



Extending Credit or Providing Inventory to Foodservice,
Beverage, or Hospitality Industries?

**FILE UCCs TO PROTECT
YOUR BOTTOM LINE**

| HIGH RATE OF FAILURE

Supplying goods, equipment, or services to the foodservice, beverage, or hospitality industries, means you face unique credit challenges. File UCCs to protect your company's financial interests.



"Various studies estimate that among the 60% of operations that fail within the first three years, 44% failed the first year, 33% within the second year, and 23% in the third year."

- Christine Letchinger,
professor at Chicago's Kendall College

If you're supplying goods, equipment, or services to the foodservice, beverage, or hospitality industries, you are faced with a unique set of credit challenges. The most common challenge?

The high rate of company failure.

According to data collection by Statistic Brain, the top 3 reasons companies in these industries fail are incompetence, unbalanced experience or lack of managerial experience, and lack of experience in line of goods or services.

46%

fail due to "**incompetence**," which includes emotional pricing, lack of planning and inexperience with recordkeeping / financing.

30%

fail due to "**unbalanced experience or lack of managerial experience**," which includes inadequate borrowing practices and poor credit granting processes.

11%

fail due to "**lack of experience in line of goods or services**."

HOW YOU CAN PROTECT YOUR COMPANY

Creditors actively and aggressively implement UCC filings for security.

Article 9 of the Uniform Commercial Code (UCC) provides an opportunity for trade creditors to secure goods and/or accounts receivable by leveraging the personal property assets of their customer as collateral.

Properly perfected security interests via UCCs will mitigate (though not eliminate) risk.

UCCs are a form of consensual security, which means your customer must grant you the security interest.

Creditors often include security language within their credit applications and establish standard business practices by always obtaining a signed Security Agreement.

UCCs are a basic risk mitigation tool; they are a low-cost solution, requiring nothing more than a signature from your customer.



"Article 9 created a system where we establish priority of a creditors' claims in the event the business must be dismantled due to failure. It also created a system of public registration of these encumbrances, allowing potential lenders to search against a business to see how many encumbrances there are and the nature of those encumbrances."

*- Jerry Bailey
Executive Sales and Education Services Manager, NCS Credit*

WHICH UCC FILING IS RIGHT FOR YOUR BUSINESS?

There are a variety of UCC filings available. Determining which UCC filing is right for your business may be a challenge. Let's take a look at four types of filings and how they could fit into your business model.

BLANKET FILING

A Blanket filing is a security interest in all assets of your customer on a non-priority basis, eliminating potential conflict with your customer's primary lender. (Think of it as a blanket that lays down over all customer assets.)

The priority or payout in a bankruptcy is determined by the filing date (first in time, first in right). Blanket filings are popular among those supplying to restaurants, as they are most commonly used in situations when your customer "consumes" or otherwise does not stock your goods.



PMSI FILING

A Purchase Money Security Interest (PMSI) filing provides the same benefits as the Blanket filing but gives you priority of repossession of specific identifiable goods, primarily inventory or equipment that your company would provide.

Inventory or Equipment? It depends on what your customer is doing with the goods you provide. If you sell goods to your customer and your customer intends to resell them to other entities, then your goods would be considered inventory. Within the food/beverage/hospitality industries, we don't often see creditors using inventory filings.

PMSI in Equipment filings are much more common in the food, beverage, and hospitality industries.

Creditors who would benefit from a PMSI in Equipment would supply items like copy machines, beverage dispensing machines, flatware, ice machines, stoves/hoods and walk-in coolers; equipment your debtor would keep, use in their ordinary course of business and not re-sell.

FIXTURE FILING

There are circumstances where a Fixture filing may be more appropriate than an Equipment filing. To take it one step further, there may even be occasions where securing mechanic's lien rights would be better than a Fixture filing.

In the foodservice industry, fixtures could include ranges, ovens, coolers, sinks, dishwashers, and external signage. Notice the overlap? How can a cooler be a piece of equipment and a fixture? Based on the definition under Article 9, a fixture is anything that is "so related to a particular property."

