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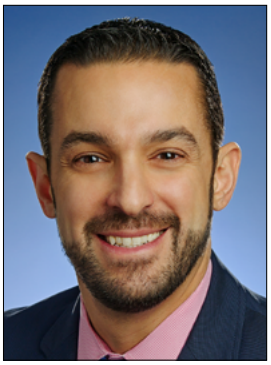
CONTENTS



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Attention, Sellers of Goods on Credit: A "Retention of Title" (Eigentumsvorbehalt) is Not Sufficient Under U.S. Law, and the U.S. Equivalent is Changing

When a company sells goods on credit in Germany, it usually retains title in the goods until payment has been made in full (Eigentumsvorbehalt). But, when a German company sells goods on credit to a buyer in the U.S., it cannot assume that it will be protected in the same manner. Rather, if the German seller ships goods to the buyer in the U.S. before full payment has been made, it runs the risk of losing title to the goods if the buyer becomes insolvent. The law in the U.S. does not recognize a retention of title as a matter of course – rather, the seller must take certain affirmative steps to protect itself before shipping its goods to the buyer. The precise requirements of the protection are a matter of state law, and the state of New Jersey recently issued a noteworthy amendment to its law on this issue.

The Law in the U.S.

In the U.S., sellers of goods on credit can obtain a security interest in the sold goods under Article 9 of the Uniform Commercial Code (UCC). A version of Article 9 of the UCC has been adopted in all 50 states and Washington, DC; however, there are some differences among the jurisdictions. A security interest under Article 9 of the UCC requires two things – "attachment" and "perfection." One method of satisfying a critical element of "attachment" is to have express language in a written contract between the seller and the buyer granting the security interest. Perfection of a lien on goods may be accomplished with the filing of a Form UCC-1 financing statement, generally with the Secretary of State of the state where the buyer entity is incorporated or organized. Filed financing statements are publically available, survive for an initial period of five years, and can thereafter be renewed.

In general, a secured party will conduct a UCC lien search to determine whether there are existing perfected security interests filed against the debtor with regard to the collateral in question. This is important, as, between competing security interests in the same collateral, "first to file" usually governs the priority of the security interests. However, a seller of goods on credit can also obtain a purchase money security interest (PMSI), which provides a higher priority interest over competing creditors in the same collateral, even if the other creditors' competing security interests were recorded first. Simply put, a PMSI is a super priority security interest in goods in favor of the creditor who has financed the purchase price of the goods.

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The requirements to obtain a PMSI differ depending on whether the security interest is in "inventory" or "equipment." For example, a PMSI in inventory requires, without limitation, notification to the holders of conflicting security interests prior to delivery of the goods. In contrast, a PMSI in equipment must merely be filed within 20 days after the transfer of the goods to be perfected, without any such notice requirement. Inventory under Article 9 of the UCC refers to specific goods purchased for resale or further processing, whereas any other goods generally are deemed to be equipment.

Recent Changes in New Jersey

Although Article 9 of the UCC is largely the same throughout the different jurisdictions, a recent change in New Jersey is worth noting. Specifically, New Jersey adopted a change to Article 9 of its UCC to address fraudulent UCC and lien filings being made against judges and court personnel. There are two primary changes that may impact how liens are perfected in New Jersey. The first change arguably requires a secured party or representative to use its proper legal name or a filed (in New Jersey) trade name on the Form UCC-1 (as opposed to an unfiled trade name or DBA). The second change alters the requirements for the indication of the collateral in N.J.S.A. § 12A:9-502(a)(3). Under the new law, the Form UCC-1 must indicate not only the collateral covered by the security interest, but also that "the collateral is within the scope of this chapter."

Conclusion

Similar to a retention of title in Germany, a filed security interest or PMSI pursuant to Article 9 of the UCC is an effective means of creditor protection. However, a seller must ensure that it complies with the requirements of Article 9 of the UCC in the relevant U.S. jurisdiction.

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