

Secured Transactions Midterm Review

The Big Picture

Part One: The Creditor-Debtor Relationship

Chapter 1-2: Creditors' remedies

Chapter 3: Creation and scope of security interests

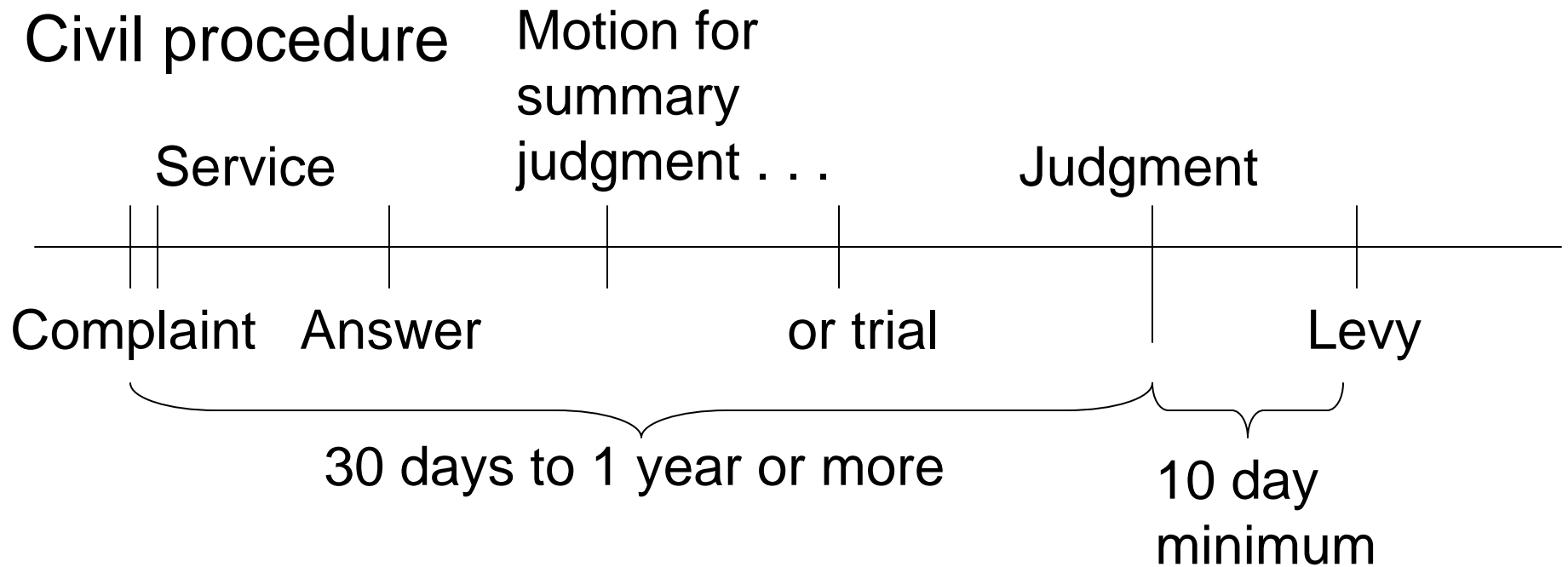
Chapter 4: Default Acceleration and Cure

Chapter 5: The Prototypical Secured Transaction

Secured Transactions Assignment 1

Remedies of Unsecured Creditors
under State Law

Limitations on Remedies of Unsecured Creditors



Discovery: before jmt, only on issues of liability and damages

Money Judgment: piece of paper, does not compel payment

Execution by Levy: process, subject to state exemptions

Self help: Unavailable, exposes creditor to conversion claim

Secured Transactions Assignment 3

Repossession of Collateral

Basic concepts

Title and possession are independent

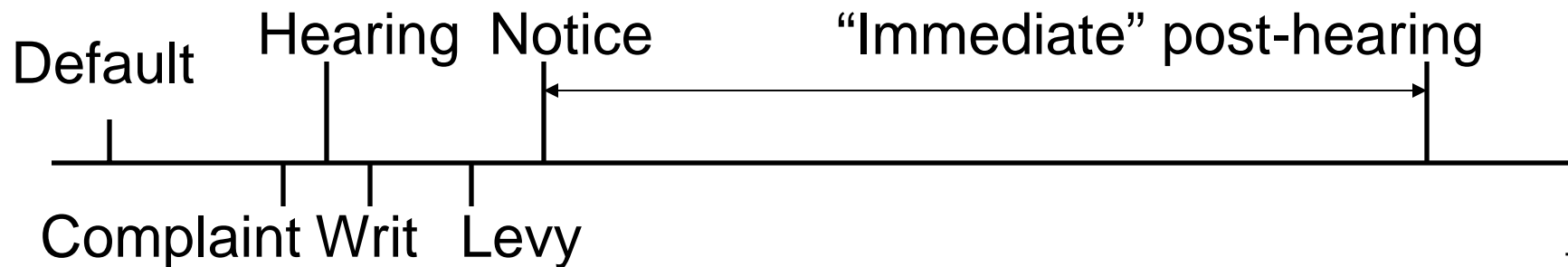
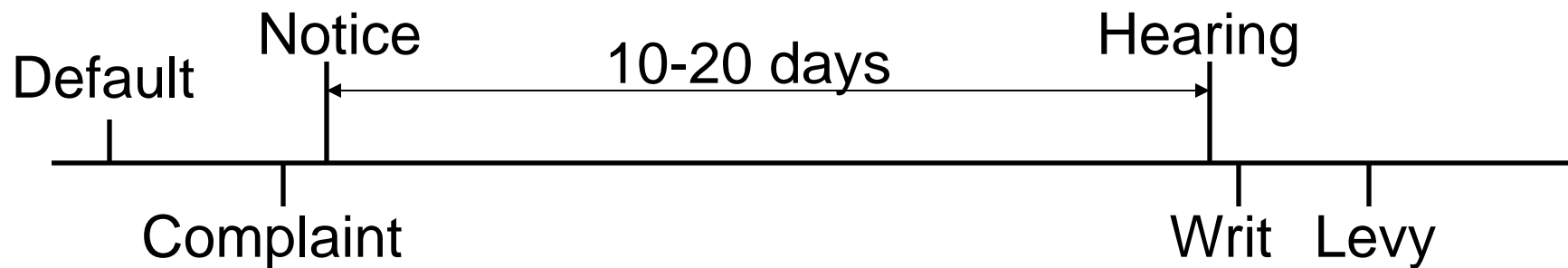
There can be foreclosure without repossession

