



## Credit Agreements Act: One of Banks' Best Statutory Friends

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Because such lawsuits have almost entirely faded into history for the past thirty years, some younger bankers (i.e., much younger than CBAI's General Counsel) might not be familiar with the "lender liability" lawsuit era of the 1980s, and even some "more mature" bankers might not recall the perils of that time and the rescue in Illinois named the "Credit Agreements Act" ("the Act").

The Act does not apply to consumer credit.

Lender liability lawsuits were the product of the creative minds of attorneys who represented corporations and/or corporate officers that/who were in financial jeopardy due to massive business losses to the extent that they defaulted on their commercial loans. Instead of their clients being on the ropes, with a lender liability lawsuit the defaulting borrower could turn the tables and sue their lender .....actually, it was often raised as a counterclaim in defense of a collection lawsuit brought by the lender.....arguing that the losses were sustained because the lender breached a promise or failed to fulfill a commitment.

A typical scenario was a businessman ("Proprietor") who obtained a \$200,000 line of credit from The Bank of Verbal Commitments ("Bank") for the purpose of buying inventory, office space rental and other business necessities. At the time Bank extended the initial line of credit, Since-Fired Loan Officer met with Proprietor and verbally advised him (yes, Proprietor could be a "her" but that would make subsequent pronouns in my story more complicated) that when he maxed out on the initial \$200,000, Bank would have no problem granting him an additional \$200,000. However, at the time that the first \$200,000 was fully disbursed, Bank decided that Proprietor was no longer a good credit risk and did not advance him another \$200,000. In reliance on Since-Fired Loan Officer's promise, Proprietor had executed contracts with suppliers and contractors for the purchase of additional inventory and for physical office improvements. When the additional \$200,000 did not come through, Proprietor defaulted on contracts and rent obligations and ultimately went out of business. After suffering those losses, his new, unhappy circumstances resulted in his wife leaving him, his children telling friends that he was not their biological father, his dog no longer fetching his slippers and his cat refusing to be lazy.

Buford Plaintiff's Attorney comes along and convinces Proprietor that the ruin which had become his life was not his fault but was the bank's fault for renegeing on a promised extension of credit. Buford agrees to represent Proprietor on a contingency fee basis. When Bank sues to collect any unpaid loan balance or to enforce any security agreement that it might have, Proprietor responds with a counterclaim seeking damages for loss of his business, reputational ruin, alienation of affection (separation from family), and emotional suffering. A jury, sympathetic to Proprietor (who showed up in court each day in tattered clothes and without shoes) and seeing Bank as "deep pockets," awards Proprietor \$15 million (Buford gets his one-third).

After one or two of those cases turned out well for the debtor, attorneys started coming out of the woodwork seeking clients who had similar sad stories to tell about a bank breaching a promise and driving them to the poorhouse. In some of the most high-stakes cases involving large businesses and large banks, it was not unusual for jury awards to reach \$100 million. Successful lender liability lawsuits caused some banks, even if confident that they had done nothing wrong, to settle cases rather than gamble on a multimillion dollar jury judgment.

In 1990, Illinois enacted the Act, Section 2 of which prohibits a debtor from asserting any claim "in any way related to" a credit agreement unless the bank's commitment was reduced to writing and signed by both the debtor and creditor. With the adoption of the Act, the tide immediately turned against lender liability lawsuits in Illinois and a long string of Appellate Court opinions generously interpreted the Act's protections on behalf of creditors. In fact, in one case the judge who authored the Court's opinion went out of her way to suggest that the law was one-sided and could result in unfair outcomes for debtors, but the law had to be interpreted as meaning what it said. Furthermore, some of those cases made it clear that the defense provided by the Act was not limited to arguments made by principal borrowers, but also extended to alleged verbal commitments to guarantors that their guarantees would not be fully enforced in certain circumstances. Those courts ruled that a guaranty is among the items "in any way" related to the credit agreement.

An additional protection is found in Section 3.1 of the Act, which states that a creditor has no liability to a third party that is not in privity of contract with the creditor if the alleged liability relates back to a credit agreement. Effectively, this means that, in my lengthy example above, when Creditor defaulted on his obligations to suppliers and service providers, those parties could not sue Bank under a "causation theory" asserting that they did not get paid because Bank breached its promise to Proprietor.

Because my only "clients" are CBAI and CBSC, I am restricted with regard to providing legal **advice** to outside parties (including CBAI Members); legal advice and representation must come from the bank's own attorney. However, I do not interpret my limitation as a bar against me dispensing common sense, and so.....unless your attorney advises to the contrary.....if a commercial loan agreement does not have a choice-of-law clause stating that the loan and all of its terms shall be governed by the law of the state of Illinois, a very valuable tool may have been left on the shelf.

Feel free to contact [Jerry Cavanaugh](#) or CBAI Paralegal [Levette Shade](#) if you want any additional information.

*Legal Link is a free CBAI member benefit. For answers to your general, banking-related legal questions, contact CBAI General Counsel [Jerry Cavanaugh](#) at 800/736-2224 (IL only), 217/529-2265].*