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**“CLEAR TITLE” FOR FARM PRODUCTS: CONGRESS
AND THE ARKANSAS LEGISLATURE ATTEMPT TO
SOLVE A TROUBLESOME PROBLEM**

*D. Fenton Adams**

Until recently the law in Arkansas, as in most other states, was notably more protective of holders of security interests in farmers' products than it was of creditors whose claims were secured by inventory of other debtors. With the enactment in 1985 of the federal Food Security Act,¹ and amendments in 1986² and 1987³ of Arkansas' version of the Uniform Commercial Code,⁴ the positions of those who finance on the security of farm products have abruptly worsened, though they remain favorites of the law to some degree. This article considers the nature, purposes and effect of the 1985-1987 legislation.

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1. The Food Security Act of 1985, Pub. L. No. 99-198, 99 Stat. 1354 (1985). The Food Security Act was omnibus legislation, dealing with many aspects of food production and marketing. Only one section of it, the so-called “clear title” section (§ 1324, 7 U.S.C. § 1631 (Supp. IV 1986)), is pertinent to the subject of this article. For convenience of reference, the expressions “Food Security Act” and “Federal Act” will sometimes be used to refer to that section.

2. Act of May 19, 1986, No. 16 (2d Ext. Sess.) (codified at ARK. CODE ANN. §§ 4-9-307, -407 (1987)).

3. Act of Mar. 3, 1987, No. 108, 1987 Ark. Acts 267 (Adv. Leg. Ser.) (codified at ARK. CODE ANN. §§ 4-9-307, -407 (1987)).

4. ARK. CODE ANN. §§ 4-1-101 to -9-507 (1987 & Supp. 1987).

I. THE PRIOR LAW

To put the new legislation in perspective, it may be useful to review the Arkansas law as it stood before these changes.

Assume that an Arkansas bank, Bullion Bank, makes separate loans to Harry Holmes and Fred Farrow, two customers who reside and do business in Arkansas. Holmes is the sole proprietor of a small manufacturing concern, his principal product being refrigerators. Farrow owns and operates a family farm, his principal product being soybeans. Both loans provide the borrowers with operating funds for their businesses. As part of each written loan agreement, the bank requires the borrower to grant it an interest in the borrower's property as security for the loan. The loan to Holmes is secured by his present and future inventory of refrigerators; in Farrow's case the security is an interest in his growing crop of soybeans.

Assume, further, that before either loan is repaid, each of the borrowers sells to a third party property securing Bullion Bank's loan. Holmes sells and delivers several of the refrigerators that he has manufactured to Carl Cooper, a retail refrigerator dealer, while Farrow harvests his soybean crop and sells it to Stanley Smith, a broker, who plans to resell the beans. Both buyers pay cash for their purchases and buy without knowledge of the existence of the bank's interests and without suspicion that the sales to them are improper in any way.

Assume that neither of the debtors turns the proceeds of his sale over to the bank, that both debtors are in default on their obligations to Bullion Bank, and that the bank seeks to protect itself by foreclosing on its security. It learns of the sales to Cooper and Smith, and finds that Cooper still has the refrigerators that he bought from Holmes and that Smith still has Farrow's soybeans. The bank asserts against Cooper and Smith a right to take possession of the refrigerators and soybeans, to sell them, and to apply the proceeds of those sales to the loan obligations of Holmes and Farrow. Are the bank's claims valid?

Article 9 of the Uniform Commercial Code⁵ would provide most of the governing substantive law, as it would in most states.⁶ In the

5. ARK. STAT. ANN. §§ 85-9-101 to -507 (Supp. 1985) (current version at ARK. CODE ANN. §§ 4-9-101 to -507 (1987 & Supp. 1987)).

6. Forty-nine of the fifty states have enacted the Uniform Commercial Code (also referred to in this article as the "U.C.C." or the "Code"). Louisiana has adopted portions of it, but not Article 9. Congress enacted the U.C.C. as the law of the District of Columbia, and it has been adopted in the Virgin Islands. U.C.C., 1 U.L.A. 1 (Supp. 1988).

The U.C.C. is the joint product of the American Law Institute and the National Conference of Commissioners on Uniform State Laws. Its text, as approved by the sponsoring orga-

terminology of Article 9 the agreements giving the bank interests in the refrigerators and soybeans are "security agreements;"⁷⁷ the property interests obtained by the bank through those agreements are "security interests;"⁷⁸ and the refrigerators and soybeans covered by the agreements are "collateral."⁷⁹ Bullion Bank is termed the "secured party,"¹⁰ and Holmes and Farrow are "debtors."¹¹

The basic Article 9 rule defining the rights of the secured party is found in section 9-201: "Except as otherwise provided by this Act a security agreement is *effective according to its terms* between the parties, *against purchasers of the collateral*, and against creditors."¹² Thus, as a general rule, the rights of the bank, as provided in the security agreements, are just as effective against third-party purchasers of the collateral as they would be between the bank and its debtors.

However, the rule does direct attention to the terms of the security agreements. One must inquire whether those agreements authorize the debtors to sell the collateral. This point is underlined by section 9-306(2): "Except where this Article otherwise provides, a se-

nizations, is termed the "Official Text." There have been a series of Official Texts, as the two organizations have approved changes in the U.C.C.'s wording from time to time since its original promulgation in 1951. In this article references to the Code are to the 1978 Official Text, unless otherwise indicated.

When the Arkansas legislature enacted the U.C.C., the current Official Text was that of 1958, and the Arkansas version of the Code was generally in accord with that text. Subsequent amendments brought it into general conformity with the 1978 Official Text by 1985. Therefore, references in this article to the "U.C.C.," the "Code" or the "Uniform Commercial Code" will apply not only to the 1978 Official Text but also to the corresponding sections of the Arkansas U.C.C. as it read prior to the 1986 and 1987 legislation discussed below, unless otherwise indicated. (In the Arkansas Code Annotated, section numbering corresponds to that of the Official Text, except that each section number is preceded by "4-".)

7. U.C.C. § 9-102(1)(a) (1978) provides that, with certain exceptions not relevant here, Article 9 applies "to any transaction (regardless of its form) which is intended to create a security interest in personal property or fixtures," and subsection (2) of the same section provides that "[t]his Article applies to security interests created by contract including . . . chattel mortgage." The term "security agreement" is defined as "an agreement which creates or provides for a security interest." *Id.* § 9-105(1)(l).

8. *Id.* § 1-201(37): "'Security interest' means an interest in personal property or fixtures which secures payment or performance of an obligation . . ."

9. *Id.* § 9-105(1)(c): "'Collateral' means the property subject to a security interest . . ." Note that the particular type of collateral involved in the hypothetical case posed in the text is "goods," defined as including "all things which are movable at the time the security interest attaches" and also as including "growing crops." *Id.* § 9-105(1)(h).

10. *Id.* § 9-105(1)(m): "'Secured party' means a lender, seller or other person in whose favor there is a security interest . . ."

11. *Id.* § 9-105(1)(d): "'Debtor' means the person who owes payment or other performance of the obligation secured, whether or not he owns or has rights in the collateral . . ."

12. *Id.* § 9-201 (1978) (emphasis added).

curity interest continues in collateral notwithstanding sale, exchange or other disposition thereof *unless the disposition was authorized by the secured party in the security agreement* or otherwise, and also continues in any identifiable proceeds"¹³

Now it may be that the security agreements did authorize sales such as those made by Holmes and Farrow. After all, the loans financed the debtors' business operations, and since both engaged in the business of selling the types of products covered by the agreements, the bank quite likely expected the debtors to obtain the funds needed to repay their loans by selling the very products covered by the security agreements. Since the bank's security interest "continues in any identifiable proceeds" of the original collateral, it would seem that the bank would be protected by its interest in those proceeds.

Indeed, in many instances where loans are made to sellers of goods, with the borrowers' inventory serving as collateral, the lenders do not even expect the borrowers to turn over the proceeds of each sale for the purpose of reducing their indebtedness. Rather, the lenders are willing to permit the borrowers to use the proceeds to acquire additional inventory or to meet other expenses of their businesses, expecting the borrowers to repay their loans from the general revenues of their businesses. The lenders contract for liens on new inventory as

13. This sentence of the Code, as originally enacted in Arkansas in 1961, was differently worded. Act of Mar. 7, 1961, No. 185, 1961 Ark. Acts 421 (codified as amended at ARK. CODE ANN. § 4-9-306(2) (Supp. 1987)). The present wording was adopted by amendment in 1973. Act of Feb. 13, 1973, No. 116, 1973 Ark. Acts 345 (codified at ARK. CODE ANN. § 4-9-306(2) (1987)). Prior to the amendment it read: "Except where this Article otherwise provides, a security interest continues in collateral notwithstanding sale, exchange or other disposition *by the debtor* unless *his action* was authorized in the security agreement or otherwise, and also continues in any identifiable proceeds" (emphasis added). This was one of a number of changes in the text of Article 9, with some conforming amendments to other articles, made to bring the Arkansas U.C.C. into conformity with the 1972 Official Text of Article 9. See Note, *Filing and Perfection Under the New Article Nine of the Uniform Commercial Code*, 27 ARK. L. REV. 507 (1973). The words "by the debtor" were deleted from the Official Text and the words "the disposition" substituted for "his action" in order to avoid any suggestion that an unauthorized disposition of the collateral by someone other than the debtor would divest the security interest. See Hawkland, *The Proposed Amendment to Article 9 of the U.C.C.—Part I: Financing the Farmer*, 76 COM. L.J. 416, 418-20 (1971). As most litigation involving this passage of the Code does involve dispositions by debtors, and as that sort of disposition is the subject of this article, the discussion in the text frequently refers to authorization of disposition "by the debtor" without specific notation that the observations made are usually equally applicable to dispositions by others.

Section 9-306(2) does not explicitly provide that an "authorized" disposition of collateral operates to divest the security interest, but that implication is clear. See, e.g., *Commercial Credit Corp. v. National Credit Corp.*, 251 Ark. 541, 473 S.W.2d 876 (1971).

it is acquired, as well as on the proceeds of all inventory.¹⁴

Nevertheless, a secured party may well have reason not to authorize the debtor's sale or other disposition of the collateral in any general way, or at least to put restrictions on the debtor's freedom of sale. The secured party may not have sufficient confidence in the continued vitality of the debtor's enterprise to be satisfied with a lien that "floats" from the original collateral to new inventory as the original collateral is sold;¹⁵ he may want the proceeds of each sale of any of the original collateral applied to the reduction of the secured debt. Moreover, he may not feel adequately protected by his security interest in the "proceeds" of the original collateral. Proceeds in the form of cash or a check payable to the debtor alone are an extraordinarily mobile form of collateral. The debtor may be tempted to apply the proceeds to more pressing needs than the claim of the secured party; by the time the creditor learns that the original collateral has been sold, the proceeds may have disappeared. A secured party may very well believe that he will be adequately secured only if he can retain and enforce his security interest in the original collateral until he gets *control* of its proceeds. Thus, he may withhold any generalized consent to sales of the collateral, instead requiring his prior consent to specific sales, and on terms satisfactory to him. Alternatively, he may grant a more general authorization for sales by the debtor but only on conditions that assure him of control over the proceeds, as by requiring that any payment for such collateral be made by check payable jointly to the debtor and himself.

Business custom may also prompt the secured party to decline to authorize sales of the collateral. Financers of farm operations have very commonly not been willing to grant authorizations for sale of encumbered crops or other farm inventory without the consent of the financers to the specific sales.¹⁶ One must therefore inquire whether the secured party *has* "authorized" any particular sale of the collateral "in the security agreement."¹⁷

14. See Dolan, *Section 9-307(1): The U.C.C.'s Obstacle to Agricultural Commerce in the Open Market*, 72 Nw. U.L. REV. 706, 709 (1978).

15. For general discussion of the "floating lien" see B. CLARK, *THE LAW OF SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE* § 10.1 (1980).

16. See Dolan, *supra* note 14, at 710.

17. Security agreements and financing statements frequently contain express provisions that the security interests are to apply to "proceeds" of the collateral. The very fact that a security interest is claimed in proceeds may be thought to imply authorization for the debtor to sell or otherwise dispose of the collateral, especially where the original collateral is inventory of the debtor. 2 G. GILMORE, *SECURITY INTERESTS IN PERSONAL PROPERTY* 715 (1965). That idea was given qualified support by the Official Comments to the 1958 Official Text of the

In this connection, note that the express terms of the security agreement are not the exclusive source of information as to its "terms." Under the Code's general provisions in Article 1, "agreement" is defined as "the bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing and usage of trade or course of performance as provided in this Act (Sections 1-205 and 2-208)."¹⁸ Consent to sale of the collateral by the debtor may thus be implied by reason of prior dealings between the same parties¹⁹ or on the basis of prevailing business practices in a locality or trade.²⁰ While the parol evidence rule may operate to exclude some evidence of agreements which are not set forth in the written security agreement,²¹ evidence of "course of dealing" and

U.C.C., where comment 3 to § 9-306 stated that: "A claim to proceeds in a filed financing statement might be considered as impliedly authorizing sale or other disposition of the collateral, depending on the circumstances of the parties, the nature of the collateral, the course of dealing of the parties and the usage of trade . . ." Since the 1958 Official Text was the current Official Text when Arkansas adopted the U.C.C., the quoted comment might be an indication of legislative intent as to how § 9-306(2) should be applied in Arkansas. The quoted passage was deleted from the comments to the 1972 Official Text and replaced with a statement that, "[t]he right to proceeds, either under the rules of this section or under specific mention thereof in a security agreement or financing statement does not in itself constitute an authorization for sale," U.C.C. § 9-306 comment 3 (1972), but this change followed Arkansas' enactment of the U.C.C. and may not be legitimate legislative history. On the other hand, the adoption in 1973 by the Arkansas legislature of the change in wording of § 9-306(2) which was effected by the 1972 Official Text, *see supra* note 13, may justify resort to the official comments to that text for aid in interpretation of the rule as modified. Thus far, Arkansas cases do not treat a claim to proceeds as authorizing the debtor's disposition of the collateral, and there are cases in other jurisdictions, construing the Code prior to 1972, which rejected the argument that a claim to proceeds implied that the debtor was authorized to sell the collateral. *Vermilion County Prod. Credit Ass'n v. Izzard*, 111 Ill. App. 2d 190, 249 N.E.2d 352 (1969); *Overland Nat'l Bank v. Aurora Coop. Elevator Co.*, 184 Neb. 843, 172 N.W.2d 787 (1969). *See Dolan, supra* note 14, at 727-28; Richards, *Federal Preemption of the U.C.C. Farm Products Exception: Buyers Must Still Beware*, 15 STETSON L. REV. 371, 380-81 (1986).

18. U.C.C. § 1-201(3) (1978).

19. *Id.* § 1-205(1): "A course of dealing is a sequence of previous conduct between the parties to a particular transaction which is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct." Subsection (3) of the same section provides that, "A course of dealing between parties [as well as usage of trade] give particular meaning to and supplement or qualify terms of an agreement." *Id.* § 1-205(3).

20. "Usage of trade" is defined as "any practice or method of dealing having such regularity of observance in a place, vocation or trade as to justify an expectation that it will be observed with respect to the transaction in question." *Id.* § 1-205(2). Subsection (3) of the same section provides that both course of dealing between parties and "any usage of trade in the vocation or trade in which they are engaged or of which they are or should be aware give particular meaning to and supplement or qualify terms of an agreement." *Id.* § 1-205(3).

21. Although Article 9 of the U.C.C. does not codify the parol evidence rule, it is presumably applicable to written security agreements by authority of § 1-103: "Unless displaced by the particular provisions of this Act, the principles of law and equity . . . shall supplement its provisions." *See also* U.C.C. § 1-201(3) (1978) (the definition of "agreement").

"usage of trade" is presumably admissible at least as an aid to interpretation of the writing and to show terms which supplement the express terms of the writing.²²

The significance of these possibilities was demonstrated in the case of *Planters Production Credit Association v. Bowles*,²³ a 1974 decision of the Arkansas Supreme Court. A production credit association had a security interest in the 1971 cotton crop of one of its members, Bowles, as security for a loan made to him that year and for indebtedness from prior years. The written security agreement did not expressly forbid the debtor to sell his cotton crop, but it did not expressly authorize sale either. The debtor sold parts of his crop to several buyers and did not turn any of the proceeds over to the association in payment of his secured debts. The production credit association brought suit in chancery against the debtor and the cotton buyers, praying that the latter be required either to turn over to the association the cotton they had bought or to pay its value to the association. The chancellor held in favor of the buyers on findings that the plaintiff had for a number of years prior to 1971 followed a practice of permitting all of its borrowers, including Bowles, to sell or otherwise dispose of collateral as they saw fit, and that by such conduct it had "waived its lien under the financing statement and security agreement" covering Bowles' 1971 cotton crop.²⁴ The Supreme Court

22. An analogy may be drawn to § 2-202 of the Code, which, though it appears in the article dealing with sales of goods, is based on reasoning that would be equally applicable to a written security agreement. The section provides that an integrated agreement "may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be explained or supplemented (a) by course of dealing or usage of trade (Section 1-205)" The comment explains that written agreements "are to be read on the assumption that the course of prior dealings between the parties and the usages of trade were taken for granted when the document was phrased. Unless carefully negated they have become an element of the meaning of the words used." U.C.C. § 2-202 comment 2 (1978).

Subsection (4) of § 1-205 appears to be a rule of construction, rather than an application of the parol evidence rule, but it is not in conflict with the view expressed in the text. It provides that express terms of an agreement are to be construed, wherever reasonable, as consistent with applicable course of dealing or usage of trade, but that when such construction is unreasonable, express terms control over both course of dealing and usage of trade. This subsection has been drawn upon in other states to nullify courses of conduct which arguably established secured parties' consent to debtors' disposition of collateral, when the implied consent contradicted express prohibitions of sale in the security agreements. *E.g.*, *Wabasso State Bank v. Caldwell Packing Co.*, 308 Minn. 349, 251 N.W.2d 321 (1976); *Garden City Prod. Credit Ass'n v. Lannan*, 186 Neb. 668, 186 N.W.2d 99 (1971); *Fisher v. First Nat'l Bank of Memphis*, 584 S.W.2d 515 (Tex. Civ. App. 1979). *But see* *Clovis Nat'l Bank v. Thomas*, 77 N.M. 554, 425 P.2d 726 (1967) (discussed *infra* note 27).

23. 256 Ark. 1063, 511 S.W.2d 645 (1974).