There can be possession without foreclosure (Stedman case, p. 29)

Basic concepts

Replevin: A cause of action (writ) for possession

1. Secured party has right to possession UCC § 9-609
2. Writ of temporary possession, enforced by sheriff
3. Quick remedy: Two procedures both Constitutional:



Basic concepts

Self help repossession (alternative to replevin)

1. Not by mortgagors (except rents)
2. Not by lessors
3. Yes by Article 9 secured parties

Basic concepts

Breach of the peace (limits self help, not sheriff levy)

1. Criminal standard: Public disturbance
2. Article 9 standard: “Tending to provoke others to break the peace,” *Callaway v. Whittenton*

Secured Transactions Assignment 4

Judicial Sale and Deficiency

Judicial Sales

- Procedure:
1. Sell collateral to highest bidder
 2. Apply proceeds to the debt
 3. Return surplus to the debtor
 4. Creditor can move for “deficiency”

- Reasoning
1. Property sells for “market (true) value”
 2. Secured party receives full value of collateral (up to debt) and, with deficiency, full amount of debt
 3. Debtor pays no more than it owes (no “forfeiture”)

Judicial sale procedure problems

Inadequate price (*Armstrong v. Csurilla*)

Legal notice advertising

Buyers unable to inspect (Holy Toledo!)

Caveat emptor as to title and condition
(*Marino v. United Bank of Illinois, N.A.*)

Hostile situations

Statutory right to redeem

Credit Bidding

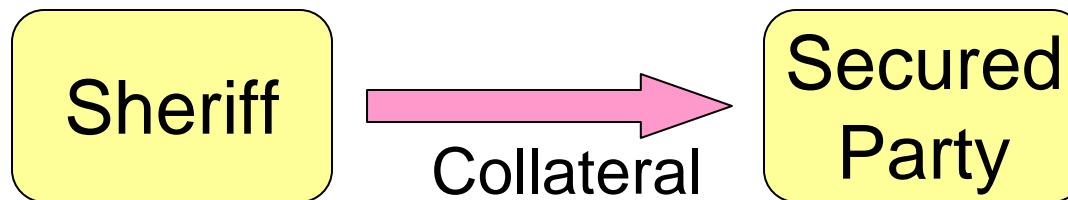
If the secured party is the Buyer,
the money would go in a circle.
So the law excuses both payments



Secured Party bids "\$100K" (amount of debt)

Credit Bidding

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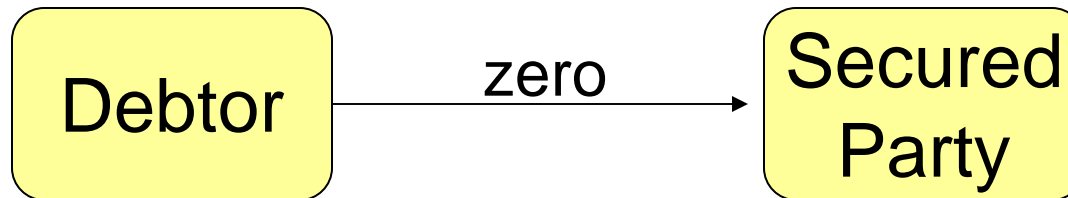


Secured Party bids "\$100K" (amount of debt)

Sheriff transfers collateral

Credit Bidding

If the secured party is the Buyer,
the money would go in a circle.
So the law excuses both payments



Secured Party bids "\$100K" (amount of debt)

Sheriff transfers collateral

Debt is reduced by amount of the bid

Antideficiency Statutes

- Three basic types:
 - No deficiency judgment allowed
 - Deficiency judgment allowed in court's discretion
 - Limit amount of deficiency judgment
- Most common: credits debtor for fair market value of property
- Generally, no corollary in Art. 9

Secured Transactions Assignment 5

Article 9 Sale and Deficiency

Using Article 9

1. Definitions §9-100
2. Attachment §9-200
3. Perfection and Priority §9-300
4. Rights of Third Parties §9-400
5. Filing §9-500
6. Default §9-600
7. Transition §9-700

Sale procedures compared

	Judicial sale	Article 9 sale
Purpose	Protect the debtor from forfeiture; fix creditor's deficiency	Protect the debtor from forfeiture; fix creditor's deficiency
By whom?	Sheriff, clerk	Secured party
Legal standard?	Fixed procedural requirements	Commercially reasonable
When final?	On confirmation	Upon sale
Judgment for full deficiency?	Varied rules	If procedure OK, and secured is not buyer
Effect	Double sale	Single sale

