Cassels

Lessons Learned - Lesson Two: Serve A Demand Notice Before Taking Enforcement Action

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*Cassels developed this **Lessons Learned** series based on our experience working with a range of secured parties and debtors. This series has grown from the realization that many secured parties make fundamental errors that may impact the priority of, or their ability to enforce, their security. Each lesson in the series will outline a basic mistake and the lesson to be learned…*

Lesson Two: Serve A Demand Notice Before Taking Enforcement Action

Before a secured party can enforce its security, it should review its security and finance documentation in order to determine exactly what obligations, rights and remedies it has and what preliminary steps it must take in order to enforce its security. In addition to those bargained for obligations, common law requires that a secured party's right to enforce its security or accelerate any loan (including a loan stated to repayable "on demand") is dependent on providing the debtor with reasonable notice to pay. A secured party may also need to serve a Section 244 notice under the *Bankruptcy and Insolvency Act*, which we will explore in a subsequent lesson.

Demand Notice

A demand notice is sometimes called a default notice, a demand letter or an acceleration notice. It is a written notice that provides the debtor with details of the indebtedness owed (including the quantum, the secured party's details and any interest payable on that indebtedness), reasonable notice and an opportunity to pay. It should also set out the consequences of the debtor's failure to pay by the stated deadline.

There is no statutory form of demand notice or prescribed notice period. In fact, what constitutes "**reasonable notice**" is very fact-specific and may include the terms of the security agreement, which may entitle the debtor to a specified period of time to "cure" the default; the size of the obligation secured (i.e., the size of the loan); past practice between the parties and prior evidence or instances of default; the debtor's ability to raise funds or remedy the default in question; and/or the nature of the collateral (e.g., is it rapidly depreciating in value?).

Default

Where the underlying debt obligation is ***not*** payable on demand, a default must have occurred under the terms of the security agreement before a secured party issues a demand notice. Furthermore, some security agreements will require that such default must also be continuing.

Parties are free to define "default" as they see fit. However, "default" under a security agreement will typically include non-payment of interest or principal and insolvency or bankruptcy of the debtor. If not defined in the agreement, a security agreement will often include a provision stating that terms used but not defined in the security agreement will have the meaning given to those terms under the Ontario *Personal Property Security Act*, where default is defined as follows:

the failure to pay or otherwise perform the obligation secured when it becomes due or the occurrence of any event whereupon under the terms of the security agreement the security becomes enforceable.
Section 1(1) of the Ontario PPSA[1]

Lesson Learned

Following an event of default under a security agreement, provide the debtor with prior written notice before taking enforcement action. Your lawyer can work with you to determine what notice period is reasonable.

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[1] Substantially same definition appears in every *Personal Property Security Act* (or equivalent) in all of the Canadian provinces (excluding Quebec).