

LITIGATION PLANS AND LEGAL FEE REIMBURSEMENT REQUESTS



**WHAT THEY ARE AND WHY
THEY ARE IMPORTANT FOR
SBA LENDERS**

What they are.



- Two separate and distinct submissions Lenders must make to SBA when pursuing litigation against an Obligor of an SBA loan.
 1. Litigation Plan
 - Lender's litigation strategy, estimate of recovery, and proposed legal budget.
 - Reviewed by SBA *before* an active litigation commences.
 2. Fee Reimbursement Request
 - Lender's legal expenses that are eligible for SBA reimbursement.
 - Reviewed by SBA *after* litigation concludes.
- Submissions are made to the SBA loan centers and reviewed by District Counsels.

Timing of Litigation.



- Litigation takes place after borrower defaults on payments of a Note and loan is placed “in liquidation.”
 - A lawsuit affecting repayment of the loan is brought by Lender against Obligor. Some legal issues which commonly arise include:
 - Foreclosure action.
 - Bankruptcy.
 - The business will most likely shut down.
 - Collateral may be in danger of disappearing/losing value/stolen.
- Routine Litigation is part of the liquidation process.

Considerations for Litigation on SBA Loans.



- Litigation should be *necessary, reasonable and customary* for the locale.
- Litigation should be *cost effective*.
 - Potential recovery amount, or lack thereof, is important to know ahead of time.
 - Lenders *must* conduct due diligence prior to embarking on litigation!
- Treasury referral
 - May be better option if litigation does not appear to be cost effective.
 - Treasury can implement enforced collection on delinquent loans through offset, wage garnishment or DOJ litigation.

Selecting Outside Counsel.



- An attorney retained by Lender must:
 - Be licensed in the state where the litigation will be conducted.
 - Have expertise in debt collection and bankruptcy law, as well as any other specialization the case calls for.
 - Be covered by adequate legal malpractice insurance.
 - Have no conflicts of interest with *any* parties to the loan.

1. LITIGATION PLANS.



Required when litigation is *non-routine*, as defined in the CFR.

- Must amend/update plan as necessary.
- Plan must to be sent to SBA loan center prior to commencing litigation.
- Exceptions to litigation plan requirements acceptable in “emergency” situations.

RULES & REGS: THE SOP.



SOP 50 57 Chapter 21 Section C:

Except with regard to emergencies, all Lenders, including PLP Lenders **must** submit a Litigation Plan for SBA's written approval prior to initiating Non-routine Litigation. (13 CFR 120.540(c)). Lenders are not required to submit a Litigation Plan to SBA prior to initiating Routine Litigation.

BUT

all Lenders **must** submit a Litigation Plan if a material change arises during the course of Routine Litigation that transforms it into Non-routine Litigation, e.g. the legal fees exceed \$10,000 in the aggregate. (13 CFR 120.540(c))

RULES & REGS: THE CFR.



13 CFR 120.540

(c) *Litigation plan.* An Authorized CDC Liquidator and a Lender must obtain SBA's prior approval of a litigation plan before proceeding with any Non-Routine Litigation, as defined in paragraph (c)(1) of this section. SBA's prior approval is not required for Routine Litigation, as defined in paragraph (c)(2) of this section.

What is a “Routine Litigation”?



13 CFR 120.540 (c)

(2) Routine Litigation means uncontested litigation, such as non-adversarial matters in bankruptcy and undisputed foreclosure actions, having estimated legal fees not exceeding \$10,000.

What is “Non Routine Litigation”?



13 CFR 120.540 (c)

(1) Non-Routine Litigation includes:

(i) All litigation where factual or legal issues are in dispute and require resolution through adjudication;

(ii) *Any litigation where legal fees are estimated to exceed \$10,000;*

(iii) Any litigation involving a loan where a Lender or Authorized CDC Liquidator has an actual or potential conflict of interest with SBA; and

(iv) Any litigation involving a 7(a) or 504 loan where the Lender or CDC has made a separate loan to the same borrower which is not a 7(a) or 504 loan.

How to Submit a Litigation Plan.