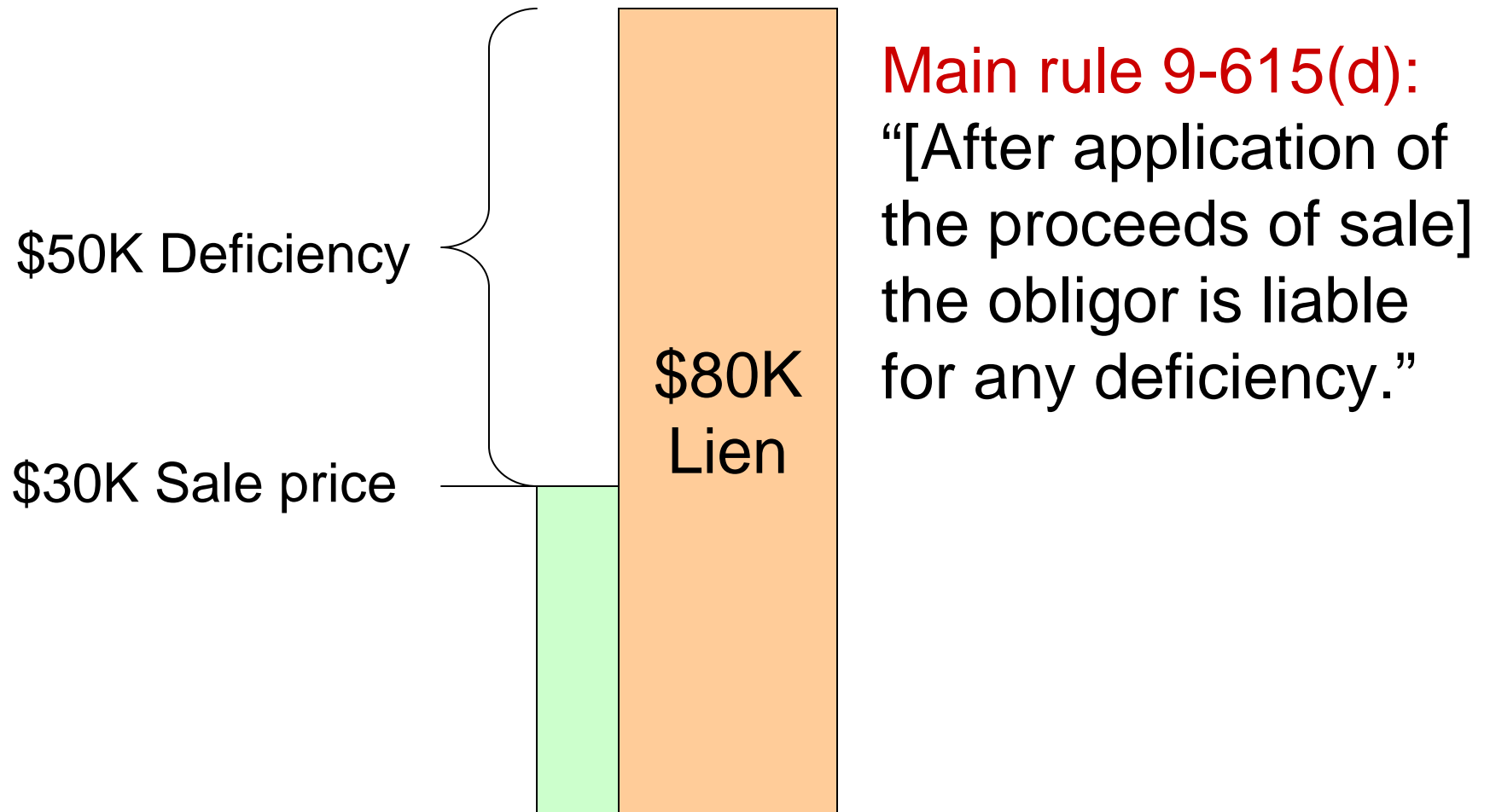
Settlement procedures compared

"Let's just give the !&@# thing back!"	Deed in lieu	Acceptance of collateral, § 9-620
System	Real estate	Personal property
Purpose	Settlement that avoids foreclosure	Settlement that avoids foreclosure
Formal requirements	Deed	<ol style="list-style-type: none"> 1. Authenticated agree- ment, partial satisfaction 2. Lack of objection if in full satisfaction
Consumer exceptions	No	<ol style="list-style-type: none"> 1. Sale required if debtor has paid 60% 2. No partial satisfaction 3. Not while debtor has the collateral

Procedures for Acceptance (Consent)

Lack of objection (only for full satisfaction)	Actual agreement (for partial or full satisfaction)
<p>Secured party consent: Secured party sends unconditional proposal to accept in full satisfaction §9-620(b)(1).</p>	<p>Secured party consent: Secured party consents in an authenticated record §9-620(b)(1).</p>
<p>Debtor consent: Secured party receives no objection to proposal within 20 days, § 9-620(c)(2)(C).</p>	<p>Debtor consent: Debtor agrees to terms in a record authenticated after default, § 9-620(c)(1).</p>

Article 9 deficiency provisions



Article 9 deficiency provisions

9-615(d)(2). “[After application of the proceeds of sale] the obligor is liable for any deficiency.”

Protection against secured party buying collateral cheaply:

9-615(f). “If the transferee . . . is the secured party” then “the deficiency is based on the amount of proceeds that would have been realized in a sale to [some other transferee]”

Protection against secured party not complying with rules:

9-626(a)(3) If the secured party did not comply with Article 9 procedures for “collection, enforcement, disposition or acceptance,” liability is limited to the amount by which the secured obligation exceeds the greater of (1) the proceeds or (2) the amount that would have been realized by compliance.

Secured Transactions Assignment 6

Bankruptcy and the Automatic
Stay

Liquidations: Chapter 7

Deal:

1. Debtor surrenders all property to trustee
(Except exempt)
2. Trustee sells property and distributes proceeds
3. Court discharges all debt
(Except nondischargeable and reaffirmed debt)

Reorganizations: Chapter 11

Deal:

1. Debtor remains in possession during case
2. Debtor proposes plan to repay debt
3. Creditors vote (each “class” has a veto)
4. Court can “confirm” despite veto (“cramdown”)
5. Plan binds all creditors
6. Plan can call for payment over any number of years

Debt Adjustment: Chapter 13

Eligibility: Individuals with unsecured debt less than \$300k and secured debt less than \$1 million

Deal:

1. Debtor keeps all of debtor's property
2. Debtor proposes plan to pay all "disposable income" to creditors for three years (five years for debtors with above median incomes)
3. No voting
4. Court confirms plan if it meets statutory requirements
5. If debtor performs plan, remaining debt is discharged

Bankruptcy Code §362(a)

- (a) [A bankruptcy] petition operates as a stay ... of --
 - (1) The commencement or continuation . . . of [an] action . . . against the debtor . . . to recover a claim . . . that arose before the commencement of the [bankruptcy] case
 - (2) The enforcement , against the debtor or against property of the estate, of a judgment obtained before [bankruptcy]
 - (3) Any act to obtain possession of property of the estate or of property of the debtor
 - (4) Any act to create, perfect, or enforce any lien against property of the estate
 - (6) Any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case.

Bankruptcy Code §362(d)

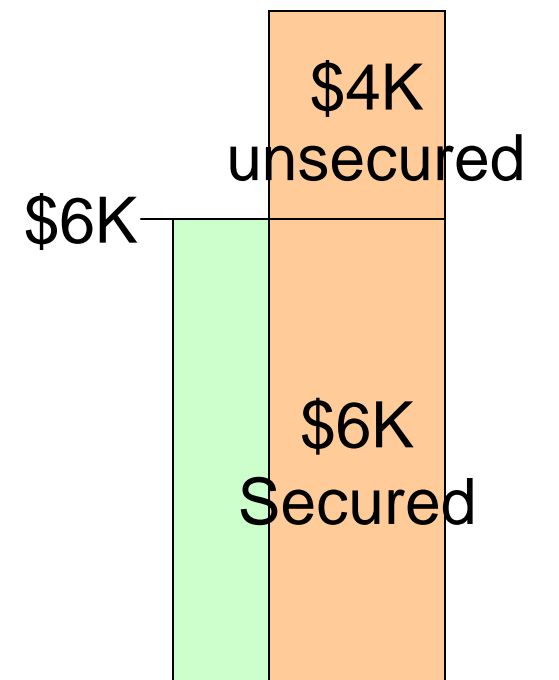
- (d) [T]he court shall grant relief from the [automatic] stay:
 - (1) For cause, including the lack of adequate protection of an interest in property of such party in interest **[or]**
 - (2) With respect to a stay of an act against property . . . if
 - (a) The debtor does not have an equity in the property; **and**
 - (b) Such property is not necessary to an effective reorganization

Secured Transactions Assignment 7

Treatment of Secured Creditors in
Bankruptcy

What secured creditors get in bankruptcy

1. Bifurcation of claim §506(a)
2. Secured portion: payment in full
3. Unsecured portion: prorata payment with other unsecured claims (creditor is “undersecured”)



What secured creditors get in bankruptcy

What are secured creditors options?