24. *Id.* at 1066, 511 S.W.2d at 646-47.

affirmed the judgment, saying that the question, one of first impression in Arkansas, was

whether a secured creditor may waive his security interest in collateral in favor of a third party purchaser of the collateral simply by his course of dealing with the debtor rather than by express or written waiver under the Uniform Commercial Code, as adopted in this state. We agree with the chancellor that PCA did so²⁵

The emphasis in the passage just quoted is on "course of dealing with the debtor." But, in summing up, the court's opinion calls attention to the fact that the production credit association "had a policy among all its member-debtors of permitting them to sell and dispose of collateral at will and be individually responsible to [plaintiff] in applying the proceeds of such sales to the loan indebtedness" ²⁶ Although the opinion does not expressly rely on "usage of trade" as a justification for finding the sales to have been authorized, it would appear that the production credit association's consistent dealings with all of its member-debtors would fit the definition of "usage of trade" in section 9-205 of the Code.²⁷

25. *Id.* at 1067, 511 S.W.2d at 647.

26. *Id.* at 1073, 511 S.W.2d at 650. The court was apparently also influenced by the fact that the lender followed a policy of refusing to comply with requests from prospective purchasers of farm products for lists of its member-debtors. As to why a secured lender might legitimately refuse such a request, see Meyer, *The 9-307(1) Farm Products Puzzle: Its Parts and Its Future*, 60 N.D.L. REV. 401, 428 (1984).

27. See *supra* note 20. Two additional features of the *Bowles* opinion call for comment: (1) In finding that the secured party lost its security interest by reason of ARK. STAT. ANN. § 85-9-306(2) (current version at ARK. CODE ANN. § 4-9-306(2) (1987)) (a security interest continues in collateral despite its disposition by the debtor "unless his action was authorized by the secured party in the security agreement or otherwise") the court observed: "Of course, such action was not authorized except by implication in the security agreement in the case at bar so the question boils down to whether it was authorized under the 'or otherwise' phrase." 256 Ark. at 1071, 511 S.W.2d at 649. It is submitted that under the Code provisions discussed above, see *supra* text accompanying notes 18-22, the authorization can quite legitimately be found "in the security agreement." Indeed, the court seems to concede that there was an implied authorization in the security agreement. Its apparent assumption that the phrase "in the security agreement" in § 85-9-306(2) refers to an *express* authorization in that agreement is not consistent with the Code's definition of "agreement" in § 85-1-201(3), quoted in the text above at note 18. (That wording has not changed since the original enactment in Arkansas of the U.C.C.) But see Nickles, *Rethinking Some U.C.C. Article 9 Problems—Subrogation; Equitable Liens; Actual Knowledge; Waiver of Security Interests; Secured Party Liable for Conversion Under Part 5*, 34 ARK. L. REV. 1, 133-36 (1980) [hereinafter Nickles, *Rethinking Some U.C.C. Article 9 Problems*].

(2) In reaching its conclusion that authorization for sale of the collateral could be found in the "course of dealing" of the parties, the Arkansas court relied, in part, on a New Mexico decision, *Clovis Nat'l Bank v. Thomas*, 77 N.M. 554, 425 P.2d 726 (1967). That case did find such an implied authorization for sale of the collateral by the debtor, but it did so in the face of an express provision in the security agreement which forbade sale without the secured party's

The *Bowles* decision produced a prompt legislative reaction. By Act 215 of 1975 the Arkansas General Assembly amended U.C.C. section 9-306(2) by adding a sentence: "A security interest in farm products shall not be considered waived nor shall authority to sell, exchange or otherwise dispose of farm products be implied or otherwise result from any course of dealing between the parties or by any trade usage."²⁸ The emergency clause of the amending act stated that it was prompted by the *Bowles* decision.²⁹ This amendment, of course, restricts the use of trade usage and course of dealing as bases for finding "authorization" to sell collateral in the form of "farm products," but it does not necessarily render evidence of such facts entirely irrelevant for purposes of interpreting security agreements,³⁰ and it does not apply at all to security agreements covering collateral other than farm products.

Even if the security agreement contains no authorization for sale of the collateral by the debtor, section 9-306(2) of the U.C.C. indicates that such an authorization may be found in words or conduct of the secured party which are not part of the security agreement; authority to dispose of the collateral may be found "in the security agreement *or otherwise*." The principal application of the "or otherwise" phrase would logically be to conduct of the secured party after the security agreement has been made.³¹ The parol evidence rule would present no problem there,³² and the question would simply be whether an expressed or implied authorization could be found.³³

written consent. The New Mexico decision is inconsistent with the rule of U.C.C. § 1-205(4), that in case of conflict between an express term and a course of dealing, the express term controls, *see supra* note 22, and the decision has been criticized on that ground. *E.g.*, Dolan, *supra* note 14, at 727-28. However, the Arkansas decision is not vulnerable for that reason. *See* Nickles, *A Localized Treatise on Secured Transactions—Part II: Creating Security Interests*, 34 ARK. L. REV. 559, 661 (1981) [hereinafter Nickles, *A Localized Treatise on Secured Transactions*].

28. Act of Feb. 18, 1975, No. 215, 1975 Ark. Acts 311 (codified at ARK. CODE ANN. § 4-9-306(2) (1987)). In New Mexico the *Clovis* decision, 77 N.M. 554, 425 P.2d 726, was repudiated by a similar statute. N.M. STAT. ANN. § 55-9-306(2) (1978). (That statute was cited in the *Bowles* case, but the court's response was that Arkansas had no similar statute. *Bowles*, 256 Ark. at 1071-72, 511 S.W.2d at 649-50.)

29. Act of Feb. 18, 1975, No. 215, § 3, 1975 Ark. Acts 311, 312 (emergency clause).

30. The language of the amendment might allow use of course of dealing or trade usage as aids to fixing the meaning of express terms of the security agreement which arguably relate to authorization for disposition of the collateral by the debtor.

31. *But see supra* note 27 (discussion of the *Bowles* decision).

32. It is well established that the parol evidence rule bars only evidence of prior and contemporaneous agreements which are inconsistent with an integration. *See* City Nat'l Bank of Fort Smith v. First Nat'l Bank & Trust Co. of Rogers, 22 Ark. App. 5, 732 S.W.2d 489 (1987). *See also* U.C.C. § 2-202 (1978) (quoted in part *supra* note 22).

33. Perhaps the statement in the text would be more accurate if stated as: "the question

Just what section 9-306(2) means by "unless the disposition was authorized by the secured party" has provoked difference of opinion. This wording could mean that if the secured party has authorized the debtor to dispose of the collateral at all, then any disposition is one free of the security interest. Another possible reading is that if the secured party has authorized disposition conditionally (as, for exam-

should simply be whether an expressed or implied authorization can be found to have been expressed or implied." Some of the cases that have found U.C.C. § 1-205(4) operative to nullify evidence of implied authorizations for sale of collateral, on the ground that express terms of the security agreement control over course of dealing and trade usage, have involved conduct of the secured party occurring *after* the security agreement was made. An example is *North Central Kansas Prod. Credit Ass'n v. Washington Sales Co.*, 223 Kan. 689, 577 P.2d 35 (1978), where it was argued that the secured party had authorized further sales of collateral in a manner inconsistent with the express terms of the security agreement by acquiescing in the debtor's disposition of some of the collateral in violation of the security agreement. It appears that all of these instances of acquiescence occurred after the security agreement was executed. The court quoted U.C.C. §§ 1-205(4), 9-306(2) and 9-307(1), 223 Kan. at 692-93, 577 P.2d at 38, and concluded that the rationale of the New Mexican *Clovis* decision, 77 N.M. 554, 425 P.2d 726, was inconsistent with the intent of the framers of the Code, "particularly as expressed in the sections of the Code set forth above." 223 Kan. at 696, 577 P.2d at 41. Section 1-205(4) is logically irrelevant to conduct following the execution of a security agreement for "course of conduct" is defined as "a sequence of *previous* conduct . . . which is fairly to be regarded as establishing a common basis of understanding for interpreting [the parties'] expressions and other conduct." (Emphasis added.) See Dugan, *Buyer-Secured Party Conflicts Under Section 9-307(1) of the Uniform Commercial Code*, 46 U. COLO. L. REV. 333, 340 (1975).

Article 2 of the U.C.C. provides that post-agreement conduct of the parties may be resorted to in some circumstances as an aid to interpretation of a contract for the sale of goods, as a "course of performance," U.C.C. § 2-208(1) (1978), though not when it contradicts an express term of the agreement, *id.* § 2-208(2). But even if in conflict with express terms it may be effective as establishing a modification of the contract or as a waiver. *Id.* §§ 2-208(3), 2-209. If these provisions are applicable to Article 9 security agreements as well, they broadly authorize modification and waiver of contract terms after the parties reach an express agreement. It can be argued that these Article 2 provisions *are* applicable, since § 9-105(4) has the effect of adopting the definition of "agreement" in § 1-201(3), which incorporates by reference the "course of performance" rules of § 2-208. See *National Livestock Credit Corp. v. Schultz*, 653 P.2d 1243 (Okla. Ct. App. 1982); Dugan, *supra*, at 340-41. (This reasoning has been questioned (see Dolan, *supra* note 14, at 728), but even if the "course of performance" rules of Article 2 are not directly applicable to security agreements, they can legitimately be drawn upon by analogy, as expressive of sound contract law.) See Nickles, *A Localized Treatise on Secured Transactions*, *supra* note 27, at 662; Richards, *supra* note 17, at 389-91.

Some of the cases refusing to recognize post-security-agreement conduct of the secured party as impliedly authorizing future sales by the debtor are influenced by the fact that the security agreements in question expressly required *written* authorizations for disposition of collateral. While these cases have not usually gone to the extreme of holding that nothing but written authorization would do, they have insisted on *clear* oral or implied authorizations to overcome the contracts' express limitations. See, e.g., *Central California Equipment Co. v. Dolk Tractor Co.*, 78 Cal. App. 3d 855, 144 Cal. Rptr. 367 (1978); *Garden City Prod. Credit Ass'n v. Lannan*, 186 Neb. 668, 186 N.W.2d 99 (1971). *But see Oxford Prod. Credit Ass'n v. Dye*, 368 So. 2d 241 (Miss. 1979), which can be read as refusing to recognize any authorization of sale except by a writing, when the security agreement requires it in express terms.

ple, by authorizing sale on condition that the price be paid by check payable jointly to the debtor and the secured party), the security interest is divested only if the conditions of the authorization are complied with. A third possible reading is that a security interest continues in collateral despite the debtor's disposition of it unless the secured party has not only authorized that disposition but also consented to give up his security interest upon its occurrence. While there is substantial support for the third reading,³⁴ it adds more to the natural meaning of the statutory language than seems justified.³⁵ The first reading has been defended as well,³⁶ but it is also objectionable as reading too

34. See, e.g., *North Central Kansas Prod. Credit Ass'n v. Washington Sales Co.*, 223 Kan. 689, 577 P.2d 35 (1978); *Farmers State Bank v. Edison Non-Stock Coop. Ass'n*, 190 Neb. 789, 212 N.W.2d 625 (1973); *Garden City Prod. Credit Ass'n v. Lannan*, 186 Neb. 668, 186 N.W.2d 99 (1971); J. WHITE & R. SUMMERS, *HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE*, § 25-12, at 1066 (2d ed. 1980). The cases rely heavily on "waiver" reasoning and find no waiver of the security interest to result from the secured party's implied consent to the debtor's disposition of the collateral because it cannot be inferred (on the facts of the case) that the secured party knowingly surrendered his security interest. See Dolan, *supra* note 14, at 729-30; Nickles, *Rethinking Some U.C.C. Article 9 Problems*, *supra* note 33, at 108-9. See also *Fisher v. First Nat'l Bank*, 584 S.W.2d 515, 27 U.C.C. Rep. Serv. (Callaghan) 284 (Tex. Ct. App. 1979) (also relying on the "waiver" rationale but emphasizing a need for the party claiming waiver to show that he has been misled); *but cf.* *Farmers State Bank v. Farmland Foods*, 225 Neb. 1, 402 N.W.2d 277 (1987). (*Brown v. Arkoma Coal Corp.*, 276 Ark. 322, 634 S.W.2d 390 (1982) may reflect an assumption that consent to surrender the security interest must be found, but the opinion is not clear on this point.)

U.C.C. § 9-402(7) (1978) may also be considered to support this reading of § 9-306(2). It provides, in part, that, "[a] filed financing statement remains effective with respect to collateral transferred by the debtor even though the secured party knows of or consents to the transfer" and seems to imply that a security interest can continue in collateral notwithstanding a disposition by the debtor which has been authorized by the secured party. Some courts have sought to reconcile the two subsections by reading § 9-306(2) as operating to divest a security interest only when the secured party's consent to the disposition is clearly an authorization to dispose of the collateral *free and clear* of the security interest. E.g., *In re Matto's, Inc.*, 8 Bankr. 485 (Bankr. E.D. Mich. 1981). And see *In re Franchise Systems, Inc.*, 46 Bankr. 158 (Bankr. N.D. Ga. 1985) (purporting to follow *In re Matto's, Inc.*, 8 Bankr. 485, but stating its holding in narrower terms).

35. See *In re Hodge Forest Industries*, 59 Bankr. 801 (Bankr. D. Idaho 1986) (reasoning that continuance of a security interest after an authorized disposition of the collateral without refileing in the name of the transferee as debtor permits the existence of "secret liens", contrary to the underlying policy of Article 9). Cases cited *supra* note 34 as relying on "waiver" reasoning are not supported by the statutory language, which speaks of "authorized" "disposition" of the collateral, not "waiver" of the security interest. See Dolan, *supra* note 14, at 730. The apparent conflict with § 9-402(7) (see *supra* note 34) can be reconciled by reading that subsection as referring to a case where the secured party's authorization of the sale of the collateral is expressly conditioned on the transferee's taking the goods subject to the security interest. As is argued in the text *infra*, at notes 38-39, expressly imposed conditions of sale ought to be effective. That appears to be the actual holding of *In re Franchise Systems, Inc.*, 46 Bankr. 158, with the added limitation that the effectiveness of the condition is dependent on the transferee's awareness of the condition at the time of the transfer.

36. See Dolan, *supra* note 14, at 730 (arguing that the "unless" clause of § 9-306(2) is an

much into the statutory text; there is little reason to believe that section 9-306(2) was intended by the legislature to impose so stark a choice on secured parties.³⁷ The second reading enjoys considerable case support³⁸ and seems the soundest reading of the Act.³⁹

"open market rule . . . designed to protect purchasers," and that "[p]ermitting the lender and seller to modify it by a condition is as unjustified as permitting an entruster and bailee to modify the rule of Section 2-403(2) by private agreement.")

37. Professor Dolan's inference that § 9-306(2) embodies an "open market rule" comparable to that of § 2-403(2), *see supra* note 36, is not persuasive, because the rule of § 2-403(2) appears to be an application of the estoppel principle. *See infra* notes 61-63 and accompanying text for a discussion of this rule. An authorization by the secured party for the debtor's disposition of the collateral gives the debtor the power to transfer the goods free of the security interest under § 9-306(2) even though the purchaser of the collateral is unaware of the authorization, as Professor Dolan recognizes in another connection. Dolan, *supra* note 14, at 729. The rationale of § 9-306(2) is not that the secured party loses his security interest because he has led the purchaser to believe that he is willing to do so; it appears to be based simply on the fact that he has authorized the disposition.

38. *In re Sunriver Farms, Inc.*, 27 Bankr. 655, 36 U.C.C. Rep. Serv. (Callaghan) 416 (Bankr. D. Ore. 1982); *North Central Kansas Prod. Credit Ass'n v. Washington Sales Co.*, 223 Kan. 689, 577 P.2d 35 (1978); *Farmers State Bank v. Edison Non-Stock Coop. Ass'n*, 190 Neb. 789, 212 N.W.2d 625 (1973); *Baker Prod. Credit Ass'n v. Long Creek Meat Co.*, 266 Ore. 643, 513 P.2d 1129 (1973); *Southwest Washington Prod. Credit Ass'n v. Seattle-First Nat'l Bank*, 92 Wash. 2d 30, 593 P.2d 167 (1979). Some courts distinguish between an authorization for sale by the debtor on condition that he remit the proceeds of the sale to the secured party, and an authorization subject to such other condition as that payment for the collateral be made by check payable jointly to the debtor and the secured party, that the buyer's draft be honored, or that the debtor not have committed a prior default. These courts hold that non-compliance with a condition of the first type does not prevent the buyer from taking the collateral free of the security interest under § 9-306(2). *E.g.*, *North Central Kansas Prod. Credit Ass'n v. Washington Sales Co.*, 223 Kan. 689, 577 P.2d 35 (1978); *Anon, Inc. v. Farmers Prod. Credit Ass'n*, 446 N.E.2d 656, 37 A.L.R. 4th 776 (Ind. App. 1983). *Contra* *Southeast Washington Prod. Credit Ass'n v. Seattle-First Nat'l Bank*, 92 Wash. 2d 30, 593 P.2d 167 (1979). *See* Richards, *supra* note 17, at 382-84.

39. If the secured party is to lose his security interest on the ground that he has consented to the debtor's disposition of the collateral, it is logical to treat it as lost only if the disposition is the one authorized, not merely as to the type of disposition (*e.g.*, sale rather than gift) but also as to compliance with conditions imposed by the secured party regarding the manner in which the disposition is to be made. That also seems to accord with the natural reading of the statutory language: "unless *the* disposition was authorized." U.C.C. § 9-306(2) (1978) (*emphasis added*). The distinction between types of conditions drawn in some cases, *see supra* note 38, is not inconsistent with this reading of the Code, since a condition that the debtor remit the proceeds of the sale to the secured party is not a condition of the *disposition of the collateral* at all. Argument for a broader reading of the "unless" clause of § 9-306(2) as an "open-market" rule, *see supra* note 36, loses force in the light of other Code rules which protect purchasers of collateral in many instances even though the debtors' dispositions of the collateral were not authorized. Rules of this sort which protect buyers of encumbered goods are discussed in detail in the following text.

Most of the cases involving controversy over the application of the "unless" clause of U.C.C. § 9-306(2) have involved farm products collateral. Strains have developed in that context because of two phenomena. First, agricultural financiers have commonly declined to authorize the farmer-debtors to sell the collateral by the express terms of their security agreements (very frequently expressly forbidding sale of the collateral without the secured

At any rate, it is clear that if the secured party has not "authorized" the debtor to dispose of the collateral "in the security agreement or otherwise," the thrust of section 9-306(2) is to enable the secured party to pursue the collateral into the hands of purchasers and take it in foreclosure of his security interest.⁴⁰ For purposes of further analysis, let us assume that the sales by Holmes and Farrow to Cooper and Smith were *not* "authorized" by Bullion Bank. Does the bank win? Perhaps not. Despite the sweeping language of protection for the secured party that appears in sections 9-201 and 9-306(2), other Code rules command consideration. The rule of section 9-201 applies "[e]xcept as otherwise provided by this Act," and that of section 9-306(2) applies "[e]xcept where this Article otherwise provides." And much of the rest of Article 9 consists of rules punching holes in the impressive armor with which these basic rules appear to clothe the secured party.⁴¹

party's written authorization), or they have authorized sales only under specific conditions, yet the lenders in practice have allowed the debtors to dispose of the collateral as they saw fit, until trouble developed from particular sales; then they have insisted that the terms of the security agreements prevented application of the "unless" clause of § 9-306(2). Second, the exemption of farm products from the open-market rule of § 9-307(1) has forced buyers of such products to seek protection by way of § 9-306(2)'s "unless" clause more innovatively than buyers of other types of encumbered inventory have found necessary. See discussion in *Moffatt County State Bank v. Producers Livestock Marketing Ass'n*, 598 F. Supp. 1562 (D. Colo. 1984).

