

## Reasons Why Collateral Matters to Creditors

Collateral may be the most ignored of the Five Cs of Credit (character, capacity, capital, collateral and conditions).

It is most often thought of as a way banks and consumers securitize certain loans and other transactions by listing the value of such assets as cars and homes. But collateral provides trade creditors with an alternative source to draw from should their customer lack the character or the capacity to make payment. Here's a list of reasons why creditors that aren't banks should pay attention to collateral:

**Flexibility:** Collateral doesn't simply have to be a house or a building. Under the Uniform Commercial Code (UCC) there are six different types of collateral:

- a. Accounts and general intangibles
- b. Deposit accounts
- c. Goods, such as inventory and equipment
- d. Instruments
- e. Investment property, such as securities and brokerage accounts
- f. Chattel paper, which is any writing evidencing a debt secured by personal property

Any of these items can be considered collateral, and used by a creditor to protect themselves from the risk of nonpayment.

**Voluntary/Involuntary:** Assets can be pledged voluntarily by the debtor, but can also be acquired involuntarily through the use of legal instruments like liens or judgments which liquidate property and use the funds for repayment. Encumbering assets like this isn't often a friendly process and takes work, but could end up being worth it if you aren't sure about a customer.

**Personal Property:** Business owners can place personal assets up for collateral for a business transaction, offering the creditor a source of repayment separate from the actual company's finances. This also incentivizes payment, giving the company a more personal reason to pay on time.

**Nonjudicial Repossession:** Article 9 of the UCC permits a lender to repossess collateral upon default without *any* court action, if it may do so peacefully. While this means that any attempt to retake collateral involving the use of force, or the threat of force, by either party will likely be considered improper, recovery efforts that involve stealth and deception *are* permitted. There are very few other repayment mechanisms where this is the case.

Learn more about collateral, contact us at **(INSERT CONTACT INFORMATION OR OTHER MESSAGE.)**