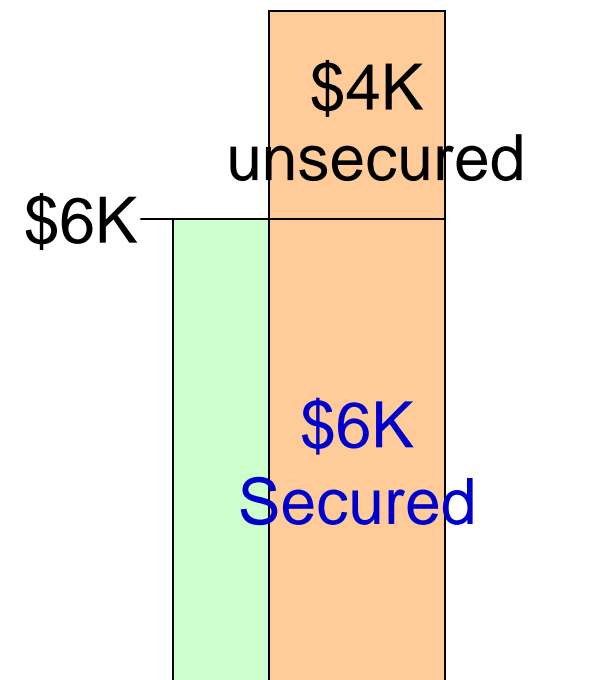
§1325(a)(5). With respect to each allowed **secured** claim . . .

(A) The holder of such claim has accepted the plan;

(B)(i)(I) the plan provides that the holder of such claim retain the lien securing such claim; and

(ii) the value, as of the effective date of the plan, of property to be distributed ... under the plan on account of such claim is not less than the allowed amount of such claim; or

(C) the debtor surrenders the property securing such claim to such holder



Time Value of Money



I will gladly pay you
Tuesday for a
hamburger today.

Payment on Tuesday is worth less than the value of having the hamburger today.

Or, put in financial terms, \$1 now is worth more than \$1 next Tuesday

Or, put in mathematical terms, $PV = FV / (1 + r)^n$

Interest on claims

Interest on claims is important.

Is a creditor entitled to interest on its claim?			
	Prepetition	Pendency	Post-confirmation
Unsecured	Yes, §502(b)	No, §502(b)	Yes §1129(b)(2)(B)
Undersecured		No, Timbers	Yes §1129(b)(2)(A)
Over secured		Yes, §506(b)	Yes §1129(b)(2)(A)

Secured Transactions Assignment 8

Formalities for Attachment

Basic Concepts

Attachment: creation of a security interest



§9-203(a) A security interest attaches to collateral when it becomes enforceable . . .

(b) [A] security interest is enforceable . . . only if:

(1) **value** has been given (§1-204)

(2) the debtor has **rights in the collateral** (§2-501(1)(a));

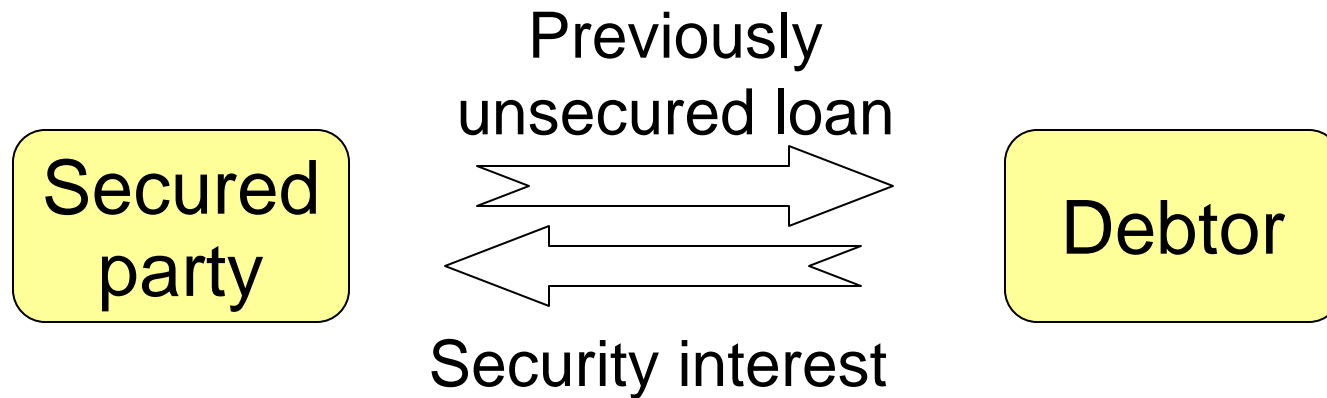
and

(3)(A) the debtor has **authenticated a security agreement** that provides a **description of the collateral** . . .

