

FILED
 3/12/13
 DATE: _____ TIME: _____ am/pm
 By: LMW
 CLERK, FSM SUPREME COURT
 KOSRAE
 TRIAL DIVISION

IN THE SUPREME COURT OF THE
 FEDERATED STATES OF MICRONESIA
 TRIAL DIVISION — STATE OF KOSRAE

FSM DEVELOPMENT BANK,)
)
 Plaintiff,)
)
 v.)
)
 TROPICAL WATERS KOSRAE, INC.,)
 CLAUDE PHILLIP, and RONALD BICKETT,)
)
 Defendants.)
 _____)

CIVIL ACTION NO. 2012-2003

ORDER GRANTING
 PRE-JUDGMENT POSSESSION

On May 30, 2012, the plaintiff, the FSM Development Bank ("Bank") filed its Application for Enforcement of Right to Possession through Prejudgment Order, along with an Application for Expedited Hearing, and supporting affidavits. The Bank is represented by Nora Sigrah, Esq. The defendants, Tropical Waters Kosrae, Inc., Claude Phillip, and Ronald Bickett (collectively "Tropical Waters") filed their Opposition to Motion for Prejudgment Order of Possession on June 11, 2012. The defendants are represented by Stephen V. Finnen, Esq. On February 26, 2013, the court heard the Bank's application. The hearing should have been held earlier on an expedited basis, 33 F.S.M.C. 1053(3), but was delayed in part because Tropical Waters raised the question of the court's jurisdiction and that was a matter of first impression that had to be addressed before the court could turn to the Bank's application. The application is granted in part. The reasons follow.

I. BACKGROUND

The Bank seeks the right to possess and sell or lease the collateral in this matter. A Chattel Mortgage Agreement was executed between the parties on February 26, 2004. The

agreement lists various equipment, vehicles, and machinery as the chattels¹ for security on the loan. A notice of security interest was filed at the FSM Secured Transactions Filing Office on November 29, 2006.²

Title 33 of the FSM Code governs various aspects of commercial law. Congress amended Title 33 through Public Law No. 14-34. Among the amendments were the repeal of sections 921 through 933 of Title 33, chapter 9 was renamed, and a new chapter 10 ("The Secured Transactions Act") was enacted (with sections 1001 through 1071), creating a statutory scheme to govern secured transactions. These amendments became law on November 4, 2005.

II. DISCUSSION

A. *The Secured Transactions Act's Effectiveness*

Tropical Waters opposes the Bank's the application and contends that it is unclear if this matter falls within the Secured Transactions Act's parameters because sections 1070 and 1071(3) state:

Section 1070. Effective date of this Act. This Act shall come into effect upon the date certified by the Department to the President of the Federated States of Micronesia as the date on which the filing office is prepared to perform the duties required in subchapter 3 of this Act.

Section 1071. Transactions concluded prior to effective date of this Act. This section applies to transactions concluded prior to the effective date of this Act that would be subject to this Act if this Act had been in effect at the time the transactions were concluded. In this section, such a transaction is referred to as "prior transaction."

¹ A list of these items is labeled attachment "C" in Plaintiff's Application for Enforcement of Right to Possession through Pre-Judgment Order.

² A copy of this document is listed as attachment "D" in Plaintiff's Application for Enforcement of Right to Possession through Pre-Judgment Order.

(3) A secured party under a prior transaction may file a notice of the property interest created by the prior transaction within sixty days of the effective date of this Act, in the same manner as provided for a notice of a security interest. The secured party shall deliver a copy of the notice to the debtor. If a notice establishes priority in a property right created in a collateral under a prior transaction, the priority of the property right over a perfected security interest under this Act shall be measured from the effective date of this Act.

On October 2, 2006, then Secretary of the Department of Economic Affairs ("DEA") Akillino Susaia transmitted a letter to then President Joseph J. Urusemal, certifying that the DEA was prepared to perform the duties as required under 33 F.S.M.C. 1070.³

On November 29, 2006, the Bank filed its Notice of Security Interest,⁴ in compliance with 33 F.S.M.C. 1071(3)'s 60-day requirement. By filing this Notice of Security Interest, the Bank has a Perfected Monetary Security Interest. 33 F.S.M.C. 1012(1)(a) and (2). Accordingly, since the Bank has met the section 1071(3) requirements, Title 33, chapter 10 governs this matter.

Additionally, FSM Civil Procedure Rule 64 outlines the procedure for the seizure of persons or property in civil matters. Rule 64 provides in pertinent part that:

At the commencement of and during the course of an action, all remedies providing for seizure of person or property for the purpose of securing satisfaction of the judgment ultimately to be entered in the action are available under the circumstances and in the manner provided by the law of the state in which the court is held, existing at the time the remedy is sought, subject to the following qualifications: (1) any existing statute of the

³ The Bank did not provide evidence on when the memorandum was transmitted to the President. However, through the court's independent inquiry, a copy of the memorandum was obtained confirming the date of transmittal.