40. See U.C.C. § 9-306 comment 3 (1978). Repossession of the collateral is not the only possible remedy open to the secured party. An alternative remedy often available against the purchaser into whose hands the collateral can be traced is an action for conversion. *E.g.*, *United States v. Riceland Foods, Inc.*, 504 F. Supp. 1258 (E.D. Ark. 1981); *Baker Prod. Credit Ass'n v. Long Creek Meat Co.*, 266 Ore. 643, 513 P.2d 1129 (1973). A conversion action will sometimes lie as well against an auctioneer or other selling agent who participates in the debtor's unauthorized sale of the collateral. *E.g.*, *North Central Kansas Prod. Credit Ass'n v. Washington Sales Co.*, 223 Kan. 689, 577 P.2d 35 (1978); *First National Bank & Trust Co. v. Atchinson County Auction Co.*, 10 Kan. App. 2d 382, 699 P.2d 1032 (1985). See B. CLARK, *supra* note 15, § 8.4[3][c] at 8-28; Nickles, *A Localized Treatise on Secured Transactions*, *supra* note 27, at 654-56; Van Hooser, *Farm Products: Recent Legislative Changes to Section 9-307*, 29 S.D.L. REV. 346, 348-49 (1984).

41. No attempt is made in this article to canvass all of the rules of Article 9 which operate to create exceptions to the general rules protecting secured parties in U.C.C. §§ 9-201 and 9-306(2) (1978), as many are irrelevant or only remotely related to the type of fact situation with which this article is concerned. Article 9 includes, for example, elaborate rules for determining priority between conflicting security interests in the same collateral, but these rules are not pertinent to contests between secured parties and buyers of collateral. *E.g.*, U.C.C. § 9-312 (1978). Discussion of Article 9 rules governing contests between buyers of collateral other than goods and secured parties, *see, e.g., id.* §§ 9-308, 9-309, is omitted as too remotely connected with the type of problem dealt with here, as is discussion of rules relating to security interests in fixtures, *id.* § 9-313, accessions, *id.* § 9-314, and commingled and processed goods, *id.* § 9-315, and special rules governing priorities where proceeds of collateral are involved, *e.g., id.* § 9-306(5).

Occasionally, rules appearing in other articles of the U.C.C. can be invoked by a buyer of

One such rule is found in section 9-301(1)(c):

Except as otherwise provided in subsection (2), an unperfected security interest is subordinate to the rights of . . .

(c) in the case of goods, . . . a person who is not a secured party and who is a transferee in bulk or other buyer not in the ordinary course of business or is a buyer of farm products in ordinary course of business, to the extent that he gives value and receives delivery of the collateral without knowledge of the security interest and before it is perfected; . . .⁴²

The impact of this rule is difficult to grasp at first reading because, although it clearly protects some buyers of goods from some security interests in the goods, it appears to offer such protection only to an oddly assorted group of buyers: (1) those who are *not* "buyers in ordinary course of business" and (2) those who *are* "buyers in ordinary course of business" but only *if* they are buyers of "farm products." This selection makes more sense when the quoted passage is read together with the rule of section 9-307(1), for the latter section (which will be discussed at length below) grants a broader protection to the types of buyers of goods who are left out of the coverage of section 9-301(1)(c). Thus, the buyers not protected by the earlier section are those who do not need its protection.⁴³

encumbered collateral as protection against the claim of a secured party. It should be noted that the broad rule of § 9-201 applies "[e]xcept as otherwise provided by this Act," not "this Article." For example, § 2-403(2) has at times been useful to buyers who could not find their protection in Article 9. *E.g.*, *Executive Financial Services v. Pagel*, 238 Kan. 809, 715 P.2d 381 (1986). See Dugan, *supra* note 33, at 333. Such possibilities are not comprehensively explored in this article.

42. U.C.C. § 9-301(1)(c) (1978). The words "or a buyer of farm products in ordinary course of business" were added to Arkansas' § 9-301(1)(c) in 1973. Act of Feb. 13, 1973, No. 116, 1973 Ark. Acts 345 (codified at ARK. CODE ANN. § 4-9-301(1)(c) (1987)). See *supra* note 13. The new language appears to have been inserted to remedy an oversight in the drafting of the prior version of this subsection.

43. There is one apparent exception to the statement in the text. A buyer who qualifies for the protection of § 9-301(1)(c) is protected against an unperfected security interest, without regard to whether the security interest was created by the immediate seller of the goods or by some prior owner. Under § 9-307(1) a buyer in ordinary course of business (other than a buyer of farm products from a farmer) takes free of a security interest whether it is perfected or not, whether the buyer is aware of the security interest or not, and whether he takes possession of the collateral or not, but only if the security interest was "created by his seller." See *infra* notes 55-56 and accompanying text. That leaves open the relation between a buyer in ordinary course of business of inventory other than farm products and the holder of an unperfected security interest which was created by a predecessor of the immediate seller and which was enforceable against the seller. Such a buyer may be protected by the rule of § 2-403(2). See *infra* notes 61-63 and accompanying text. But that rule would not necessarily apply, and if not, the general rule of § 9-201 would probably make the security interest enforceable against the buyer. *But see* Dugan, *supra* note 33, at 351-54 (arguing that the "created by his seller"

The substance of section 9-301(1)(c) is that if a buyer buys goods subject to an "unperfected" security interest and he both gives value for them and takes possession of them without knowing of the security interest and before it is perfected, he takes the goods free of the security interest,⁴⁴ and that is true even if the secured party has not "authorized" the sale "in the security agreement or otherwise." If Bullion Bank's security interests were "unperfected" when Holmes and Farrow made their unauthorized sales to Cooper and Smith, since we are assuming that both buyers gave value and received possession of the goods purchased without knowledge of the bank's security interests, they would be immune to the bank's claims to the goods.

"Perfection" is a technical term of some complexity, but on the facts of the problem posed, it would probably⁴⁵ require that Bullion Bank have filed notices of its security interest in public offices.⁴⁶ The notices that are required to be filed are termed "financing statements" in Article 9. Although the Code imposes formal requirements for

limitation in § 9-307(1) should be construed as applicable only if the security interest involved is a perfected one; by this reading § 9-307(1) would protect the buyer).

It should be noted also that subsection (2) of § 9-301 creates a very limited exception to the rule of § 9-301(1)(c): when a secured party who has a "purchase money security interest", see U.C.C. § 9-107, perfects his interest by filing within 10 days after the debtor receives possession of the collateral, he takes priority over a "transferee in bulk" who would otherwise be entitled to priority under subsection (1)(c). U.C.C. § 9-301(2) (1978). In Arkansas, subsection (2) was amended in 1983 to change the time limit for filing from 10 days to 21 days. See Act of Mar. 21, 1983, No. 561, § 2, 1983 Ark. Acts 1190 (codified at ARK. CODE ANN. § 4-9-301(2) (1987)).

44. Though § 9-301(1) says that the security interest is "subordinate to the rights of" the buyer, rather than that the buyer takes the goods "free of" the security interest, the practical effect is the same. The security interest is not enforceable against the buyer, and the buyer can pass on his immunity to a purchaser from him, under § 2-403(1).

45. U.C.C. § 9-302(1): "A financing statement must be filed to perfect all security interests except the following:" The principal alternative method of perfection is for the secured party to take possession of the collateral, and perfection by that method normally continues only as long as possession is retained. *Id.* §§ 9-302(1)(a), 9-305. In some instances, none of much significance in the context of the cases discussed in this article, a security interest can be perfected without either filing or possession, sometimes permanently (in the case of a purchase money security interest in consumer goods, *id.* § 9-302(1)(d)), sometimes temporarily (as in the case of certain proceeds, *id.* §§ 9-302(1)(b), 9-306(3)). Statutes other than the Code may control perfection of security interests in some types of collateral. See, e.g., *id.* § 9-302(3) (motor vehicles subject to certificate of title laws).

46. The security interest must also have "attached" to the collateral. *Id.* § 9-301(1). A security interest attaches when

- (a) the collateral is in the possession of the secured party pursuant to agreement, or the debtor has signed a security agreement which contains a description of the collateral and in addition, when the security interest covers crops growing or to be grown or timber to be cut, a description of the land concerned; (b) value has been given; and (c) the debtor has rights in the collateral.

Id. § 9-203(1). See also *id.* § 9-203(2).

such statements,⁴⁷ they are not onerous. Basically, a financing statement must identify the parties to the security agreement, provide addresses for both, describe the collateral by item or type, in the case of growing crops as collateral describe the real estate where the crops are growing or to be grown, and be signed by the debtor.⁴⁸ The terms of the security agreement need not otherwise be shown, as the purpose of the financing statement is merely to give notice of any potential outstanding security interest in the described collateral and give the searcher of the record leads to sources of further information.⁴⁹

As to where the filing must be made, the Official Text of the Uniform Commercial Code offers enacting legislatures a choice of rules;⁵⁰ the Arkansas legislature has chosen the "Third Alternative."⁵¹ Under this version of section 9-401(1) the bank would have to

47. *Id.* § 9-402.

48. *Id.* § 9-402(1). Additional requirements apply to financing statements covering timber to be cut, minerals and accounts arising from their sale, and fixtures. *Id.* § 9-402(1), (5). In some instances, the signature of the secured party may be substituted for that of the debtor. *Id.* § 9-402(2). "A financing statement substantially complying with the requirements of this section is effective even though it contains minor errors which are not seriously misleading." *Id.* § 9-402(8). Furthermore, "any description of personal property or real estate is sufficient whether or not it is specific if it reasonably identifies what is described." *Id.* § 9-110. See *United States v. Riceland Foods, Inc.*, 504 F. Supp. 1258 (E.D. Ark. 1981).

The Arkansas U.C.C., as originally enacted, conformed to the then-current Official Text by requiring the signatures of both the debtor and the secured party on a financing statement. Act of Mar. 7, 1961, No. 185, 1961 Ark. Acts 421, 686 (codified at ARK. STAT. ANN. § 85-9-402(1) (1961) amended 1973, current version at ARK. CODE ANN. § 4-9-402(1) (1987)). The requirement that the secured party sign the statement was deleted by a 1973 amendment to conform to a change in the Official Text. Act of Feb. 13, 1973, No. 116, § 1, 1973 Ark. Acts 345, 391 (codified at ARK. CODE ANN. § 4-9-402(1) (1987)). See *supra* note 13.

49. U.C.C. § 9-402 comment 2 (1978).

50. *Id.* § 9-401(1). This subsection of the Official Text is offered to enacting legislatures in three forms. Under all three versions filing as to collateral in the form of timber to be cut, minerals or the like or accounts arising from their sale, or fixtures as to which fixture filing is planned must be made in the office where a mortgage on the real estate involved would be filed or recorded. Filing as to all other forms of collateral is required in a state central filing office (such as the office of the state Secretary of State) under the First Alternative. Under the Second and Third Alternative, local (county) filings are prescribed for farm equipment collateral, farm products, accounts or general intangibles arising from farmers' sales of farm products, and consumer goods. As to all other forms of collateral, the Second Alternative calls simply for filing in a central state office, while the Third Alternative calls for central filing plus, in some cases, local filing. *Id.*

51. ARK. CODE ANN. § 4-9-401(1) (1987):

The proper place to file in order to perfect a security interest is as follows:

- (a) When the collateral is equipment used in farming operations, or farm products, or accounts or general intangibles arising from or relating to the sale of farm products by a farmer, or consumer goods, then in the office of the clerk of the circuit court and ex officio recorder in the county of the debtor's residence or if the debtor is not a resident of this state then in the office of the clerk of the circuit court and ex officio recorder in the county where the goods are kept, and in addition when the

file, as to Farrow's soybean crop, in the office of the Circuit Court Clerk of the county in which Farrow resided, and if the crop was being grown on land in another county, then in the office of the Clerk of the Circuit Court of that county as well.⁵² In the case of Holmes' refrigerators, the bank would have to file in the office of the Arkansas Secretary of State and, if Holmes had a place of business in only one county of the state, then also in the office of the Clerk of the Circuit Court of the county in which his business was located.⁵³

But let us assume that Bullion Bank *had* perfected its security interests in Farrow's crop and Holmes' refrigerators by proper filings before Cooper and Smith made their purchases. Now, is the bank on solid ground in asserting rights to the goods which Cooper and Smith purchased? Section 9-307(1) still has to be considered. It provides:

A buyer in ordinary course of business (subsection (9) of Section 1-201) 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 even though the buyer knows of its existence.⁵⁴

The term "buyer in ordinary course of business" is elaborately defined by the Code.⁵⁵ Its main features are as follows:

"Buyer in 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 interest of a third party in the goods buys in ordinary course from a person in the business of selling goods of that kind "Buying" may be for cash or by exchange of other property or on secured or unsecured credit and

collateral is crops growing or to be grown, in the office of the clerk of the circuit court and ex officio recorder in the county where the land is located;

(b) When the collateral is timber to be cut or is minerals or the like (including oil and gas) or accounts subject to § 4-9-103(5), or when the financing statement is filed as a fixture filing § 4-9-313 and the collateral is goods which are or are to become fixtures, then in the office where a mortgage on the real estate would be filed or recorded;

(c) In all other cases, in the office of the Secretary of State and in addition, if the debtor has a place of business in only one county of this state, also in the office of the clerk of the circuit court and ex officio recorder of such county, or, if the debtor has no place of business in this state, but resides in the state, also in the office of the clerk of the circuit court and ex officio recorder of the county in which he resides.

The Arkansas Code version of this subsection contains minor differences in style from the previous version in the Arkansas Statutes Annotated.

52. *Id.* § 4-9-401(1)(a).

53. *Id.* § 4-9-401(1)(c).

54. U.C.C. § 9-307(1) (1978).

55. *Id.* § 1-201(9).

includes receiving goods or documents to title under a pre-existing contract for sale but does not include a transfer in bulk or as security for or in total or partial satisfaction of a money debt.⁵⁶

Cooper and Smith may well qualify as "buyers in ordinary course of business." Both paid cash. Both were unaware of Bullion Bank's security interests and *a fortiori* "without knowledge that the sale [was] in violation of the . . . security interest[s]." Both were probably acting in "good faith."⁵⁷ Both were buying from persons who were "in the business of selling goods of [the] kind." And both may have bought "in ordinary course."⁵⁸ If so, are they protected from the bank's claim by section 9-307(1)? Cooper is; Smith is not. Cooper

56. *Id.* The definition does not say that the buyer must have taken possession of the goods to qualify as a "buyer in ordinary course of business," and the omission appears to have been deliberate. See 2 G. GILMORE, *supra* note 17, § 26.6, at 693-97. However, failure of the buyer to take possession may affect the decision whether he has bought "in good faith." See *Sherrock v. Commercial Credit Corp.*, 277 A.2d 708, 9 U.C.C. Rep. Serv. (Callaghan) 294 (Del. Super. 1971), *rev'd* 290 A.2d 648, 10 U.C.C. Rep. Serv. (Callaghan) 523 (Del. 1972).

57. "Good faith" is defined, in the "General Provisions" article of the U.C.C. (Article 1) as meaning "honesty in fact in the conduct or transaction concerned." U.C.C. § 1-201(19) (1978). In the "Sales" article (Article 2) there is a special definition of "good faith": "In this Article unless the context otherwise requires . . . 'Good Faith' in the case of a merchant means honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." *Id.* § 2-103(1)(b). The applicability of this special definition to a buyer who is a "merchant" and claims to be a "buyer in ordinary course of business" is questionable, since the definition of "good faith" in § 2-103(1)(b) applies "[i]n this Article," *i.e.*, in Article 2, and the definition of "buyer in ordinary course of business" appears in Article 1. *Id.* § 1-201(9). See *Sherrock v. Commercial Credit Corp.*, 290 A.2d 648, 10 U.C.C. Rep. Serv. (Callaghan) 523 (Del. 1972). However, it is tempting to read the definition of "merchant's good faith" in § 2-103(2) into the definition of "buyer in ordinary course of business" because it is hard to see any justification for holding merchant buyers to a stricter standard of conduct in some sales contexts than in others. Some courts have adopted this reading. See, *e.g.*, *Swift v. J. I. Case Co.*, 266 So. 2d 379, 11 U.C.C. Rep. Serv. (Callaghan) 190 (Fla. Dist. Ct. App. 1972). See *also* B. CLARK, *supra* note 15, § 3.4[1], at 3-20.

Both Cooper and Smith, in the hypothetical case discussed in the text of this article, would be "merchants," as defined in § 2-104(1). The term includes "a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction." If the Article 2 "good faith" definition applies under § 1-201(9), they could not qualify as "buyers in ordinary course of business" unless they observed the "reasonable commercial standards of fair dealing in [their trades]" in making their purchases. To avoid extended discussion of a topic peripheral to the main concern of this article, such compliance is assumed.

58. Buying "in ordinary course" is not defined in the Code or its comments. It has been suggested that the concept is similar to "ordinary course of trade," as used in the Uniform Trust Receipts Act (one of the Uniform Acts which the U.C.C. replaced). 2 G. GILMORE, *supra* note 17, § 26.6, at 695. The idea is that the sale is of a sort that the seller normally makes in the course of his business, or which is normal for a person in his line of business to make. See *Merchants & Planters Bank & Trust Co. of Arkansas v. Phoenix Housing Systems*, 21 Ark. App. 153, 729 S.W.2d 433 (1987); *cf.* J. WHITE & R. SUMMERS, *supra* note 34, § 25-13, at 1069.

is protected because he qualifies for protection under the general rule stated in 9-307(1). Smith is not because he falls within the exception to that rule; he bought "farm products"⁵⁹ from a person engaged in farming operations."

Would Smith be protected by any other rule of Article 9? Not on the facts we've got. As the Arkansas Code stood prior to the recent legislation, Bullion Bank could take the soybeans from Smith and sell them to obtain funds to apply to Farrow's loan, but the bank would have no valid claim to the refrigerators which Cooper bought from Holmes if Cooper qualified as a "buyer in ordinary course of business."

Why does section 9-307(1) protect most buyers in ordinary course from security interests created by their sellers, even if the buy-

59. The term "farm products" is defined, in the 1978 Official Text of the Code, as follows: Goods are . . . "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 states (such as ginned cotton, wool-clip, maple syrup, milk and eggs), and if they are in the possession of a debtor engaged in raising, fattening, grazing or other farming operations. If goods are farm products they are neither equipment nor inventory.