Basic Concepts

(1) **Value** has been given [by the secured party]

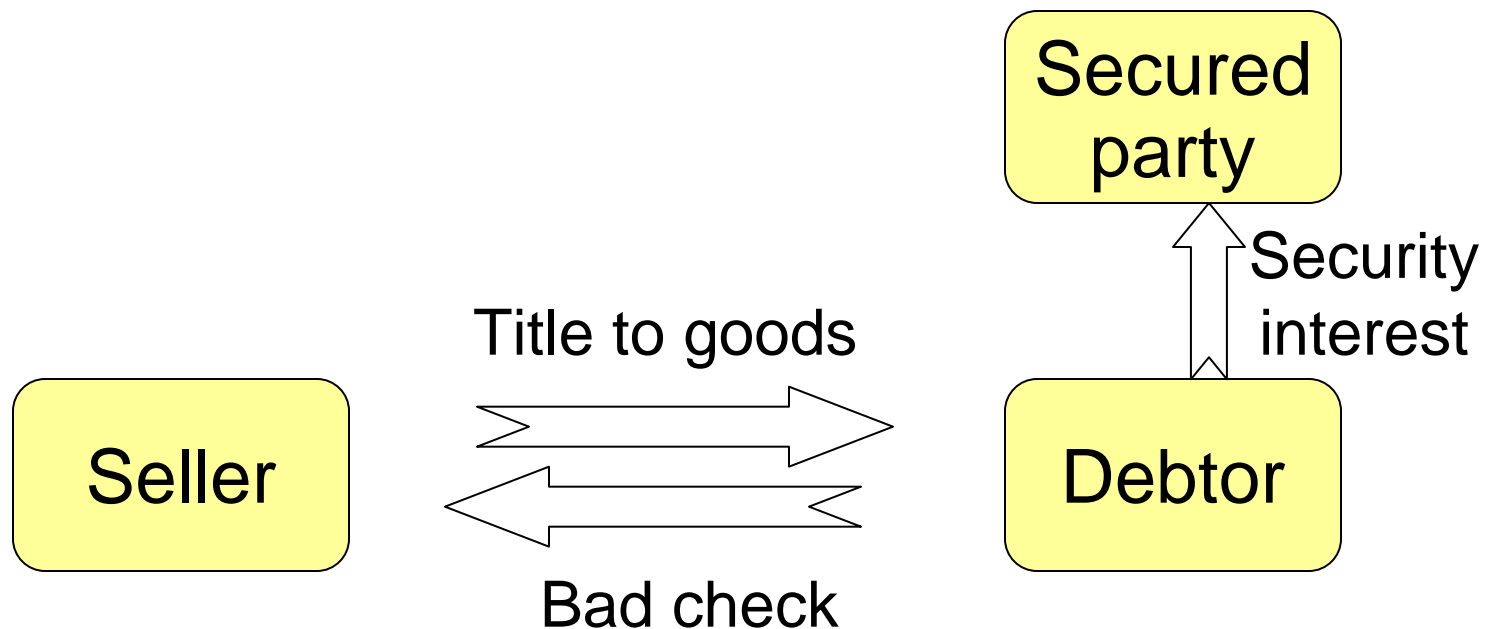
§1-204. [A] person gives “value” for rights if the person acquires them . . . (2) as security for . . . a pre-existing claim . . . or (4) in return for any consideration sufficient to support a simple contract.



A loan made unsecured (“past consideration”) is value with respect to a later-granted security interest

Basic Concepts

(2) Debtor has **rights in the collateral** [ownership, lease, etc.]



Basic Concepts

(3) Debtor has **authenticated** a security agreement . . .

§9-102(a)(7). Authenticate means:

(A) to sign; or

(B) to execute or otherwise adopt a symbol, or encrypt or similarly process a record in whole or in part, with the present intent of the authenticating person to identify the person and adopt or accept a record.

Record . . . means information that is inscribed on a tangible medium or which is stored in an electronic or other medium and is retrievable in perceivable form.

§9-102(a)(69)

Basic Concepts

Security agreement . . .

§9-102(a)(73). Security agreement means an agreement that creates or provides for a security interest.

[and] . . . that provides a **description of the collateral.** 9-203(b)(3)(A)

§9-108:

(a) [A] description of personal or real property is sufficient, whether or not it is specific, if it reasonably identifies what is described.

(b) [A] description of collateral reasonably identifies the collateral if . . . the identity of the collateral is “objectively determinable.”

Basic Concepts

Composite document rule

1. The writing “objectively indicates the parties may have intended a SA”
2. “Parties actually intended a SA”

Secured Transactions Assignment 9

Collateral and Obligations
Covered

Two issues in Assignment 9



What collateral
secures the
obligations?

What
obligations are
secured?

Whatever the
security
agreement says

Contract interpretation and validity

Interpretation

1. Generally: The rules of contract govern
2. The security agreement speaks as of its execution
3. “All equipment” means “all equipment presently owned”
4. Exception for inventory, accounts, other rapid turnover assets
5. But see §9-108 comment 3

“Much litigation has arisen over whether a description in a security agreement is sufficient to include after-acquired collateral if the agreement does not explicitly so provide. This question is one of contract interpretation and is not susceptible to a statutory rule. Accordingly, this section contains no reference to descriptions of after-acquired property.”

Contract interpretation and validity

Validity (of descriptions)

9-203(b)(3)(A) requires a description

9-108 permits

1. Specific
2. Category
3. UCC category
4. Quantity
5. Computational formula
6. Any other if “objectively determinable”
7. Not “all assets”
8. Not “commercial tort claims”
9. Not “consumer goods”

Contract interpretation and validity

§9-108(a)(6) “Objectively determinable” by whom? Using what additional information?

1. Example: “Crops growing on real estate described by ASCS Farm Serial Number J-528” **Yes.**
2. Example: “Creditor shall have a security interest in all items purchased on this account” **Maybe (not under Shirel).**
3. Example: “The equipment in the restaurant at 123 Main Street.” **Yes, as to currently existing equipment.**

Shirel is an exception. Most courts allow extrinsic evidence. Otherwise, most descriptions would fail.

Charles v. Fidelity State Bank (D. Kan. 1987) (“Crops growing” is present tense; for future crops the security interest should say “crops to be grown.”)

Other Description Concepts

Supergeneric Descriptions

§9-108(c): A description of collateral as “all the debtor’s assets” or “all the debtor’s personal property” or using words of similar import does not reasonably identify the collateral.

Consumer Nonpossessory S.I. in “household goods”

16 CFR 444.2(a)(4): It is an “unfair act or practice” to take from a consumer “a nonpossessory security interest in household goods other than a purchase money security interest”

Secured Transactions Assignment 10

Proceeds, Products, and Value-
Tracing: State Law

Basic Concepts

§9-102(a)(64) “Proceeds” . . . means the following property:

- (A) whatever is acquired upon the sale, lease, license, exchange, or other disposition of collateral
- (B) whatever is collected on, or distributed on account of, collateral
- (C) rights arising out of collateral
- (D) to the extent of the value of collateral, claims arising out of the loss . . . of, . . . or damage to, the collateral.
- (E) to the extent of the value of collateral . . . insurance payable by reason of the loss . . . of, . . . or damage to, the collateral.

