Assignment 3
Repossession of Collateral

Reference: Understanding Secured Transactions, §§ 17, 18.01, 19.01

Article 9: Default and Repossession

- Upon default, secured party can take possession of the collateral (usually called “repossession”) [§ 9-609(a)]
- Secured party may take possession either
  - By judicial process [§ 9-609(b)(1)], or
  - By “self-help,” as long as secured party does not “breach the peace” [§ 9-609(b)(2)]

Repo by Judicial Action: Missouri

- Judicial repossession occurs by *replevin*
  - \( \pi \) (secured party) files a verified petition [Rule 99.03], \( \Delta \) has 30 days to answer [Rule 55.25(a)]
  - Prior to judgment, \( \Delta \) keeps possession of the collateral, unless \( \pi \) posts bond = 2x value of collateral [Rule 99.06]
  - If \( \pi \) posts bond (and complaint demonstrates \( \pi \) has right to possession), court will issue pre-judgment replevin order [Rule 99.04]
- If pre-judgment replevin ordered, \( \pi \) must give \( \Delta \) notice of right to hearing; if \( \Delta \) requests hearing, it must occur w/in 10 days [Rules 99.05, 99.09]
- Pending final judgment, \( \Delta \) can recover possession if it posts bond = 2X value of property [Rule 99.07] (most debtors can’t do this, of course)
- Once collateral is seized by sheriff, \( \Delta \) usually doesn’t answer \( \Rightarrow \) default judgment results
Once final judgment is entered, sale of the property can occur.

Sale can occur either by:
- **Execution sale** conducted by sheriff (public auction sale) [Assignment 4], or
- Article 9 sale (only if π is an Article 9 secured party)
  - This sale can be a public auction sale or a private sale [Assignment 5]

Sale proceeds are applied to reduce judgment; excess proceeds (if any) returned to Δ.

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**Problem 3.1**

Lisa granted a SI in her lawn furniture to secure payment of $1,000 debt owed to Jeff.

Lisa is in default.

Jeff asks you: “Can I go take the furniture off her patio?”

What’s your response?

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**“Breach of the Peace”**

Is it a breach of the peace for Jeff (in attempting repossession) to:
- Go onto Lisa’s land?
- Go onto Lisa’s deck?
- Go into Lisa’s screened porch?
- Go into her living room?

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**Pro:** Jeff can avoid costs of replevin action (filing fee, bond, attorney fees, additional costs of delay)

- Even if Lisa is liable to reimburse these costs by contract, Jeff may not actually recover them (she may be “judgment proof,” furniture’s value may not cover debt + costs)
- Self-help is arguably efficient in reducing costs of collection (which might otherwise be passed on to other borrowers, increasing the cost of credit)

**Con:** Jeff runs the risk of potential liability if he commits a “breach of the peace” in the course of the repossession [§ 9-609(b)]

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• Courts have typically held that it is not a breach of the peace to enter someone’s yard or driveway to effect a repossession
  – Not considered a “trespass” per se; security agreement is presumed to authorize secured party to enter onto debtor’s land to repossess (a “license coupled with an interest”), if it can be done without breach of peace [Salisbury Livestock, pp. 44-45]
• Courts have typically held it is a breach of the peace to enter a dwelling, or a closed/locked building. Why?

Rationale for Limiting Self-Help

• Repossession effected through “breach of the peace” is not efficient, as it fails to take account of external costs (risk of violence, injury to debtor, creditor, or bystanders)
  – Ordinarily, self-help is justified by cost savings (no need to pay for cost of legal process, which would increase amount of debt)
  – But, risk/costs of violence/injuries (if that transpires) is likely to outweigh any efficiency benefit to be gained from self-help

Self-Help

• Note: under Louisiana’s version of Article 9, no self-help is permissible (must use judicial process unless debtor voluntarily turns over possession of the collateral)
  – Rationale: potential threat of confrontation and/or violence is always present, can’t be readily predicted/avoided; better to avoid such harms by requiring resort to judicial process
Problem 3.1: As Jeff starts to remove the furniture from the deck, Lisa emerges and says “Stop,” but he ignores her and completing the repossession without further consequence. Has he breached the peace?