⁴ Attached as "D" in Plaintiff's Application for Enforcement of Right to Possession through Pre-Judgment Order. An amendment to this document was filed on March 16, 2012.

Federated States of Micronesia governs to the extent to which it is applicable

....

The Secured Transactions Act is an existing, applicable FSM statute and thus, as noted by FSM Civil Rule 64(1), the Act [Title 33, chapter 10] governs the Tropical Waters transaction. The court notes that while Congress has the authority to amend rules by statute, FSM Const. art. XI, § 9(f), the Chief Justice does not have the authority to amend statutes by creating rules. People of Tomil ex rel. Mar v. M/V Mell Sentosa, 17 FSM Intrm. 478, 479 (Yap 2011); FSM v. Wainit, 12 FSM Intrm. 376, 383 (Chk. 2004).

B. Bank's Application for Pre-Judgment Order of Possession

The Bank seeks a pre-judgment order for possession of collateral under a Chattel Mortgage Agreement executed by the parties on February 26, 2004. Based on a promissory note executed on February 26, 2004, Tropical Waters was to make monthly payments of \$28,439 with interest for the first two years, then increasing to \$30,665 per month, with full repayment completed by February 25, 2015. On September 2, 2011, the debt was restructured to \$5,000 monthly payments beginning July, 2011 through June, 2012, and increasing to \$24,433.06 per month beginning in July, 2012 until the note is satisfied.⁵ Tropical Waters' last payment was January, 2012.

Because Title 33, chapter 10 applies, the court turns to 33 F.S.M.C. 1053, which confers on the court the authority to grant a secured creditor the right to possession of the collateral before final judgment. The statute specifically provides that:

If the court finds, after hearing, that it is probable that a default has occurred under the security agreement and that the secured party has a right to take possession of the collateral, the court shall enter a pre-judgment order

⁵ This document was signed on September 2, 2011, but refers to payments beginning in July, 2011.

granting the secured party possession of the collateral pending final judgment or further order of the court. The order may direct the debtor to take such action as the court deems necessary and appropriate so that the secured party may take possession.

33 F.S.M.C. 1053(3).

Here, based on the Chattel Mortgage Agreement's language and the Bank's court filings, the court finds that a default has occurred. The mortgage provides "[t]he occurrence of the following events shall constitute a default hereunder: Nonpayment, when due of any amount payable on the promissory note" Chattel Mortgage Agreement § 5 (Feb. 26, 2004). The Bank supports its claim of default through the affidavit of Sihna Lawrence, the Bank's Chief Financial Officer, and an attached printout showing the outstanding balance on the Tropical Waters loan. The filings show that the last payment made by Tropical Waters was on January 6, 2012, and, as of May 25, 2012, the outstanding balance is \$3,478,582.07.

The Bank's application contains a statement under oath verifying the existence of the attached security agreement and identifies two events of Tropical Waters' default. The Bank's application therefore complies with 33 F.S.M.C. 1053(1). As stated above, because the Bank has perfected its security interest by properly filing it with the FSM Secured Transactions Filing Office, and since Tropical Waters has defaulted on the loan payments, the Bank has, under 33 F.S.M.C. 1052, a right to take lawful possession of the collateral.

A mortgagee under the provisions of a chattel mortgage covering all the personal property of the insolvent may, on default, be entitled to take possession of the property and sell it to satisfy his claim. In re Hymes Buggy & Implement Co., 130 F. 977, 980 (W.D. Mo. 1904). In re Yale Exp. System, Inc., 370 F.2d 433 (2d Cir. 1966), the U.S. Second Circuit

Court of Appeals ruled that,

it does not matter whether the security agreement is in the form of a chattel mortgage or a conditional sales contract. In either case, the secured party has the right upon default by the debtor to take possession of the collateral (§ 9-503) and to sell, lease or otherwise dispose of it, applying the proceeds to the indebtedness (§ 9-504).

In re Yale Exp. System, Inc., 370 F.2d at 437. The language of Article 9, sections 9-503 and 9-504, as cited in the case above, mirrors 33 F.S.M.C. 1052 and 1054 respectively.⁶ Here, because the submitted documents indicate that Tropical Waters has defaulted on the loan by not making the required monthly payments, the Bank is entitled to take possession of the chattels that are collateral for the defaulted loan.

