to execute the real estate enforcement? Think about the practical aspects of the implementation and whether there is a chance that the company directors could oppose the proposed strategy.

7. Selling the Asset	How will the real estate asset actually be sold? This is a secured creditors' key remedy. It is crucial to understand what the enforcement strategy will look like, how much it will cost, timings, any additional regulatory or statutory hurdles, and whether or not management input will be needed.