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Crop Financing and Article 9: A Dialogue with Particular Emphasis on the Problems of Florida Citrus Crop Financing

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CROP FINANCING AND ARTICLE 9: A DIALOGUE WITH PARTICULAR EMPHASIS ON THE PROBLEMS OF FLORIDA CITRUS CROP FINANCING

PETER F. COOGAN* AND C. PARKHILL MAYS, JR.**

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This article reconstructs and expands conversations initiated at a seminar in New Orleans when a Florida attorney asked various questions as to the effect of article 9 upon the financing of the citrus industry. The seminar was presented by the ALI-ABA Joint Committee in February, 1967. The authors have not limited themselves to either the specific questions or the answers suggested at the New Orleans meeting.

I. ARTICLE 9 IN GENERAL

Mr. Mays: Florida has only recently adopted the Uniform Commercial Code (UCC). Florida attorneys are concerned as to how the Code is going to adopt to or change the practices of lenders and borrowers in the citrus fruit industry. There are other problems, of course, but, apart from the special problems of financing cattle, the citrus industry seems to present more problems in a concentrated area than do other commodities raised in Florida. With these thoughts in mind, Mr. Coogan, could you give us a brief introduction and history of article 9, with particular reference to the special rules applicable only to "farm products."

Mr. Coogan: In general article 9 merges into one body of law most of the rules and doctrines governing security interests created by contract which, prior to the UCC, were found in the separate statutory and case law of the pledge, chattel mortgage, conditional sale, statutes governing inventory liens in the form of trust receipts, field warehousing, so-called factors liens, statutes and common law governing assignments of ac-

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counts receivable, other rights under contracts, and some other intangibles. Because the division of chattel security law into these bodies was largely historical, at an early state in the drafting of article 9 it was contemplated that the law be restated, not in terms of the security device employed, but in terms of what were thought to be separable problems, such as those facing the financier of consumer goods—those purchased primarily for individual or family use; those facing the financier of “equipment”—goods purchased primarily for use by business entities; or those faced by one who financed “inventory”—goods held for sale or lease. It was thought that “farm products” were sufficiently different from these other categories to require separate treatment. However, when the rules were put together in this manner it was found that the similarities greatly out-weighed the differences. Hence, now only vestiges of the idea of separate sets of rules based upon the type of collateral can be found. They remain in the special treatment given particular kinds of collateral in certain sections. One such vestige relates to “farm products.”

Mr. Mays: Does the Code cover all contractual security interests in personal property or fixtures?

Mr. Coogan: Article 9 governs most but not all transactions involving personal property security. Your question already eliminates a substantial number of liens—those which are not created by contract but are rather imposed by statute, usually over the objection of the obligor.¹ Further, article 9 is wholly or partly inapplicable to a number of security interests created by contract. In the first instance, federal law controls to a greater or lesser extent such matters as are governed by the Copyright Act or the Federal Aviation Act or the Ship Mortgage Act. State law also governs special areas of contractually created security interests. For instance, security interests in motor vehicles are governed to a greater or lesser extent by non-uniform certificate of title laws, and consumers are protected by varying special police type statutes.² Of course the Code does not affect real estate mortgages as such, but this does not mean that the real estate lawyer can disregard a knowledge of article 9. Chattels attached to the land in a certain manner—fixtures and crops—become subject to certain claims by the owner of interests in the real estate, and crops produced by trees which are real estate become subject to chattel interests.

Mr. Mays: The confrontation of new UCC law and the old real estate law is perhaps responsible for many of the questions on the applicability of the Code to crop financing.

Mr. Coogan: Problems are quite common when these two bodies of

1. Uniform Commercial Code §§ 9-102, 9-104 (hereinafter cited as U.C.C.).

2. U.C.C. §§ 9-201, 9-203.

law collide. We cannot give much time to the special problems of fixtures, but we will, of course, discuss this real estate-UCC problem as it relates to crops. But before we get into that question I would like to spend a few more minutes on the general framework of article 9.

Within article 9 most security transactions are governed by the same set of rules. There can be no security interest in a particular item of collateral enforceable even between the parties unless and until the last of three simple requisites has been satisfied: (a) the debtor has signed a security agreement which reasonably describes the collateral, or in the alternative he evidences the agreement by surrender of some particular collateral (the pledge), (b) the secured party gives "value" (ordinarily by furnishing goods not yet paid for or by advancing money to be repaid), and (c) the debtor owns or later acquires some rights in the collateral.³ The security interest which has "attached," is not generally good against third parties unless and until public notice has been given,⁴ most generally by filing in a public office, sometimes by surrender of possession of the collateral of the secured party or his agent. In designated situations (*e.g.*, a purchase money security interest in consumer goods) public notice is excused.⁵ In certain other cases, public notice may be temporarily excused—*e.g.*, for ten days in purchase money security transactions.⁶ When requirements (a), (b), and (c) are met and public notice is given or excused, a security interest is said to be "perfected."⁷ The giving of public notice may be the first, the third, the second, or the fourth step. The time of filing and the time of "perfection" will thus be the same only where filing is the last of the four steps.

But a perfected security interest may be of little value unless the prior steps have been taken in such a manner that this particular security interest has priority over other possible security interests. To be entirely safe, a lender should not make his advance until after a search of the records, made at the same time that he files for himself, discloses that there is no other security interest ahead of his. Because of the peculiarities of the "first to file rule," which we shall mention later, he must also be assured that there is on record no financing statement with respect to the same class of collateral under which there could be a later security interest which would jump ahead of his present security interest.

Particular problems arise where the security agreement relates to collateral which is not in existence, or at least is not owned by the debtor at the time that he enters into a valid security agreement. The Code clears up much confusion in the law of some states with respect to the

3. U.C.C. §§ 9-203, 9-204.

4. U.C.C. §§ 9-303, 9-301.

5. U.C.C. §§ 9-302(1)(c)-(d).

6. U.C.C. § 9-304.

7. U.C.C. § 9-303.

status of after-acquired property. It does not say that a Florida crop financier obtains a present security interest in a crop which will be acquired by his debtor three years from now when that years' blossoms first appear. But it does say that if and when the debtor acquires this item of collateral which fits within the description of the collateral covered by the security agreement, the debtor's interest, whatever it may be, will automatically fall under the existing security agreement without any further documents being executed. Property acquired within four months of bankruptcy may create problems under the National Bankruptcy Act over which the Code has limited effect.^{7a}

Here we might mention a problem sometimes involving acquisitions of future property. Prior to the Code many states had the rule that where the secured party allowed the debtor to deal with the property too freely (which usually meant freedom to sell the collateral without strict accountability in applying the proceeds) the mortgage was fraudulent as a matter of law. This is the familiar doctrine of *Benedict v. Rattner*,⁸ The Code permits the debtor and the secured party to make any agreement they may wish with respect to the degree of dominion which the respective parties are allowed to exercise over the collateral. The secured party will, of course, continue to lose his collateral where his trust in the debtor was misplaced, but he will no longer lose it because of his having so trusted the debtor, without regard to what the debtor did with that trust.

Article 9 also contains provisions which permit the parties to provide for future advances. Future advances made under the earlier filing take priority over intervening advances protected by a later filing. Article 9 is not so clear as to the priority of the security interest created with respect to those advances in some other cases. The common situation is where a third party claims that between the time of the first advance and the second advance he has obtained a security interest perfected by a method other than filing or has obtained a lien by attachment or other legal process on the collateral in question.

In general article 9 makes it easier to create security interests than it was under the old law, but this very ease probably makes necessary a more complicated system of priorities.

Mr. Mays: Mr. Coogan, the problems which Florida attorneys will now encounter under the Code are not all new. Some were in a very unsettled status prior to the enactment of the Code. Of course, in many instances existing Florida law will lay the predicate for the solution under the Code. Aside from these questions which we shall discuss at a later time,

^{7a.} See generally Note, *After Acquired Property Security Interests in Bankruptcy: A Substitution of Collateral Defense of the U.C.C.*, 77 YALE L.J. 139 (1967).

^{8.} 268 U.S. 353 (1925).

why do you feel that a discussion such as this on the application of article 9 rules to farm security transactions is necessary?

Mr. Coogan: The rules which we have touched upon so far apply to all collateral and to all secured parties, but there are some important variations. It is often said that details as to compliance (*e.g.*, place of filing) and the effect thereof (*e.g.*, rights of certain buyers) may vary with the character of the debtor or the nature of the collateral. It would, perhaps, be more accurate to say that in the great bulk of the cases, rules will vary not so much with physical differences in the collateral but rather with the manner in which it is used. A hi-fi system purchased "on time" by a farmer is "consumer goods"⁹ (as to which no filing may be required¹⁰ and subject to one rule as to rights of buyers)¹¹ if purchased primarily for his own or his family's use. The same hi-fi system is "equipment" (subject to a different rule as to filing and as to rights of buyers) if it is purchased primarily for use in his milking parlor room to keep his cows contented.¹² Since neither item of consumer goods or equipment was purchased primarily with an eye to resale and neither is so held out to the public, no special rules are necessary to protect buyers—they take only the interest the seller then has—that is, subject to any existing security. A farmer's financier is like the financier of any other person when his debtor acts in a nonbusiness capacity (when the farmer gives him a security interest in "consumer goods").

But the Code continues what was probably the majority pre-Code view in treating the farmer-businessman's financier more favorably than the financier of the non-farmer businessman when the collateral consists of goods destined for sale by the farmer in the ordinary course of his business. Further, the Code, in refining the concept of "products" (9-315) may increase the protection heretofore given to the farmer's financier at the expense of the farm products processor. Some of the problems which we shall discuss grow out of the Code's prescription of different rules for different debtors—*i.e.*, businessmen who operate farms and businessmen who operate businesses other than farms. Should a security interest in wheat stored in a farmer's bin be subject to different rules as to "buyers in the ordinary course" than those which apply to the same buyer if he purchases from the operator of a grain elevator?

This difference in the rules based on the fact that one debtor may be a farmer while another may not is one of the reasons why this discussion is important. It so happens that the sponsors of the Code were unsuccessful in enlisting the aid of anyone with a technical knowledge of farm financing comparable to knowledge of other business financing supplied

9. U.C.C. § 9-109.

10. U.C.C. § 9-302(d).

11. U.C.C. § 9-307.

12. U.C.C. § 9-302.

by some of the advisors to the draftsmen. Since article 9 is now under a long-range re-examination by the sponsors it is hoped that discussion like this may stimulate contributions by those knowledgeable in farm financing.

But other reasons require special treatment of Code security interests created in the operation of farming. In addition to article 9's wise or unwise special rules which apply only where the debtor is a farmer, there are other problems which complicate farm finance. Both livestock and growing crops present, in acute form, familiar problems of obtaining a security interest in property not owned by the debtor, and often not in existence, at the time the debtor signs his security agreement. And farm financing, like inventory financing problems of other businessmen, presents the usual problem of advances that must be made from time to time after that security agreement is made. Farm equipment which is attached or affixed to the land presents all the usual fixture problems. In addition, farm finance is likely to present two problems not commonly found in other nonbusiness financing: (1) when are security interests in crops governed by real estate law and when by the Code, and (2) what are the priorities in conflicts between contractually created Code security interests and liens created by statute in favor of those who supply services or materials in the growing of the collateral?