U.C.C. § 9-109(3) (1978). (In Arkansas the definition is the same, except that a sentence has been inserted after "farming operations" by an amendment of 1971 providing that: "'Farm products' shall also include fish grown for sale on any fish farm." Act of Mar. 23, 1971, No. 363, 1971 Ark. Acts 881 (codified at ARK. CODE ANN. § 4-9-109(3) (1987)). Note that, to qualify as "farm products," goods must not only be crops, livestock or supplies "used or produced in farming operations" but also must be "in the possession of a debtor engaged in . . . farming operations." See Meyer, *The 9-307(1) Farm Products Puzzle: Its Parts and Its Future*, 60 N.D.L. REV. 401, 405-15 (1984).

"Farm products" is one of four mutually exclusive classifications of goods collateral in Article 9, the others being "consumer goods," U.C.C. § 9-109(1) (1978); "equipment," *id.* § 9-109(2); and "inventory," *id.* § 9-109(4). The classification into which collateral in the form of goods falls is significant because a number of the rules governing perfection of security interests, *e.g.*, *id.* § 9-401(1) (Second and Third Alternatives); priorities, *e.g.*, *id.* §§ 9-301(1)(c), 9-307(1); and rights and remedies upon default, *e.g.*, *id.* § 9-505, vary in their operation depending upon the classification of the collateral.

The critical time for classifying the collateral, with respect to any particular security interest, is the time the interest "attaches" to the goods. See R. HENSON, *HANDBOOK ON SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE* § 5-2, at 119 (2d ed. 1979); J. WHITE & R. SUMMERS, *supra* note 34, § 23-7 at 925. Unfortunately, the U.C.C. does not clearly so provide, and even the comments can be read as indicating otherwise. See, *e.g.*, *United States v. Progressive Farmers Mktg. Agency*, 788 F.2d 1327 (8th Cir. 1986) (relying on comment 4 to § 9-109 of the Official Text to conclude that under the Iowa U.C.C. goods are to be classified as "farm products" or "inventory," for purposes of § 9-307(1), as of the time they are sold, so that a sale of hogs by a commission merchant to whom they had been delivered by the farmer-debtor for sale was not a sale of "farm products" and hence not within the "farm products" exception to § 9-307(1)).

Although in this article farm products are sometimes described as a farmer's "inventory," that categorization refers to economic function. For purposes of the *rules of Article 9*, "farm products" are to be distinguished from "inventory."

ers know of the security interests, but except buyers of farm products who buy from farmers?

The general rule of section 9-307(1) is readily accounted for; it is consistent with the historical trend of Anglo-American law over the past century or more, a trend away from the classic doctrine of *caveat emptor*, with its emphasis on security of property rights, toward protection of good faith purchasers in the marketplace. A need to promote trade has powered the trend. Although the progress of the law has not been a smooth one, the cumulative effect of the resulting changes has been to provide greatly increased protection for those who purchase in good faith, without knowledge that the property rights of third persons are being infringed.⁶⁰

The Uniform Commercial Code codified much of the law as it had developed in the pre-Code cases and statutes, and it pushed the trend along. In section 2-403(2), for example, it laid down a principle that went beyond prior law⁶¹ by providing that, "[a]ny entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business."⁶² The rationale of the rule apparently is that persons buying, in normal course of business, goods of a sort which the seller is in the business of selling are justified in assuming that the seller has the right to make the sales, and should be protected in that reasonable assumption since the "entruster" can fairly be held responsible for creating the misleading impression of the seller's right

60. See Gilmore, *The Commercial Doctrine of Good Faith Purchase*, 63 YALE L.J. 1057 (1954).

61. See 2 S. WILLSTON, *THE LAW GOVERNING SALES OF GOODS AT COMMON LAW AND UNDER THE UNIFORM SALES ACT*, Ch. 14 (Rev. ed. 1948) (see especially § 314).

62. U.C.C. § 2-403(2) (1978). In Arkansas the corresponding subsection was, and remains, identical to the Official Text, ARK. STAT. ANN. § 85-2-403(2) (1961) (current version at ARK. CODE ANN. § 4-2-403(2) (1987)), but the scope of this portion of the Arkansas U.C.C. was reduced by an enactment in 1981, § 2 of which provides that

ownership of grain shall not change by reason of an owner delivering grain to a public warehouseman. No public grain warehouseman shall sell or encumber any grain within his possession unless the owner of the grain has by written document transferred title of the grain to the warehouseman. Notwithstanding any provision of the Uniform Commercial Code . . . to the contrary, . . . all sales and encumbrances of grain by public grain warehousemen are void and convey no title unless such sales and encumbrances are supported by a written document executed by the owner specifically conveying title to the grain to the public grain warehouseman.

Act of Mar. 10, 1981, No. 401, § 2, 1981 Ark. Acts 705 (codified at and quoting from ARK. CODE ANN. § 2-17-303 (1987)). See also Note, *Warehousemen—Storers of Grain—Arkansas Stands Alone in Protecting the Rights of Depositors of Grain in Public Warehouses*, 9 UALR L.J. 699 (1986-87) (further discussion of Act 401).

to sell.⁶³

The general rule of section 9-307(1) can be thought of as an application of this principle, though as a matter of legal history it is based on precedents that antedate the rule of section 2-403(2).⁶⁴ When a secured party leaves possession of goods collateral in the hands of a debtor who is in the business of selling such goods, buyers from the debtor are no more likely to suspect that the sales to them violate rights of a secured party than they are to anticipate violation of the rights of an owner, and they ought to have the same sort of protection against the security interest. Furthermore, the secured party is as much responsible for creating a deceptive appearance of the debtor's right to sell as is any other "entruster" of goods to a "merchant who deals in goods of that kind."⁶⁵

The protection of good faith purchasers provided by the Code has not gone so far as to protect *all* such purchasers from adverse property claims. The rule of section 2-403(2) operates only to cut off the rights of an "entruster"⁶⁶ of the goods, and then only in favor of a rather narrowly defined class of good faith purchasers. Similarly, the rule of section 9-307(1) protects only a "buyer in ordinary course of business," and the protection is against only security interests "created by his seller." The security of property rights of owners of the goods is protected under section 2-403(2) if they have not made or authorized the "entrustment," and section 9-307(1) does not imperil the security interests of persons whose interests were granted by prior owners of the goods.

Nevertheless, the general rule of section 9-307(1) is a sweeping one, applicable to all cases where security interests have been taken in

63. A number of cases treat the rule of § 2-403(2) as based on the principle of estoppel, although applicable to cases where common law cases had not found estoppels. *See, e.g.,* Porter v. Wertz, 68 A.D.2d 141, 416 N.Y.S.2d 254 (N.Y. App. Div., 1st Dep't 1979), *aff'd*, 53 N.Y.2d 696, 439 N.Y.S.2d 105, 421 N.E.2d 500 (1981) ("statutory estoppel"). Consistently with that rationale, a lower court held that the rule does not apply unless both the entruster and the buyer were aware that the seller was in the business of selling goods of the kind being sold. *Atlas Auto Rental Corp. v. Weisberg*, 54 Misc. 2d 168, 281 N.Y.S.2d 400 (1967).

64. Professor Gilmore considered the antecedents of § 9-307(1) to be pre-Code chattel mortgage cases, the conditional sales acts, the Uniform Trust Receipts Act, and the various factor's lien acts. 2 G. GILMORE, *supra* note 17, §§ 26.2-6.

65. *See Merchants & Planters Bank & Trust Co. v. Phoenix Housing Systems, Inc.*, 21 Ark. App. 153, 729 S.W.2d 433 (quoting *Ex parte* General Motors Acceptance Corp., 425 So. 2d 464 (Ala. 1983)).

66. "Entrusting" is defined in the U.C.C. as including "any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor's disposition of the goods have been such as to be larcenous under the criminal law." U.C.C. § 2-403(3) (1978).

the inventory of businessmen to secure their debts, *except* where the debtor is a farmer and the security interest is in his "farm products" inventory. Why this exception? It appears originally to have been incorporated into the section to reflect the case law prevailing at the time the U.C.C. was drafted.⁶⁷ Professor Grant Gilmore, one of the principal draftsmen of Article 9,⁶⁸ has written that pre-Code cases had quite uniformly been ruling in favor of the holders of crop and livestock mortgages against good faith buyers from the mortgagors, when those sales had not been authorized by the mortgagees, "for reasons . . . never precisely articulated,"⁶⁹ and without attempting to explain why the rule should be different in such cases from that applied in cases involving sales of inventory by other types of businessmen.⁷⁰

One justification for the farm-products exception is that it is essential if farmers are to obtain the credit they need to finance their farming operations, because the major suppliers of such credit insist on that protection.⁷¹ That insistence, in turn, is attributed partly to historical patterns of agricultural financing,⁷² partly to a concept that farmers are less to be trusted to deal responsibly with their creditors than other debtors,⁷³ and partly to the large role played by the federal government in agricultural financing in the past half-century, a type of financing characterized by concern for maximum protection of the federal financing agencies displayed both by the agencies themselves and by the federal courts.⁷⁴

67. See 2 G. GILMORE, *supra* note 17, § 26-10, at 707.

68. See J. WHITE & R. SUMMERS, *supra* note 34, § 1, at 4.

69. 2 G. GILMORE, *supra* note 17, § 26.10, at 707.

70. See *id.*, § 26.10, at 714.

71. See Dolan, *supra* note 14, at 716; Note, *Agricultural Financing Under the U.C.C.*, 12 ARIZ. L. REV. 391, 411 (1970). See also Meyer, *supra* note 26, at 436-37.

72. Dolan, *supra* note 14, at 712.

73. "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.

Professor Peter Coogan, in Coogan & Mays, *Crop Financing and Article 9: A Dialogue with Particular Emphasis on the Problems of Florida Citrus Crop Financing*, 22 U. MIAMI L. REV. 13, 19 (1967). See also Hawkland, *supra* note 13, at 418; Richards, *supra* note 17, at 375.

74. Dolan, *supra* note 14, at 720-22; Hawkland, *supra* note 13, at 420. Supporting arguments have been that most sales of farm products more nearly resemble bulk sales than sales of inventory; that the typical buyers of farm products are knowledgeable professionals who can look out for themselves; and that agricultural lenders more commonly rely on the proceeds of sales of collateral for repayment of their loans than is true of most lenders on the security of inventory. See Clark, *Uniform Commercial Code Survey: Secured Transactions*, 42 BUS. LAW. 1333, 1335 (1987); see also sources cited *supra* notes 71 and 73. The numerous other discussions of the reasons for the "farm products" exception to the general rule of § 9-307(1)

That the exception has its inconvenient side for farmers, and agricultural lenders as well, seems fairly obvious, however. The effect of the exception is to place a risk on buyers of farm products with which ordinary course buyers of the inventory of other businessmen need not concern themselves. It is thus likely to make potential buyers of farm products wary of entering into such transactions; if they do, the prices they are willing to pay are likely to be lower than they would be if the general rule of section 9-307(1) applied, since the buyers must either bear the expense of investigating the farmers' titles to the goods they offer for sale or must pay for a title of unknown quality. Furthermore, these limitations on the marketability of farm products do not stop with the first sale; resale buyers of farm products are also subject to the claims of the agricultural lenders.⁷⁵ The net effect is not only to hamper the farmers' ability to sell their products at favorable prices but also to hamper their ability to repay those who financed their operations.⁷⁶

It is also unfair to buyers in ordinary course of farm products to compel them, in effect, to pay twice for the goods they buy. Not only are they more vulnerable than other ordinary course buyers of inventory, but they are often less capable of protecting themselves by discovering the existence of security interests in the goods they buy. As has been noted above,⁷⁷ under the Arkansas U.C.C. (and under the Codes of many other states as well)⁷⁸ a person making a loan to a businessman on the security of his inventory must usually make a fil-

include: Fry, *Buying Farm Products: The 1985 Farm Bill Changes the Rules of the Game*, 91 COM. L.J. 433, 437-38 (1986); Meyer, *Agricultural Credit and the Uniform Commercial Code: A Need for Change?*, 34 U. KAN. L. REV. 469, 484-86 (1985); Sanford, *The Reborn Farm Products Exception Under the Food Security Act of 1985*, 20 U.C.C. L.J. 3, 5 (1987); Note, *The Federalization of the Farm Products Exception Rule of U.C.C. 9-307(1): Anomaly or Opening Salvo*, 36 DRAKE L. REV. 115, 116-17 (1987) [hereinafter Note, *The Federalization of the Farm Products Exception*]; Note, *Section 1324 of the Food Security Act of 1985: Congress Preempts the "Farm Products Exception" of Section 9-307(1) of the Uniform Commercial Code*, 55 UMKC L. REV. 454, 456-58 (1987) [hereinafter Note, *Section 1324 of the Food Security Act*]; Note, *Federal Legislation Provides Protection for Buyers of Farm Products: Food Security Act Supersedes the Farm Products Exception of U.C.C. Section 9-307(1)*, 47 U. PITT. L. REV. 749, 752-54 (1986) [hereinafter Note, *Federal Legislation Provides Protection*].

75. This follows because the buyer from the farmer takes subject to the security interest, by virtue of the "farm products" exception to § 9-307(1), and no subsequent buyer can qualify for the protection of that subsection because the security interest is not one "created by his seller." See Dolan, *supra* note 14, at 713-14; Hawkland, *supra* note 13, at 419-20. But see Dugan, *supra* note 33, at 345-51.

76. See Dolan, *supra* note 14, at 712-15.

77. See *supra* notes 50-53 and accompanying text.

78. The great majority of jurisdictions adopting the U.C.C. have chosen either the Second or Third Alternative version of § 9-401(1). U.C.C. § 9-401 notes, 3A U.L.A. 20 (1981 & Supp. 1987). The only difference between the Second and Third Alternatives is that paragraph

ing in a state office (the office of the Secretary of State in Arkansas), with or without an additional local filing. But holders of security interests in farm products need file only in county offices, perhaps only in one such office. A buyer of farm products, particularly a resale buyer (for example, one who buys from a broker who has acquired the goods from the farmer who created the security interest) may not know the source of the goods with sufficient particularity to know where he should go to find filed financing statements covering the products.⁷⁹ And whether one regards this as unfair to the buyer or not, it surely has an additional inhibiting effect on the marketability of farm products.⁸⁰

Another criticism of the farm-products exception has been that the security it affords to agricultural financiers has encouraged lax lending and financing practices, that suppliers of agricultural credit count on the law to protect them, rather than taking the trouble to select borrowers with a view to their trustworthiness or attempting to police their debtors' use of the collateral,⁸¹ shifting the burden of the risk of debtor default to innocent buyers of the collateral.⁸²

Discontent with the "farm products" exception of section 9-307(1) was reflected in a large minority of states (prior to the passage of the recent legislation discussed below) by amendments of the Codes of those states. A study published in 1985 found that nineteen states had modified section 9-307 or related sections of the U.C.C., fourteen of them since 1983.⁸³ These departures from the Official Text were of

(c) of the Third Alternative requires local filing in some instances, in addition to central filing, whereas that paragraph of the Second Alternative requires only central filing.

79. See Dolan, *supra* note 14, at 717-18. Livestock buyers are at a special disadvantage, since the Packers and Stockyards Act, 7 U.S.C. § 228b(a) (1982), requires that payment be made on the day following the sale. See Meyer, *Agriculture Credit and the Uniform Commercial Code: A Need for Change?*, 34 U. KAN. L. REV. 469, 490 (1985); Richards, *supra* note 17, at 395.

80. See Dolan, *supra* note 14, at 719.

81. See Note, *Clear Title: A Buyer's Bonus, a Lender's Loss—Repeal of UCC § 9-307(1) Farm Products Exception by Food Security Act § 1324 [7 U.S.C. § 1631]*, 26 WASHBURN L.J. 71, 77 (1986).

82. See H.R. REP. NO. 271, 99th Cong., 1st Sess., pt. 1, at 109, quoted *infra* note 136. For other criticisms of the "farm products" exception to U.C.C. § 9-307(1) (1978), see S. Rep. No. 147, 99th Cong., 1st Sess., 2-3 (1985); Fry, *supra* note 74, at 438-39; Meyer, *supra* note 74, at 486-87; Richards, *supra* note 17, at 374-77, 395; Van Hooser, *supra* note 40, at 347-48; Note, *The Federalization of the Farm Products Exception*, *supra* note 74, at 117-18; Note, *Federal Legislation Provides Protection*, *supra* note 74, at 752-54.

83. Uchtmann, Bauer & Dudek, *The U.C.C. Farm Products Exception—A Time to Change*, 69 MINN. L. REV. 1315, 1316 (1985). See also Meyer, *supra* note 26, at 433-34. The latter article cites Arkansas as one of the 16 states that had modified the operation of § 9-307(1) as of the Fall of 1983, but the reference is apparently to Arkansas' modification of the rule of § 9-306(2), discussed above at notes 28-30. For other discussion of state variations

great variety, ranging from total⁸⁴ or partial⁸⁵ repeal of the "farm products" exception to elaborate arrangements for central filing of security interests in farm products,⁸⁶ requirements that secured parties give direct notice of their security interests to potential buyers of farm products collateral in order to preserve the enforceability of their security interests,⁸⁷ and requirements that buyers of farm products follow specified procedures to learn of security interests in those products and see that payments for the products were applied to secured debts of which they learned, in order to take the goods free of the security interests.⁸⁸

II. THE NEW FEDERAL LEGISLATION

A. Summary of the Legislation

The "clear title" section⁸⁹ of the Food Security Act of 1985,⁹⁰ overriding any contrary provision of state law,⁹¹ decrees that (subject to some exceptions) "a buyer who in ordinary course of business buys a farm product from a seller engaged in farming operations shall take free of a security interest created by the seller, even though the security interest is perfected, and the buyer knows of the existence of such interest."⁹² For good measure, the section also provides that, notwithstanding any contrary provision of state law (and subject to some exceptions),

a commission merchant or selling agent who sells, in the ordinary course of business, a farm product for others, shall not be subject to a security interest created by the seller in such farm product

from the Official Text of the U.C.C., see Fry, *supra* note 74, at 442-44; Meyer, *supra* note 74, at 487-89; Richards, *supra* note 17, at 396-409; Van Hooser, *supra* note 40, at 349-58; Note, *The Federalization of the Farm Products Exception*, *supra* note 74, at 118-21; Note, *H.291: Ohio's Attempt to Remedy Security Interests in Farm Products Under the U.C.C.*, 9 U. DAYTON L. REV. 607 (1984); Note, *Section 1324 of the Food Security Act*, *supra* note 74, at 461-63; Note, *Federal Legislation Provides Protection*, *supra* note 74, at 761-63.

84. California. Uchtmann, Bauer & Dudek, *supra* note 83, at 1344.

85. Tennessee. *Id.*

86. *E.g.*, Nebraska. See *id.* at 1332-36.

87. *E.g.*, Illinois. See *id.* at 1340-43.

88. *E.g.*, North Dakota. See *id.* at 1336-40.