Basic Concepts

Every security interest automatically includes “proceeds.”

§9-203(f): The attachment of a security interest in collateral gives the secured party the right to proceeds [of same]. . . .

The proceeds of proceeds are proceeds.

§9-102(a)(12). “Collateral” . . . includes . . . “proceeds.”

§9-203(f): The attachment of a security interest in collateral (read: and proceeds) gives the secured party the right to proceeds . . . [of same]

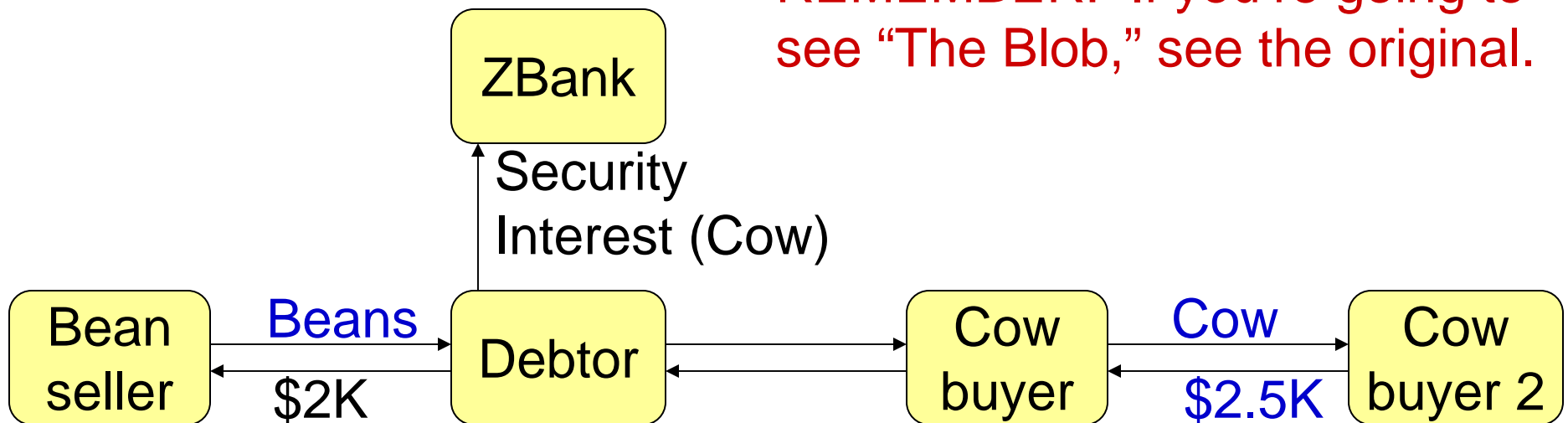
That means the secured party has a right to the proceeds of proceeds.

Basic Concepts

§9-315(a)(1) a security interest . . . continues in collateral notwithstanding . . . disposition thereof unless the secured party authorized the disposition free of the security interest

(2) a security interest attaches to any identifiable proceeds of collateral.

REMEMBER: If you're going to see "The Blob," see the original.



ZBank is secured by Beans (\$2K), Cow (\$2K-\$2.5K) and Cash (\$2.5K)!₅₁

Basic Concepts

§9-315(a)(2) a security interest attaches to any identifiable proceeds of collateral.

(b) Proceeds that are commingled with other property are identifiable proceeds:

(1) if the proceeds are goods, to the extent provided by §9-336

§9-336. “commingled goods” means good that are physically united with other goods in such a manner that their identity is lost in a product or mass.

Examples: Grain in a grain silo. Steel in an automobile.

Basic Concepts

§9-315(a)(2) a security interest attaches to any identifiable proceeds of collateral.

(b) Proceeds that are commingled with other property are identifiable proceeds:

(1) if the proceeds are goods, to the extent provided by §9-336 and

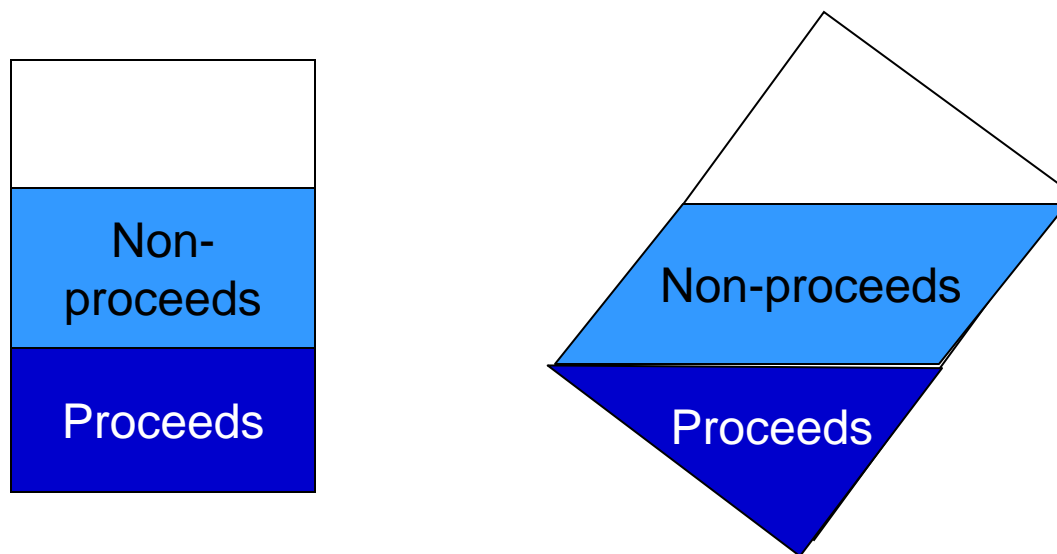
(2) if the proceeds are not goods, to the extent that the secured party identifies the proceeds by a method of tracing . . . permitted under law other than this article

Example: Money commingled in a bank account

Basic Concepts

The lowest intermediate balance rule:

The amount of the secured creditor's collateral remaining in a bank account is equal to the lowest balance of all funds in the account between the time the collateral was deposited to the account and the time the rule is applied.



