



SECURED PROMISSORY NOTE (DEMAND) & GUIDE

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Sample Secured Promissory Note (Demand)

1. Overview

Successful businesses are built on big ideas and long-range goals, but without sufficient capital, those dreams may never be realized. Limited start-up funds can stop a company in its tracks: business owners often underestimate the amount of money they will need to keep their organization running, and close their doors before they've had a chance to get a market foothold. Many owners also expect their companies to turn a profit on Day 1, failing to consider expenses, competition, and the time it takes to build a customer base.

Whatever the reasons, individuals and companies often must borrow money to keep their businesses afloat. They can turn either to large financial institutions or to friends, colleagues, and relatives for support. The enclosed documents may prove more useful for a company looking to borrow money from less formal sources, since commercial lenders may be reluctant to loan money to businesses without defined income streams and, moreover, will usually require businesses to use their standardized forms. Nonetheless, the sample form and instructions that follow may provide a good starting point for any person or business seeking information about loan terms and deal structures.

Borrowers who agree to sign secured notes may find loans more readily available to them. Lenders know that if a default occurs, they can sell the property used as collateral under the secured note. This protection may, in turn, make a borrower more comfortable with the loan arrangement. Nobody wants to default on a loan or force others to absorb losses on their behalf. With a secured note, you can be sure you're not leaving lenders – who may be colleagues or other individuals close to you – out in the cold.

This package contains everything you'll need to customize and complete your secured promissory note. A written note can minimize confusion, misunderstanding, and error, and clearly set forth the parties' expectations and fulfillment obligations. In every way, this promotes a successful and profitable business arrangement.

2. Dos & Don'ts Checklist

- Before sitting down to sign, decide exactly what your goals are for the note. How much will be borrowed? What interest rates will be applicable? A good agreement is one that captures the intentions of the parties accurately. Take a moment to clarify the terms and conditions of your loan before memorializing them in written form.
- Allow each party to spend some time reviewing the promissory note. This will reduce the likelihood, or at least the efficacy, of claims that a party did not understand any terms or know what their obligations were under the document.
- Both parties should review the note carefully to ensure that all relevant deal points have been included. Do not assume that certain expectations or terms are agreed to if they are not stated expressly in the document.

- The following form is a secured promissory note. This means that the lender takes a secured interest in the borrower's property. If the borrower defaults on the loan, the lender can seize that property almost immediately. By contrast, with an unsecured note, the lender would have to go to court to demand payment if a default occurred.
- In general, secured promissory notes are supplemented with and supported by security agreements. Those security agreements are what allow lenders to take property if a default occurs. The enclosed note assumes the existence of a security agreement, but that agreement is not included with this package.
- A security interest in property can (and should) be memorialized with a financing statement (more specifically, a document called a UCC financing statement). Once a financing statement is completed and filed with the correct governmental authority, the lender's interest in the property is considered "perfected." This means that if future lenders also seek a security interest in the same asset, the lender with the perfected interest would have top priority and could take the property for itself after a default.
- The enclosed document is also a demand note. This means that the lender can demand repayment of the loan at any time. This is a point that should be emphasized to the borrower – it may be required to pay back that loan on very little notice.
- Choose a fair interest rate. Although the enclosed note will "rewrite" any illegal interest rate to make it legal, it's a good idea to select a more reasonable number. This will decrease the chances of default and make for a less strained relationship between the parties.
- The parties should sign only the one original document, and that original should be given to the lender. Make at least one photocopy, make sure that the document says "COPY" in bold letters, and give the copy to the borrower. After the note has been paid in full, the lender should return the original document to the borrower.
- Depending on the nature of its terms, you may decide to have your note witnessed or notarized. This will limit later challenges to the validity of a party's signature.
- If your agreement is complicated, do not use the enclosed form. Contact an attorney to help you draft a document that will meet your specific needs.

3. Secured Promissory Note (Demand) Instructions

The following provision-by-provision instructions will help you understand the terms of your secured promissory note.

The numbers below (e.g., Section 1, Section 2, etc.) correspond to the provisions in the note. Please review the document in its entirety before starting the step-by-step process.