89. "Clear title" is the popular designation of § 1324 of The Food Security Act of 1985. See, e.g., H.R. REP. NO. 271, 99th Cong., 1st Sess., pt. 1, 110 (1985); Clark, *Uniform Commercial Code Survey: Secured Transactions*, 42 BUS. LAW. 1336 (1987).

90. The Food Security Act of 1985, Pub. L. No. 99-198, § 1324, 99 Stat. 1354, 1535 (1985) (codified at 7 U.S.C. § 1631 (Supp. IV 1986)). See *supra* note 1.

91. The rule explicitly applies "notwithstanding any other provision of Federal, State, or local law." 7 U.S.C. § 1631(d) (Supp. IV 1986).

92. *Id.* § 1631(d).

even though the security interest is perfected and even though the commission merchant or selling agent knows of the existence of such interest.⁹³

However, these broad rules do not provide as much protection as they appear to, for the section goes on to provide, in elaborate detail, for means by which holders of security interests in farm products can preserve their rights to the collateral against buyers, commission merchants and selling agents.⁹⁴

First, it is provided that, “[a] buyer of farm products takes subject to a security interest created by the seller” if the buyer has received, within a year prior to the sale, either from the secured party or from the seller, a written notice of the security interest and the buyer has failed to perform “payment obligations imposed on the buyer by the secured party as conditions for waiver or release of the security interest.”⁹⁵ The notice must be “organized according to farm products.”⁹⁶ It must contain: (1) “the name and address of the secured party” and “the person indebted to the secured party;”⁹⁷ (2) the social security number or (in the case of an organization) the Internal Revenue Service taxpayer identification number of the “debtor;”⁹⁸ (3) “a description of the farm products subject to the security interest created by the debtor, including the amount of such products where applicable, crop year, county or parish, and a reasonable description of the property;”⁹⁹ and (4) a statement of any “payment obligations” with which the buyer is required to comply as conditions for waiver or release of the security interest.¹⁰⁰ If “material changes” occur, the

93. *Id.* § 1631(g)(1).

94. Neither “buyer” nor “buying” is defined in the Federal Act. “Commission merchant” is defined as “any person engaged in the business of receiving any farm product for sale, on commission, or for or on behalf of another person.” *Id.* § 1631(c)(3). “Selling agent” means “any person, other than a commission merchant, who is engaged in the business of negotiating the sale and purchase of any farm product on behalf of a person engaged in farming operations.” *Id.* § 1631(c)(8).

95. *Id.* § 1631(e)(1).

96. *Id.* § 1631(e)(1)(A).

97. *Id.* § 1631(e)(1)(A)(ii)(I), (II).

98. *Id.* § 1631(e)(1)(A)(ii)(III).

99. *Id.* § 1631(e)(1)(A)(ii)(IV).

100. *Id.* § 1631(e)(1)(A)(ii), (v). There is some slippage in the grammar of subsection (e)(1)(A). It refers to a

written notice of the security interest organized according to farm products that—

(i) is an original or reproduced copy thereof;

(ii) contains,

(I) the name and address of the secured party;

(II) the name and address of the person indebted to the secured party;

(III) the social security number of the debtor or, in the case of a debtor doing

notice must be "amended in writing, within three months, similarly signed and transmitted, to reflect" those changes.¹⁰¹ The effectiveness of a written notice of security interest lapses "either [on] the expiration period of the statement or the transmission of a notice signed by the secured party that the statement has lapsed, whichever occurs first."¹⁰² Virtually identical provisions are made for notices to be given to commission merchants and selling agents, in order that secured parties may retain security interests which will be enforceable against them.¹⁰³

Even if no such notice is received by the buyer, he may take the goods "subject to" a security interest created by the seller (and the same is true of a commission merchant or selling agent). That is so only if the state in which the farm product involved was produced has established a "central filing system" complying with the section, and then only if certain additional events occur. A "central filing system," within the meaning of the Act, is one "which has been certified by" the federal Secretary of Agriculture.¹⁰⁴ The Secretary is directed to certify a state's central filing system if he finds that it has the features

business other than as an individual, the Internal Revenue Service taxpayer identification number of such debtor;

(IV) a description of the farm products subject to the security interest created by the debtor, including the amount of such products where applicable, crop year, county or parish, and a reasonable description of the property and

(iii) must be amended in writing, within three months, similarly signed and transmitted, to reflect material changes;

(iv) will lapse on either the expiration period of the statement or the transmission of a notice signed by the secured party that the statement has lapsed, whichever occurs first; and

(v) any payment obligations imposed on the buyer by the secured party as conditions for waiver or release of the security interest

Id. § 1631(e)(1)(A). Taken literally, this language does not require that "payment obligations" be contained in the notice, but the reference to such obligations makes no sense unless the notice is required to show them. See Sanford, *The Reborn Farm Products Exception Under the Food Security Act of 1985*, 20 U.C.C. L.J. 3, 20 (1987).

The subsection does not expressly require that the notice be signed by anyone. However, an amendment filed to reflect "material changes" must be "similarly signed and transmitted," which suggests that the phrase "written notice" implies a signed notice, presumably signed by the secured party or seller who is giving the notice. *But cf.* Note, *Clear Title: A Buyer's Bonus, A Lender's Loss—Repeal of UCC § 9-307(1) Farm Products Exception by Food Security Act § 1324 [7 U.S.C. § 1631]*, 26 WASHBURN L.J. 71, 86 (1986) [hereinafter Note, *Clear Title*] (reading the Act as not requiring that an original notice be signed). Certainly, prudence would call for the party giving the notice to sign it.

101. 7 U.S.C. § 1631(e)(1)(A)(iii) (Supp. IV 1986).

102. *Id.* § 1631(e)(1)(A)(iv).

103. *Id.* § 1631(g)(2)(A), (B).

104. *Id.* § 1631(c)(2).

prescribed by the Act.¹⁰⁵ These include: (1) provision for the filing of "effective financing statements or notice of such financing statements" in the office of the Secretary of State or other state designee;¹⁰⁶ (2) recording by the filing officer of the times when such statements or notices are filed (by date and hour);¹⁰⁷ (3) compilation by the state filing officer of a "master list" of all such filings;¹⁰⁸ (4) maintenance by the filing officer of a list of buyers, commission merchants and selling agents who have registered with him to indicate their interest in receiving copies of the master list or parts thereof;¹⁰⁹ (5) periodic distributions to those who have so registered of copies of the master list or such parts of it as they have requested;¹¹⁰ and (6) provision on request to persons not registered with the filing officer of confirmation of the filing of financing statements or notices showing security interests created by particular sellers of farm products.¹¹¹

The filing officer must compile a "master list" which is "organized according to farm products;" and within each product category, financing statements are to be listed in four ways: alphabetically, by names of "debtors;" numerically, by debtors' social security or taxpayer ID numbers; geographically, by county or parish; and chronologically, by crop year.¹¹² As each financing statement listed, the master list must contain the information which is required by the definition of "effective financing statement" to be included in such a statement.¹¹³ Persons registering as desiring to receive information contained in the master list are given the option to receive copies of only those portions of the master list relating to the types of farm

105. *Id.*

106. *Id.* § 1631(c)(2)(A). The Act refers to the "Secretary of State" as the state's central filing officer, but "Secretary of State" is defined as meaning "the Secretary of State or the designee of the State." *Id.* § 1631(c)(11).

107. *Id.* § 1631(c)(2)(B).

108. *Id.* § 1631(c)(2)(C).

109. *Id.* § 1631(c)(2)(D).

110. *Id.* § 1631(c)(2)(E).

111. *Id.* § 1631(c)(2)(F). The statement in the text appears to be what the statutory language means. The actual text requires that a central filing system include provision for the

Secretary of State [to furnish] to those who are not registered pursuant to (2)(D) of this section oral confirmation within 24 hours of any effective financing statement on request followed by written confirmation to any buyer of farm products buying from a debtor, or commission merchant or selling agent selling for a seller covered by such statement.

Id. The reference to "(2)(D) of this section" should probably be to "subparagraph (2)(D) of this subsection." See editorial note following 7 U.S.C. § 1631 (Supp. IV 1986).

112. 7 U.S.C. § 1631(c)(2)(C)(i), (ii) (Supp. IV 1986).

113. *Id.* § 1631(c)(2)(C)(iii).

products in which they are interested.¹¹⁴

If such a central filing system exists in the state in which the farm products sold have been produced, and a buyer of such products, or a commission merchant or selling agent selling such products, has failed to register with the state's central filing officer, then he will be subject to the security interest of any secured party who has filed an effective financing statement or notice that covers the products being sold.¹¹⁵ If the buyer, commission merchant or selling agent has registered, he will be subject to a security interest in the farm product being sold only if he "receives from the Secretary of State . . . written notice" of the filing of an effective financing statement or notice covering the product being sold, and he fails to obtain a waiver or release of the security interest from the secured party.¹¹⁶ The "written notice" here referred to may be given by the filing officer either by distribution of a portion of the master list showing the filing or by responding to a specific request for information on filings as to a particular seller.¹¹⁷

"Financing statements," to be treated as "effective," must comply with detailed requirements as to form¹¹⁸ which are similar to, but not identical with, those applicable to the written notices of security interests which secured parties and sellers may give directly to buyers, commission merchants and selling agents.¹¹⁹ An "effective financing statement" is a statement, the original or a reproduced copy of which is "signed and filed with the Secretary of State of a State by the secured party"¹²⁰ and which is also signed by "the debtor."¹²¹ It con-

114. *Id.* § 1631(c)(2)(D), (E).

115. *Id.* § 1631(e)(2) (buyers), (g)(2)(D) (commission merchants and selling agents).

116. *Id.* § 1631(e)(3) (buyers), (g)(2)(D) (commission merchants and selling agents). "What constitutes receipt, as used in this section, shall be determined by the law of the State in which the buyer resides." *Id.* § 1631(f), (g)(3).

117. *Id.* § 1631(e)(3)(A) [buyers], (g)(2)(D)(i) [commission merchants and selling agents] (incorporating by reference paragraphs (c)(2)(E) and (F)). There is an inconsistency in the wording of the act here. Subsections (e)(3)(A) and (g)(2)(D)(i) are applicable to buyers, commission merchants and selling agents who *have registered* with the state's central filing officer, yet they refer to a "written notice as provided in subparagraph . . . (c)(2)(f)," which provides that a central filing system must include provision for the central filing officer to furnish information about filings as to particular sellers in response to requests of "those who are *not registered* pursuant to (2)(D) of this section." (Emphasis added.) Perhaps the reference to subparagraph (c)(2)(F) in subparagraphs (e)(3)(A) and (g)(2)(D)(i) is meant to apply where the state setting up a central filing system elects to require the central filing officer to respond to requests for information as to filings received from registered buyers, commission merchants and selling agents, as well as from those who are not registered.

118. *Id.* § 1631(c)(4).

119. See *supra* notes 95-100 and accompanying text.

120. 7 U.S.C. § 1631(c)(4)(A), (B) (Supp. IV 1986).

121. *Id.* § 1631(c)(4)(C).

tains: the names and addresses of the secured party and "the person indebted to the secured party,"¹²² the social security number of the "debtor" or the taxpayer identification number of an organizational debtor,¹²³ and "a description of the farm products subject to the security interest created by the debtor, including the amount of such products where applicable; and a reasonable description of the property, including county or parish in which the property is located."¹²⁴

The financing statement must be filed with the state's central filing officer, accompanied by the specified fee.¹²⁵ If "material changes" occur, a filed financing statement or notice must be amended in writing within three months.¹²⁶ A filing remains effective for five years from the date of filing unless the statement itself indicates an earlier termination date or the secured party files a notice of lapse; the original five year period of effectiveness may be extended for additional five year periods by the filing of continuation statements.¹²⁷

Presumably so that secured parties may know to whom they should send notices of their security interests if they elect that method of protecting themselves,¹²⁸ the "clear title" section authorizes inclusion, in any "security agreement" covering a farm product, of a requirement that the debtor furnish the secured party with a list of "the buyers, commission merchants and selling agents to or through whom [the debtor] may sell such farm product."¹²⁹ If the security agreement contains such a requirement, and the debtor sells the collateral to a buyer or through a commission merchant or selling agent who is not on a list he has furnished to the secured party, the debtor is subject to a "fine" of \$5,000 or "15 [%] of the value or benefit received for such farm product . . . , whichever is greater." This fine is not imposed if (1) he has given the secured party written notice of the identity of the buyer, commission merchant or selling agent at least seven days prior to the sale, or (2) he has "accounted to the secured party for the proceeds of such sale not later than 10 days after such sale."¹³⁰

The Act includes numerous definitions of terms, some of which

122. *Id.* § 1631(c)(4)(D)(i), (ii).

123. *Id.* § 1631(c)(4)(D)(iii).

124. *Id.* § 1631(c)(4)(D)(iv).

125. *Id.* § 1631(c)(4)(B), (H).

126. *Id.* § 1631(c)(4)(E).

127. *Id.* § 1631(c)(4)(F), (G).

128. See *supra* notes 95-103 and accompanying text.

129. 7 U.S.C. § 1631(h)(1) (Supp. IV 1986).

130. *Id.* § 1631(h)(2), (3).

have been incorporated into the preceding summary. Two key definitions should be quoted, the definitions of "buyer in the ordinary course of business" and "farm product":

The term "farm product" means an agricultural commodity such as wheat, corn, soybeans, or a species of livestock such as cattle, hogs, sheep, horses, or poultry used or produced in farming operations, or a product of such crop or livestock in its unmanufactured state (such as ginned cotton, wool-clip, maple syrup, milk, and eggs), that is in the possession of a person engaged in farming operations.¹³¹

The term "buyer in the ordinary course of business" means a person who, in the ordinary course of business, buys farm products from a person engaged in farming operations who is in the business of selling farm products.¹³²

To allow time for states to adjust their laws to the new federal law, its effective date was postponed until December 23, 1986 (twelve months after the date of enactment).¹³³ The Secretary of Agriculture was directed, within 90 days after the date of enactment, to prescribe regulations "to aid States in the implementation and management of a central filing system."¹³⁴

B. Analysis of the Federal Act

There is no doubt that the "clear title" section of the Food Security Act was aimed directly at the "farm products" exception to section 9-307(1) of the Uniform Commercial Code. It was intended to replace the farm products exception with a Congressionally mandated scheme which affords some protection against perfected security interests to buyers of farmers' inventory, but which stops short of giving them as much protection as buyers of other types of inventory can enjoy under section 9-307(1).¹³⁵

Among the reasons given for preempting the "farm products"

131. *Id.* § 1631(c)(5).

132. *Id.* § 1631(c)(1).

133. *Id.* § 1631(j).

134. *Id.* § 1631(i).

135. See HOUSE AGRICULTURE COMMITTEE, REPORT ON FOOD SECURITY ACT OF 1985, H.R. REP. NO. 271, 99th Cong., 1st Sess., pt. 1, 108, 110 reprinted in 1985 U.S. CODE CONG. & ADMIN. NEWS 1103, 1212-13 [hereinafter HOUSE REPORT]. But see Note, *The Federalization of the Farm Products Exception Rule of U.C.C. 9-307(1): Anomaly or Opening Salvo?*, 36 DRAKE L. REV. 115, 130-32 (1987) (arguing that congressional intent to preempt all state law dealing with the problem, other than state laws setting up central filing systems for farm product liens, is not clear and that a state law entirely repealing the farm products exception might be found valid).

exception were that it had the unhealthy trade-inhibiting effects which have been discussed above, was unfair to purchasers of farm products and constituted a burden on interstate commerce.¹³⁶ It was also argued that since some twenty states had adopted their own modifications of the "farm products" exception to section 9-307(1), the national uniformity of the law which the Code was intended to produce had already been destroyed, and federal legislation was needed "to restore consistency to this area of the law."¹³⁷

The federal statute bears the marks of Congressional compromise and hasty drafting, however. The Department of Agriculture has made an effort, in regulations under and interpretations of the Act,¹³⁸

136. HOUSE REPORT, *supra* note 135, at 108-09:

Currently, under Section 9-307 of the [U.C.C.], a buyer of goods "in the ordinary course of business" takes those goods free and clear of any security interest in them held by a lender even if the buyer knows of the existence of that lien. The lone exception to this general rule applies to agricultural commodities.

As originally drafted and adopted by 49 of the 50 states, the "farm products exception" essentially permitted a lender to obtain payment from the purchaser of agricultural commodities for any valid unpaid security interest in those goods—even if the buyer didn't know that the lien existed.

This exception presents significant commercial problems for buyers and sellers of farm products. With the advent of 24-hour final payment rules for some commodities, there is insufficient time to check the liens and, thus, greater potential liability for buyers. In addition, with some lenders pursuing buyers several years following their purchases, many buyers limit who they do business with, thus restricting the markets of farmers and inhibiting the free-flow-of-commerce in the United States.

Current State law forces innocent buyers of farm products to become unwilling loan guarantors, in essence assuming the credit supervision responsibilities that rightly belong with the lender who is making the profit off the loan to begin with. At the same time, farm product buyers have no control over the lender's practice, and receive no compensation in the form of interest to cover the risk exposure and jeopardy unknowingly and unwittingly assumed.

Moreover, the current exception for farm products places an undue financial burden on markets to which producers sell their commodities, thus reducing the economic vitality of our nation's domestic agricultural markets. As the problem worsens, it adversely affects individual farmers, as well as their markets. Farmers buy products from other farmers, such as feeder cattle and pigs, breeding stock, grain and hay, and potentially may be forced to pay twice for these products as their suppliers default on secured debts. Risk exposure and actual losses from double payment are reflected in the prices paid to farmers and are passed on other [*sic.*] producers in terms of higher marketing fees and processing costs, and eventually are reflected in higher consumer prices for meat, milk, and eggs, etc.

Additionally, there is a question of equity—is it fair to require a purchaser of farm products to pay a second time for those commodities simply because of a financial dispute between the producer/borrower and his lender?

137. *Id.* at 109.

138. Federal regulations were issued in August, 1986, effective September 17, 1986, as Part 205 of Title 9 of the Code of Federal Regulations. 9 C.F.R. § 205 (1987). Part 205 consists of one section of "Definitions", seven sections of "Regulations" and 14 sections of "Interpretive

to clarify its meaning and operation in some respects. But the clarifications have been made cautiously, since the statute authorizes regulations for the limited purpose of aiding the states to implement and manage central filing systems,¹³⁹ and the Secretary of Agriculture is not expressly authorized to enforce the Act other than by certifying state central filing systems as being in conformity with it.¹⁴⁰

1. Definitions

One type of problem that is troublesome arises from the fact that the Federal Act employs, but defines differently, terms which are also terms of art in the U.C.C.¹⁴¹ "Farm products" is an example. The U.C.C. definition is somewhat broader than that of the Federal Act. "Farm products" in the Code includes "supplies used or produced in

Opinions." The weight to be accorded to the "Interpretive Opinions" is not clear. Federal cases have drawn a distinction between "substantive regulations", which have the force of law if the administrative agency issuing them has been authorized by Congress to legislate on the subject, and "interpretative rules", which lack the force of law. *Chrysler Corp. v. Brown*, 441 U.S. 281 (1979); *United States v. Walter Dunlap & Sons, Inc.*, 800 F.2d 1232 (3rd Cir. 1986). Classification of an administrative rule as "substantive" or "interpretative" may be controversial. Compare the majority opinion in *Walter Dunlap*, 800 F.2d at 1238, with the concurring opinion at 1243-45. However, assuming that the "Interpretive Opinions" in 9 C.F.R. § 205 do not have the force of law, they may be of persuasive authority as to the meaning of the "clear title" section of the Food Security Act (see Sanford, *The Reborn Farm Products Exception Under the Food Security Act of 1985*, 20 U.C.C. L.J. 3, 13 n.35 (1987)), and they should be, since they are issued by an agency which has been directed to promulgate regulations governing "central filing systems", they are fairly clearly addressed to those who administer and use such systems, and they are likely to be relied on by such persons in their efforts to adapt to the requirements of a perplexingly drafted statute.