C. Collateral Subject to Chattel Mortgage Agreement

Tropical Waters questions what property the Bank may seek to possess. Def.s' Opp'n to Mot. for Prejudgment Order of Possession at 8 (June 11, 2012). The Chattel Mortgage Agreement, section 1 identifies the collateral as "Water Bottling Machines & Equipment (See Attachment "C")." "Attachment C" lists various "Machinery, Equipments, and Vehicles," as items subject to the agreement. However, attached to the Tropical Waters' opposition is the affidavit of Ronald Bickett, President of Tropical Waters Kosrae, Inc., who states that when the agreement was executed, there was no "Attachment C," and that he did not sign or approve such attachment. Aff. of Ron Bickett at 3 (June 11, 2012).

Since the court has determined that there is a valid security interest entered with the FSM Secured Transaction Filing Office, the analysis turns to the two documents filed with

⁶ When an FSM statute mirrors and appears to have been drawn from a U.S. statute, U.S. caselaw construing the U.S. statute may be consulted for guidance in construing the FSM statute. See *Estate of Mori v. Chuuk*, 10 FSM Intrm. 6, 13 (Chk. 2001); *Plais v. Panuelo*, 5 FSM Intrm. 179, 204 (Pon. 1991).

that office. On November 29, 2006, the Bank filed its Notice of Security Interest, listing the collateral as: "Water Bottling Machines, Equipments, Furnitures, Fixtures, Goods and inventories now in existing or hereafter acquired." On March 16, 2012, the filing was amended, and the collateral description lists the following:

- 1) Factory building;
- 2) Factory filling line;
- 3) 1992 Model Mazda Titan chassis No. WGLM-170038;
- 4) 1993 Toyota Hiace chassis No. YHB1-002044;
- 5) Chrysler Grand Cherokee (jeep) with chassis no. 1J4-GZ78Y4VY533401;
- 6) 2 diesel generators model no. Xc275 SAE;
- 7) Raw Water Storage Tank 20'x8x8' 6", 27,000 Litre capacity;
- 8) Air compressor 323/52/35 & all spare parts;
- 9) PET Resin PET GRADE BK-3180;
- 10) Sleeve wrapper model no. 65SSW35;
- 11) Labeling machine;
- 12) Water Bottling Machineries;
- 13) Electrical equipments;
- 14) Furniture;
- 15) Fixtures;
- 16) Goods;
- 17) and inventories now existing or hereafter acquired.

The items listed in "Attachment C" are identical to the first 11 items listed above. The last six items above are the properties listed in the November 29, 2006 filing. When the security interest was filed, all potential creditors, and Tropical Waters themselves, were put on notice that those items were deemed collateral in this transaction.

Tropical Waters contends that the Bank cannot obtain or does not have a perfected security interest in some or all of the listed items, particularly the factory building and the fixtures and any items listed only in the March 16, 2012 amended filing. The Secured Transactions Act "does not apply to: (a) the transfer of an interest in real property, except as provided with respect to fixtures, crops, timber to be cut, or minerals to be extracted

...." 33 F.S.M.C. 1003(3). Real property is "[l]and and anything growing on, attached to, or erected on it, excluding anything that may be severed without injury to the land. Real property can be either corporeal (soil and buildings) or incorporeal (easements)." BLACK'S LAW DICTIONARY 1337 (9th ed. 2009). The factory building is thus real property. Cf. 33 F.S.M.C. 1022(2) ("a security interest in ordinary building materials is unenforceable when the building materials are incorporated into real property"). For the Bank to have perfected a security interest in the factory building, the Bank would have had to have obtained a mortgage on the factory building (and presumably the land underneath it or an easement) and recorded that mortgage with the Kosrae Land Court. It does not claim to have done so. The Bank is therefore not entitled to pre-judgment possession of the factory building since the Bank does not have a perfected security interest in it under the Act.

Fixtures are "goods that are fixed to real property, or are intended to become fixed to real property in a manner that causes a property right to arise in the goods under the prevailing law." 33 F.S.M.C. 1002(18). Goods are "all things that are movable when a security interest attaches. The term includes fixtures" 33 F.S.M.C. 1002(19). "Readily removable factory machines, office machines, and domestic appliances are not fixtures." 33 F.S.M.C. 1002(18). They are goods. When a security agreement covers fixtures, the secured party may, if it chooses, proceed under the Act. 33 F.S.M.C. 1048(1)(a). The Bank is thus entitled to seek and obtain a 33 F.S.M.C. 1053(3) order for pre-judgment possession of the fixtures.

Since 33 F.S.M.C. 1006 states that a general description of the collateral is sufficient for purposes of this section, the general description in the November 29, 2006 filing is

sufficient to cover the items in the more detailed amended March 16, 2012 filing except for the factory building which, since it is real property and not a chattel, cannot be the subject of a perfected security interest under Title 33, chapter 10. Except for the factory building, the vehicles, and the inventory, the rest of the listed items would fit the general description as water bottling machines and equipment needed to produce bottled water and thus collateral subject to the Bank's security interest even if Attachment C was an illegitimate expansion of the Bank's security interests. The Bank is therefore entitled to immediate possession of the chattels in which it has a perfected security interest.