We should first make clear that article 9 has gone a long way towards establishing a rational chattel security system. Experience over a number of years in a number of states testifies to its general workability. The question is not whether it has gone too far in changing pre-Code law, but whether, in fact, it has gone far enough. While in isolated instances article 9 may have adopted a rule less workable than the pre-Code law of a particular state, there is no general demand for a retreat to the old ways. If the real accomplishments of article 9 are not repeated here, it is only because its praises have been well sung in the past.

II. SPECIAL TREATMENT FOR FARM PRODUCTS:^{12a} REASON AND NON-REASON IN SECTION 9-307

Mr. Mays: Mr. Coogan, perhaps the most unusual provision of the Code distinguishing the farmer from any other non-farmer businessman is Section 9-307 which allows the buyer in the ordinary course of business to take free of a security interest perfected by his seller, although he knows of it, while denying such protection to the buyer of farm products

12a. The better discussions on farm products financing include the following: Clark, *Some Problems in Agricultural Lending Under the UCC*, 39 U. COLO. L. REV. 352 (1967); Note, *Secured Interests in Growing and Future Growing Crops Under the Uniform Commercial Code*, 49 IOWA L. REV. 48 (1964); Smith, *Security Interests In Crops*, 10 HASTINGS L.J. 23, 156 (1958); Coates, *Farm Secured Transactions Under the UCC*, 23 BUS. LAW. 195 (1967).

from the farmer. What are your views on this provision and do you think that it should be retained in future revisions of the Code?

Mr. Coogan: The difficulties of a business debtor's using his inventory as security for a loan have been told and retold so often that even a short summary may seem superfluous, but the present general acceptance of the idea so long fought over may have caused us to forget the battle. For a century the courts (and sometimes the legislatures) resisted the use by business debtors of inventory as collateral. This was partly because of conceptual difficulties, but also for the sound policy reason that one who buys goods held out for sale should not have to worry about security interests created by his seller. Over the years the courts have developed the rather simple idea that, regardless of what the document says, the security interest in such goods will not be honored against a buyer in the ordinary course. This rather sensible idea was adopted by the Uniform Trust Receipts Act and by practically all recent factor's lien acts. The secured party who takes a security interest in such goods knows they must end up in the hands of a buyer if he is to be paid in ordinary course, and he, not the innocent buyer in ordinary course of business, must take the risk that a dishonest debtor-seller will fail to pay over the proceeds. A combination of 9-307 plus 1-201(9) adopts this philosophy generally—but not for the buyer of farm products.

Essentially, the exception in 9-307 reflects a philosophy that a farmer who borrows on his inventory cannot be trusted to turn over the proceeds from its sale in the way a lender has learned to trust other businessmen to do. The buyer of farm products, not the lender, must take the risk that the seller does not live up to his promise.

A minor reflection of the UCC's concept of the farmer as a non-business person is the exemption in 9-302(1) from filing for purchase money security interests in any number of items of farm equipment providing that each costs less than \$2500. The net effect may well be to make such collateral of less than normal use to the farmer who wishes to borrow on his equipment, but can point to no public record to evidence the absence of previously perfected purchase money security interests.

In the late 1960's a relatively small part of farm financing involves a person who, like the Vermont hill farmer of a century ago, is primarily a "consumer." Such a borrower got his sugar from the maple trees, raised a few cows for milk, butter, and meat, carried his wheat to the local miller, raised enough apples and potatoes for cider and food, raised sheep for wool out of which his wife and daughter made the family clothes, and perhaps sold enough lumber to provide the little cash needed for salt pepper, rum and other necessities of life. If such subsistence farmers exist somewhere, it is doubtful that they obtain much credit, however secured.

Whatever the rule may be elsewhere, in the citrus fruit industry large amounts of capital are required, and the citrus grower is likely to be not only like other businessmen, but like other *large* businessmen. It would no doubt sometime be convenient for one who financed the seller of steel to a maker of widgets to repossess the widgets from an innocent buyer, if the widget seller did not repay his inventory loan, on the theory that widgets are "products" of the steel. But 9-307 reflects not only business morality but business necessity in rejecting that philosophy—for all but farm products!

Mr. Mays: A possible justification for 9-307's treatment of farm products is that while the buyer of widgets at the local hardware store is an amateur deserving the law's protection against a professional lender, the typical buyer of farm products is a purchaser at wholesale and more likely to be a "professional" than is the local banker who financed the crop.

Mr. Coogan: It might be thought that the once-a-year wholesale professional buyer of the year's wheat crop was in a better position to search for liens on his seller's record than for the seller's lender to police his debtor. But conclusions are no more valid than the facts they are based on. In another setting the typical milk dealer buys from dozens, hundreds, or thousands of small producers. It is impossible for him to know when Farmer Green gives a chattel mortgage on cow Bessie and her products (including, by definition of 9-109(3), her milk). And when mortgaged Bessie's milk is sold to Mrs. Black, the security interest created by the mortgage on Bessie follows the milk down Baby Black's throat.

Mr. Mays: Although the milk had ceased to be farm products, and had become inventory of the milk dealer, nevertheless the security interest in the milk was not cut off by 9-307.

Mr. Coogan: Exactly, because 9-307(1) cuts off only security interests created *by the seller* (the retail milk dealer in this case), and here, of course, the security interest was created by the seller's seller. If we substitute orange juice for milk, we come to the same result, except to the extent that citrus producers tend to sell in larger units; here the buyer's making a search for security interests in the crops they are buying becomes merely *difficult*, rather than *impossible*.

Mr. Mays: Can we say generally, Mr. Coogan, that, except for the provisions of 9-307, one who furnishes money to a farmer based on the security of goods purchased by the farmer primarily for his own or his family's use is governed by no special rules unless the item is so close to being business equipment that filing for that category is expedient, in which case the place to file may be different than if the business were other than farming? Can we not also say that except for the place of filing (or possible exemption from filing under 9-302(1)(c)) there is

no basic difference between perfecting security interests in farm equipment and in other business equipment and assignment by a farmer of accounts, contract rights or general intangibles and assignment of such collateral by a non-farmer?

Mr. Coogan: This is true, but when we come to the rights of a financier and those of a buyer in the ordinary course, we find a great difference between comparable assets of the farmer and the non-farmer.

Mr. Mays: I think it would be beneficial if you would explain the general rule under the Code covering the continuity of security interests—the concept of “proceeds”—and then discuss in detail the special protective provisions of 9-307.

Mr. Coogan: We start first with the general rule of 9-306:

(2) *Except where this article otherwise provides, a security interest continues in collateral notwithstanding sale, exchange or other disposition thereof by the debtor unless his action was authorized by the secured party in the security agreement or otherwise, and continues in any identifiable proceeds received by the debtor. (Emphasis added).*

Section 9-307 gives special protection to certain buyers against application of this rule of 9-306 (2) when it provides in 9-307 (1):

(1) A buyer in the ordinary course of business . . . other than a person buying farm products from a person engaged in farming operations takes free of a security interest created by his seller even though the security interest is perfected and the buyer knows of its existence.

Before examining the exception for those who buy farm products, we might take a look at the definition of “farm products” and the definition of this “buyer in ordinary course of business” who is protected for all but farm products.

Section 9-109 defines “farm products” as follows:

Goods are (3) “farm products” if they are crops or livestock or supplies used or produced in farming operations or if they are products of crops or livestock in their unmanufactured state (such as ginned cotton, wool clip, maple syrup, milk and eggs) and if they are in the possession of one engaged in raising, fattening, grazing or other farm operations. . . .

The definition of “buyer in ordinary course” covers a considerable amount of substantive law. Section 1-201(9) provides:

Buyer in the ordinary course of business means a person who in good faith and without knowledge that the sale to him is in violation of the ownership rights or security interests of a third

party in the goods buys in the ordinary course from a person in the business of selling goods of that kind Buying . . . does not include a transfer in bulk or as security for or in total satisfaction of a money debt.

It might be argued that sale by a farmer to a grain elevator operator of a year's crop of wheat might be a transfer in bulk and thus exclude the buyer from the class of "buyers in the ordinary course of business" without the special exclusion in 9-307(1). Bulk transfer, however, is a word of art. While the definition of 6-102 may not be technically applicable it indicates what is meant—a transfer not in the ordinary course of business. Here the buyer, even if he buys "in bulk" is not taking a "transfer in bulk."

One might justify the lack of the usual protection given to buyers of farm products on the basis that the buyer is likely to be fully as sophisticated as the growers' financier, and, since he ordinarily buys at infrequent intervals, it is not too great a burden to require him to search the record. However, from a practical standpoint I am advised by you, Mr. Mays, that such a procedure would indeed be a costly and time-consuming burden, and, as a matter of fact, is hardly ever done. The same argument would impose a similar burden on, say, a shoe wholesaler or a retail shoe store chain—but the Code requires no such duty as a condition to the wholesale or retail shoe buyer's taking free of all security interests created by his seller. Further, the policy argument breaks down completely when it is applied to the milk dealer who daily buys 110 pounds of milk from farmer *A*, 215 pounds from farmer *B*, and so on until farmer *Z*. But leaving aside for the moment the relative rights of the fruit-processor-buyer and the grower's financier, the Code, by its elaboration in 9-315 of the heretofore vague doctrine of "products" may extend the problem.

Mr. Mays: Suppose a crop of oranges subject to *S*'s security interest is sold to a concentrate processor and the debtor fails to pay over the proceeds. Under 9-307(1) *S* can follow the oranges into the hands of the processor, and, unless I am misreading 9-315, *S*'s security interest continues in the frozen concentrate. To stretch a point, suppose that *S* can trace only 25% of his collateral, and only 15% of the value of the concentrate was contributed by the oranges, nevertheless *S* seeks to collect 100% of his debt by enforcing his "products" security interest in the concentrate. Will the courts allow him to do so, notwithstanding what 9-315 says?

And suppose further that the processor sells ten cases of packed frozen juice to a grocery wholesaler, who sells it to a corner grocery store, where you buy a can, Perhaps you are safe on the theory that no one will attempt to repossess your purchase, but what about the wholesaler?

Mr. Coogan: He seems to be out of luck. While as a practical matter a security interest is ordinarily cut off by a rightful sale by anyone in the chain of title, and the frozen concentrate is no longer farm products after it leaves the farmer, 9-307's cut-off applies, as we have discussed, only to security interests *created by the seller*. The security interest, of course, was created by the farmer, as to whom the rule does not apply. I can only say that the treating of the farmer as a second-class businessman who cannot be trusted to turn over proceeds of collateral raised for sale is the result of conditions long since changed.

Mr. Mays: I note with much interest that in the first reported case that I have seen on this subject, the court has found a way to obviate the provisions of 9-307 which we have been discussing.

Mr. Coogan: You refer no doubt to the recent case in New Mexico where the court allowed a cattle dealer to disregard a security interest in cattle which he had purchased from a cattleman.