139. 7 U.S.C. § 1631(i) (Supp. IV 1986).

140. *Id.* § 1631(c)(2).

141. In addition to the defined terms discussed in the text of this article, the Food Security Act's definition of "security interest" is "an interest in farm products that secures payment or performance of an obligation." *Id.* § 1631(c)(7). This may pose problems. The definition is not expressly limited to interests created by contract, as security interests within the scope of Article 9 of the U.C.C. are. U.C.C. § 9-102(2) (1978). Might the Federal Act definition include a statutory landlord's lien for rent on a tenant's crops, for example? If so, the definition probably has little practical impact, since the "open-market" rules of the Federal Act refer only to security interests "created by the seller," which appears to limit their operation to consensual liens. 7 U.S.C. § 1631(d) and (g)(1) (Supp. IV 1986). See Sanford, *supra* note 138, at 17. See also *infra* note 367. However, there remain possibilities of contractual liens being within the scope of the Federal Act which would clearly or arguably be excluded from the scope of Article 9 by § 9-104 or by the more particularized definition of "security interest" in § 1-201(37). See Sanford, *supra* note 138, at 17 (raising questions of whether "true consignments, entrustments, bailments, and leases" would create "security interests" within the scope of the Federal Act, or real estate mortgages claiming crops as "rents, issues and profits."). Since the legislative history of the Federal Act makes it clear that the dominant purpose of the act is to overcome the pernicious effects of the "farm products" exception to U.C.C. § 9-307(1) (see *supra* note 135 and accompanying text), the Federal Act definition of "security interest" was probably intended to refer to an Article 9 security interest.

farming operations"¹⁴² (such as chemicals acquired by a farmer for the spraying of his crops), while the Federal Act definition omits reference to such "supplies."¹⁴³ Since the Federal Act definition closely tracks the Code definition as a whole, it may be inferred that the omission was deliberate.¹⁴⁴ If so, this category of U.C.C. "farm products" is not affected by the federal legislation, and buyers in ordinary course of business of such "farm products" from farmers would still be subject to the "farm products" exception to section 9-307(1).

Of potentially greater significance is the difference between the definitions in the two statutes of "buyer in ordinary course of business." The Federal Act tracks the U.C.C. definition only part way. Under the Code, to be a buyer in ordinary course of business, one must not only buy in the ordinary course of business from a person engaged in the business of selling goods of the type involved, but must also be acting "in good faith and without knowledge that the sale to him is in violation of the ownership rights or security interest of a third party in the goods."¹⁴⁵ The Federal Act definition of the term does not say that the buyer must have bought in good faith nor that he must be without knowledge that the sale violates the rights of third parties; it makes no reference to the buyer's state of mind or knowledge at all.¹⁴⁶

The legislative history of the "clear title" section of the Food Security Act makes it clear that the omission was deliberate. The House bill which ultimately became the Food Security Act of 1985¹⁴⁷ contained a definition of "buyer in the ordinary course of business" which did include "good faith" and "without knowledge" limitations identical to those of the Code definition.¹⁴⁸ However, a Senate amendment deleted the language, and a conference committee accepted the Senate's wording.¹⁴⁹

The reason for the dropping of that part of the definition is not clear. A possible explanation is, of course, that a policy decision was made not to require that a buyer buy in good faith and without awareness of impropriety in the sale in order to qualify for protection

142. U.C.C. § 9-109(3) (1978), *supra* note 59.

143. 7 U.S.C. § 1631(c)(5) (Supp. IV 1986); *see supra* text accompanying note 131.

144. *See Note, Clear Title, supra* note 100, at 82-83.

145. U.C.C. § 1-201(9) (1978).

146. *See* Federal Act definition of "buyer in ordinary course of business," 7 U.S.C. § 1631(c)(1) (Supp. IV 1986); *supra* text accompanying note 132.

147. H.R. 2100, 99th Cong., 1st Sess. (1985).

148. *See* HOUSE REPORT, *supra* note 135, at 294-95.

149. *See* H.R. CONF. REP. NO. 447, 99th Cong., 1st Sess. 486-87, *reprinted in* 1985 U.S. CODE CONG. & ADMIN. NEWS 2251, 2412.

against security interests under the Federal Act.¹⁵⁰ Why Congress should wish to protect buyers who are knowingly participating in sales which violate the sellers' duties to secured parties is hard to imagine, though. The only merit of such a rule would be its simplicity of application, but simplifying the law can hardly have been the objective of the "clear title" section as a whole, and there is no reason to believe that it was a major consideration in the definition of this term.

A more probable explanation for the truncated definition in the Federal Act is that the omitted language was thought unnecessary, because it was assumed that the courts would read the definition as requiring that the buyer act in good faith and without knowledge of violations of property rights of third persons. Certainly nothing in the "clear title" section affirmatively indicates a desire to protect bad faith buyers. In laying down its general rule that buyers who, in the ordinary course of business, take free of security interests created by their sellers, the Act limits itself to saying that the rule applies even though the security interest is perfected and "even though . . . the buyer knows of the existence of such interest."¹⁵¹ Knowledge of the *existence* of a security interest falls well short of knowledge that the rights of the secured party are being violated, and even section 9-307(1) of the U.C.C. protects most buyers in ordinary course of business against security interests created by the sellers despite their knowledge that the security interests *exist*.

Moreover, the operative rules of the Federal Act are introduced by explicit Congressional findings that "certain State laws" inhibit competition and obstruct interstate commerce by permitting a secured lender to enforce his security interest in farm products "even if the purchaser does not know that the sale of the products violates the lender's security interest in the products."¹⁵² The concern expressed

- 150. Cf. comment by the Department of Agriculture in 51 Fed. Reg. 29,449, 29,450 (1986) (observing, in connection with the Federal Act's omission from the definition of "buyer in the ordinary course of business" of the definition of "buying" which is included in the U.C.C. definition of the same term, that "the phrase must have been intended to have a different meaning since a different definition was written"). See also Meyer, *Agricultural Credit and the Uniform Commercial Code: A Need for Change?*, 34 U. KAN. L. REV. 469, 491-93 (1985) [hereinafter Meyer, *Agricultural Credit*]; Note, *Section 1324 of the Food Security Act*, *supra* note 74, at 463-64; Note, *Clear Title*, *supra* note 100, at 81.

151. 7 U.S.C. § 1631(d) (Supp. IV 1986).

152. *Id.* § 1631(a)(1). The full text of the Congressional findings, *id.* § 1631(a), is as follows:

Congress finds that—

- (1) certain State laws permit a secured lender to enforce liens against a purchaser of farm products even if the purchaser does not know that the sale of the products violates the lender's security interest in the products, lacks any practical

is for the welfare of *good faith* purchasers of farm products, and a Congressional explanation of the reasons for adopting legislation, incorporated into the legislation, is unquestionably a legitimate guide to the intended meaning of the statute. The conclusion which seems best to accord with probable legislative intention, then, is that the definition of "buyer in the ordinary course of business" in the "clear title" section of the Food Security Act does include, by implication,¹⁵³ requirements that the buyer buy in good faith and without knowledge that the sale violates the rights of third parties in the goods.¹⁵⁴

It might be argued that the differences in the Federal Act definition of "buyer in the ordinary course of business" and that of the U.C.C. are of no significance, no matter how the Federal Act definition is read, since the "clear title" section of the Food Security Act does not employ the term in any of its operative rules; it appears only

method for discovering the existence of the security interest, and has no reasonable means to ensure that the seller uses the sales proceeds to repay the lender;

(2) these laws subject the purchaser of farm products to double payment for the products, once at the time of purchase, and again when the seller fails to repay the lender;

(3) the exposure of purchasers of farm products to double payment inhibits free competition in the market for farm products; and

(4) this exposure constitutes a burden on and obstruction to interstate commerce in farm products.

Id.

The next subsection declares that: "The purpose of this section is to remove such burden on and obstruction to interstate commerce in farm products." *Id.* § 1631(b).

153. *But see Meyer, Congress's Amendment to the U.C.C.: The Farm Products Rule Change*, 8 J. AGRIC. TAX'N & LAW 3, 6 (1986) [hereinafter *Meyer, Congress's Amendment*] (arguing that the difference between the Federal Act definition of "buyer in the ordinary course of business" and that of the U.C.C. indicates a Congressional choice to make buyers' knowledge of violation of security interests immaterial and to substitute a test of whether they have received notice of the security interests in the manner prescribed by the Federal Act).

154. It must be conceded that the portion of the Federal Act which protects commission merchants and selling agents from liability to the secured party for participating in unauthorized sales of farm products collateral (7 U.S.C. § 1631(g)(1) (Supp. IV 1986)) does not explicitly require that the commission merchants and selling agents act in good faith and without knowledge that security interests are being violated either, and there is somewhat less reason for reading in such requirements, since the Code does not deal with the liability of such agents and the Congressional findings do not mention the problems of commission merchants and selling agents as reasons for enactment of the law. However, such agents are required by the Act to sell "in the ordinary course of business", and perhaps that implies that they must be acting in good faith or at least without knowledge that secured parties' rights are being violated; unfortunately, "ordinary course of business" is not defined in the Federal Act or the U.C.C. The Code seems more limited in scope. *See supra* note 58.

It is to be hoped that the courts will construe the Federal Act as incorporating "good faith" and "without knowledge" requirements, as being consistent with the evident desire of Congress to provide protection for the innocent.

in the definitions subsection.¹⁵⁵ It is true that the precise phrase is not used in any of the subsequent provisions of the Act. But, in view of the legislative history of the "clear title" section, subsection (d) cannot reasonably be read as referring to anyone but a "buyer in the ordinary course of business" when it lays down its general rule protecting "a buyer who in the ordinary course of business buys a farm product from a seller engaged in farming operations."¹⁵⁶

2. *Effect on the "Farm Products" Exception of U.C.C. Section 9-307(1)*

Assuming that the type of buyer referred to in subsection (d) of the "clear title" section of the Food Security Act is a "buyer in the ordinary course of business," the impact of that subsection can be seen to be to delete from section 9-307(1) of the U.C.C., almost completely, its "farm products" exception and to place most such buyers of farm products on a par with other buyers in ordinary course of business inventory. Having done that, however, the Federal Act reverses course and sets up a different, and very complex, set of rules creating new vulnerabilities for such buyers.

3. *Direct Notification of Security Interests*

First, a secured party may preserve the effectiveness of his security interest in farm products by delivery to the buyer of a "written notice of the security interest" which includes a statement of "payment obligations imposed on the buyer by the secured party as conditions for waiver or release of the security interest."¹⁵⁷ (Such a notice may also be given by "the seller,"¹⁵⁸ though the likelihood of a seller doing so seems negligible). If such a notice is "received"¹⁵⁹ by the buyer within one year before the sale of the collateral, the notice pro-

155. See Sanford, *supra* note 138, at 6 n.10, 11. Mr. Sanford contends that the only operative rules which use the expression "in the ordinary course of business", subsections (d) and (g)(1) of the "clear title" section, avoid the use of the defined term "buyer in ordinary course of business" and therefore Congress must have intended to refer to persons who do not fit that definition.

156. 7 U.S.C. § 1631(d) (Supp. IV 1986). Mr. Sanford, *see supra* note 138, gives little consideration to legislative history. His focus is on the text of the act, and he finds his clues as to meaning almost exclusively within the four corners of the "clear title" section. On that basis his position may be defensible. However, a statute as loosely drafted as this one cannot be given a sensible reading without considering all legitimate clues to legislative intention.

157. 7 U.S.C. § 1631(e)(1)(A) (Supp. IV 1986). This device is sometimes referred to, in commentary on the Federal Act, as "prenotification". *E.g.*, Clark, *Uniform Commercial Code Annual Survey: Secured Transactions*, 42 BUS. LAW. 1333, 1337 (1987).

158. 7 U.S.C. § 1631(e)(1)(A) (Supp. IV 1986).

159. State law (the law of the buyer's residence) defines "receipt". *Id.* § 1631(f).

duces the result that the buyer, even if he is a "buyer in the ordinary course of business,"¹⁶⁰ "takes subject to" the security interest *if* "the buyer has failed to perform the payment obligations."¹⁶¹

Under this rule the secured party apparently cannot prevent loss of his security interest through an unauthorized sale merely by notifying the buyer of his security interest, nor even by notifying him that sale by the debtor is prohibited or authorized only under conditions which are not within the buyer's control. He can protect himself against loss of his security interest through a sale to a buyer in ordinary course of business *only* by notifying the buyer of his security interest *and* including in the notice terms as to payment, which are to be complied with by the buyer, as conditions for waiver or release of the security interest. These "payment obligations" must then be complied with by the buyer if he is to take the goods free of the security interest. A notice which specified no such "payment obligations" would be ineffective against a buyer in ordinary course of business. What are "payment obligations?" The Act does not say, but presumably they may be any obligations performable by the buyer and relating to payment for the collateral which are consistent with the security agreement, such as a requirement that the buyer make payment directly to the secured party, or that payment be made by check payable jointly to the secured party and the seller of the collateral.¹⁶²

The purpose of this method of notification, then, is not to prevent unauthorized sales of farm products collateral, nor to preserve the security interest in the event of such a sale, but to ensure that the proceeds of sales of collateral, whether authorized or not, will be applied to the secured debt. The secured party might use this device to protect himself against damage to the value of his security, by imposing "payment obligations" setting minimum prices for which collateral may be sold and other terms of sale. How far the concept of "payment obligations" can be pushed by ingenious secured parties remains to be seen.

However, a secured party who wishes to employ this method of protecting himself faces formidable problems. One is that of finding the buyer before the sale of the collateral occurs. The Act suggests that the secured party include in the security agreement a term obligating the debtor to furnish a list of potential buyers of the collat-

160. The rule that "a buyer who in the ordinary course of business buys a farm product from a seller engaged in farming operations shall take free of a security interest created by the seller" applies "[e]xcept as provided in subsection (e) of this section." *Id.* § 1631(d).

161. *Id.* § 1631(e)(1)(B).

162. *See* Clark, *supra* note 157, at 1338.

eral;¹⁶³ the secured party can then send notices to all persons on the list. But if the debtor makes a sale to a buyer (in ordinary course of business) whom he has not included in his list, and to whom no notice of the security interest has been given, the debtor's offense will not prevent the buyer from taking the goods free of the security interest. (Of course, there is nothing in the Act to prevent the secured party from distributing notices of his security interest more widely,¹⁶⁴ but the effectiveness of the notice as to any actual buyer depends on its having reached him.)

The Federal Act seeks to protect the secured party from loss of his security by reason of a sale to an off-list buyer by requiring that the debtor give the secured party advance notice of an intended sale to such a buyer or account promptly to the secured party for the proceeds of the sale after it occurs.¹⁶⁵ The debtor is liable for a substantial "fine"¹⁶⁶ in the event of his failure to do either, but it is not clear whether this is a civil or a criminal penalty, nor whether the fine is payable to the secured party.¹⁶⁷ In any event, the deterrent effect of the threat is questionable.¹⁶⁸

Another problem for a secured party who desires to employ the direct-notification device is that of drafting a notice which meets the requirements of the Act. His problem here is the ambiguity of the Act's prescriptions for an effective notice.¹⁶⁹

One question posed by the statutory text is that of who must be

163. 7 U.S.C. § 1631(h)(1) (Supp. IV 1986).

164. See Clark, *supra* note 157, at 1338; Meyer, *Agricultural Credit*, *supra* note 150, at 496; Meyer, *Congress's Amendment*, *supra* note 153, at 9-10.

165. 7 U.S.C. § 1631(h)(2)(A), (B) (Supp. IV 1986).

166. *Id.* § 1631(h)(3) (15% of the "benefit or value received" for the farm products or \$5,000, whichever is greater).

167. See Sanford, *supra* note 138, at 23; Note, *Section 1324 of the Food Security Act of 1985*, *supra* note 74, at 470-71.

168. See Meyer, *Agricultural Credit*, *supra* note 150, at 495.

169. The pertinent text of the Act is as follows:

(e) A buyer of farm products takes subject to a security interest created by the seller if—
(1)(A) within 1 year before the sale of the farm products, the buyer has received from the secured party or the seller written notice of the security interest organized according to farm products that—

- (i) is an original or reproduced copy thereof;
- (ii) contains,
 - (I) the name and address of the secured party;
 - (II) the name and address of the person indebted to the secured party;
 - (III) the social security number of the debtor or, in the case of a debtor doing business other than as an individual, the Internal Revenue Service taxpayer identification number of such debtor;
 - (IV) a description of the farm products subject to the security interest created by the debtor, including the amount of such products where appli-

identified in the notice as "the debtor." Doubtless, the answer is easy enough in the usual case, where the same person is both the one owing the secured debt and the owner of the collateral, but that is not invariably so.¹⁷⁰ If the person obligated to pay the debt and the owner of the collateral are different persons, which of them is required to be identified (1) by name and address and (2) by social security number or taxpayer ID number? The Act calls for the "name and address of the person indebted to the secured party,"¹⁷¹ which seems plainly to refer to the obligor, but the following subparagraph calls for disclosure of the social security number or taxpayer ID number of "the debtor."¹⁷² "Debtor" is a term not defined by the Act. Is it used here with reference to "the person indebted to the secured party," or does it refer to the owner of the collateral? The fact that different wording is used suggests that a different meaning is intended. However, if "debtor" refers to the owner of the collateral, then the Act requires identification of the obligor by name and address, but allows the owner of the collateral to be identified only by a cryptic number. On the other hand, if "debtor" refers to the "person indebted," then it appears that the owner of the collateral, if another person, need not be identified at all. Yet it would seem that if the notice is to serve its evident purpose of warning the recipient of need to comply with "payment obligations" in the event of his purchase of particular farm products, it would be more important for the prospective buyer to be informed of the identity of the owner of those products than of who owes the secured debt, since the owner of the products is the one who is most likely to be selling them. Perhaps the best advice that can be

cable, crop year, county or parish, and a reasonable description of the property and

(iii) must be amended in writing, within 3 months, similarly signed and transmitted, to reflect material changes;

(iv) will lapse on either the expiration period of the statement or the transmission of a notice signed by the secured party that the statement has lapsed, whichever occurs first; and

(v) any payment obligations imposed on the buyer by the secured party as conditions for waiver or release of the security interest; and

(B) the buyer has failed to perform the payment obligations,

7 U.S.C. § 1631(e)(1) (Supp. IV 1986).

170. Article 9 of the U.C.C. recognizes that one person may subject his property to a security interest to secure the debt of another, by providing, in § 9-105(1)(d), that the term "debtor" may refer either to the owner of the collateral or to the "obligor"; that which meaning the term has when used in an Article 9 rule depends on whether the provision in question deals "with the collateral" or "with the obligation", and the term may refer to both "where the context so requires". U.C.C. § 9-105(1)(d) (1978).