- A request for approval of a proposed Litigation Plan (or amended Litigation Plan) must be submitted to the appropriate SBA Loan Center.
- A Litigation Plan must be amended if the proposed budget increases by 15%.
- Litigation Plans are submitted by using the 7 Tab System a template can be found at:

https://www.sba.gov/sites/default/files/forms/Litigation_Plan_Tabs_.pdf

Elements for Obtaining Approval.



Key Elements in getting your Litigation Plan approved:

- *Cost-effectiveness*
- *Necessity*
- *Reasonableness*
- *Customary*

2. Fee Reimbursement Requests.



- Legal fees and costs that Lender seeks to recoup from SBA as a Recoverable Expense.
- Requests are submitted to the appropriate SBA Loan Center pursuant to requirements contained in Chapter 22 (*Expense and Recoveries*) of SOP 50 57.

Types of Fees.



- Attorney fees and litigation costs are covered by SBA.
 - E.g., attorney bills, court costs, transcription fees, filing fees, etc.

- Fees and costs *not* reimbursable include:
 - Administrative overhead.
 - Intra-law firm communications; communications with SBA.
 - Loan servicing or liquidation tasks.
 - Legal action taken with respect to claims brought against SBA.
 - Rectifying errors that would justify a partial Denial of Liability, Repair or full Denial.
 - Defense of a claim brought against Lender by an Obligor for wrongful conduct.
 - Non-routine services pertaining to litigation that were not pre-authorized by SBA.
 - Services pertaining to litigation that are not reasonable, customary, or cost effective.

Fees Presumed Unreasonable.



- Un-justified travel expenses, including those not pre-approved by SBA.
- Multiple law firm billings for the same task.
- Attorney fees and costs that exceed recovery when no litigation plan was submitted.
- Appointment of a receiver to perform routine liquidation activities.
- Non-itemized bills.

Litigation Plan Case Study #1



- Obligor and collateral in foreclosure action located in New Jersey.
 - Lender retains a law firm in Texas.
 - Out of state law firm advertises itself as having “nationwide expertise” in litigating SBA loan-related litigation.
 - The firm’s business model is to spearhead the litigation while using local counsel to make court appearances on their behalf. They intend to pass along the cost of local counsel to SBA.
- Treated by SBA as “routine” litigation with \$10,000 cap; SBA will not cover extra cost of using local counsel.

Litigation Plan Case Study #2



Litigation Plan with projected \$85,000 in fees and expenses:

- Plan was to bring an adversary proceeding against a guarantor in a Chapter 7 bankruptcy.
- No substantial assets were listed in the bankruptcy.
- Collateral (BPP) was “missing” or “disappeared”.
- Additional collateral (RRE) was abandoned (we had 3d position).
- Lender had already incurred \$50,000 in fees without prior approval.
- No viable plan for recovery (likely \$0).

→ Plan denied because it was not cost effective to pursue.

Fee Reimbursement Case Study #1



Lender submits fee reimbursement request for approx. \$28,000.

- The Lender provided a summary of the work completed.
- The Lender initiated a foreclosure action and defended against a guarantor in bankruptcy.
- The Lender recovered approx. \$220,000 from the sale of the collateral and obtained a judgment for approx. \$132,000 against the guarantor.
- The Lender retained an expert witness without prior approval concerning a Phase I Environmental Assessment and ordered an appraisal of the property after the sale.

→The SBA approved approx. \$24,000 in fees disallowing the fees and expenses related to the Phase I because that should have been addressed prior to litigation and the appraisal because it was after the sale.

Fee Reimbursement Case Study #2



Lender submits fee reimbursement request for \$85,000 in a foreclosure action.

- No litigation plan was filed.
- Recovery is \$0.
- No explanation as to why the legal fees are so high in an otherwise routine matter; only voluminous pages of invoices from outside counsel submitted for SBA review.

→ SBA approves \$0 reimbursement. Lender did not obtain SBA's approval to incur higher than normal legal fees. Lender also did not perform their due diligence to find out ahead of time that the collateral had been non-recoverable. Invoices indicate that legal fees were inflated by meaningless administrative tasks performed by outside counsel.

Questions



SBA Legal Counsel for New York, New Jersey and Connecticut

- Diana St. Louis: diana.stlouis@sba.gov
(212) 264-7770
- Suzanne Ulicny: suzanne.ulicny@sba.gov
(212) 264-1482