

# community BANKER

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Welcome to the latest issue of the COMMUNITY BANKER.

The Community Banker is prepared by attorneys at Olson & Burns P.C. to provide information pertaining to legal developments affecting the field of banking. In order to accomplish this objective, we welcome any comments our readers have regarding the content and format of this publication. Please address your comments to:

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The attorneys at Olson & Burns represent a wide range of clients in the financial and commercial areas. Our attorneys represent more than 30 banks throughout North Dakota.

## YOU ARE ASKING . . . .

**Q: What sort of information should we obtain regarding potential litigation against a potential borrower as part of our due diligence for a loan to a corporation or other entity?**

**A:** You may want information on the following:

A. A list and description of pending or threatened litigation, claim, arbitration proceeding, or investigation relating to the entity or its officers, directors, employees, or agents, including, but not limited to: (1) litigation involving alleged violations of laws or regulations relating to discrimination, the protection of the environment, or the health or safety of employees or others, and (2) governmental or administrative proceedings.

B. A description of any allegations of unfair labor practices, and any suits or administrative proceedings instituted by employees within the past three (3) years.

C. A description of and copies of all judgments, decrees and orders to which the entity is presently, or during the past five (5) years, has been subject to. (Exclude money judgments which have been satisfied and which were under \$10,000, unless the judgment was a fine or penalty, in which case, describe the nature of such fine or penalty.)

D. Anything else about any dispute you think might impact your loan.



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**Q: What are the ways that we can get back personal property collateral and which should we choose?**

**A:** The method you choose varies depending on the collateral, the debtor, and the risks. The very brief breakdown below should answer your question.

Manner of Repossession	Pros	Cons
<b>Self-Help</b>	Cheap and usually fast.	May “breach the peace” or wrongfully repossess property, which equals liability.
<b>Having Debtor Assemble Collateral</b>	Cheap, quick, and no risk of breaching the peace.	Have to notify debtor of your intent to repossess. Will he hide it or wreck it?
<b>Disable the Collateral</b>	Cheap and fast.	Debtor retains possession, and it’s only available for <i>equipment</i> collateral.
<b>Notify Account Debtors (debtors of your debtor)</b>	Cheap, quick, no risk of breaching the peace.	What if the account debtors don’t pay you?
<b>Judicial Foreclosure</b>	No risk of breaching the peace, and you can have the sheriff pick up the collateral.	Very slow and expensive.

**Q: We have a loan and a security agreement giving us a security interest in collateral. If a borrower defaults and we want to pick up that collateral, what sort of things can get us in trouble for a breach of the peace?**

**A:** Going out and getting your collateral without involving lawyers, judges, and sheriffs is “self-help” repossession. Only *secured* creditors can do this, and a secured creditor can get his stuff only so long as there is no “breach of the peace.” This isn’t defined in the UCC, but its generally agreed that a breach of the peace occurs when *either* party uses force, violence, or a threat of violence. Does a breach of the peace occur when a homeowner assaults someone trespassing on his property in an effort to repossess a car? Yes. Imagine that the same homeowner does not notice his property being repossessed, but the creditor has to cut a lock and go through a gate to repossess the car. Does this breach the peace even if there is no confrontation? Probably. While you have a “common law privilege” to go upon the debtor’s land to repossess your collateral, never ever enter houses or garages. In jurisdictions that have addressed this issue directly, courts agree that the home is sacred and a breach of the peace occurs anytime someone enters without permission.

Commercial buildings would not have the same privacy considerations, but as a general rule, if it has four walls and a roof and you open the door to get in, the risk of a breach of the peace rises. In general, if the collateral is located on open land under sky, go ahead. Drive off in the car that’s parked on the street, hook up the cultivator out in the field, or use another boat to tow away the boat at the dock when the owner is taking a nap.

Which brings us to a *Breach of the Peace* Pop Quiz!

**Julia buys a new Honda Accord from Wally's Car Sales, using money borrowed from your bank. Julia has signed a security agreement giving your bank a security interest in the Accord. Julia defaults, and you hire Mean Max, a repo man to get the Accord. Mean Max sees the Accord parked in the street behind Julia's work place.**

**1. Can Mean Max seize the Accord without judicial process and without notifying Julia in advance?**

Yes. A secured creditor has a right to self-help repossession so long as it does not result in a breach of the peace. N.D.Cent.Code § 41-09-06(2)(b). Based on these few facts, there is no threatened or actual breach of the peace because stealth is permissible, notice is not required, and the repossession does not involve a trespass. (However, always notify the police or sheriff's department prior to repossessing so when they receive the report of a stolen car they know the actual circumstances.)

**2. Would your answer change if Julia came running out screaming and physically resisted the seizure?**

Yes. This is an actual or threatened breach of the peace.

**3. Would it matter at what point in your bank's exercise of self-help Julia appeared?**

Most likely. Common sense suggests that there is a point at which self-help is complete and a debtor can't provoke a breach of the peace to somehow undo the repossession. If Julia runs out while Mean Max is just hitching the Accord to the tow truck, it's arguable that self-help repossession must stop. If she hops on her bike and follows Mean Max to the repossessed vehicles storage lot and attempts by force to recover the vehicle, it's likely that whatever breach of the peace now ensuing is separate from the exercise of self-help.

**4. Would self-help repossession of the Accord from the driveway of the home of a friend of Julia's be permissible?**

Maybe, maybe not. We need more facts, such as the time of day. This self-help repossession involves a trespass, but some courts have found that the trespass is "privileged" if there was no actual or threatened breach of the peace.

**5. Would self-help repossession by Mean Max from a carport attached to Julia's house be permissible?**

Probably. Generally, a trespass without a breach of the peace does not violate the "no breach of the peace" limitations.

**6. If the self-help repossession from Julia's attached carport took place at 3:10 a.m., would the repossession be permissible?**

Probably not. Seizing property from the premises of the debtor in the middle of the night is treated less favorably than taking it in daytime.

**7. Would a self-help repossession by Mean Max from a locked garage attached to Julia's house be permissible?**

Probably not. Courts don't like entry into a closed structure attached to the home, especially when it involves forcible entry.

**8. Would consent by Julia *in* the security agreement to a forcible entry into her home make self-help repossession from the locked garage permissible?**

Probably not. Agreements that permit conduct that would otherwise be a breach of the peace are likely not enforceable.

**9. Could your bank be held liable for actions by Mean Max that violated the breach of the peace limitation on self-help repossession?**

It's possible. A secured party might be held liable for the actions of repo agents under some agency or negligent-hire theory. Never hire a violent goon to pick up your collateral.

**10. Suppose your loan officer asked Julia to come to his office so that they could work out a payment agreement. While Julia was in his office, the Accord was repossessed. Would the repossession be permissible?**

Probably not. Though this may not involve a breach of the peace (unless Julia comes storming back in and gives vent to her feelings), it might be a breach of the bank's duty of good faith required by N.D. Cent. Code § 41-01-18. "The principle is that in commercial transactions good faith is required in the performance and enforcement of all agreements or duties." *Id.*, Official Comment 1 (*emphasis added*).

**11. Suppose the bank goes to Julia's home and demands possession of the Accord. She refuses and the next day, the loan officer returns with a personal friend, an off-duty sheriff's deputy. Julia turns the car over to the bank. Is the manner of repossession permissible?**

No. Using the help of law enforcement is not *self*-help, it can be considered intimidation, and will likely take the repossession out of the arena of what a secured creditor is permitted to do.

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