171. 7 U.S.C. § 1631(e)(1)(A)(ii)(II) (Supp. IV 1986).

172. *Id.* § 1631(e)(1)(A)(ii)(III).

given to anyone drafting such a notice, in any case where the person indebted and the owner of the collateral are not identical, would be to disclose the names, addresses, *and* identification numbers of *both*.

Some support for this conclusion may be found in the interpretations issued by the Department of Agriculture pursuant to the direction in the Federal Act for the Secretary of Agriculture to "prescribe regulations . . . to aid States in the implementation and management of a central filing system."¹⁷³ The Agriculture Department's regulations and interpretive opinions do not discuss the Act's requirements relating to written notices of security interests given directly to buyers, since such notices operate independently of any central filing system. But they do deal in considerable detail with what is required to appear in an "effective financing statement" (EFS) which is centrally filed, and much of the Act's language relating to the contents of an EFS is identical to or closely resembles that which deals with the contents of a "written notice of the security interest." Moreover, there may be enough commonness of purpose of the two types of documents to warrant the inference that they should be read as laying down the same requirements to the extent that they correspond closely in wording.

With regard to identification of the debtor, the wordings of the two parts of the "clear title" section¹⁷⁴ are identical and present the same problems of interpretation. The Department of Agriculture reads the Act as requiring that an effective financing statement identify, by name, address, and social security number or taxpayer ID number, "each person subjecting the farm product to the security interest, whether or not a debtor."¹⁷⁵

Then there is the problem of what sort of description of the collateral in a direct notification will comply with the Act, which provides that the notice must contain "a description of the farm products subject to the security interest created by the debtor, including the amount of such products where applicable, crop year, county or par-

173. *Id.* § 1631(i). As the regulations are authorized by the text of the act, they probably have the force of law. See *United States v. Walter Dunlap & Sons*, 800 F.2d 1232, 1238 (3rd Cir. 1986). The interpretive opinions may not have the force of law, *id.*, but may nevertheless be of persuasive authority. However, since neither the regulations nor the interpretive opinions deal explicitly with the direct notifications under consideration at this point of the text of this article, they are, at best, of persuasive authority.

174. 7 U.S.C. § 1631(c)(4) (Supp. IV 1986) (definition of "effective financing statement"); *id.* § 1631(e)(1)(A)(ii) (contents of a direct notification).

175. 9 C.F.R. § 205.103(a)(4), (5) (1987). The regulation is discussed in greater detail in the text of this article *infra* notes 235-39.

ish, and a reasonable description of the property."¹⁷⁶ This language seems to mean that the description must be adequate to enable the recipient of the notice to determine which particular goods are subject to the security interest, *i.e.*, that it would not be enough to indicate merely the type or types of goods in which a security interest is claimed.¹⁷⁷ But must the description go further?

The requirement that "the amount of such products" be shown "where applicable" can be read as meaning that the amount of the products must be specified when that is necessary to identify the goods that are subject to the security interest. However, the Act appears to require that "crop year," "county or parish" and the land with which the products are associated ("the property") always be shown, no matter how adequately the collateral would be identified without those entries. The reason for these requirements is not apparent,¹⁷⁸ and a secured party might well wish to omit such details when they were unnecessary to identify the collateral, for the more detail he includes in his description, the more likely it is that he will have to send out amended notifications later, as changes occur which would render those elements of the description inaccurate.¹⁷⁹ Could "crop year," "county or parish" or a description of land ever safely be omitted?¹⁸⁰

176. 7 U.S.C. § 1631(e)(1)(A)(ii)(IV) (Supp. IV 1986).

177. While this reading is not unchallengeable, some support for it is found by comparing the Federal Act language with that of the U.C.C. relating to the contents of an Article 9 "financing statement." It is quite evident from the text of the Federal Act as a whole and its legislative history that the draftsmen were writing a statute designed to modify the effect of the U.C.C. and were conscious of its language. A departure from U.C.C. terminology, therefore, at least suggests an intent to produce a different rule. In the U.C.C. a "financing statement" is required to contain "a statement *indicating the types, or describing the items, of collateral.*" U.C.C. § 9-402(1) (1978) (emphasis added).

178. Identifications of "crop year" and "county or parish" would be desirable in an EFS, since the central filing officer is required to prepare a master list of filings which is organized by "crop year" and by "county or parish." 7 U.S.C. § 1631(c)(2)(C)(ii) (Supp. IV 1986). There is no comparable requirement relating to direct notices of security interests, and even as to an EFS, the only imaginable purpose of a land description is to aid in the identification of the goods subject to the security interest.

179. See discussion of the amendment requirement *infra* notes 256-64 and accompanying text.

180. See Meyer, *Agricultural Credit*, *supra* note 150, at 497; Meyer, *Congress's Amendment*, *supra* note 153, at 11. The U.C.C. is no help here. A Code financing statement is required to include "a description of the real estate concerned" only "[w]hen the financing statement covers crops growing or to be grown," U.C.C. § 9-402(1) (1978); or where it covers "timber to be cut or covers minerals or the like (including oil and gas)" or certain accounts or fixtures, *id.* § 9-402(1) and (5). No description of the land is required as to farm products in general, and even in the case of crops no land description is needed if the crops have already been harvested.

Agriculture Department interpretations of the "clear title" section of the Food Security Act are less helpful here, for several reasons. The Act's language dealing with descriptions of collateral in an EFS is not identical with that concerning a direct notification of security interest, although there is a close resemblance.¹⁸¹ Moreover, the administrative interpretations are based on an assumption that an EFS must contain enough information to enable the central filing officer to compile a master list complying with the Act, in addition to identifying the goods subject to the security interest,¹⁸² but "master list" requirements are irrelevant to direct notifications. Finally, the Act's definition of an "effective financing statement" calls merely for substantial compliance with its specifications and indicates that an EFS may be adequate "even though it contains minor errors that are not seriously misleading,"¹⁸³ but no similar language appears in the paragraphs dealing with direct notifications. Given these uncertainties as to the reliability of Agriculture Department regulations and interpretive opinions relating to effective financing statements, the prudent course for a secured party drafting a direct notice of his security interest would be to take the statutory language quite literally, and to include "crop year," "county or parish" and a land description in any such notice.

That advice does not solve all of the secured party's problems, however, for there are ambiguities in the statutory language. What is meant by "crop year," for example? The phrase most naturally sug-

181. An "effective financing statement" is required to contain "a description of the farm products subject to the security interest created by the debtor, including the amount of such products where applicable; and a reasonable description of the property, including county or parish in which the property is located" 7 U.S.C. § 1631(c)(4)(D)(iv) (Supp. IV 1986).

A "written notice of the security interest" given by the secured party or seller directly to a buyer must contain "a description of the farm products subject to the security interest created by the debtor, including the amount of such products where applicable, crop year, county or parish, and a reasonable description of the property" *Id.* § 1631(e)(1)(A)(ii)(IV).

Comparing the two passages, note that an EFS is not expressly required to show "crop year," while a direct notification is. Furthermore, "county or parish" is mentioned in the definition of an EFS as part of the "reasonable description of the property" requirement, whereas the description required in a direct notification appears to call for description of "county or parish" in addition to a "reasonable description of the property." Finally, the language applicable to an EFS is explicit that the land described, and the county or parish designated, is that on which "the property" (presumably meaning the farm product involved) "is located", whereas the specifications for a direct notification do not expressly indicate what "property" must be reasonably described. Quite possibly these differences in wording are of negligible significance, but one cannot be sure that the courts will find no difference in meaning.

182. See *infra* text accompanying notes 240-249.

183. 7 U.S.C. § 1631(c)(4)(I) (Supp. IV 1986).

gests the year that an annual crop such as wheat or soybeans is grown, but "farm products" includes animals, animal products (such as eggs), and plants that require more than one year to mature and which may be severed from the ground at varying times. How many of these have "crop years," and how are their "crop years" to be determined? Agriculture Department interpretations treat this term, as applied to a "master list" or EFS, as applicable to all farm products, and as meaning: with respect to crops grown in soil, "the calendar year in which it is harvested or to be harvested;"¹⁸⁴ with respect to animals, "the calendar year in which they are born or acquired;"¹⁸⁵ and, with respect to poultry and eggs, "the calendar year in which they are sold or to be sold."¹⁸⁶ While these are by no means the only possible readings of "crop year," the interpretations are the best guidance available for drafters of direct notifications.

The "county or parish" specification and the "reasonable description of the property" called for also present difficulties of interpretation. "[T]he property" presumably means the land with which the described farm products are associated, for the phrase would be redundant if it referred to the goods subject to the security interest,¹⁸⁷ and a "reasonable description" of it surely could be something less than a legal description.¹⁸⁸ But what land must be described: that on which the products were produced, the land on which they are located at the time the notification is given, that on which they are expected to be located at the time of sale, or something else? The Agriculture Department reads the Act as requiring that the "county or parish" designated in an EFS be that "where the product is or is to be produced,"¹⁸⁹ and this may be persuasive authority for the meaning of the similar language regarding the contents of a direct notification, as to both the "county or parish" to be designated and the land to be described.

Even that much help is not available as to another requirement for a "written notice of the security interest:" it must be "organized

184. 9 C.F.R. § 205.107(a)(1) (1987) (regulation).

185. *Id.* § 205.107(a)(2) (regulation).

186. *Id.* § 205.107(a)(3) (regulation).

187. Agriculture Department interpretations so assume with regard to the similar language applicable to effective financing statements. *See* 9 C.F.R. § 205.207 (1987) (interpretive opinion). *See also* Meyer, *Congress's Amendment*, *supra* note 153, at 11.

188. *See* Agriculture Department interpretive opinion, *supra* note 187. *Cf.* U.C.C. § 9-110 (1978): "[A]ny description of . . . real estate is sufficient whether or not it is specific if it reasonably identifies what is described."

189. 9 C.F.R. § 205.207(c) (1987) (interpretive opinion).

according to farm products,"¹⁹⁰ a requirement not appearing in the definition of an "effective financing statement;" and what it means is anything but clear. "[O]rganized according to farm products" probably means "organized according to *types of farm products*," but no guidance is offered in the statutory text as to what type-categories are to be used, nor with regard to how the notice is to be "organized." Suppose that a secured party has a security interest arising from a single security agreement in the wheat and soybean crops of his farmer-debtor, all being grown on the same farm. Must a notice of that security interest be divided into two parts: one perhaps labeled "Wheat" and giving all the information required to identify the parties, describe the collateral and show any "payment obligations imposed on the buyer" as to the wheat collateral, then another part headed "Soybeans" which repeats all of the same information as to the soybean collateral? Could he use a single heading, "Wheat and Soybeans," or simply "Crops," so as to make that duplication of information unnecessary?¹⁹¹

Perhaps the requirement that the notice be "organized according to farm products" was included with a particular type of case in mind: that where a firm engaged in agricultural financing sends out to potential buyers a blanket notice of all of its security interests, in numerous types of farm products owned by many different debtors, hoping by a single notice to protect all of its security interests. Such a document might be quite inadequate to alert a buyer to the existence of a security interest in any particular collateral unless it were organized in some way that would enable the reader to find his way through the mass of detail to that which affects him, and organization of the notice by types of farm products could be helpful for this purpose. However, it is but a small step toward the goal, and to impose it on all secured parties giving notices of their security interests, as the Act appears to do, goes further than necessary to address the problem.¹⁹²

190. 7 U.S.C. § 1631(e)(1)(A) (Supp. IV 1986).

191. See Meyer, *Agricultural Credit*, *supra* note 150, at 496.

192. The Food Security Act employs the expression "organized according to farm products" in another context. The "master list" which the officer in charge of a state "central filing system" is required to compile reflecting all current filings of "effective financing statements" must be "organized according to farm products." 7 U.S.C. § 1631(c)(2)(C)(i) (Supp. IV 1986). There the requirement makes eminent sense. Hundreds or thousands of financing statements may be on file, and if anyone checking the master list to learn whether there has been a filing as to particular farm products is to locate the relevant information without a tremendous expenditure of time, the list has to be organized in such a way as to lead him to the information he seeks. Organization of the list according to farm products is one step in that direction. The goal is further promoted by requirements that, within each product category, financing statements be listed alphabetically, by debtors' names; numerically, according to the debtors' social

Nevertheless, the Act is specific that the notice must be "organized according to farm products." The safer course for the draftsman of such a notice is apparently to divide the document by headings, each of which designates a single type of farm product, and under which all information the Act requires to be shown which is relevant to that type of farm product, including "payment obligations," is set forth. The highly detailed breakdown of farm product types which the Department of Agriculture has provided for use in "effective financing statements" and "master lists"¹⁹³ is probably a reliable guide to farm product categories.

How forgiving of error (or intentional misdescription) is the Federal Act? In defining an "effective financing statement," the Act states that a document can fit the definition if it "substantially complies with the requirements of this subparagraph even though it contains minor errors that are not seriously misleading."¹⁹⁴ But no such tolerance is suggested by the language dealing with the contents of a "written notice of the security interest."¹⁹⁵ If the description of the collateral is too narrowly drawn to cover all of the farm products subject to the security interest, it seems obvious that it will be ineffective to subject the buyer to the security interest as to collateral left out of the description. But does the error invalidate the notice even as to the collateral that is described? Suppose the description is over-broad, covering farm products which are not subject to the security interest. (A secured party might be tempted to indulge in over-broad description in order to simplify the task of description or to avoid inadvertent omission of collateral.) Is the notice then ineffective

security or taxpayer ID numbers; geographically, by counties or parishes; and chronologically, by crop years. *Id.* § 1631(c)(2)(C)(iii). The organization according to farm products serves the further purpose of making it possible for the filing officer to comply with requests from buyers to be furnished with copies of portions of the master list relating only to the types of farm products in which they are interested. *Id.* § 1631(c)(2)(D), (E). The Department of Agriculture has issued regulations and interpretive opinions giving filing officers guidance as to how to comply with these requirements. 9 C.F.R., pt. 205 (1987). This includes a list of the farm products categories to be used. *Id.* § 205.206 (interpretive opinion).

However, the requirement of organization of a written notice of security interest "according to farm products" serves little purpose unless the notice covers numerous farm products. Even then it is of dubious value, since there is no requirement that the notice be further subdivided according to debtors' names or in any other manner. The relevance of Agriculture Department interpretations of what "organized according to farm products" means in the context of a "master list" to the meaning of the same language in relation to a written notice of security interest is doubtful at best.

193. *Id.* § 205.206(a) (interpretive opinion).

194. 7 U.S.C. § 1631(c)(4)(I) (Supp. IV 1986).

195. See Note, *Clear Title*, *supra* note 100, at 86 (asserting that Congress intended to mandate strict compliance).

against the buyer as to *any* of the described collateral? Some highly creative judicial construction of this statute is called for.¹⁹⁶

Finally, the secured party who employs the direct notification method of protecting his security interest must keep in mind the requirement that the buyer have received notice of the security interest within one year prior to the sale.¹⁹⁷ If the security interest is still attached to particular farm products when the effectiveness of a prior notification approaches its one year limit, a new notice is required.¹⁹⁸ Application of the "1 year" time limit may be difficult as well, because of the Federal Act's failure to define the term "sale."¹⁹⁹

The direct notification, or "prenotification,"²⁰⁰ method of protecting a security interest is thus rather hazardous, although it has been reported that this method has in fact been employed by many agricultural lenders attempting to adapt to the new rules of the Food Security Act,²⁰¹ probably, in many instances, because they had little choice.²⁰²

4. Indirect Notification of Security Interests

The alternative method, termed here the method of "indirect notification," is available only where the state in which the farm products collateral is produced has a "central filing system" certified by

196. Other problems of interpretation relating to written notices of security interests are discussed *supra* note 100. In connection with the question of whether the notice must be signed, and if so by whom, it has been suggested that both the debtor and the secured party should sign, to avoid potential problems. Sanford, *supra* note 138, at 20.

197. 7 U.S.C. § 1631(e)(1)(A) (Supp. IV 1986).

198. See Note, *Clear Title*, *supra* note 100, at 85-86; Meyer, *Agricultural Credit*, *supra* note 150, at 498 (commenting also on the ambiguity of the "lapse" provisions of 7 U.S.C. § 1631(e)(1)(A)(iv) (Supp. IV 1986)); Meyer, *Congress's Amendment*, *supra* note 153, at 13.

199. See Sanford, *supra* note 138, at 19-20.

200. Although the term "prenotification" is sometimes used in commentary on the "clear title" section of the Food Security Act to refer to the direct notification method of protecting a security interest (see *supra* note 157), the term seems inapt, since both of the methods of notification contemplated by the Act are usually ineffective unless the buyer receives notification of the security interest before the sale. That this is so with regard to indirect notification, see *infra* text at note 212.

201. See Clark, *supra* note 157, at 1338.

202. Professor Clark reports that the Comptroller of the Currency has instructed bank examiners to treat agricultural loans as unsecured, even if the banks' security interests are perfected under the U.C.C., if the lenders have not protected their security interests under the Food Security Act as well. *Id.* at 1337. Yet, as of the time of his writing (early in 1987) only ten states had obtained federal certifications for their central filing systems. *Id.* at 1339, n. 20. Some of them were probably not in actual operation. Giving direct written notices of their security interests was thus the only available prudent course of action for many secured parties.

the Secretary of Agriculture as complying with the Federal Act.²⁰³ It involves the secured party's filing of notice of his security interest (an "effective financing statement" or "notice" thereof) with the central filing system and, usually, the central filing officer's informing the buyer of the filing, either by distributing to the buyer a summary of filings which lists that of the secured party²⁰⁴ or by his informing the buyer of the filing in response to the buyer's request for information about filings as to a particular seller's farm products.²⁰⁵ (A central filing made by the secured party is, by itself, sufficient to protect the security interest against a buyer who fails to register with the central filing officer as a person interested in receiving periodic summaries of filings.)²⁰⁶

This method of notification differs from the direct notification method, not only in its more roundabout routing, but also, it appears, in its basic purpose. Whereas a direct notification seems to be of no value to the secured party at all unless it includes a statement of "pay-

203. 7 U.S.C. § 1631(c)(2) (Supp. IV 1986). There is a question as to the conclusiveness of certification by the Department of Agriculture that a state central filing system complies with the Act. The Act might be read as meaning that a state system must *both* be certified by the Secretary of Agriculture *and* in fact be organized and operated in conformity with the statutory requirements for a "central filing system". See Sanford, *supra* note 138, at 12. The Department of Agriculture reads the Act that way. 9 C.F.R. § 205.214(a) (1987) (interpretive opinion):

The requirements for a system in subsection (c) are written as the definition of the term 'central filing system,' so that failure of a system to meet any such requirement, either at the time of its establishment or later, will mean that it is not a 'central filing system' as defined.

