



Ensuring lien perfection today and in the future



Overview



Protecting and perfecting interests in assets is essential to a sound lending strategy. Only through lien perfection — the process of ensuring that a lien is properly recorded, maintained and legally enforceable — can a bank safeguard its claim on the secure asset. Yet even under the best market conditions, lien perfection represents a complicated, labor-intensive process that, if not properly executed, puts lenders at risk to lose priority status over assets.

Today's highly volatile market conditions make maintaining lien perfection even more critical. The Federal Reserve's series of interest rate hikes — coupled with rising inflation, declining asset values and other financial industry disruptors — has left lenders increasingly vulnerable. Regardless of a bank's size or the breadth of its portfolio, failing to maintain lien perfection can result in grave consequences.

This paper will examine some of the most serious threats to lien perfection; the tools and best practices that banks can implement to protect their status; and the advantages that lenders can achieve with the optimal solutions in place.

How the current financial landscape heightens lien perfection risks



The process of attaining initial lien perfection is not enough to be successful and profitable in today's lending industry; banks must maintain this protection over time, amid both static and emerging threats. It's important to recognize that the challenges of lien perfection exist even in the most favorable market conditions; even modifying a loan can cause a loss of priority. Ensuring that liens are perfected is critical to overall portfolio health, as well as to reduce risk and promote recovery efforts in default situations. In the absence of perfected liens, a lender can lose its priority position to other creditors. And in the event of default, banks could be forced to share the proceeds from collateral sales with these other parties — or even lose their claim entirely. Although lien perfection has always been a complex and intricate task, the tumultuous conditions across today's financial landscape have made the undertaking even more critical. From elevated interest rates to the anticipated surge of non-performing loans (NPLs) and the threat of a looming global recession, today's banks face an environment steeped in uncertainty.

As these financial difficulties take a toll on the bottom lines of many borrowers, it can lead to an increase in loan defaults — making portfolios vulnerable to higher default rates and increased credit losses. Consequently, if liens are not perfected, banks may be exposed to higher credit risk while the borrower's incentive to repay the loan can be diminished. Additionally, in the absence of lien perfection, banks are likely to face difficulties foreclosing on or repossessing collateral in default situations, resulting in delays and increased costs.

The ongoing requirements of Uniform Commercial Code (UCC) filings represent another significant threat to lien perfection, regardless of the lending environment. Not only must banks spend considerable effort conducting due diligence on borrowers at the onset of a loan and completing UCC filings to establish their position over other creditors, they must also maintain that protection throughout the lifecycle of the loan. All of the effort that goes into an initial UCC filing can be eradicated if the filings are not continuously tracked and updated — and the greater the number of liens, the more opportunity for errors that could compromise priority. While it is essential to stay apprised of the numerous changes that can impact position on the perfected status of a lien, doing so is both complex and labor-intensive.

Undeniably, the perilous nature of the current lending environment has significantly heightened the risk for banks.

Harnessing the tools to conquer lien perfection challenges



Lien perfection is a cumbersome and time-consuming process — one that, if not executed correctly, puts banks at risk of losing their priority over assets. To mitigate the bevy of challenges, banks require established processes and reliable systems that will ensure lien perfection through all stages of the loan cycle. A sound lien perfection strategy begins with achieving real-time visibility across the entire portfolio; gaining reliable data on which to act; and the ability to promptly remediate issues when they arise. These advantages can be realized by lenders who implement monitoring, reporting and automation solutions that help them effectively manage the lien perfection process.



Monitoring

When it comes to maintaining lien perfection, what you don't know can most certainly hurt you. The best way to be certain about preserving ongoing lien perfection is through proactive monitoring. A robust monitoring solution helps eliminate surprises by constantly checking the status of details such as debtor name and status changes, and alerting banks to events that could compromise their position and ability to collect. With visibility into these changes, banks can quickly take action to protect their investments.

Ongoing monitoring of portfolios also helps lenders to catch errors that could compromise lien perfection. As banks grow, so does their UCC filing volume, which can spark considerable challenges around staffing constraints, inefficiencies and errors related to manual processes. This, in turn, can result in a loss of position due to missed UCC continuations, filing rejections and fragmented workflows. In order to claim first position of ownership of an asset, banks must have the tools and resources to effectively search, file and manage liens.



