



# Bernie's Brainers

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## CONSIGNMENTS AND COLLECTION

Over the past year we have been asked on a number of occasions about consignment sales. This allows a creditor to put merchandise in a warehouse or large vendor's wholesale warehouse with the idea they will be paid when sold. Title does not pass to the vendor so in the event the customer files for bankruptcy you will have access to your goods.

In many instances, creditors intend the consignment arrangement to be a security device to increase the likelihood of payment from a financially distressed customer. However, all too frequently, consignment vendors belatedly discover that they failed to satisfy all of the requirements for obtaining a special protected interest in their consigned goods, and end up being relegated to the status of general unsecured creditors in their customer's bankruptcy case. A common error is the consignor's failure to file a UCC financing statement describing the goods in the required jurisdiction.

### WHAT IS A CONSIGNMENT?

In a consignment transaction, the seller is the consignor, and the prospective purchaser is the consignee. The consignor retains title to the goods following delivery to the consignee. The consignee may hold the goods for sale or use the goods, such as converting the goods to a finished product for sale. The consignee obtains title to the consigned goods upon the consignee's use or sale of the goods. The consignor usually issues an invoice, containing the payment terms, to the consignee after the consignee's reported sale or use of the goods. If the consignee cannot sell or use the goods, the consignee can often return them to the consignor.

The terms of a consignment arrangement are frequently governed by a written agreement between the consignor and consignee. The agreement should contain all of the necessary terms and conditions to protect a consignor's interest in consigned goods. Consignments are also governed by each state's Uniform Commercial Code ("UCC").

UCC Article 9 governs most consignment transactions. UCC Section 9-102(a)(20) defines a consignment as a transaction in which a person delivers goods to a merchant for purposes of sale, and (a) the merchant deals in goods of that kind under a name other than the name of the person making delivery, is not an auctioneer and is not generally known by its creditors to be substantially engaged in selling the goods of others; (b) the goods must have a value of at least \$1,000.00 at the time of delivery; (c) the goods are not consumer goods immediately before delivery; and (d) the transaction does not create a security interest.

Bottom line: for most consignment arrangements, a consignor must comply with Article 9's requirements for obtaining a perfect interest in its goods and protecting its interest from competing secured creditors and lien creditors, including the consignee's bankruptcy trustee. That includes a proper consignment agreement between the consignor and consignee and filing a UCC-I financing statement describing the consigned goods in the jurisdiction where the consignee is located. And under Article 9, the consignor could file a UCC on its own, *without the consignee's signature*, as long as there is a consignment agreement executed or otherwise authenticated by the consignee that describes the consigned goods. The consignor uses the same UCC form that a secured creditor uses in perfecting a security interest in personal property collateral. The UCC form also allows the consignor to identify the existence of a consignment transaction. And the consignor must do more to obtain a priority interest in the consigned goods over the rights of the consignee's secured creditor with a prior floating security interest in the consignee's inventory. UCC Section 9-103(d) states that a consignor has a purchase money security interest in its consigned goods. As such, the consignor would have priority over a prior floating security interest in the consignee's inventory if the consignor satisfies all of the following requirements for a valid purchase money security interest contained in UCC Section 9-324: (a) perfection of the consignment interest prior to the consignee's

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possession of the goods; (b) dispatch of an authenticated notification to the holders of conflicting security interests in the consignee's inventory that states that the consignor has, or expects to, acquire a consignment interest in the goods and describes the goods; and (c) receipt of the notice by the holders of conflicting security interests in the goods within five years before the consignee's receipt of possession of the



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goods. Otherwise, the consignee would be behind the prior perfected floating lien secured creditor.

#### Conclusion

A consignor seeking to protect its interest in goods consigned to a financially distressed debtor needs a consignment agreement that contains all of the necessary 'bells and whistles' to protect the consignor's interest in the consigned goods. And, most important, the consignor should file a UCC financing statement, describing the consigned goods, in the state where the debtor is located in order to protect the consignor's interest in the goods from the risk of the consignee's bankruptcy filing and the consignee's bankruptcy trustee's avoidance of the consignment.

Special thanks for excerpts of this article provided by Bruce Nathan of Lowenstein, Sandler PC in NY

### Bernie's Brainers

E-mail your answer to Bernie's Brainers to [bkurzdorfer@commercialcollection.com](mailto:bkurzdorfer@commercialcollection.com) or fax to (800) 873-5211

A palindrome is a word or phrase that reads the same backward as forward, such as "Madam, I'm Adam." The following two palindromes are more difficult, but not impossible. Word divisions are shown:

A zookeeper announces that he has captured two fewer than a dozen beasts by hitting them hard with a reticulated object and putting them inside it.

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Spoiled children of performing luminaries:  
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#### **Answer to last Bernie's Brainers:**

You have fifty coins totaling \$1.00. You drop one down an open drain while tossing the coins in your hand. What is the chance that you have lost a quarter? Explain.

There are two ways you can have fifty coins totaling \$1.00: two dimes, forty pennies, and eight nickels; or two dimes, forty-five pennies, two nickels, and one quarter. These arrangements are equally probable, so there is a one-half chance you had a quarter to begin with. The probability that you then dropped a quarter from all the coins in your hand is one fiftieth. Therefore, the total probability that you lost a quarter is one half times one fiftieth or one one-hundredth.

### Do you hunt bear without a gun?

By: Bob Ingold, President

Preference Hunting; how many of us have encountered the dreaded preference months and sometimes years after the payment was made. We all know the scenario; through diligent collection work we have bailed our company out of a big loss just before the offending debtor files for bankruptcy. We breathe a sigh of relief we weren't "taken" for more money like our competitor and go on to the next project.

Then the letter arrives from the law firm; "You are hereby directed to return \$22,000 that you received from company a-z or risk a lawsuit. Your heart sinks and management either directs you to pay it or hires an expensive bankruptcy attorney to defend, analyze and charge almost as much as the preference payment itself.

Now there is a new choice available. Commercial Collection has entered into an agreement with a Chicago preference company that assists you in defense, analysis and negotiation. The fee is strictly contingent and it allows you to deal with preferences without the high costs and worry that is associated with this endeavor. The next time you encounter a large preference and need an alternative to expensive legal fees and large checks being written, call or email Bob Landel at Commercial Collection and we will assist you with your preference defense. (800-873-5212 ext. 252 or [blandel@commercialcollection.com](mailto:blandel@commercialcollection.com)). I know the title is a bit misleading but the next time a high price law firm comes after your money think of it as trying to hunt a bear without a gun. You need the best tools available in this situation and we can help.

**For more information or to place a claim, please contact us at:**

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