Mr. Mays: Yes. In *Clovis National Bank v. Thomas*¹³ a New Mexico bank made a loan secured by cattle and expressly provided in the security agreement that the debtor was not to sell or dispose of the cattle "without the prior written consent of the Secured Party." The debtor marketed the cattle through a commission house and failed to apply the proceeds to the payment of the loan at the bank. The bank brought an action against the commission house for conversion. The court found that the same sequence of events had occurred previously between the same parties except that the cattleman had paid off the bank. The court further found that the plaintiff bank, although perhaps not expressly consenting to the sale in question, did impliedly acquiesce in and consent to the sale, although fully aware of its right to require written consent, and therefore, the bank waived its rights under the security agreement.

Mr. Coogan: The case you mention indicates that the courts have already begun to whittle away the exception that 9-307 purports to give the financier of farm products. This whittling away is in accord with previous case and statutory law. The two principal inventory security devices, namely, the Uniform Trust Receipts Act and the non-uniform factors liens act protected the buyer in the ordinary course of business of inventory that was subject to a security interest. In doing so they merely followed the courts in a line of cases growing out of the various conditional sales and chattel mortgage acts, most of which did not specifically provide for this problem at all. This case is also doubly interesting in that here in spite of the language of 9-307 and the language of the security agreement the court found that there was a course of conduct by which the secured party had authorized the sale and therefore the exception in section 9-307 did not apply to this sale of farm products. Under 9-306,

13. 77 N.M. 554, 425 P.2d 726(1967).

the right to follow the collateral after a sale is cut off if the secured party gives the debtor express or implied permission to sell.

III. FRUIT ON THE TREE: REALTY OR PERSONALTY? A BASIS FOR DISPUTE

Mr. Mays: Problems relating to farm products under the Code are not limited to the differences in the fact that farm products are subject to some special rules under article 9. Another question which we must consider is very basic: to what extent are security interests in growing crops subject to real estate law and to what extent are they subject to the Code?

Mr. Coogan: Your question is indeed very basic, but I confess that until you brought up this question several months ago I had never given it much thought. Before I give you my present thinking, I would like to ask you, as a Florida lawyer, to outline the law of Florida prior to the Code on the question of when real estate law controlled and when personal property law controlled.

A. *The Pre-Code Law in Florida*

Mr. Mays: Let me attempt to present a very brief description of the pre-Code Florida law on the question of whether growing crops constitute real estate or chattels.

On the question of whether crops are governed by real estate law or personal property law there appears to be an inconsistency between several Florida cases. Basically, the cases of *Adams v. Adams*¹⁴ and *Simmons v. Williford*¹⁵ among others provide what I feel to be a clear analysis of the Florida law. These cases hold that fruit crops unseparated from trees or vines whether regarded as *fructus naturalaes* or *fructus industriales* are part of the realty unless otherwise actually or constructively severed by the intention of the owner. A different rule, however, exists as to unharvested crops of corn, hay, beans or other such *fructus industriales* growing only by yearly cultivation, which are generally held to be personal property and not a part of the real estate.¹⁶

Mr. Coogan: I don't want to interrupt your trend of thought as to what pre-UCC cases hold, but I would like to make two preliminary points. As I read the cases you referred me to, in late years Florida courts tended to accept decisions from other states that fruits crops are no different than, say, a corn crop. But I don't think this distinction is now important for our purposes because the UCC may very well change

14. 158 Fla. 173, 28 So.2d 254 (1946).

15. 60 Fla. 359, 53 So. 452 (1910).

16. See *Summerlin v. Orange Shoes, Inc.*, 97 Fla. 996, 122 So. 508, 510 (1929); see also *Stoltzfus v. Covington County Bank*, 154 So.2d 866 (Fla. 1963) citing the *Summerlin* case.

whatever that law was. I refer to the definition of "goods" both in article 2 and in article 9, each of which includes growing crops, and the specific inclusion of "farm products" (which includes crops) as one of the main categories of article 9 collateral.

Mr. Mays: I am not sure that I agree with your comment as to the holdings of the later Florida cases, however, we will come back to that question.

Concentrating for the present on the question of the priority between a pre-existing real estate mortgage and a crop mortgage encumbering the fruit of a growing tree held to constitute a part of the realty until severed, the *Summerlin* case sets forth what I feel to be the law in Florida. In this case, the supreme court held that before default in payment of a debt secured by a pre-existing real estate mortgagee, an owner may give a chattel mortgage upon the fruit in being and upon subsequent default in the chattel mortgage, the chattel mortgage may take possession of the crop but that the owner cannot create a lien superior to the first mortgage upon the land by attempting to mortgage fruit which does not come into existence until after default in the first mortgage and institution of foreclosure proceedings. The real estate mortgage in the *Summerlin* case did not specifically cover crops and was executed prior to the 1925 Florida law recognizing the validity of liens on future crops.

The *Hughes v. Summit Realty Company* case¹⁷ in distinguishing the *Summerlin* case, pointed out that the law in *Summerlin* was only valid insofar as mortgages executed prior to the 1925 crop lien act were concerned, and held that where a prior real estate mortgage did not specifically encumber crops, a subsequent crop mortgage could encumber the crops upon the realty for the present year and until the mortgagor's note was fully paid. The court discounts arguments by the appellant (which I feel to be the better view) that the holder of a mortgage on the real estate, as an incident to the mortgage, maintains the right to sell the land as well as the growing crops thereon which have not matured and been severed, and that such right is superior to the rights of the holder of a subsequently acquired crop lien.

Mr. Coogan: May I, as a lawyer totally ignorant of any peculiarities of Florida real estate mortgage law, timidly express the opinion that the view adopted by the court is the "better view"?

Mr. Mays: In any event, the court based its holding upon the economic purposes to be served by allowing a farmer the right to encumber a citrus crop for labor and fertilizer in order to continue the productivity of the land.

The *Hughes* case cites with approval *Haines City Citrus Growers'*

17. 120 Fla. 141, 162 So. 343 (1935).

*Ass'n v. Petteway*¹⁸ which involved a purchase money real estate mortgage which did not specifically encumber the fruit, and which was executed after the 1925 crop lien act. In the *Haines City* case, however, the chattel mortgage was dated prior to the date of the execution and delivery of the real estate mortgage, *but was not recorded* prior to the default in the real estate mortgage, and as a matter of fact, only the present crop was required in order to pay off the sums outstanding under the chattel mortgage. Although the *Haines City* case distinguished the *Summerlin* case as did *Hughes*, this distinction was not necessary to the decision, as the court held that the crop lien was prior in time to the real estate mortgage and did not have to be recorded to be valid against the real estate mortgage, since the real estate mortgagee was not in the position of a subsequent encumbrancer or subsequent purchaser under the provisions of the crop lien act.

The foregoing cases to the contrary notwithstanding, I believe that the current Florida position is set forth in the case of *E. C. Fitz & Co. v. Eldridge*.¹⁹ This case involved the conflict between a pre-existing real estate mortgage which was executed after the effective date of the 1925 crop lien act and a subsequently executed crop mortgage. Although the court adopted the ruling of *Summerlin* and quoted at length the rules of law pronounced therein, the real estate mortgage was in default prior to execution of the crop mortgage and proceedings to foreclose the real estate mortgage had been instituted prior to the bloom of the crop in question. For this reason it may be argued that much of the reasoning of the *Fitz* case is mere dicta. Nevertheless, the court held that the "opinion and judgment" of the *Summerlin* case was controlling and that although an owner could give a chattel mortgage upon fruit, he could not give a valid chattel mortgage upon fruit for an indefinite period of time extending over years operating to give a superior lien over a prior real estate mortgage upon the land only, so as to subject the fruit not yet mature or even in existence to the lien of the chattel mortgage. The court also negated the validity of a bill of sale purporting to constructively sever and transfer title to the mature crop upon the trees on the basis that such bill of sale was not effective until one day after final foreclosure had been entered. There was further evidence to the fact that the bill of sale was given without present consideration.

It is my opinion that the foregoing cases will be extremely important in determining the priorities question between a valid crop lien under the Code and a pre-existing real estate mortgage which either specifically covers fruit, or covers only the real estate. It appears, however, that the questions raised by the *Hughes* and *Haines City* cases have never been adequately resolved and that therefore, even under the Code, a very good

18. 107 Fla. 344, 145 So. 183 (1932).

19. 129 Fla. 647, 176 So. 539 (1937).

argument could be made that a subsequent secured party holding a crop lien could take a valid interest in fruit to mature on trees in the future although the real estate upon which the trees are located is encumbered by a prior real estate mortgage. Of course, the counter-argument, and what appears to me to be the better view, is that such a secured party can only acquire an interest in the matured fruit, or fruit which matured from a bloom on the trees which was in existence prior to a default in the real estate mortgage. Consequently, any such security interest would be enforceable only as against the current fruit crop, or at most, two year's crops, in any priority conflict with rights under a prior real estate mortgage. In my opinion, any holding other than in accordance with *Summerlin* would effectually destroy the value of farm lands in and of themselves, as security, and require lenders to obtain a crop security interest in addition to a real estate mortgage. It is unfortunate that the facts of the *Fitz* case do not clearly substantiate the rules of *Summerlin* which were apparently adopted by *Fitz*.

Mr. Coogan: I am glad to hear a Florida lawyer admit that he has some difficulty in deciphering the pre-UCC law on the possible conflicts between a chattel mortgagee of a crop, and the rights of a real estate mortgagee whose mortgage did not purport to cover crops. I must say, however, that these interesting cases add very little to the result obtained under (1) the UCC and (2) the law relating to the foreclosure of the debtor's interest in land under real estate law. Let us take an example.

Suppose that, before the UCC became effective, *O* the Owner, gave a 20-year mortgage on a 100 acre citrus grove to Mortgagee, *M*. The mortgage said nothing about fruits or crops but it contained the standard language encumbering the real estate and its "rents, issues and profit." While the real estate mortgage was in good standing, and after the citrus trees were in bloom, *O* borrowed \$50,000 from his local bank, to be repaid from the proceeds of the current fruit crop. A crop mortgage in accordance with chapter 700, Florida Statutes, 1965, was recorded in the public records of the county where the real estate is located. The crop was greatly damaged by a hail storm, and *O* defaulted in his quarterly payment on the real estate mortgage. *M*, the real estate mortgagee, claimed this year's crop as part of the rents and profits after default in the real estate mortgage, and bank claims under its current crop mortgage.

Mr. Mays: As evidenced by my foregoing discussion of the applicable Florida law under a pre-existing real estate mortgage that does not contain provisions encumbering the crop, prior to default the owner may deal with the fruit as personalty. In this case, prior to a default in the real estate mortgage, *M* constructively severed the growing fruit by giving a crop mortgage thereupon to bank. Although the real estate mortgagee could have taken possession of the real estate after *M*'s default, the bank's interest had by that time intervened, and was properly perfected.

Mr. Coogan: I assume that Florida courts, like courts almost everywhere, have construed the "rents, issues and profits" clause, almost regardless of its wording, as becoming effective only after default or more likely after the appointment of a receiver, and therefore this additional wording would add little to the foregoing discussion and your conclusions as to the case law in Florida.

