Week Four Lecture

**Secured Transactions**

This week, we’ll examine the use of secured transactions as part of doing business. In short, security interests, or secured transactions, is another term used to describe the lending of money to an individual or entity based upon that person’s/entity’s credit and/or access to assets to be used as collateral—the lending of money.

We’ll examine the relevant terms in more detail, but here are some short definitions to help guide you:

* Creditor: Person/entity lending money in exchange for promises and/or collateral.
* Debtor: Person/entity receiving loan and promises to pay loan back.
* Collateral: Property, personal or real, that can be used to pay back creditor if debtor is unable to repay loan.
* Secured Interest: Loan secured with collateral (e.g. mortgage secured by the actual home).
* Unsecured Interest: A loan not secured with collateral; debtor agrees to pay back the cash.

The benefit of commercial lending is that businesses don’t have to rely on banks to utilize secured transactions. Businesses and individuals can lend to other businesses and individuals. Pursuant to that, the creation of a security interest is very simple. For example, a security interest can be created by using one sentence: “I agree to have a lien attached to this property.” That’s it!

Additionally, many assets or property interests can be used to secure a secured transaction. Some examples include:

* Real estate/real property
* Inventory
* Equipment
* Accounts
* Accounts receivable
* Intellectual property (e.g. patents)
* Instruments

Almost anything that has monetary value can be used in the lending of money based on a secured transaction. Again, the overall benefit of allowing secured transactions is that it opens credit and lending to businesses of all sizes, regardless of whether these businesses have access to banks or financial institutions, and with less regard to the debtor’s creditworthiness. To that end, it helps the economy.

**Bankruptcy**

The other major topic that we’ll be reviewing this week is bankruptcy. In short, bankruptcy is the ability of a debtor to have some or all of his or her debts forgiven when he or she is financially unable to pay them. This creates a “fresh start” for that individual. More importantly, bankruptcy is a constitutional right (U.S. Const. art. I, § 8).

On the surface, allowing for people and entities to declare bankruptcy seems unfair, as the forgiven debtor is seen as just getting a pass on their debts. Although the debtor may get out of some financial obligations, they first have to prove that they are financially unable to pay their obligations. Thus, one cannot just declare bankruptcy just to get out of debt because they want to. If the debtor is able to pay even part of their debts then they are expected to do that.

Second, the effects of bankruptcy will stay with the debtor. This decision will be on their credit record for several years to come. So, although the debtor is discharged from some or all of their debts, they probably will be frozen out of the credit market for years to come. That is one of the downsides to bankruptcy.

On the side of the creditor, having one of their debtors declare bankruptcy is not a complete loss.  Although the creditor won’t be able to collect on the original debt, the creditor is able to write off the loss of the debt on their taxes, which has its own financial benefit.

Having said all this, filing for bankruptcy can be a very emotionally charged event.  However, there are ways of handling this emotional and financial decision, as discussed in the Forbes article, “[4 Tips for Coping With the Emotional Cost of Bankruptcy](http://www.forbes.com/sites/entrepreneursorganization/2014/08/21/4-tips-for-coping-with-the-emotional-cost-of-bankruptcy/)” (Apfelbaum, 2014).

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References

Apfelbaum, J. (2014, August 21). [4 tips for coping with the emotional cost of bankruptcy](http://www.forbes.com/sites/entrepreneursorganization/2014/08/21/4-tips-for-coping-with-the-emotional-cost-of-bankruptcy/). *Forbes*.  Retrieved from http://www.forbes.com/sites/entrepreneursorganization/2014/08/21/4-tips-for-coping-with-the-emotional-cost-of-bankruptcy/

U.S. Const. art. I, § 8.