A. Yes  
B. No

Effect of Debtor’s Verbal Objection

- Weight of authority: repossession over debtor’s unequivocal protest likely to cause confrontation, breaches the peace \([\textit{Morris}, \text{p. 46}]\)
- Some courts: may ignore protest so long as secured party doesn’t threaten debtor w/ physical harm \([\textit{Williams}, \text{p. 48}; \textit{Koontz} (\text{Ill. App. 1996})]\)
  - Problem: this encourages a debtor who wants to retain the collateral to resort to intimidation, threats, or actual violence (which may exacerbate potential problems)
Problem 3.2(e)

- These agreements are ubiquitous in security agreements, but
  - Agreement can’t waive secured party’s obligation not to breach the peace [§§ 9-602(6), 9-603(b)] (i.e., debtor can’t “authorize” secured party to do something that breaches the peace)
  - There’s no guarantee debtor will comply with this provision after default (i.e., may object anyway)
  - They don’t strengthen secured party’s position much

Breach of the Peace

- Suppose Jeff did breach the peace in repossessing the furniture
- Does it really matter, if Lisa really was in default in repayment?

Consequences of Breaching Peace

- Secured party is liable for damages caused by its failure to comply w/Article 9 [§ 9-625(b)]
- What actual damages might debtor suffer due to a wrongful repossession?
  - Lost use value of property repossessed (but Lisa is unlikely to recover if she really was in default)
  - Physical injury or injury to collateral (Lisa didn’t suffer any, apparently)
  - But “breach of peace” can result in punitive damages in egregious cases

Problem 3.9: Zabriskie Autos has SI in a car sold to Evans, who has missed 3 payments but who has complaints about the quality of the car. What should Zabriskie Autos do?

A. Repossess the car by self-help (cost: $300)
B. File a replevin action (cost: $600 or more)
• Problem: if Zabriskie warranted the car and that warranty has been breached, Evans may have a valid defense to payment of the debt
• In that case, there would be no “default,” and Zabriskie could not legally repossess [§ 9-609(a)]!
  – Repo absent default would expose Zabriskie to liability
    • Under § 9-625(b) (failure to comply w/Article 9), or
    • Under common law (conversion)
• If existence of default is subject to any doubt, judicial process may be preferable (existence of default is judicially determined before repo)

Payment Rights as Collateral
• Often, a business uses its right to be paid by its customers as collateral
• E.g., Davis is a plumber
  – He gives his customers 30 days to pay him
  – His right to payment from a customer is an “account” [§ 9-102(a)(2)] (“right to payment of a monetary obligation, whether or not earned by performance, (i) for property that has been or is to be sold … (ii) for services rendered or to be rendered”)

Payment may use his accounts as collateral for line of credit from Bank
• This gives him access to capital to pay employees and business expenses during the month
• When his customers pay 30 days later, he can “pay down” the amounts borrowed
• Davis’s customer = “account debtor” [§ 9-102(a)(3)]; Bank = assignee; Davis = assignor

Collection of Accounts
• After default, secured party with a SI in accounts may act to collect those accounts
• This can be done by “self-help” by notification [§ 9-607(a)(1)]
  – E.g., “Your account to Davis has been assigned to Bank as collateral for a loan that is now in default. You are hereby instructed to pay this account to Bank.”
Problems 3.5, 3.6

- Deare Distributors sells farming supplies
- Deare has a line of credit with Firstbank, secured by all of its accounts
- Deare is in default to Firstbank
- 2 months ago: Firstbank gave notification under § 9-607(a) to all of Deare’s customers to pay Firstbank directly

Horne’s Feed and Seed owed Deare $20,000. Horne’s: “We paid Deare in full last month.” [Assume this is true.]
Which statement is correct?

A. Horne’s owes nothing to Firstbank, which has to get the money from Deare
B. Horne’s must pay $20,000 to Firstbank

Problem 3.5(a)

- Until receiving notification from Firstbank, Horne’s (the account debtor) could satisfy account (i.e., “discharge” its obligation) by paying the debtor (Deare) directly
- After receiving notification, Horne’s cannot satisfy its obligation by paying the debtor directly; it can only satisfy the obligation by paying the assignee (Firstbank) [§ 9-406(a)]
- If Horne’s received notification from Firstbank before it paid Deare, it is still obligated on the debt, and Firstbank could recover $20,000 from Horne’s
  - If Horne’s has to pay Firstbank too, it can recover original payment from Deare

Problem 3.6(b). Wilson’s billed $42,000 by Deane, and has received notification to pay the account to Firstbank. Wilson’s refuses, claiming $19,000 of the goods it purchased were defective. [Assume this is true.] How much, if any, can Firstbank recover from Wilson’s?

A. Zero
B. $42,000
C. $23,000
• Unless an account debtor has made an enforceable agreement not to assert defenses, the rights of assignee (Firstbank) as to the account are subject to all of the terms of the agreement between the account debtor (Wilson’s) and the assignor (Deare), including any defenses to the contract [§ 9-404(a)(1)]
  – Assignee’s rights are “derivative” of assignor’s
  – In Problem 3.6(b), Wilson’s has a partial defense (K not enforceable in full due to warranty claim)
  – If that defense is valid, Firstbank may collect only $23,000 from Wilson’s