Mr. Mays: In *Haines City* the court cites *Pasco v. Gamble*,²⁰ an early case in 15 Florida which I suppose adopts the usual lien theory rule as to the mortgagor's rights to control rents and profits until his rights are set aside by a receivership or foreclosure. However, in our present discussion I am considering the real property characteristics of the unsevered fruit and its attachment as a part of the real estate security, rather than as a "profit" of the land. Of course, as you apparently are implying, and as indicated by several of the Florida cases, if the unsevered fruit is personally, the inclusion of a "rents, issues and profits" clause and appointment of a receiver would have much more meaning. In my opinion a crop mortgage covering existing fruit would take priority over a pre-existing real estate mortgage whether or not covering "rents, issues and profits," unless the real estate mortgage were in default prior to the first bloom of the fruit to be covered by the crop mortgage. Of course, although we have spoken of the emphasis to be placed upon the pre-existing real estate mortgage being *in default*, the Florida cases are not at all specific as to whether the pre-existing real estate mortgage must merely be in default, or must be in default and foreclose proceedings instituted thereon, or whether final decree in foreclosure is the critical factor.

Mr. Coogan: Before I give the reasons which prevent me from agreeing with Mr. Mays as to the "real property characteristics of the unsevered fruit" let us first discuss another topic which may aid in the understanding of this problem.

Suppose, Mr. Mays, *O*, the owner gives to *M* a real estate mortgage in the usual form—and by that I mean no mention of crops as such—on a citrus grove and prior to default on his real estate mortgage, *O* gives to *S* an article 9 security interest on the crop. There is now a default under both the real estate mortgage and the security agreement. If I understand what you said earlier, the article 9 interest will have priority?

Mr. Mays: On the assumption that pre-Code analogies continue to apply, as I think they should, that is correct. However, if the real estate mortgagee had adequately covered present and future crops by making it clear that the same instrument granted both a real estate mortgage and an article 9 security interest, *M*'s earlier security interest, if properly perfected, would have given him priority without regard to a default in

20. 15 Fla. 562 (1876).

the real estate mortgage. In your example, however, where *S* claims future crops, *S* takes priority over crops which come into bloom prior to a default in the real estate mortgage. When a default later exists, assuming that *Fitz v. Eldridge* and its adoption of *Summerlin* constitutes the Florida law, *S* is subordinate to *M*.

B. Old Law and Article 9-Recording

Mr. Coogan: Suppose that the pre-UCC real estate mortgage also claimed crops which it adequately described, or suppose that the old mortgage was one recorded under chapter 700, Florida Statutes, would you recommend that the mortgagee now file a financing statement under article 9?

Mr. Mays: Whether this was a combined real estate-crop mortgage, or a crop mortgage under chapter 700, the short answer is "yes." It is always more advisable to make a recording which may be unnecessary than to get involved in litigation.

Mr. Coogan: One can argue that under 10-101 this is a transaction to be "completed" under the old law. However, a trustee in bankruptcy would maintain that the security interest in the new crop "attached" after the new crop came into existence (9-102, 9-204) (at a time when the UCC was in effect) and that therefore failure to comply with the UCC resulted at best in an unperfected security interest. To be safe, the mortgagee should file under article 9 and he should also execute a supplementary agreement (which could be on a postcard) by which the parties agree that henceforward they are operating under the rules of article 9.

Mr. Mays: How necessary is the second step—the execution of a supplementary agreement?

Mr. Coogan: I would argue that in a state (like Florida) that allowed a security agreement to pick up future crops, such an agreement merely confirmed the obvious. Section 9-203 does not say that the "agreement" must be made after the effective date of the UCC, but in at least one case a court has held that a Code filing was insufficient without a security agreement executed after that date. The safe position, whether the future crop interest is to arise under a chapter 700 crop mortgage, or a combined real estate-crop mortgage, is to execute a supplemental agreement and to record under 9-401 after the effective date of the UCC. Such a course of action guards against the argument that under 9-102 the crops coming into existence after the effective date of the Code would be a "transaction" under 9-102 which occurred after that date and to which the Code would apply. This argument would apply also as to any new money advanced after the effective date of the Code. I think that the best recommendation which we can offer at this point is that all old security agreements of this

nature which are presently in effect should be modified to comply with the Code to prevent future disputes from arising.

Mr. Mays: Now that I have discussed the pre-Code Florida law on the interests of those claiming crops as collateral under a chattel mortgage and those claiming under a real estate mortgage, I'd like to hear your comments as to how much of the old law survives for transactions after the effective date of the Code.

Mr. Coogan: When, several months ago, I asked you to summarize pre-Code Florida crop law for me, I was under the impression that the effect of the UCC on crops, like the effect of the UCC on fixtures, would to a considerable degree depend on the pre-Code law. After studying the cases and the statutes to which you called my attention, and after further considering the Code provisions, I am presently of the opinion that the rights of those claiming a security interest in crops in any state are to be found primarily in article 9 in the form adopted by that state's legislature. The state's pre-Code law has a limited effect.

Crops are one of five categories of property which have some characteristics of realty and some characteristics of personalty. Article 9, and the Code generally, does not treat each of these categories in the same way. After reflection, I am presently of the opinion that, *so far as sales of, and security interests in, crops* are concerned the UCC controls. This conclusion is not weakened by the fact that local law may treat crops as realty for some other purposes—suppose *O* sells his land to *X* without mention of growing crops. The law of some state might say that *O*'s interest in the crops goes to *X*. But if *O* had given a crop security interest to *S*, *X* takes subject to *S*'s security interest.

Mr. Mays: How have you reached your conclusions?

Mr. Coogan: Both article 2 on sales and article 9 on secured transactions define "goods" to include growing crops. Sales of goods are governed by article 2 and security interest in goods are governed by article 9. By these definitions the Code adopts the view towards which courts and legislatures have been moving for some time—sales of and security interests in growing crops are governed by personal property law. This is true without distinction between industrial crops and natural crops, and without the fiction of constructive severance affected through the intention of the parties. For these reasons, I question your earlier assumption that your hypothetical real estate mortgagee was claiming an interest in the crops in their character as real estate. For security purposes, crops are now goods, and for security purposes are governed only by the Code. Either the real estate mortgagee perfected his interest in crops under the UCC, or he has no more interest in crops than he has in other personal property. For what it is worth, it is my observation that most cases interpreting the 1925 crop statute looked on it as producing the same

effect, except where the real estate mortgage had been executed prior to enactment of the 1925 Act.

Mr. Mays: But section 2-107(3), which governs sales of goods somehow related to real estate, recognizes that such goods may form a part of the realty at the time of contracting, and that a contract for the sale of such property may be invalid against certain real estate interests unless recorded in the real estate records.

Mr. Coogan: In the first place, I am not at all sure that 2-107(3) applies to crops. It may well apply only to gas, oil, minerals, etc., which have much more of a real estate flavor than crops. But suppose a state does have such a statute that applies to a sale of crops, it is perfectly conceivable that the legislature may require notice to be made available in the real estate records of certain transactions affecting personal property closely associated with realty. For some purposes other than sales and security interests (for example taxation), growing crops may well be treated as realty.

Mr. Mays: You referred to other classes of property which have some characteristics of both realty and personalty. What have you in mind, in addition to fixtures?

Mr. Coogan: Section 2-107 treats several categories of "goods to be severed from the realty." It provides that a contract for the sale of timber, minerals or the like, or materials to be removed from realty, is a contract for the sale of goods only if to be severed by the seller. Contracts for the sale of growing crops, on the other hand, are treated as personalty whether they are to be severed by the buyer or the seller. This same emphasis on the chattel nature of crops is repeated in 9-204. There can be no security interest in timber until it is cut, in gas, oil or minerals until they are extracted. Up until that moment these properties are under real estate law. But again, for security purposes, crops are treated as personalty from the instant they are planted or otherwise become growing crops. Both 9-204 and 9-312(2) treat encumbrances on crops, even when covered in real estate documents, as security interests (*i.e.*, article 9 interests) not as realty interests. In this respect crops are treated quite differently from the other categories of mixed personalty-realty, particularly the category we have not discussed at length—fixtures.

Mr. Mays: I'd like to postpone my questions on fixtures. Are you taking the position that the old Florida agricultural cases have no bearing on the treatment of security interests created in crops?

Mr. Coogan: It is my present position that unlike the UCC's treatment of fixtures, where some part of pre-Code law is adopted, the UCC largely sets its own standards for crop security interests. In the absence of a Code provision as to when annual fruit becomes a crop, I suppose a rule

like Florida's rule that a fruit crop becomes such when the first maternal blossoms appear would control.

Mr. Mays: You then take the position that the rules pronounced in the *Summerlin* and *Fitz* cases—if they constitute the Florida law—are no longer applicable?

Mr. Coogan: First, let me confess that even after reading *Fitz* and all the other cases to which you have referred me, I am not quite sure what that case holds. It may mean only that where *O* owns a citrus grove subject to *M*'s earlier real estate mortgage, and *O* agrees that *S* will automatically acquire a security interest in a crop when it later comes into existence, *S*'s potential security interest in that future crops may be cut off by the land being taken out of *O*'s possession by *M*'s foreclosure proceeding before the hoped-for collateral becomes a crop. If that is what *Fitz* means, it is consistent with 9-204's provision that no security interest in a particular crop exists until that crop comes into existence.

Mr. Mays: You are treating crops from a citrus tree purely as a series of yearly productions like crops of corn, rather than as a continuous output of a tree which constitutes a part of the real estate.

Mr. Coogan: On this interpretation, yes. The Code is not entirely clear as to whether a crop means an annual production, or the entire output of a plant. I suppose it is clear that two separate plantings of spinach in one year are two crops—but what about three crops of alfalfa grown on irrigated land in one year with no new planting? To come back to citrus fruit, if you construe a "crop" as the product of the tree for one year or one season, and if you interpret *Fitz* as meaning that *S* may not get a hoped-for security interest in a crop which comes into existence after a foreclosure of an earlier real estate mortgage, I don't see that the result is basically different from the situation where a mill operator agrees that *S* will, without further act of either party, acquire a security interest in next year's out-put of the mill. The Code does not give a present security interest in collateral not yet in existence, but provides a mechanism by which that property falls under the security interest when acquired by the debtor. The debtor may never acquire the collateral. A mill operator agrees that *S* will automatically acquire a security interest in all of next year's woolen goods. Now suppose that before the year is over the holder of an earlier real estate mortgage makes manufacture of goods impossible by taking away the mill owner's factory. Or suppose the mill burns down, or that a strike prevents its operation, or the mill had been operated under a lease which terminates. The fruit grower's loss of his land is basically no different from the case I put. Particularly if the grower loses his land and his trees without bad faith on the part of the new owner, it is difficult to see how a crop not yet in existence will thereafter fall under the security agreement executed by a former owner. The former owner will

never acquire any rights in that future crop, which is necessary if a security interest is to attach to that crop under 9-204. Conceivably the parties could by special arrangement convert their security agreement into a covenant running with the land but an ordinary security agreement would not have that effect.