What are fixtures? Fixtures are "goods that have become so related to particular real property that an interest in them arises under real property law". -- Article 9-102(41)

What is a Fixture filing? A Fixture filing is "the filing of a financing statement covering goods that are or are to become fixtures and satisfy[ing] Section 9-502(a) and (b). The term includes the filing of a financing statement covering goods of a transmitting utility which are or are to become fixtures." -- Article 9-102(40)

Fixtures are "goods that have become so related to particular real property that an interest in them arises under real property law".



The key is "so related," which indicates the item isn't permanent, but is still physically attached to the real property. You will likely notice a theme here: fixtures are secured to the building or premises but can be removed, if removal won't impact the structural soundness of the building or property.

If we look closer at the differentiation of a cooler being a piece of equipment versus a fixture, the answer is gray at best. If the equipment is affixed to the floor or walls, yet is still removable, it could be considered a fixture.

For example, a cooler that has been bolted to the wall and secured to the floor, like a walk-in cooler, would likely be a fixture. Whereas, a display cooler that holds soda, (those that you often see in grocery stores at the checkout line), can easily be moved as needed.

CONSIGNMENT FILING

There are two types of consignment (scan-based trading): **Sale or Return and True Consignment.**

Sale or Return: where goods are delivered to the consignee primarily for retail purposes.

In this type of consignment, title passes to the consignee upon delivery, but the consignee remains contractually obligated to return any unused goods.

True Consignment: where the goods are delivered to be primarily used by the consignee, but the consignor retains title to the goods.

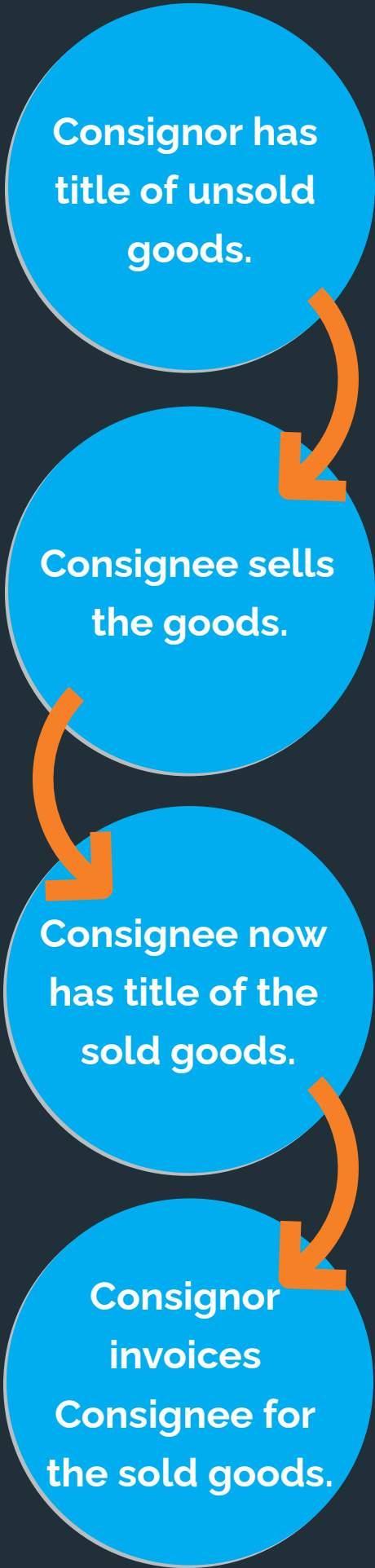
The consignee may either be pulling goods from stock on an as needed basis, or might be testing out goods on a trial basis to determine the necessity of the goods.

How Does True Consignment Work?

The consignor/owner retains title to the delivered goods, while the consignee/recipient holds and attempts to sell the goods.

If/When those goods are sold, the owner's security attaches to the proceeds of the sale. If the consignee is unable to sell the goods, they can simply return the goods to the owner.