Analytics and reporting

Analytics and reporting capabilities supply lenders with the vital information required to achieve deep visibility across their portfolios and clarity on actions that should be taken. By helping banks identify potential issues and respond proactively, these tools provide a broad but detailed snapshot that helps lenders stay on top of important details and deadlines, which is critical to successful portfolio management. Considering that many lenders have thousands of outstanding loans, it can be extremely challenging to keep track of them all. Yet by learning sooner about changes that affect their debtors — such as name and status changes — banks can act quickly to safeguard their investments.

Banks can glean detailed data on estimated lien positions and insights into lien activity against debtors, as well as knowledge about the costs, efficiency and quality of a bank's lien operation. By applying analytics to portfolio data, lenders gain a more accurate way to identify impending risks and emerging trends, while maintaining awareness of their total risk profile.



Automated processes

Relying on manual processes for lien perfection opens the door to risks. Yet by automating tasks, banks are often able to reduce errors and strain on resources while helping to ensure that liens are automatically continued. Regardless of a bank's volume of continuations, even a single lapsed filing can significantly and negatively impact a lender. By enabling banks to take a more timely, accurate and efficient approach to lien management activities, automation can be an instrumental tool in preserving lien perfection.

There are many problems with manual processes; most notably, their susceptibility to omissions and mistakes, both of which can impact lien status. Manual procedures are also slow, labor-intensive and expensive. Additionally, they are especially vulnerable to changes in personnel, which can subsequently result in gaps in oversight and cause pending UCC expirations to get lost in the shuffle.

With the right tools, lenders can automate these tasks and better manage workflows. For example, rather than filing UCC-3 continuation statements one at a time and continuously rekey lien information, the process can occur largely automatically with staff focusing just on issues that require their review. An automated continuation process reduces the likelihood that a UCC filing will lapse unexpectedly, since these systems can be set to automatically monitor dates, prepare forms and file continuation statements based on predetermined criteria — dramatically reducing the time required by banking staff to manage continuations.

Deploy the optimal solutions for lower risk, greater rewards



Maintaining lien perfection isn't easy — especially in today's risk-intensive financial environment. But with the right solutions, banks can gain visibility into their portfolios, improve their decision-making capabilities based on up-to-date data and analytics, and bolster efficiency and productivity. Monitoring, analytics and automation solutions give lenders greater confidence in the health of their portfolio, helping them to:



Improve accuracy in recording and maintaining liens

By deploying a holistic, real-time and proactive monitoring solution, banks are not only helped in attaining perfection of their interests but also helped in maintaining protections over time. Monitoring helps solve one of the bigger challenges that lenders face: knowing what actions to take and when to implement them.



Maximize efficiency

Banks can save time, costs, and resources by using automated solutions that enhance accuracy, speed and service to help manage risk and simplify complexity across their entire portfolio.



Reduce risk of errors

By replacing manual processes that often lead to errors, oversights and the need to repeat steps, automation tools help banks to lower risk due to missed filings; maintain position over other creditors; reduce the need for staff intervention; provide reassurance that key dates and required actions won't be inadvertently missed; and increase productivity.



Streamline processes

Monitoring, reporting and automation solutions ease the process of lien perfection for lenders by helping them to simplify UCC filings; protect their ability to collect; overcome resource restraints; and better manage data.



Improve compliance with regulatory requirements

The right solutions help lenders meet compliance and legal requirements, ensuring their security interests are protected and enforceable.

Conclusion

As new risks continue to escalate across the lending landscape, the challenges to lien perfection magnify, as well — making it vital for banks to constantly assess the state of their portfolios. It is difficult to overemphasize the importance of maintaining visibility when protecting and perfecting liens. Banks that wish to be proactive about gaining and maintaining perfection are best served by robust monitoring, reporting and automation tools to help optimally manage their portfolios and act on issues. Through using these types of ongoing lien perfection measures, banks can help safeguard their claim on the secure assets.



See where you stand

Wolters Kluwer provides a free, online self-assessment that can uncover lien perfection vulnerabilities and opportunities to improve decision making. These are high-impact questions that every lending and/or compliance leader should ask themselves to stay competitive.

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Wolters Kluwer reported 2022 annual revenues of €5.5 billion. The group serves customers in over 180 countries, maintains operations in over 40 countries, and employs approximately 20,000 people worldwide. The company is headquartered in Alphen aan den Rijn, the Netherlands.

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