D. Assignment of Income and Exclusive Possession

The Bank also relies on an Assignment of Income and Exclusive Possession executed between the Bank and Tropical Waters Kosrae, Inc. (but not Phillip or Bickett) on February 26, 2004. That agreement provides that, in the event of a default, the Bank is "the sole and exclusive party entitled to possession of the subject property/premises and to operate the subject business and to receive all income therefrom." Assignment of Income & Exclusive Possession para. 4 (Feb. 26, 2004). It further provides that within sixteen days after the Bank serves notice of the default, Tropical Waters should vacate the premises and transfer all personalty and fixtures to the Bank and execute all necessary documents to do so. *Id.*

This right to possession and operation, although a security interest, is not a security interest that can be, or was, perfected under Title 33, chapter 10, because it involves real property—the factory building—and the incorporeal right to operate the business from that building. On its face, this is an executory contract for which there was an offer, acceptance, definite terms, and consideration. The Bank seeks to enforce the contract's terms since the

condition precedent, the borrower's default and notice thereof, has occurred.

The Bank contends that this contract has been breached because, although it served notice of the default, it has not been allowed to take possession of the premises and to (try to) operate the water bottling business. The Bank seeks specific performance of this agreement. The statute, 33 F.S.M.C. 1053, gives a secured party the right to pre-judgment possession of collateral — chattels — in which the secured party has perfected a security interest. It does not authorize the court to issue a pre-judgment order enforcing specific performance of a contract designed to give a lender further security in the event of a default or to issue an order granting the lender pre-judgment possession of property in which it does not have a perfected security interest and in which it could not perfect a security interest. It appears that any court order enforcing the specific performance of the February 26, 2004 Assignment of Income and Exclusive Possession must await a final judgment on the merits.

To the extent that the Bank's application seeks specific performance of the February 26, 2004 Assignment of Income and Exclusive Possession, the application is denied. The Bank may renew its motion to enforce this contract should the circumstances permit.

The February 26, 2004 Assignment of Income and Exclusive Possession also assigns to the Bank the right to Tropical Waters' income. This is an intangible property right in which the Bank could have perfected a security interest, 33 F.S.M.C. 1009 and 1002(4), but apparently did not. Since Tropical Waters lacks any income at present, the lack of a perfected security interest will not affect the court's present ruling. The Bank's right to Tropical Waters' income will await the resolution of the Bank's claim for specific

performance of the February 26, 2004 Assignment of Income and Exclusive Possession in a final judgment.

E. *Effect of Seizure of Property*

Tropical Waters also raises the issue of the Bank waiving a deficiency judgment should the Bank elect to possess the collateral. The Secured Transactions Act generally recognizes an obligor's liability for any deficiency. 33 F.S.M.C. 1058(4)(b) and (6). Furthermore, 33 F.S.M.C. 1053(6) provides:

Nothing contained herein shall affect the right of a secured party to proceed under sections 1405 and 1406 of title 6 of this Code at any time with respect to collateral or to bring any civil action for foreclosure in such manner as may be authorized under any other law.

Under 6 F.S.M.C. 1405 and 1406 the Bank also has the remedies of writ of attachment and release and modification. More importantly, 33 F.S.M.C. 1053(6) allows the Bank to seek a foreclosure action against a debtor's secured or unsecured property whether or not it has taken possession of the collateral.

In order for a creditor's seizure of collateral to be a waiver of the creditor's right to a deficiency judgment, that waiver ordinarily would have to be expressly provided for in the mortgage documents or in a statute. There is no such provision in the Tropical Waters mortgage or in a statute.


The Bank's possession of the Tropical Waters collateral will not constitute a waiver by the Bank of its right to proceed and obtain a judgment for any deficiency.

III. CONCLUSION

ACCORDINGLY, the Plaintiff Bank's Application for Enforcement of Right to Possession through Pre-Judgment Order is HEREBY GRANTED. The Bank shall, pending final

judgment or further court order, take possession of the properties listed in the March 16, 2012 filing with the FSM Secured Transactions Office except the factory building, the vehicles, and the existing inventory. The Bank shall proceed within the parameters set forth in Title 33, specifically in 33 F.S.M.C. §§ 1053 to 1061. Although the factory building is real property to which the Bank does not have a right to pre-judgment possession, the Bank must be afforded access to the building so that it may take possession of the chattels to which it does have a right of pre-judgment possession.

SO ORDERED the 12th day of March, 2013.


Dennis K. Yamase
Associate Justice

ENTERED this 12th day of March, 2013.


Linson Waguk
Assistant Clerk of Court