Mr. Mays: It is my opinion that the *Summerlin* and *Fitz* cases mean only that a lien cannot be created on crops to come into existence in the future so as to subject the future fruit to a lien superior to the lien of a properly recorded pre-existing real estate mortgage. Under your conclusions, the Florida amendment allowing future security interests to attach for seven years under an after-acquired property clause covering crops is meaningless, except merely as a matter of convenience in effecting a new loan. This would actually mean that agricultural financing under the Code is much more restricted than under old Chapter 700, which is certainly contrary to what I feel was the intent of the legislature in enacting the Code. You are in effect disagreeing with both *Summerlin* and *Fitz* as well as what I feel is the reasoning behind the holdings of the *Hughes* and *Haines City* cases which arguably uphold the efficacy of the after-acquired provisions of the old crop lien act, without regard to the continued ownership of the property by the debtor. It is my feeling that under the old law, and under the UCC, a valid crop lien can be given that will bind subsequent disposition of the real estate, voluntarily or involuntarily, but that such an interest will not bind enforcement under a pre-existing real estate mortgage which may not specifically include crops, the recording of which constitutes constructive notice to the holder of a subsequent crop lien. In effect you are saying that a debtor cannot assure himself of a perfected security interest in future crops to cover an initial advance that may not be completely repaid from a current crop due to crop failure.

Mr. Coogan: Not at all; between the debtor and secured party, such an agreement is good. Further, it is difficult to imagine any circumstances in which the crop secured party who first recorded could be deprived of his first priority [9-312(5)(a)]. (In a rare combination of circumstances, at a time when no debt was outstanding under the early recorded agreement, a second secured party conceivably could perfect through taking possession of the crop—9-312(5)(b).) If through any cause the debtor loses the trees on which the future crop is to be grown, he can never acquire the “rights” in the future crop necessary to create a security interest in that crop under 9-204(2)(a). If you are saying only that the existence of the debtor’s agreement to give a security interest to S in next year’s crop does not prevent a real estate mortgagee from enforcing his mortgage, we agree. Section 9-311 says that the debtor may voluntarily or involuntarily part even with property which has already become collateral (and next year’s crop cannot become such until next year). That disposi-

tion is valid even if the agreement makes it a default. If *Fitz v. Eldridge* means more than what I have said, I don't think it should be followed after adoption of the Code. Conceivably a court could find that a real estate mortgage which predated the 1925 crop mortgage act carried with it rights to crops as realty; I am not sufficiently well informed on Florida law to discuss that point.

Mr. Mays: I agree with your analysis of the provisions of the Code which would seemingly require that the debtor have rights in the real estate, and therefore the crops, as a condition precedent to the perfection of a security interest at the time future crops come into being. Technically, I see no alternative to this result, from a literal reading of the Code. As previously indicated, however, it is my opinion that under pre-Code Florida law, the citrus fruit would constitute a part of the real estate and therefore a Florida court, in order to obtain a satisfactory result, may continue to classify citrus fruit as real estate, notwithstanding the various uses of the term "growing crops" under the Code. The Code terminology of "growing crops" could be held to apply only to those industrial crops which do not, by Florida case law, constitute a part of the real estate and the Code by virtue of the specific provisions of 9-104(10) could be construed not to apply to crops constituting a part of the real estate. If this would be the holding of a Florida court, it is my further opinion that the *Fitz* and *Summerlin* cases would be held to constitute the Florida law insofar as conflicts with pre-existing real estate mortgages are concerned, and the holding of the *Hughes* case would constitute the Florida law as to the rights to be attributed to a mortgagee of future citrus crops. In my opinion, the *Hughes* case specifically substantiates the pre-Code Florida law that under Chapter 700 the lien on a crop of citrus fruit in being would succeed to future crops, as they come into existence, until the debt secured thereby is paid in full. This is the specific question which was framed by the *Hughes* court and answered in the affirmative. The court concluded that the holder of the fee can mortgage his crops at will so long as he complies with the provisions of the crop lien act and could therefore mortgage his crops "for the year and until his note was fully paid."

The case of *Neal v. Bradenton Production Credit Ass'n*^{20a} further substantiates what I feel to be the holding of the *Hughes* case. In this case a production credit association filed suit to foreclose a mortgage which encumbered both the real estate and "all crops, fruit and other products planted, growing and to be planted, grown and raised (during the current and five succeeding crop seasons and until said indebtedness is paid), upon the lands hereinabove described . . ." In the meantime the mortgagors had entered into an agreement with a fruit company whereby it delivered the real estate and fruit crops to the fruit company

20a. 200 So. 845 (Fla. 1941).

for the production and handling of all the fruits to be thereafter grown on the property. It was alleged by the fruit company that the mortgagor turned over and delivered the property to the fruit company and the fruit company had been in actual, adverse and exclusive possession since the date of delivery and had advanced all money and fertilizer for the upkeep and maintenance of the grove and had actually produced the citrus crop and the mortgagor had not been in possession of the property since delivery. The opinion did not state whether or not the property was actually deeded to the fruit company; however, the production credit association-plaintiff alleged that the fruit company claimed an interest in the real estate under a written instrument which was not of record. The court cited the 1925 crop lien act and provided that mortgages on crops not in being may operate as a lien on such crops as soon as they come into existence provided that they are properly executed, acknowledged and recorded as a mortgage upon real estate, in order to be valid against subsequent encumbrancers or subsequent purchasers in good faith. The court further provided, however, that such a fruit crop mortgage would not take preference over a prior existing recorded mortgage in terms covering the fruit crops and lands, unless subordinated by the prior mortgage. The court then ruled that

[I]t is well settled that a valid mortgage lien may be created on crops of citrus fruit to be grown in the future . . . and the mortgagor may not defeat the right so acquired by the mortgagee by turning over the mortgaged citrus grove to a third party to produce a crop of fruit covered by the terms of the mortgage, where the mortgage carried a proper description of the lands upon which the crops are to be produced and has been executed, acknowledged and recorded according to law.

The court pointed out that the fruit company had legal notice by the record of the mortgage that the production credit association held the first lien on the crop produced to secure the payment of an outstanding indebtedness and that it could not defeat the lien of the mortgage by the operation of any agreement between it and the mortgagor to which the mortgagee was not a party. If the foregoing is not the result to be applied by a Florida court under the Code, then it is my feeling that the Florida Legislature misinterpreted the effect which it felt would be given to the amendment to the uniform code allowing security interests to attach for seven years under an after-acquired property clause. Of course, I realize that in suggesting the foregoing (since Chapter 700 has been repealed) one who takes a crop lien on citrus fruit or other such natural crops, out of an abundance of precaution, should perhaps perfect his crop lien both under the Code and under the real estate law, by insuring that the security agreement itself, in addition to a financing statement, is filed in the office of the clerk of the circuit court and that this security agreement complies with the requirements for a Florida real

estate mortgage and is properly acknowledged. The Code, however, does not expressly repeal Chapter 698, Florida Statutes, covering chattel mortgages, and certain language therein applicable to crops may be argued in support of my proposition, without the further analogies to the real estate characteristics of citrus fruit. (Although 698.12 provides that the chapter shall not apply to transactions governed by the Code.) I realize that we have come to an impasse on this subject and we are really unable to predict what might be the rulings of the courts, although I feel that we have adequately framed the issues. I do feel strongly, however, that, if necessary, the literal construction of the Code provisions must give way to the specific requirements of the agricultural industry in Florida, as it has developed over the years, and I do not believe that a court will place a construction upon the Code which will differ so vastly, as you suggest, from what I feel to be the clear meaning of old Chapter 700 and the court cases in Florida. But let us continue with our discussion.

We have sometimes made the assumption that the cut-off date under *Fitz* was the time of foreclosure. Actually the Florida cases vacillate between talk of foreclosure of the real estate mortgage and a mere default under that mortgage.

Mr. Coogan: I would hope that the courts would limit the doctrine to crops which become such after some public, affirmative act of the real estate mortgagee. If I understand Florida mortgage law, a real estate mortgage leaves the mortgagor (and those claiming under him) in possession and control of rents and profits until the real estate mortgagee ousts him through a receivership or the more drastic act of foreclosure. Trivial defaults (failure to pay an insignificant tax) may not have come to the attention even of the parties, much less are they known to third parties. I have great difficulty in believing that real estate mortgage law in most states would cut off a UCC security interest in a future crop by anything less than a receivership or a foreclosure. If a mere default is effective in cutting off a future crop mortgage, the secured party must get from the real estate mortgagee evidence that on the date the maternal blossoms appear no default exists under the mortgage.

Mr. Mays: Perhaps the appointment of a receiver would be the only effective manner by which to enforce the mortgagee's right to the crop and proceeds, but that is merely the enforcement procedure. In my opinion the lien of the mortgage would attach or become effective after default, at which time the mortgagor could no longer deal with the crops as personalty nor create interests therein superior to the interests of the prior mortgagee. But I now recognize our point of departure as to this very important problem, so let me return to the fixtures question that we postponed.

In your book *Secured Transactions Under the UCC* you comment on similarities and dissimilarities in the UCC's treatment of two of the classes of property which have some characteristics of chattels or personalty and some characteristics of realty. In 9-313(1) the statement is made that nothing in article 9 prevents the encumbering of fixtures under real estate law. Do you attach any significance to the fact that there is no corresponding statement that crops can be mortgaged under a real estate mortgage? Was this omission intentional or through oversight, as I suspect?

Mr. Coogan: There is good reason for the lack of a corresponding statement as to crops. There is no doubt that an ordinary real estate mortgage would create a real estate interest, not a UCC or chattel interest, in a hot water heater so affixed to the land that it became a fixture; and it would be covered by the real estate mortgage without special mention. The hot water heater could retain some of its chattel characteristics only as to certain persons (typically the conditional vendor) and then only if the holder of the chattel interest had taken steps prescribed by 9-313 to preserve his rights in the hot water heater as a chattel. Under the Code, crops (including citrus fruits, as distinguished from the trees that bear them) are personalty; if they are to be covered in a real estate mortgage, you have in effect a combined real estate mortgage and a UCC security agreement. The parties must comply with formal requirements of both sets of laws.

C. Recording Formalities: Real and Personal

Mr. Mays: Suppose that O, the owner of an orange grove, gives a mortgage on the grove, and on the fruit to be grown thereon for the next five years. A real estate mortgage often does not contain the addresses of the parties, and customarily is never signed by the mortgagee. If the mortgage itself is to be used as the financing statement, what complications do you envision?

Mr. Coogan: Without question, I would advise the mortgagee—secured party to comply with the requirements of both real estate and UCC recording law in Florida (9-401, 9-402). If this caution has not been followed, I would hope to find something in the document which the mortgagee could be said to have “adopted” as his signature. “Signature” is defined in article 1 of the Code to include something less than the traditional signing associated with a real estate mortgage.

Mr. Mays: After our early discussions concerning this point I have discovered another recent New Mexico Supreme Court case which held that a secured party's signature on a financing statement was not essential.²¹ The court reasoned that such a requirement was illogical and in

21. *Stevrell-Paterson Finance Co. v. May*, 77 N.M. 331, 422 P.2d 366 (1967).

conflict with the liberal construction required by the Code to be placed upon its provisions.

Suppose that the real estate mortgage does not mention crops, but the mortgage contains the usual "rents, issues and profits" language. Would you advise that such a mortgage contain the signature and address of the mortgagee?