This falls right into scan-based trading. Grocery stores are a great example of scan-based trading. A creditor provides a grocery store with an inventory of goods. Until those goods are scanned at the counter, the title to those goods remains with the creditor.



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graph TD; A((Consignor has title of unsold goods.)) --> B((Consignee sells the goods.)); B --> C((Consignee now has title of the sold goods.)); C --> D((Consignor invoices Consignee for the sold goods.))
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Consignor has title of unsold goods.

Consignee sells the goods.

Consignee now has title of the sold goods.

Consignor invoices Consignee for the sold goods.

WHAT IF YOUR CUSTOMER SELLS THEIR BUSINESS?

In addition to securing your goods, equipment, and services, the public record of the UCC filing can protect you in the event your customer sells their business.

Unfortunately, quickly (and quietly) exiting businesses, and the buying and selling of businesses is common, especially restaurants. Fortunately, UCC filings can act like a security system.

Let's say your customer sells their restaurant; often, there is language within the sale of the business that relieves the buyer of any responsibility from the previous business owner's debt. Ultimately, erasing debt linked to the business becomes a condition of the sale of the business.

Enter your filed and perfected UCC. Your UCC filing acts as a lien on the business, therefore, before title passes from one party to another, the lien should be acknowledged and either settled or renegotiated.



"USF has a long-time customer with several restaurants. The customer is a high-volume account with annual sales exceeding \$2M. The credit worthiness of the customer remains unknown as the division does not have financials, only their payment history.

The Credit Team pursued UCC's on all locations to help mitigate risk last year. We were notified that the customer was selling a location which, at the time, had an AR in the mid six figures, all of which was past due. After their attorney did their due diligence, they noticed a lien on the business which prompted a call from the seller inquiring about the UCC. Around the same time, the attorney reached out and asked what was needed to lift the lien. The answer was simple, a lump sum check for the entire balance of \$154,000. The sale took place and our Credit Manager was contacted by the attorney who had the check in hand for the full amount. Had we not had the UCC filing in place, we would not have received this payment and very likely, only cents on the dollar.

The end result was a very good month for the division from a performance perspective based on this recovery. This success paid for the cost of filing previous UCC's and future UCC filings for years to come. This was definitely a win when looking at the cost benefit/ROI for securing our receivables with the UCC process and utilizing the services of NCS Credit."

- Division Credit Manager, US Foods, Inc.

| SECURED CREDITOR SUCCESS



SECURED CREDITORS RECOVERED 100%

Secured creditors do get paid, although every bankruptcy exit plan is different.

In the Hostess Brands Inc. bankruptcy, **secured creditors received 100%** of their claims, while **unsecured creditors received 0%.**

Unsecured creditors received 0%

In the Buffets, LLC bankruptcy, **secured creditors received 100%** of their claims and **unsecured creditors received 5%.**

In the Quaker Steak & Lube bankruptcy, **secured creditors to receive 100%** of their claims and **unsecured creditors to receive 60%** of their claims.

Disclaimer: In larger Chapter 11 re-organizations the secured creditor may receive stock options or another form of payment instead of money



"Recently, we were able to enforce our inventory lien in a high profile bankruptcy case. NCS Credit made all of the proper notifications when filing the lien and this placed our position as high as the lender and the floorplan company. The net result was payment in full for a low 6 figure balance. Using NCS Credit provides the peace of mind of knowing that the proper procedures are being followed to validate our secured positions."

- Credit Manager, Onkyo

If you are not securing your rights through UCC filings, you are taking an unnecessary risk and allowing your company to be competitively disadvantaged.

UCCs are more than risk mitigation. UCCs give you an opportunity to expand your market and increase sales, by providing you with the security needed to sell to marginal accounts and increase existing clients' credit lines.

Ready to secure your right to get paid? Contact NCS Credit today!



SAVE TIME. SAVE MONEY. GET PAID FAST.

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