Dispositions of Personal Property Collateral: How Does a Commercial Lender Comply with Revised Article 9?

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Lawmakers have clarified the requirements for public and private foreclosure sales in connection with commercial transactions. Long overdue, Revised Article 9 of the Uniform Commercial Code (UCC) adds 21 new provisions to the original Article 9 and resolves many issues that were previously left to the courts. To comply with Revised Article 9, a Secured Party must follow several procedural requirements. Noncompliance with the statute’s procedural requirements can lead to potential liabilities that a Secured Party will obviously want to avoid.

NOTICE OF DISPOSITION

Assuming that a default has occurred and the Secured Party has elected to sell, lease or otherwise dispose of collateral, the Secured Party must follow certain steps to fulfill its duties to the debtor and certain third parties. Generally, the UCC requires a reasonable authenticated notification of disposition. Subject to limited exceptions, a Secured Party must send notice to all proper parties and the notification must be reasonable as to the manner sent, timeliness and content.

Parties Entitled to Notice

Subject to some very narrow exceptions, notice must be sent not only to the debtor, but also to every guarantor, person from whom the Secured Party received a notice of a claim of interest in the collateral, and person who held a security interest in the collateral perfected by filing of a financing statement or by compliance with a statute as of 10 days before the “notification date.” The notification date is the date notice is sent or the date when the debtor and all guarantors waived the right to notification. The statute provides a safe harbor for a Secured Party when identifying other secured creditors who have perfected by filing. The safe harbor works as follows:

- The Secured Party conducts a search regarding financing statements of record from the appropriate office.
- Twenty to thirty days after such request, the Secured Party sends notice to the other secured creditors named in the response to the search request whose financing statement covered the collateral to be disposed of.
- The Secured Party is not required to give notice to a secured creditor if the filing office fails to respond or fails to include the secured creditor in the response, unless the Secured Party received notice of the secured creditor’s interest.

Timeliness of Notice

The UCC mandates that the notice must be given a reasonable amount of time before disposition of the collateral. Although a “reasonable amount of time” is a question of fact, notification sent after default and at least 10 days before the date of disposition falls within another safe harbor.

Content of Notification

Again, reasonableness is the standard governing the required content of notification. It must be sufficient to put a debtor on notice of a disposition and satisfy the requirements of the UCC. Section 9-613 of the UCC contains a form of notice that is not another safe harbor for the Secured Party. A notification that provides only the information required under the form is deemed to be legally sufficient. Additional information in the notice may be included, but is not needed unless the parties have agreed otherwise. The inclusion of additional information that is not contractually required will not offer any greater protection to the Secured Party, and may expose the Secured Party to risks if it is found that the information was incorrect, misleading or otherwise commercially unreasonable.

COMMERCIALY REASONABLE DISPOSITION

A Secured Party may dispose of collateral in any fashion as long as all aspects of the disposition are commercially reasonable. In some cases, the collateral may be of a type that will allow the secured party to follow the guidelines of Section 9-627(b) and possibly Section 9-627(c) in order to avoid challenges as to the commercial reasonableness of a disposition. Under these provisions, a disposition is commercially reasonable if it is made i) in the usual manner on a recognized market; ii) at a price current in a recognized market at the time of disposition; or iii) otherwise in conformity with reasonable commercial practices among dealers in the subject property. Although not required, under Section 9-627(c), a collection, enforcement, disposition or acceptance is commercially reasonable if it has been approved in i) a judicial proceeding; ii) by a bona fide creditors’ committee; iii) by a representative of creditors; or iv) by an assignee for the benefit of creditors.

LIABILITY FOR NON-COMPLIANCE

If a Secured Party breaches a duty set forth under the foreclosure provisions of the UCC, then the debtor, guarantors, and certain other parties may be entitled to seek damages from the Secured Party. The injured party may seek injunctive relief
or sue for damages caused by the Secured Party’s failure to comply.

The basic obligations of a Secured Party in a disposition of goods in a commercial transaction under Revised Article 9 are to act in good faith, proceed in a commercially reasonable manner as to all aspects of a disposition, and follow the specific duties set forth in Revised Article 9. Although not required, it is certainly to a Secured Party’s greatest advantage to stay within the parameters of safe harbors where they are available. Failure to comply with the duties imposed by Revised Article 9 may result in losing the ability to collect on a deficiency after a foreclosure as well as liability for damages to injured parties. These potential liabilities can be easily avoided by following proper procedures.

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