Mr. Coogan: I note that the chief draftsman of article 9, Professor Grant Gilmore, assumes that even here compliance with the filing requirements of article 9 is necessary. This to me is not so clear. The rights given to a real estate mortgagee by the "rents, issues and profits" clause are largely judge made. Usually, the language comes into play only after a receiver is appointed for the mortgaged property. The judge may deny any benefit of this language—that is, he may not allow the receiver to resort to personal property brought in by this clause—unless the land itself is insufficient to pay off the mortgage debt. I should think that the mortgagee would be entitled to this equitable remedy even in the absence of filing. He would, of course, come behind a UCC security interest created before the receivership and possibly behind one under an after-acquired property clause. But there is some possibility of a court's saying that this language attempts to create a security interest in personal property, and that compliance with article 9's filing rules is essential.

Mr. Mays: You will recall that Florida, like the other big fruit producing state (California) rejected the provision in the Uniform Commercial Code that limited a security agreement in future crops to those to be grown within one year. Let us take a different set of facts where the UCC security interest is created before the real estate mortgage. Suppose that Owner gives to S a security interest in present and future crops to be grown during the next six years and a proper recording is made. Later O gives a real estate mortgage on the same land. At the end of the fifth year, O defaults on his real estate mortgage payment and, for your benefit, Mr. Coogan, mortgagee has a receiver appointed. Later new blossoms appear. Both the article 9 secured party and the receiver for the defaulted real estate mortgage claim the growing fruit, which at the time of the controversy is barely past the blossom state. Who gets the crop?

Mr. Coogan: I would suppose that the answer depends on the state's rules as to rights of receivers under real estate mortgages and UCC 9-204. Section 9-204(1) says that the security interest cannot attach until (among other things we assume have taken place) the "debtor has rights in the collateral." He has no such rights "in crops until they are planted or otherwise become growing crops." If this were an annual crop like wheat or spinach, that time could be easily ascertained—when the seed is planted. If the phrase "becomes growing crops" means when the fruit

tree was planted the UCC interest wins. I would expect a Florida court to say that no "crops" exist until the first maternal blossoms appear. If "crop" means this year's fruit, the appointment of a receiver under the real estate mortgage may cut off the operation of *S*'s after-acquired property clause. If the law of the applicable state is as stated in general treatises, in most states the receiver gets the crop only on a showing that the mortgagee is not adequately secured by the land. If a receiver was appointed before this year's blossoms appeared and the court makes such a finding, it can be argued that the debtor, being supplanted by this receiver, got no interest in this crop, and therefore *S* got none. If *O*'s interest is not taken away, neither is *S*'s.

Mr. Mays: As I have previously discussed, in my opinion, under the Code, the courts will favor the Code interest because it was filed first.

IV. FRUIT TWICE SOLD: CONFLICTS BETWEEN SUCCESSIVE PURCHASERS

Mr. Mays: We have previously discussed the existing Florida law as to whether growing crops are realty or personalty and the numerous cases concerning the actual or constructive severance of the fruit from the trees by the intention of the owner. Although none of the cases which we have discussed expressly involved the competing interest between a purchaser in bulk of the fruit on the tree and a later purchaser or mortgagee of the same fruit on the tree, it is my feeling that if there were an immediate passage of title by virtue of the sale of the fruit in bulk, under a valid sales contract, it being the intention of the owner to constructively sever the fruit from the tree, the purchaser or mortgagee of the fruit would have retained good title to or a lien interest in the fruit as against a subsequent purchaser of the real estate or as against an existing real estate mortgage. I have commented upon the pains taken by the court in the *Fitz* case in pointing out that the bill of sale as to the fruit on the trees which was involved in that controversy was not effective because foreclosure sale had previously been entered and further the sale was made without present consideration. Has the Code attempted to handle conflicts between a buyer of the fruit in bulk on the tree and the holder of a security interest in the crop? We have several different possible situations. Suppose, first, that *O*, the owner, gives *S*, a lender, a security interest in a growing crop, and then makes a contract to sell the crop to *B*, a Buyer. Since *O* is engaged in the business of farming, *S*'s security interest follows the fruit into the hands of *B*, because even though *B* is a buyer in the ordinary course of business, he is denied the protection ordinarily given such a buyer by 9-307—he bought "farm products." If *O* is neither an owner nor a lessee of the land but a contract processor who has a right to sell the fruit under a contract with the owner of the land, and *O* has the right to create a security interest in the crop, query as to whether

Buyer would not be entitled to protection under 9-307 as a buyer in ordinary course of business.

Mr. Coogan: You refer, no doubt, to the definition of farm products in 9-109 which makes them farm products only if in the possession of one engaged in raising . . . or other farming operations." Depending on how much caretaking the processor does, it could well be held that he is engaged in farming operations.

Mr. Mays: That being so, let me ask you, Mr. Coogan, the second part of this question: suppose that *B* contracts to buy the goods before a security interest is created?

Mr. Coogan: We must first look to the general article on sales. Section 2-105(1) defines goods as including "growing crops" and other identified things attached to realty as described in the section on goods to be severed from realty. Section 2-105(2) provides that "a purported present sale of future goods or of any interest therein operates as a contract to sell."

Section 2-107 says that

A contract for the sale apart from the land of growing crops . . . is a contract for the sale of goods . . . even though it forms part of the realty at the time of contracting, and the parties can by identification effect a present sale before severance.

Subsection (3) of 2-107 then backtracks to the extent that it keeps in force any third party rights provided by the law relating to realty records and the contract will serve as constructive notice to third parties of the buyer's rights under the contract for sale. If Florida has a non-Code provision requiring crop sales contracts to be recorded, 2-107(3) would pick up that requirement. If a recording is otherwise required, 2-107(3) makes that recording constructive notice. I would suppose a subsequent lender would be protected in the absence of a required recording by the buyer. If, outside the Code, there is no such requirement, a subsequent lender gets no more rights than the owner who has contracted to sell.

Mr. Mays: It is unfortunate that 2-107(3) appears only to be permissive rather than mandatory. Since section (2) expressly recognizes the validity of a present sale, however, the Code does give us an advantage over the old law which I do not believe adequately provided for the giving of constructive notice of such a present or long term sales contract. A knowledgeable attorney would always have advised that such a contract, involving considerable sums of money, be acknowledged and recorded, and although certain provisions of Florida statutes mention the recording of bills of sale, there was considerable doubt as to the effectiveness of such recordation.

I have one further point which I know we have previously discussed, but I merely want to emphasize its importance, in my mind.

Section 2-107(3) apparently leaves open a question as to the "laws relating to realty records." Does this merely mean the law relating to the recording statutes or does it mean case law construing what are interests in real estate? If a prior real estate mortgage specifically covering crops is only recorded under the laws relating to real estate and is not recorded in the manner required to perfect an article 9 security interest, nevertheless, if the crop is considered as a part of the real estate, it would appear that such an interest as evidenced by the mortgage would take priority over any sales contract subsequently recorded under the provisions of 2-107. If, however, a real estate mortgage does not expressly cover crops, and there has been a default under the existing real estate mortgage, it would appear that the proper recordation of any contract for the present sale of the existing crop executed prior to the default, should take precedence over the rights of the existing real estate mortgagee but, the *Hughes* and *Haines City* cases to the contrary notwithstanding, such contracts for the future marketing of the fruit should not create lien interests in crops not yet in existence even after a default in the real estate mortgage. Do you concur with this position, Mr. Coogan?

Mr. Coogan: As I have already indicated, my present position is that a combined mortgage of crops and realty is (i) a chattel mortgage of the crops (security interest) and (ii) a real estate mortgage of the land. I agree that a contract for the sale of future crops does not, of itself, create a security interest or lien at *any time*. If the contract of purchase and sale is also a security agreement, the security interest cannot attach until this crop becomes such.

V. SALES AND SECURITY AGREEMENTS: SOME FILING PROBLEMS

Mr. Mays: Suppose that an orange grove owner sells his crop in bulk on the tree two months prior to the time he expects it to be harvested. Since buyer pays only 25% down, and owner is not completely satisfied with the buyer's credit standing, he retains a security interest in the crop until it is fully paid for. How would the owner-seller perfect the security agreement? Suppose he perfects through filing, where does he file or record?

Mr. Coogan: For the sake of the point Mr. Mays desires to make, let us assume that perfection is accomplished through filing (or, in Florida, recording). In what Code category are the goods? These oranges are crops in the possession of a farmer, and look like "farm products," in which case recording should perhaps be made in the public records of the county where the real estate is located; this would be in accord with the idea that the public record, with respect to farm connected collateral is kept locally. But the definition of farm products here is a bit tricky. Goods are farm products only when in the possession of a *debtor* engaged

in farming operations. Here the farmer is not the debtor, but the secured party. The debtor is a dealer and not a farmer, and as to him the crops are inventory. As such, they are subject to central filing. This leads to a trap on description of the "land concerned" under 9-203 and 9-402 which Mr. Mays will discuss later. But Mr. Mays has offered a better solution.

Mr. Mays: Since the farmer is in possession of the fruit, his security agreement should provide for a *possessory* security interest under 9-305. Then, of course, no filing will be required. Theoretically, it is not even necessary to have a written security agreement where the farmer-secured party has possession of the collateral.

Mr. Coogan: This is a matter of proof only—a written agreement would show what the parties intended by leaving the collateral in seller's possession. Suppose the citrus grove owner lives in Miami and leaves someone else in possession?

Mr. Mays: If the person in possession is not the buyer, he can agree to act as third party pledgee for the owner under 9-305.

Suppose now that the owner is dishonest, and enters into a second purchase and sale contract with *X*. *X* checks the local records, and finds nothing (since the first buyer's interest was either perfected through possession or perfected through central filing with the first buyer as debtor). *X* pays 50% of the agreed price. Which buyer gets the crop?

Mr. Coogan: The lack of a local recording *under article 9* does not protect *X*. If there were a Florida statute which together with section 2-107 required a recording in the land records, *X* would be protected against the first buyer. Nothing in article 9 says he is protected against the security interest in favor of the double seller, but it does not take too much imagination to find an estoppel against a wrongdoer. Assuming that there is no such statute in Florida, the subsequent purchaser would probably be in the same position as the subsequent lender we mentioned earlier. He would have no more rights than the owner and the owner, having already contracted to sell, has very few rights indeed.

Mr. Mays: Assume that the citrus grower has sold the fruit on the trees to processor *X* and that the fruit has been fully paid for or that the grower does not desire to retain a security interest therein for the remainder of the purchase price. How would a lending institution to processor *X* perfect a security interest in his inventory collateral consisting of the fruit remaining on the trees in the possession of the grower?

Mr. Coogan: In Florida the security interest against the fruit as *inventory* of processor *X* must be perfected by filing centrally. Here also, non-Code local law plus UCC 2-107 may require that such a contract of purchase and sale be recorded in the public records where the real estate is located regardless of central filing. This may be necessary in

order to properly protect processor *X*'s financier from a subsequent purchaser of the fruit from the grower, or from the grower's creditors or trustee in bankruptcy, although not necessarily from creditors of processor *X*. To the extent that the grower has not been paid, and his perfection under 9-305 was the earliest, 9-312(5)(b) gives him priority over processor *X*'s lender notwithstanding other filing or recording.

Mr. Mays: Suppose that caretaker *X* operates owner's grove, and advances \$5,000 to owner against the crop. How could *X* obtain a security interest in the fruit?