Secured Transactions Assignment 11

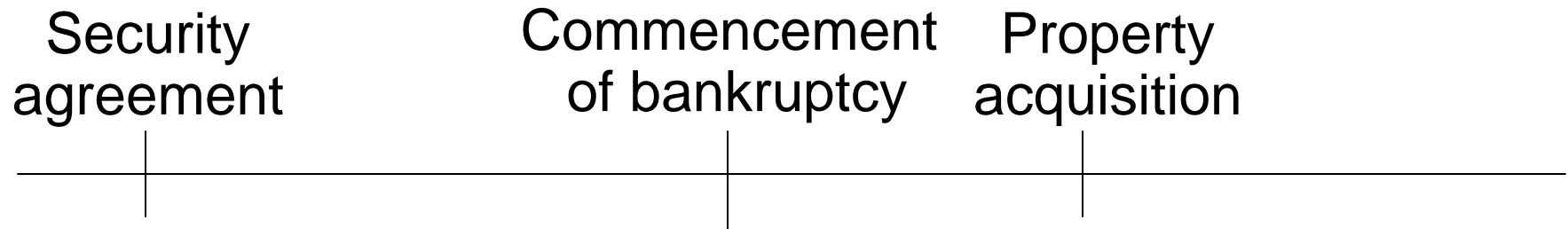
Tracing Collateral Value During
Bankruptcy

Basic Concepts

	After-acquired	Proceeds
When acquired?	After security agreement signed	After security agreement signed
Source of right	Security agreement description	§9-203(f)
Justification	Contract	Value-tracing
Criterion for coverage	Does the collateral fit the description?	Was the collateral acquired upon disposition, etc?
Available during bankruptcy?	No. §552(a)	Yes. §552(b)
Value-tracing?	No	Yes, but loosely

Basic Concepts

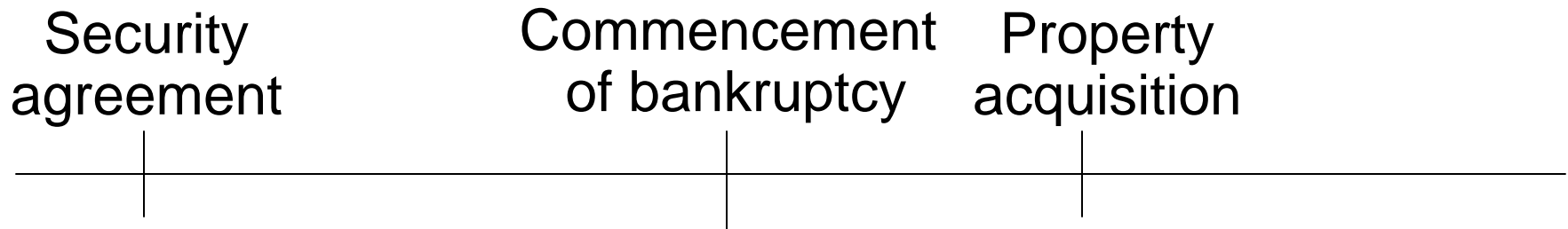
After acquired property clauses aren't good in bankruptcy:



§552(a). Except as provided in subsection (b) . . . property acquired by the estate . . . after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.

Basic Concepts

The secured party's right to proceeds continues in bankruptcy:



§552(b)(1). . . . [If] the debtor and an entity entered into a security agreement before [commencement] and if the security interest . . . extends to property . . . acquired before [commencement] and to proceeds . . . then such security interest extends to proceeds . . . acquired after [commencement] . . . except to the extent that the court . . . based on the equities of the case, orders otherwise.

Proceeds tracing in bankruptcy: Four theories

§9-102(a)(64)	Whatever is received upon disposition of collateral plus rights arising out of collateral
Former §9-306(a)	Whatever is received upon disposition of collateral
Delbridge	The collateral's contribution to the proceeds
Hotel Sierra Vista	The excess of the proceeds over the non-collateral contributions

Secured Transactions Assignment 13

Default, Acceleration and Cure
Under State Law

Basic Concepts

Default. Debtor's failure to pay the debt when due **or otherwise perform** the agreement between debtor and creditor

Acceleration. Rendering a debt previously payable at some future time due and payable now.

Cure. Reversal of a default or acceleration by payment or other action that relieved the debtor of the effects of a default

Insecurity clause. A provision that the loan is in default if the secured party deems itself insecure or the like. §1-309

Basic Concepts

§1-309: “A term providing that one party . . . may accelerate payment . . . ‘at will’ or ‘when he deems himself insecure’ or in words of similar import shall be construed to mean that he shall have the power to do so only . . . in good faith”

§1-201(19) and §9-102(a)(43). “‘Good faith’ means honesty in fact and the observance of reasonable commercial standards of fair dealing.”

Secured Transactions Assignment 14

Default, Acceleration and Cure
Under Bankruptcy Law

Two systems combine to make one

State

1. Defines default
2. Authorizes acceleration
3. Permits cure only before acceleration

Bankruptcy

1. Accepts state definition of default
2. Accepts prefiling accelerations, but stays collection
3. Permits cure before or after acceleration, conditioned on adequate protection
4. Permits modification of repayment schedules

Basic Concepts

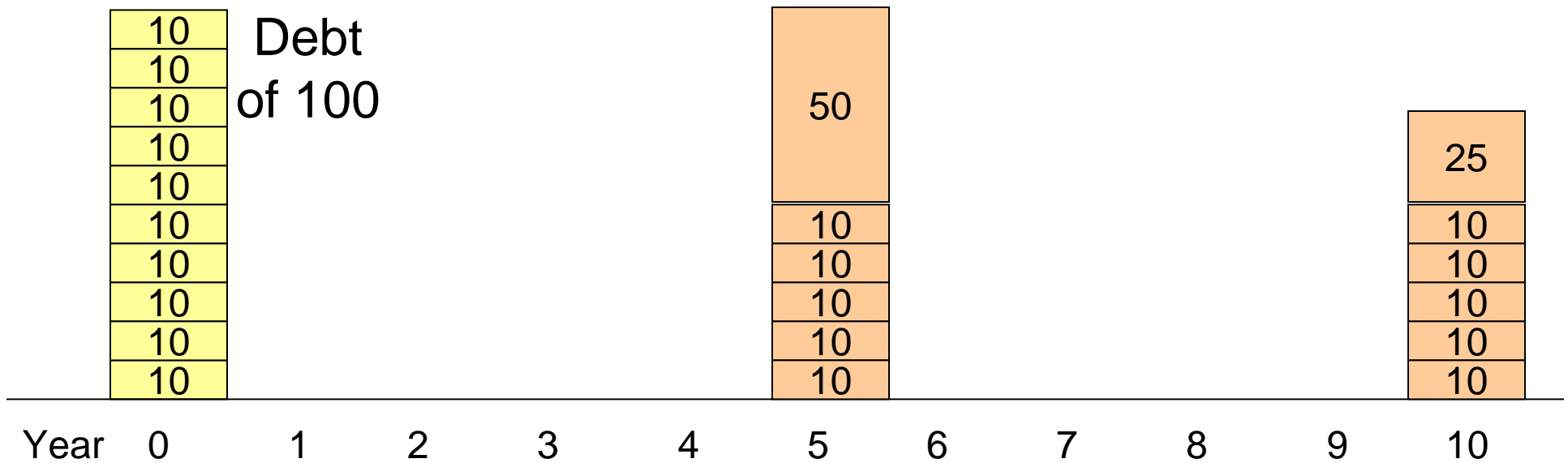
Modification. Creditors are entitled to payments of a value, as of the effective date of the plan, equal to the secured claim.