- **Introduction.** Identifies the document as a note. Write in the date on which the note becomes effective. Identify the parties and, if applicable, what type of organization(s) they are. Note that one party is called the “Payee” and the other the “Borrower.” As you may have guessed, the Borrower is the party that is borrowing money and will pay it to the “Payee.” The Payee may or may not be the same entity as the lender. Under some loan agreements, the lender requires the borrower make payments to a third party.
- **Section 1: Promise of Payment.** This is the “meat” of the note, where the total principal amount and interest rate are stated. This is also where the Payee designates where exactly it should be paid (usually the Payee’s business address). The other language ensures that the interest rates set by the parties aren’t illegal. In other words, if an agreed-to interest rate is above what the law allows, this section “rewrites” that provision to make it legal.
- **Section 2: Payment.** The parties’ agreement that the borrowed amount will be repaid immediately, whenever the Payee demands it.
- **Section 3: Prepayment.** Explains that the Borrower can pay money to the Payee before it is specifically demanded, and that there is no penalty for doing so.
- **Section 4: Security for Payment.** Ensures the Borrower’s repayment by listing certain property as collateral. Because this note contemplates the simultaneous signing of a security agreement, the details of the collateral arrangement are general. A security agreement should provide more details about the collateral pledged.
- **Section 5: Events of Default.** Lists the occasions on which the Payee can declare that a default has occurred under the loan. The first blank allows the parties to determine the amount of time the Borrower has to make its payment after the demand has been made. If you and the other party want to include additional events of default, you can do that in this section.
- **Section 6: Acceleration; Remedies on Default.** A description of the actions the Payee can take if an event of default (as listed in Section 5) occurs.
- **Section 7: Waiver of Presentment; Additional Demand.** Indicates that if an event of default occurs, the Payee doesn’t have to explain to the Borrower that it is going to take action. The Payee can simply take that action without further notice.
- **Section 8: Time of Essence (Optional).** This is an optional provision that is included to allow you and the other party to determine how strictly you want to enforce the time limits in your note. Generally, by including this provision the Payee is allowing the Borrower no leeway – if payment isn’t within the exact time agreed, the Borrower is in default. By deleting this provision, you are usually allowing the Borrower some reasonable breathing room. If you remove this section, correct the section numbers and references in the note.
- **Section 9: Successors and Assigns.** States that the parties’ rights and obligations will be passed on to heirs or, in the case of companies, to successor organizations.
- **Section 10: Notice.** Lists the addresses to which all official or legal correspondence should be delivered. Write in a mailing address for both the Borrower and the Payee.
- **Section 11: Governing Law.** Allows the parties to choose the state and county laws that will be used to interpret the note. This is not a venue provision: the included language will not impact where a potential claim can be brought. Please write the applicable state and county in the blanks provided.

- **Section 12: Entire Agreement.** The parties' agreement that the note they're signing is "the agreement" about the issues involved. Unfortunately, the inclusion of this provision will not prevent a party from arguing that other enforceable promises exist, but it will provide you some protection from these claims.
- **Section 13: No Implied Waiver.** Explains that even if the Payee ignores or allows the Borrower to break an obligation under the note, it does not mean the Payee waives future rights to require the Borrower to fulfill those obligations.
- **Section 14: Collection Costs and Attorney's Fees.** Places the responsibility for paying any costs of collecting money under the note on the Borrower's shoulders.
- **Section 15: Severability.** Protects the terms of the note as a whole, even if one part is later invalidated.
- **Section 16: Headings.** Notes that the headings at the beginning of each section are meant to organize the document, and should not be considered operational parts of the note.

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**SECURED PROMISSORY NOTE
(DEMAND)**

\$ _____ [Amount of Note]

This promissory note (the "Note") is made and effective _____ [Date], by and between _____, an [individual] [corporation] [limited liability company] [etc.] (the "Borrower"), and _____, an [individual] [corporation] [limited liability company] [etc.] (the "Payee").

1. PROMISE OF PAYMENT.

FOR VALUE RECEIVED, the Borrower promises to pay to the Payee, at _____ [Address], _____ [City], _____ [State] _____ [Zip Code], or at such other place as the Payee may designate in writing from time to time, the principal amount of _____ Dollars (\$ _____), together with interest accruing on the unpaid balance thereof until due. The interest rate on this Note shall be an annual rate of interest equal to [Rate] ([Rate]%) percent, or the maximum amount allowed by applicable law, whichever is less. Interest shall be computed on the basis of a year of 365 days and the actual number of days elapsed.

2. PAYMENT.

The entire principal balance, including any accrued interest, shall be immediately payable **UPON DEMAND**.

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