Mr. Coogan: If *X* is truly in possession, again a possessory security interest seems to be the easy answer. If he records locally, he is doubly safe and may give notice to innocent parties.

Mr. Mays: Suppose that an owner who operates his grove accepts an advance from *X* against the sale price of the crop; owner's reputation for honesty is good, but he has other unhappy creditors—how can *X* perfect a security interest in the crop it has purchased? Clearly local recording is essential.

Mr. Coogan: The first question is whether owner has sold a crop in existence, or has contracted to sell a future crop. I will suppose it is the former. As security for owner's obligation to deliver the fruit, he gives a security interest therein to *X*. Here we are dealing with the filing provisions applicable to farm products—the debtor is a farmer and the goods are in his possession. The land on which crops are grown must be referred to both in the security agreement and in the financing statement, which in Florida is recorded in the county records. I will ask Mr. Mays to comment on the ease or difficulty of describing the land in the security agreement and in the financing statement.

Mr. Mays: Chapter 67-264, *Laws of Florida*, 1967, which became effective on July 1 of this year requires that the financing statement contain a specific legal description of the land upon which the crops are growing, which, as you know is a departure from the reasonable identification provisions of 9-110. Of course, this is no big problem from the standpoint of the owner of the real estate as he no doubt will have within his possession complete legal descriptions on all lands which he owns, and a description of even a five acre tract would not, in most instances, be particularly difficult. The rub comes, however, as we have already discussed, when one other than the owner must file and is involved with recording hundreds of various contracts calling for such descriptions. Not only would the fees for recording be substantial, but also the buyer-secured party must run the risk of the ill will of the grower who is perhaps unaccustomed to such refined treatment of a citrus contract and the inferential question as to his honesty and integrity. And even if the crops are inventory (and

hence centrally filed), this requirement applies, although I believe this requirement is an oversight.

But let's take this problem: Suppose *T* leases a citrus grove from *L*. *T* makes an agreement with a high credit fruit processor *C* for the purchase by *C* of *T*'s crop for the next two years. Against what collateral can *T* borrow for some improvements with a life of, say, five years?

Mr. Coogan: *T* may be able to convince a lender that his rights to payments under his contract with *C* are sufficiently certain for him to borrow what he needs on the strength of his contract rights, which article 9 recognizes as a form of collateral. But generally lenders are not willing to take the gamble that the debtor may become unable or unwilling to perform, in which case no money would be due under the contract, and the lender would find himself unsecured. For example, *T*'s contract with *C* might mean nothing if *L* can terminate *T*'s lease. But contract rights may be additional back-up collateral where other collateral is almost adequate. *T* might assign existing accounts, and give a purchase money security interest on so much of the improvements as constitute chattels or fixtures. I assume that *T*, as a tenant, would have no title to any improvements which become real property, but I assume that the courts of Florida like many other courts would be slow to characterize as realty any improvements made by a tenant unless they are almost nonremoveable or he has something close to a fee—say a 99 year lease.

I suppose you would advise this bank that *T* has enough rights in the collateral to create a security interest therein—*T*'s right to collect from the purchaser the proceeds of his contract. Evaluation of these rights requires a credit judgment. What assurance have we that there will be a crop each year? Will there be sufficient proceeds? If a crop is destroyed by frost, will insurance proceeds be specifically assigned? Can owner be counted on not to sell to someone other than purchaser? Will *T* lose his lease? On a long term contract, it may be wise to notify the purchaser that the contract proceeds have been assigned.

Contract rights against high credit companies furnish the basis upon which multimillion dollar transactions are financed. Here all risks are studiously evaluated at the outset, and the contracts are especially drawn to furnish loanable collateral.

Mr. Mays: For the reasons you have given the person who makes an advance to a grower in reliance on the existence of a marketing arrangement is more likely to be the processor-purchaser himself, rather than a bank. The processor is more able to evaluate the situation, and in a measure, control it. An accounts financier may find that a financier of inventory or farm products is claiming some of the accounts as proceeds realized from the sale of those goods. This conflict could, of course, arise between one who claims contract rights or accounts and one who claims inventory or farm products dealt with under the applicable contract.

Mr. Coogan: This would not seem too likely in the case of one who is primarily a citrus grower, rather than a dealer. If it happens, the Code offers no clear rule as to priority. The only safe rule is that the same lender should control credit on both farm products or inventory and contract rights and accounts resulting therefrom. If another lender is to be allowed to come in, there should be a satisfactory subordination agreement between the secured parties as to who gets what collateral.

Mr. Mays: Mr. Coogan, give us your thoughts as to why you would expect a lender to give a higher value to existing receivables than to future receivables or contract rights?

Mr. Coogan: In short, a bird in the hand is worth two in the bush. The existence of a contract usually means that the debtor can sell his goods if he has them to sell and does not go back on his word. The certainty or uncertainty that *T* will have future receivables is a matter of foretelling the future from the past. The lender will be *almost* assured that he will get the receivables if they come into existence, but he does not have complete certainty that he will get the receivables, even if he was the first to file as to accounts.

Mr. Mays: Since one can perfect a security interest in accounts *only* through filing, insofar as farm products are concerned, is there any question whether the lender who files first can be certain that any accounts covered by his agreement will be his?

Mr. Coogan: The accounts might be claimed as "proceeds" of a security interest in farm products, including a purchase money security interest therein. Perhaps there is no great practical problem as to purchase money interests where the collateral is farm products, because ordinarily the farmer raises those farm products. Suppose, however, that *T* is a bit of a trader as well as a grower.

Mr. Mays: You mean that *T* is what we call a "bird dog."

Mr. Coogan: *T* gives to *S* a security interest in present and future accounts. *T* later buys from *X* on credit a load of oranges which *T* resells to *C*. *X* and *T* perfect a purchase money security interest in the oranges and *X* claims "proceeds." *X* claims a designated account produced by the sale of these oranges on the theory that they are "proceeds" of his oranges, and *S* claims under his general assignment of accounts.

Mr. Mays: Did *X* give any notice of his claim to *S*, who held a previously perfected security interest in *T*'s accounts?

Mr. Coogan: You refer no doubt to the provisions of section 9-312(3) which require the holder of a purchase money interest in inventory to give notice and to file before he delivers the inventory to the debtor as a condition to his coming ahead of earlier filers. Let us assume here that *S* had filed as to accounts and contract rights but not as to inventory. No notice is required under that section except to other inventory financiers.

Mr. Mays: I suppose another reason that no notice was required is that 9-312(3) refers only to purchase money security interests in inventory and here the collateral was probably farm products.

Mr. Coogan: Again, what the businessman thinks of as inventory is not "inventory" if it is farm products, and the notice requirements of section 9-312(3) do not apply. As we have seen, crops can be inventory if not in the possession of a debtor engaged in farming.

Mr. Mays: If the purchase money man claims accounts as proceeds which are automatically perfected under section 9-306 when they came into existence, I suppose that section 9-312(5)(b) would apply. We look to see which security interest was first "perfected."

Mr. Coogan: And we are left with the apparent answer that both are perfected simultaneously when the account arises. *X* will argue that he should take priority because his accounts are a continuation of a security agreement created in farm products or inventory weeks or months before the account came into existence. *S* will argue that *X* could have learned of *S*'s interest from his public filing as to accounts. The short answer is that we do not know how the courts will resolve an issue left open by article 9.

VI. STATUTORY LIENS: THE EFFECT OF ARTICLE 9

Mr. Mays: May I change the subject? Section 9-310 says that certain liens created by statutes other than the Code take priority over Code created security interests unless the statute expressly provides otherwise.

Mr. Coogan: I should point out that Section 9-310 applies only to statutory liens for persons who supply materials and services on goods in their possession. No Florida statutory lien of this character has been called to my attention.

Mr. Mays: I would mention a lien which is not entitled to priority under 9-310, because it is non-possessory, but is given priority by the statute which creates it. Section 85.22, Florida Statutes, 1965, gives a lien to one who makes advances or supplies goods to one "in the business of planting, farming . . ." which is superior to a lien of prior dignity [saving liens for certain labor] on crops grown. This lien can be created only with consent of the owner, and only if a recording is made. This is, therefore, not the usual statutory lien which ordinarily is created without regard to the wishes of the owner.

It is common for an owner of a citrus grove to employ someone else, who may or may not purchase the crop, to perform caretaking services for the citrus grove—to fertilize, cultivate, spray and pick the fruit. Hence, under section 85.22, as we have discussed, with written consent of the owner, a lien could be given on the crop.

Also, section 85.04 provides for a lien on the real estate, for certain labor performed on groves, and section 85.10 provides for a lien on crops for certain labor or overseeing performed on the crops. Although section 84.22 clearly sets forth the circumstances under which that lien shall take priority, what would be the possible effect of the other two lien statutes? I feel that under the general provisions of sections 85.25 and 85.26, although not so expressly stated, the liens created under chapter 85 should not take priority over existing interests, unless notice thereof is recorded, or such interests arise at approximately the same time that services are being rendered and therefore the holder of the existing interest is or should be placed on notice of the possibility of the lien. In such event, the notice or posting of the groves by those performing caretaking services may have a great effect upon the provisions of sections 85.25 and 85.26, for such posting should no doubt give subsequent purchasers or mortgagees notice and render them subordinate to the lien for caretaking services. This type of posting, of course, is normal practice by most large grove caretakers.

Would such an agreement need to comply with article 9, including recording, or would the usual practice of posting give adequate public notice?

Mr. Coogan: It seems to me that section 85.22 fits pretty squarely into the area pre-empted by article 9. If I am correct 85.22 should have been repealed specifically, and was repealed by implication. In any event the section 85.22 lien transaction would seem to be unlike the ordinary statutory lien, which is imposed without regard to the consent of the owner. As I see it, no lien comes into existence unless as a result of a contract—it therefore seems to be a security interest created by contract in personal property, and hence falls under section 9-102(1)(a). Assuming that it is an article 9 security interest, posting is not a substitute for filing under article 9. The other lien interests which you have pointed out appear to constitute the normal statutory lien situations to which article 9 does not apply under the provisions of section 9-104(3), and their priorities will therefore be governed by the provisions of the lien statute itself or case law. On the basis of general security law (“first in time, first in right”), I would hazard the guess that these statutory liens, not being entitled to section 9-310’s priority, because not possessory liens, would taken priority over an article 9 interest only if prior in time and “perfected” as the statute prescribes.

Mr. Mays: You therefore advise that every caretaker who wishes to take advantage of section 85.22 should file a financing statement with respect to each of his customers?

Mr. Coogan: That conclusion by no means follows. In most business transactions before and after the Code the parties rely on each other’s

general credit. But if any protection against third parties is sought, filing is called for. The question raises the same problems as did the question whether a buyer who makes an advance against a crop should take a security interest therein, with all the trouble of describing the real estate. Each case is a matter of business judgment.

Mr. Mays: Those rendering services or goods or materials to groves should insure, if they are relying upon the normal type of statutory lien, that they fall within the provisions of the Florida lien statutes and will be governed accordingly as to their priority to pre-existing interests and those interests arising in the future. Or, if they are relying upon section 85.22, then they should consider the specific problems which we have discussed. Likewise, a grower's lender or a purchaser of the grove or of only the fruit must also consider the possibility of statutory liens which have arisen or which shall or may arise in the future and note that they cannot always rely upon the existence or non-existence of a financing statement or other such instrument recorded pursuant to a particular statute.