To have that value, payments must equal the secured claim plus interest at the market rate. (Till v. SCS Credit)

Basic Concepts

Modification. Creditors are entitled to payments of a value, as of the effective date of the plan, equal to the secured claim.

To have that value, payments must equal the secured claim plus interest at the market rate. (Till v. SCS Credit)



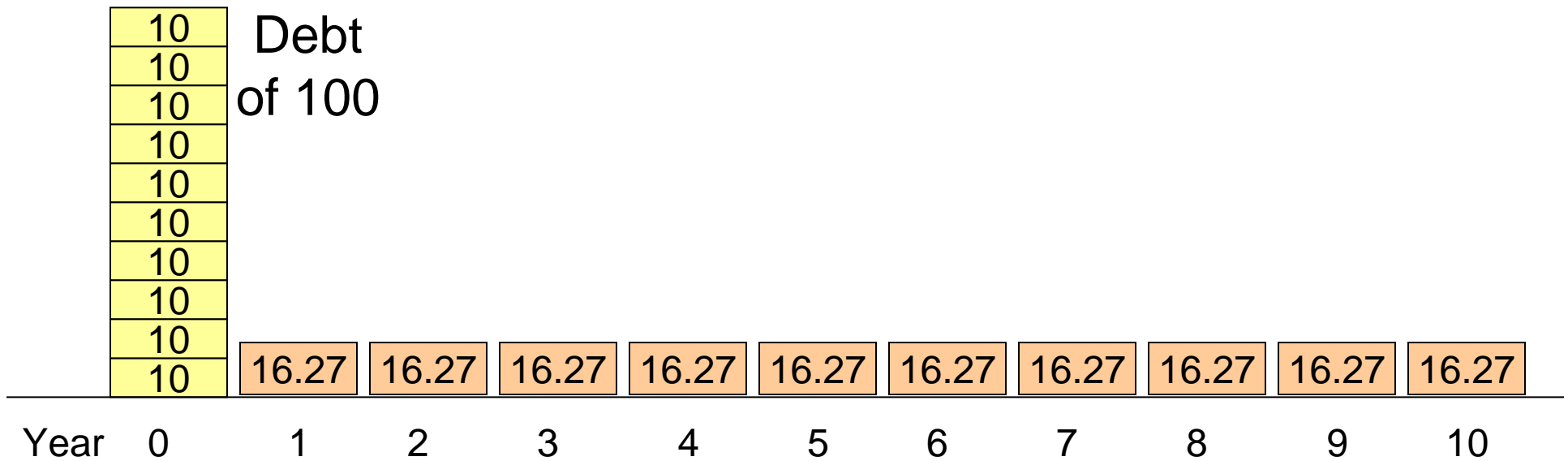
Assumptions: The “market” rate of interest is 10%

Debtor will repay 50 of principal at 5 years and 50 at 10 years⁶⁶

Basic Concepts

Equal monthly payments. Most plan repayment is in equal monthly payments that include principal and interest.

Amortize. To pay in installments.



Assumptions: The “market” rate of interest is 10%

Debtor will repay in ten equal annual installments

Modification Compared With Cure and Reinstatement

Modification (rewrite loan)	Cure and reinstatement
New payment schedule	Return to original payment schedule
Arrearage included in payments	Arrearage paid separately
Interest at <u>market rate</u>	Interest at <u>contract rate</u> on reinstated portion of debt

Availability of modification or reinstatement

	Chapter 11	Chapter 13
Modification	<p>No limit on length of payments</p> <p>Not home mortgages, 1123(b)(5)</p> <p>Must file before sale. <u>DeSeno</u>, 1123(a)(5)</p>	<p>Payment only for plan period, 1322(d)</p> <p>Only short home mortgages, 1322(c)(2)</p> <p>Must file before sale. <u>Roach</u></p>
Reinstatement and cure	<p>Cure due at effective date. Case law.</p> <p>Must file before jmt? <u>DeSeno</u></p> <p>Contract &/or state law fixes cure amt, 1123(d)</p>	<p>Cure over reasonable time, 1322(b)(5)</p> <p>Must file before sale 1322(c)(1)</p> <p>Contract &/or state law fixes cure amt, 1322(e)</p>

UCC Code Sections

- 1-201(b)(20): “Good faith”
- 1-204: “Value”
- 1-309: Option to Accelerate at Will
- 9-102(a)(7): “Authenticate”
- 9-102(a)(12): “Collateral”
- 9-102(a)(64): “Proceeds”
- 9-102(a)(69): “Record”
- 9-102(a)(73): “Security agreement”
- 9-108: Sufficiency of Description
- 9-109(a)(1): General scope of article
- 9-201(a): General effectiveness
- 9-203: Attachment, Enforcement, Proceeds

UCC Code Sections

- 9-204(a): After-acquired collateral
- 9-315(a), (b): Disposition of collateral: continuation of S.I.; when commingled goods identifiable
- 9-336: Commingled goods
- 9-608(a)(1): Application of Proceeds
- 9-610(a), (b), (c): Disposition of Collateral After Default
- 9-615(a), (d): Application of proceeds; deficiency
- 9-620: Acceptance of Collateral in Full or Partial Satisfaction of Obligation
- 9-626: Action in Which Deficiency or Surplus in Issue

Bankruptcy Code Sections (11 U.S.C.)

- §362(a), (d)
- §502(b)
- §506(a), (b)
- §552(a), (b)
- §1123(a)(5), (b)(5), (d)
- §1124
- §1129(b)(2)(A)
- §1322(b)(5), (c)(2), (e)
- §1325(a)(5)