Mr. Coogan: This brings up the question often raised in business loans: *B* agrees with lender *L* that he will not create liens in favor of any other person. Now he violates that agreement and the person in whose favor the lien is created knows that the "negative pledge" has been violated. Or suppose the person gets the lien without knowledge of the prohibition against it?

Mr. Mays: You have stated the questions—what are the answers?

Mr. Coogan: The courts have never, to my knowledge, definitely answered the question, but most corporate lawyers assume that one who takes a lien in violation of a "no lien" clause is in trouble.

VII. THE LIMITED SCOPE OF SECTION 9-312(2)

Mr. Mays: We have not discussed section 9-312(2), which reads as follows:

A perfected security interest in crops for new value given to enable the debtor to produce the crops during the production season and given not more than three months before the crops become growing crops by planting or otherwise takes priority over an earlier perfected security interest to the extent that such earlier interest secures obligations due more than six months before the crops become growing crops by planting or otherwise, even though the person giving new value had knowledge of the earlier security interest.

Apparently you do not attach much importance to this section?

Mr. Coogan: I do not attach too much importance to this section only because its scope is so limited. Let us say that *O* mortgages his land to *M*

and the parties make it clear that this mortgage specifically covers crops. *O* goes into default in December on his combined realty-crop mortgage. In February he applies to Bank *A* for a loan to produce this year's crop. Subsection (2) is of no avail, because its priority is only over other security interests securing obligations more than six months overdue, and *O*'s obligation here is only four months overdue.

If the law of Florida as expressed in *Fitz v. Eldridge* is that a prior real estate mortgagee takes priority as to a crop which comes into bloom after a default in the real estate mortgage occurs, 9-312(2) would never come into operation, because no chattel security interest can arise after default in the real estate mortgage. If we interpret *Fitz* in the light of *Summerlin*, on which it relies, the crucial test is whether foreclosure has begun before the first blossoms appear. The real estate mortgagee would argue that section 9-312(2) properly interpreted has no application to his rights to the crops as rents, issues and profits because "security interest" means an *article 9 interest*, and he only claims a judicially created ancillary remedy under real estate law. My own feeling is that section 9-312(2) does not go far enough to accomplish its purpose. If the Code is adopted with the Code's one year limit on future crops, the new security interest protected under 9-312(2) could take priority only over another security interest created under a long term real estate transaction mentioned in 9-204. The obligation secured must be in default for six months, but the real estate mortgage securing it must not have been foreclosed. The after-acquired property clause of the new security agreement for the new crop advance will, when the crop comes into existence, take priority over the after-acquired property clause of the defaulted security agreement.

VIII. PARTICIPATION AGREEMENTS: PROBLEMS IN OWNERSHIP

Mr. Mays: Much of the citrus fruit in Florida is sold by individual growers under the type of contract we have been discussing. A great amount of fruit however, is sold by growers to various processors on what is called a participation basis. Basically, under such agreements, citrus fruit is both picked and delivered by a grower to a processor under provisions in the participation agreement under which the buyer is vested with the authority to direct the fruit to the facilities for which they are best suited. This may be for processing into frozen orange concentrate or single strength juice, the cannery, fresh fruit packing houses, or somewhere else. The returns to the grower are based upon the amount received on the ultimate sale of the processed products less all cost of processing and marketing and a fixed fee per unit processed which represents the processor's profit. The individual grower's fruit is handled in a pool with other growers similarly situated who have delivered the same variety fruit, and his receipts are based on average return, no matter how

marketed. The processor may be a non-profit marketing co-operative or may be a corporation for profit, and may also engage in conventional purchases of fruit, in which instance the processor takes title to the fruit upon delivery. The customary fruit participation agreement may not specifically mention the passage of title, but the grower may assume (correctly or not) that he owns the product up to the point when sales are made by the processor, but that the processor *is* authorized to deliver title. Almost universally, the various processors enter into inventory, warehouse receipts and accounts receivable financing upon their entire inventory and accounts, and their inventory may include participation basis fruit, conventionally purchased fruit and fruit from groves owned by the processor.

Mr. Coogan: To an outsider, these participation agreements seem to be the product of one of two causes: either they grew up among businessmen without benefit of counsel, or each counsel felt that his client had a vested interest in an arrangement so loose that he could argue whatever position later seemed most favorable. Granted that ambiguities sometimes serve useful purposes, it would seem desirable for the industry to determine the pattern under which it is operating—or several alternative patterns, if that is better. It is impossible to draw a clear-cut security pattern where one cannot determine who owns the collateral.

Mr. Mays: Suppose we consider two alternatives; (a) the contracts make it clear that the grower retains title to the crop until the processor effects a sale; (b) the contracts become contracts of sale by the grower to the processor, with the selling price to be determined by the average price of oranges or orange products sold for all categories during a certain period of time.

Mr. Coogan: Take the first one: if title to the goods remains in the grower, his creditors can attach the goods by legal process, if they can identify them. The processor could not borrow against that part of this "inventory" which represents goods owned by someone else. This may make both inventory and accounts financing by the processor very difficult. If grower *A*'s goods are subject to a security interest, *A*'s secured party may seek to recover the goods or their proceeds. If there are a hundred "*A*'s," the processor is in trouble. The language of section 9-315 allows *A*'s secured party to assert his security interest in the frozen orange concentrate.

Mr. Mays: Suppose under alternative (b) that the contract calls for a sale by grower to processor. The grower is not particularly happy with the processor's credit and retains a security interest. Or the grower's financier insists on retaining the security interest he obtained at an earlier stage. As we have seen, where the collateral is farm products, section 9-307(1) does not protect the rights of a buyer in ordinary course of business.

Mr. Coogan: The processor has the same problems that bedevil any purchaser of farm products. If he purchases from a small number of suppliers, he should be able to work out an acceptable understanding. With many suppliers, I do not know of any solution.

Mr. Mays: Since a grower who pools his fruit in a participation agreement may not receive any receipts from the sale thereof for an extended period of time, there may be instances in which the grower will need to borrow money using the participation agreements as collateral. Borrowing from an institutional lender on the basis of these participation agreements is not a customary practice, perhaps because many of the processors, themselves, are willing to finance or make advances to the grower. Although the processor will certainly be in a better position to evaluate the worth of the agreements as collateral than a financing institution, both such possible lenders would face the same vexing problems in perfecting a security interest in the receipts from the pool. Section 9-401 provides that accounts, contract rights or general intangibles arising from or relating to the sale of farm products by a farmer are perfected by recording in the Office of the Clerk of the Circuit Court in the county of the debtor's residence, although at first blush it may appear to the unwary that filing should be done centrally.

Bank counsel should always bear in mind, however, that there can be conflicts between the secured party who holds a perfected security interest in the crops themselves as well as those involving inventory and accounts receivable financing between the processor and another lender. Therefore, prior to making any loan based on these participation receipts as collateral, a search of the records should be made both locally against the debtor and centrally against the processor. The risks involved in such financing may be a considerable deterrent to loans by a financial institution on the basis of such collateral and it is apparent why the processor is in much better position to make advances on these receipts. Of course, these processors should take the steps required for perfection in order to protect themselves against the grower's creditors or trustee in bankruptcy.

Mr. Coogan: All you say is true, but you do not cover all the risks. Unfortunately the UCC does not tell us who has priority when one secured party claims an account as "proceeds" (9-306) of this inventory or farm products and a second secured party claims the same account under an accounts financing agreement. We can juggle the facts—the farm products financier filed first, the accounts financier filed first; or we can suppose that the farm products security interest was perfected through a method other than filing. No amount of care, no searching of the record can give absolute protection. In most situations one probably can get all secured parties to sign an agreement which sets forth an

agreed order of priorities. Anything less that that leaves some uncertainty and risk.

IX. PRIORITIES UNDER ARTICLE 9

Mr. Mays: Among the conflicts you just referred to there are very real conflicts under the Code involving the competing interests between an inventory financier of a processor, accounts receivable financier of a processor, and a lender who relies on either negotiable or non-negotiable warehouse receipts issued upon citrus concentrate in bulk, placed in warehouses. Of course, the textbook rule which would always be desirable to heed, is that when a search of the records (or inquiry as to possible security interests perfected by a method other than filing) reveals the likelihood of financing by more than one lender in any of the foregoing types of collateral, either subordination agreements should be obtained, or one lender should do all the financing. For many practical reasons, however, counsel for the various lenders should be aware of the provisions of the Code which are applicable to the conflicting security interests represented by the foregoing collateral.

Mr. Coogan: If we are to discuss priorities, let us run through some typical cases.

Mr. Mays: Bank *A* records a financing statement on *D*'s farm products. Before *D* receives any advance from *A*, *D* borrows \$1000 from Bank *B* against the same farm products. Now *D* goes back to *A* and gets \$2000. Whose security interest has priority?

Mr. Coogan: This hypothesis involves one of the real changes made by article 9. This case is not handled by any of the special priority rules referred to in section 9-312 and therefore falls under the catchall of subsection (5). Since both security interests were perfected through filing, clause (a) governs, giving priority to the secured party who *filed first*, regardless of when other requisites for a security interest were completed.

Mr. Mays: Bank *A* again records before any other transaction. Bank *B* however, makes its advance against a non-negotiable warehouse receipt made out in *B*'s name.

Mr. Coogan: Here we have the other side of section 9-312(5)—this time clause (b) gives priority to the person who first completed all the steps to create a perfected security interest.

Mr. Mays: Bank *A* again records first, claiming inventory which it wrongly believes to be in *D*'s possession. *A* advances \$1000 to *D*. The inventory is in fact in a warehouse. Bank *B* makes an advance against a negotiable warehouse receipt of which it takes delivery.

Mr. Coogan: Under 9-304(2), because the goods were at the time rep-

resented by a negotiable document, a security interest in the document controls. Suppose, Mr. Mays, that Bank *B* had taken possession of a non-negotiable document in this case?

Mr. Mays: The non-negotiable document is not the kind of collateral in which perfection can be achieved through possession alone (section 9-305 limits documents to those in negotiable form); but section 9-304(3) permits perfection through the secured party's taking a non-negotiable document in his own name. Considering the provisions of both article 7, and article 9, and the manner by which they affect the priorities question, it is apparent that Bank *B* which takes its security interest in non-negotiable warehouse receipts, would take subject to *A*'s previously perfected security interest in the inventory itself. Section 7-504(1) and (2) provides that a transferee of a negotiable or non-negotiable document to whom the document has been delivered, but not duly negotiated, acquires title and rights which his transferor had or had authority to convey.

Mr. Coogan: We have by no means exhausted the possible combinations with respect to warehouse receipts, negotiable and non-negotiable. We can do no more than call attention to sections 9-310, 9-304, 9-305 and 9-309 of article 9 and various sections of article 7 and Documents of Title.

X. CONCLUSION

This drama ends with a whimper. Both players declined to include a lengthy summation, feeling that perhaps, for the moment at least, the field of crop financing has been adequately tilled. (*Ed.*)