Thus, even though a state has a federally certified central filing system, the secured party has filed a proper financing statement in the prescribed manner, and the buyer has received notice of the filing from the central filing officer, there could be litigation over the applicability of subsection (e)(2) or (3) of the "clear title" section. See *id.* § 205.214(b); Sanford, *supra* note 138, at 12-13.

204. See *supra* text accompanying notes 104 *et seq.*

205. *Id.* The inclusion of this alternative method of a buyer's being given notice of a central filing is confusing. The Federal Act requires the central filing officer to furnish information as to filings with respect to particular sellers or farm products, on request, only "to those . . . not registered pursuant to (2)(D)" (emphasis added). 7 U.S.C. § 1631(c)(2)(F) (Supp. IV 1986). Such persons are subject to the security interests of secured parties who filed effective financing statements, whether or not they received notices of the filings, under subsection (e)(2). See 9 C.F.R. § 205.208(b) (1987) (interpretive opinion). Inquiries to central filing officers by such persons about filings as to particular farm products, before they buy, would be prudent behavior. However, if a buyer *has* registered with a state central filing officer to receive copies of master lists, he need not worry about filings as to goods he buys as a buyer in ordinary course of business unless he has actually *received* notice of such filings from the central filing officer. Why would such a buyer make inquiry of the central filing officer about particular filings covering goods he plans to buy? It would seem that he could only prejudice his own security by doing so.

206. See *supra* text accompanying note 115.

ment obligations" with which the buyer must comply in order to obtain the goods free of the security interest, there is no indication in the text of the Act that an "effective financing statement" must include any statement of such payment obligations. Nor is there any indication that, if such obligations are shown in the financing statement, the central filing officer must include such information in his master list or in information given about filings in response to specific requests. Under the indirect notification rules, the effectiveness of the security interest appears to be preserved against the buyer, even if he is a buyer in ordinary course of business, if the secured party has filed a proper notice of the existence of his security interest and the central filing officer has informed the buyer of the filing, giving him only the information required by the Act, unless the buyer, on his own initiative, contacts the secured party and secures a waiver or release of the security interest from him.²⁰⁷

The rationale of these rules is hard to fathom. Under the general protective rule of subsection (d) of the "clear title" section of the

207. The required contents of an "effective financing statement" are specified by 7 U.S.C. § 1631(c)(4)(D) (Supp. IV 1986). See *supra* text accompanying note 120 *et seq.* They do not include any requirement that the financing statement include a statement of "payment obligations" with which the buyer must comply "as conditions for waiver or release of the security interest," as subsection (e)(1)(A)(v) does in specifying the form required for a direct notification of security interest. Even if the financing statement does show such conditions, the central filing officer is not required to include them in the information he supplies about the filing in his "master list," copies of which are sent to registered buyers. See *id.* § 1631(c)(2)(C)(iii), which requires merely that the master list contain, as to each listed financing statement, "the information referred to paragraph (4)(D)" [sic.]. And a registered buyer "takes subject to" a security interest if he "receives from the Secretary of State . . . written notice as provided in subparagraph (c)(2)(E) [*i.e.*, a copy of the master list or portion thereof] . . . that specifies both the seller and the farm product being sold by such seller as being subject to an effective financing statement or notice" (*id.* § 1631(e)(3)(A)), unless the buyer secures a waiver or release of the security interest from the secured party (*id.* § 1631(e)(3)(B)).

There is a *reference* to performance of "payment obligation" in the portion of the Act dealing with indirect notification. Subparagraph (e)(3)(B) indicates that a registered buyer who has received notice of the filing of an EFS showing a security interest will take the collateral subject to the security interest if he "does not secure a waiver or release of the security interest specified in such effective financing statement or notice from the secured party by performing any payment obligation or otherwise." (*Id.*) (emphasis added). That language suggests to one commentator that the drafters of the Act meant to require that an EFS show "payment obligations" in much the same manner as is required of a direct notification and also meant to require that master lists show such payment obligations, with which the buyer is required to comply in order to free the goods of the security interest. See Fry, *Buying Farm Products: The 1985 Farm Bill Changes the Rules of the Game*, 91 COM. L.J. 433, 446 n.83 (1986). However, it appears that the commentator does not consider that language an adequate basis for finding any such requirements implied. See *id.* at 446 n.83, 448. The words "or otherwise" rob the reference to performance of payment obligations of much of the significance that might be read into it if it stood alone.

Food Security Act, a buyer in ordinary course of business of farm products from a person engaged in farming operations "shall take free of a security interest created by the seller, *even though . . . the buyer knows of the existence of such interest.*"²⁰⁸ Yet he "takes subject to" a security interest if he has been notified of its *existence* through the central filing system machinery.²⁰⁹ Why should knowledge of the security interest be irrelevant when such knowledge is acquired through means other than a central filing system, while mere notification of the existence of such an interest is enough to subject the buyer to the interest when such notice has come via the central filing system?

Perhaps there are two ideas at work here. First, if the secured party has gone to the trouble and expense of making a central filing, in the elaborate form prescribed by the Act, it is probably because he is worried about a real risk of his debtor's making sales of the collateral in violation of the security agreement. Thus, a buyer notified of such a filing should so much suspect the likelihood that the sale violates the rights of the secured party that he does not deserve protection as an innocent purchaser of the collateral. Second, a notice given the buyer through the central filing system will inform him not merely of the existence of the security interest but also of where he can obtain further information about his seller's freedom to sell; the notice will include the name and address of the secured party. One who knows merely of the existence of a security interest may not know where to find out more about it.

But if that is the rationale of the indirect notice provisions, why would it not also be a satisfactory rationale for the direct notification provisions, that is, why is not a direct notification effective to protect the security interest if it discloses the existence of the security interest and gives the name and address of the secured party? Why must a direct notification also specify "payment obligations" to be satisfied by the buyer?

Setting aside speculation about the policies underlying the notification machinery set up by the Federal Act, there are some problems of interpretation of the passages dealing with the indirect notification method which may worry a secured party who seeks to employ it.

An apparent inconsistency in the Act is that, although it expressly states that a direct notification, to be effective against a buyer, must have been received by him within one year prior to the sale,²¹⁰

208. 7 U.S.C. § 1631(d) (Supp. IV 1986).

209. *Id.* § 1631(e)(3).

210. *Id.* § 1631(e)(1)(A).

the provisions dealing with indirect notification do not specify that the buyer must have received notification of the filing of the security interest within any particular period of time before the sale. Indeed, the Act does not say that the notification must have been received by the buyer *before* the sale.²¹¹ The Act will probably be read as subjecting a registered buyer to a security interest by reason of his having received notification of it from the filing officer only when he has received notification before the sale.²¹² As to how long such a notification would remain effective, the answer is not certain. It may remain effective until the central filing officer issues a new list of filings, with respect to the farm products involved, which purports to be a complete listing of all current filings affecting farm products of that type. A Department of Agriculture regulation dealing with distributions of the master list, or portions of it, authorizes the central filing officer, after distributing a list of current filings, to make supplementary distributions showing only changes from the previous distribution but requires, if this is done, that "cumulative supplements . . . be distributed often enough that readers can find all the information given to them for any one crop year in no more than three distributions."²¹³ Since a buyer searching for recorded filings as to particular farm products is thus invited to look back no further than the most recent cumulative supplement, a listing appearing in an earlier distribution and not shown in the most recent cumulative supplement or its supplements should not be treated as effective against the buyer.

A point on which the Federal Act is unclear is whether a prospective buyer of farm products could immunize himself against the operation of the indirect notification rules by registering with the filing officer as interested in receiving copies of portions of the master list, but asking only for a portion or portions dealing with types of farm products which he has no expectation of buying. The Act clearly contemplates that prospective buyers may request only portions of the master list dealing with specified types of farm products, and that in the event that they do so the central filing officer is to send

211. *Id.* § 1631(e)(3).

212. The obvious purpose of distribution of copies of the master list to buyers is to enable them to discover security interests in the farm products involved before they buy the products. This is assumed by the Department of Agriculture interpretations of the Act. *See* 9 C.F.R. § 205.213(b) (1987) (interpretive opinion referring to the "purpose for which the information is supplied" as being to enable "[a]ny buyer of a farm product, commission merchant, or selling agent querying a master list or system operator about a *prospective* seller of a farm product [to learn] whether that seller has subjected that product to a security interest" (emphasis added)).

213. *Id.* § 205.105(c).

them only the portions requested.²¹⁴ Could the buyer then safely buy farm products of other types and count on immunity from security interests in those products, arguing that he never received copies of the master list showing security interests in those products, but, as he was "registered" with the central filing officer, he was not subject to the security interests for failure to register? The "clear title" section of the Food Security Act is susceptible to that reading, because subsection (e)(2) subjects a buyer to centrally filed security interests if "the buyer has failed to register with the Secretary of State . . . prior to the purchase of the farm products."²¹⁵ It does not expressly require that he have registered to receive copies of portions of the master list dealing with the farm products he actually buys in order to avoid this rule. A possible answer is that in such a case the buyer does not qualify as a "buyer in the ordinary course of business," because he does not buy in good faith, and he is therefore not protected by the general rule of subsection (d). As argued above,²¹⁶ the Act probably should be read as incorporating a "good faith" requirement for "ordinary course" buying, by implication. However, the Department of Agriculture has reached the conclusion that the ploy will not work by another route, saying in an interpretive opinion that, "[r]egistrants will be deemed to be registered only *as to those portions* of the master list for which they register"²¹⁷

Could a buyer "beat the system" by registering with the central filing officer just before the sale and buying before the next distribution of copies of the master list, so as not to have received notification of the filing of any financing statement relating to the farm products being purchased? Nothing in the text of the Act forbids it. One must hope that the definition of "buyer in the ordinary course of business" will be read as incorporating a requirement that the buying be in good faith.²¹⁸

What the secured party must file, in order to take advantage of the central filing system notification mechanism, is an "effective financing statement" (EFS) or a "notice of" such a statement.²¹⁹ The term "effective financing statement" is elaborately defined²²⁰ and constitutes a document which would give a prospective buyer of farm

214. 7 U.S.C. § 1631(c)(2)(E) (Supp. IV 1986).

215. *Id.* § 1631(e)(2)(A).

216. *See supra* text accompanying notes 151-54.

217. 9 C.F.R. § 205.208(e) (1987).

218. *See supra* text accompanying notes 150-56.

219. 7 U.S.C. § 1631(c)(2) (Supp. IV 1986).

220. *Id.* § 1631(e)(4).

products enough information not only to warn him of a claimed security interest in those particular goods but also to lead him to the secured party and debtor for further information.²²¹ "Notice of" an EFS, on the other hand, is not defined in the Act, and since such a "notice" may apparently be filed *in lieu of* the filing of the financing statement itself, the Act seems to open the possibility of some less informative sort of filing complying with the Act. However, if a "central filing system" is to qualify under the Act, it must include provision for compilation by the central filing officer of a "master list" which contains, as to each filing, the same sort of information that an effective financing statement is required to supply.²²² Furthermore, the distributions to registered buyers must include that information.²²³ So, the Act seems to imply that a "notice of" an "effective financing statement" must contain the same information as the financing statement.

The Department of Agriculture has tried to make sense of the Act's authorization of the filing of a "notice of" an EFS, in interpretive opinions, by reading the Act as requiring that the EFS itself be filed *somewhere* ("wherever State law requires")²²⁴ but permitting "notice of" that filing to the central filing officer by transmission (perhaps even by telephone)²²⁵ of enough of the information contained in the filed statement to enable the central filing officer to compile an adequate master list.²²⁶ Evidently the thought is that it would be consistent with the purposes of the Act for a state to accommodate secured parties by authorizing them to make local filings of "effective financing statements" (perhaps in the nearest county courthouses). The local filing officers would then inform the central filing officer of the filings, giving him enough information about the contents of the statements filed to enable him to perform his own duties of compiling a master list and sending copies of it to registered buyers. However, the Act seems to mean, and the Department of Agriculture assumes,²²⁷ that the secured party is not protected unless the central filing officer actually receives that information.

221. See summary of requirements for an "effective financing statement," *supra* text accompanying notes 118-27.

222. See 7 U.S.C. § 1631(c)(2)(C) (Supp. IV 1986).

223. *Id.* § 1631(c)(2)(E).

224. 9 C.F.R. § 205.203 (1987).

225. *Id.* § 205.204(a).

226. *Id.* § 205.203.

227. *Id.*

The Federal Act's definition of "effective financing statement"²²⁸ resembles, but is not identical with, the requirements for an effective direct notification of security interest.²²⁹ Some of the differences between the two sets of requirements are obviously due to the differing uses to be made of the documents, one to be filed in a public office, the other to be sent directly to buyers. As noted above,²³⁰ there also appears to be a difference in the underlying purposes of the two types of notification, which calls for a direct notice of a security interest to show "payment obligations" imposed on the buyer as conditions of his obtaining the goods free of the security interest, whereas no such requirement applies to an EFS. For some reason, an EFS must be signed by the "debtor" as well as the secured party,²³¹ while a direct notice of security interest apparently need be signed only by the person giving the notice.²³² And, for undecipherable reasons, a direct notice must be "organized according to farm products," no similar

228. The definition is as follows:

(4) The term "effective financing statement" means a statement that—

(A) is an original or reproduced copy thereof;

(B) is signed and filed with the Secretary of State by the secured party;

(C) is signed by the debtor;

(D) contains,

(i) the name and address of the secured party;

(ii) the name and address of the person indebted to the secured party;

(iii) the social security number of the debtor or, in the case of a debtor doing business other than as an individual, the Internal Revenue Service taxpayer identification number of such debtor;

(iv) a description of the farm products subject to the security interest created by the debtor, including the amount of such products where applicable; and a reasonable description of the property, including county or parish in which the property is located;

(E) must be amended in writing, within 3 months, similarly signed and filed, to reflect material changes;

(F) remains effective for a period of 5 years from the date of filing, subject to extensions for additional periods of 5 years each by refiling or filing a continuation statement within 6 months before the expiration of the initial 5 year period;

(G) lapses on either the expiration of the effective period of the statement or the filing of a notice signed by the secured party that the statement has lapsed, whichever occurs first;

(H) is accompanied by the requisite filing fee set by the Secretary of State; and

(I) substantially complies with the requirements of this subparagraph even though it contains minor errors that are not seriously misleading.

7 U.S.C. § 1631(c)(4) (Supp. IV 1986).

229. Compare *id.* § 1631(e)(1), quoted in note 169 *supra*.

230. See *supra* text following note 161.

231. "Signed" is not defined in the Federal Act, an omission that may cause difficulties. See Sanford, *supra* note 138, at 13.

232. See *supra* note 100.

requirement being applicable to an EFS.²³³ Beyond these requirements, however, the two parts of the Act lay down requirements of form which are defined in nearly identical terms and present much the same problems of interpretation. Fortunately, the draftsman of an "effective financing statement" is aided in his task by Department of Agriculture regulations and interpretations, which appear to be authorized by the "clear title" section of the Food Security Act.²³⁴

Among the questions addressed by the regulations are those of who must be identified in the financing statement as the "debtor" and how he is to be identified. The regulations call for the "[n]ame and address of each person subjecting the farm product to the security interest, whether or not a debtor,"²³⁵ despite the fact that the text of the Act calls for the "name and address of the person indebted to the secured party,"²³⁶ and, the regulations require inclusion of the "[s]ocial security number or, if other than a natural person, IRS taxpayer identification number, of each such person,"²³⁷ though the statute calls for such numerical identification of the "debtor."²³⁸ As the Department reads the Act, in a case where the secured debt is owed by one person but the collateral is owned by another, the EFS would have to contain full identifications of both, a sensible reading which cuts through the difficulties posed by inept statutory language.²³⁹

As to the description of the collateral to be provided in an EFS, the guiding principles of the Department's reading of the Act appear to be that the statement must describe the collateral in such a way as (a) to identify the particular goods which are subject to the security interest, and (b) to make possible preparation by the central filing officer of a "master list" of filings which complies with the Act. Since the master list must be "organized according to farm products,"²⁴⁰ the financing statement must identify the collateral by "[f]arm product name,"²⁴¹ and the Department supplies a list of farm product

233. See *supra* text accompanying notes 190-92.

234. "The Secretary of Agriculture shall prescribe regulations . . . to aid States in the implementation and management of a central filing system." 7 U.S.C. § 1631(i) (Supp. IV 1986).

235. 9 C.F.R. § 205.103(a)(4) (1987).

236. 7 U.S.C. § 1631(c)(4)(D)(ii) (Supp. IV 1986); *supra* note 228.

237. 9 C.F.R. § 205.103(a)(5) (1987) (emphasis added).

238. 7 U.S.C. § 1631(c)(4)(D)(iii) (Supp. IV 1987); *supra* note 228.

239. See also 9 C.F.R. § 205.213(b) (1987). This question also affects the question of who should sign the EFS as "debtor." The prudent course would be for the secured party to persuade all persons identified as debtors to sign. See Sanford, *supra* note 138, at 14.

240. 7 U.S.C. § 1631(c)(2)(C)(i) (Supp. IV 1986).

241. 9 C.F.R. § 205.103(a)(2) (1987) (regulation). See also 9 C.F.R. § 205.106 (1987) (regulation). Mr. Sanford, *supra* note 138, at 14, reads these regulations as requiring that any proceeds of collateral which are also farm products be described in the EFS by farm product

names from which the choice should be made.²⁴² The master list, within each product category, must be organized "geographically by county or parish;"²⁴³ therefore, the financing statement must list "[e]ach county or parish in the [state where the filing is to be made] where the farm product is produced or to be produced."²⁴⁴ The master list must be organized "by crop year."²⁴⁵ Hence, even though the Act does not expressly require that an EFS show crop year, the financing statement must show "[c]rop year *unless every crop of the farm product in question, for the duration of the EFS, is to be subject to the particular security interest.*"²⁴⁶ Beyond these specific requirements, the test of sufficiency is the adequacy of the description of any farm product which is "subject to the security interest . . . to distinguish it from other such product owned by the same person or persons but not subject to the particular security interest."²⁴⁷ Thus, for example, if the secured party claims a security interest in all of a named type of product owned by a particular person in a designated county or parish, the location of the collateral need not be more particularly described, but if only part of such goods are subject to the security interest, the description must indicate which part is subject to the security interest.²⁴⁸ Similarly, the amount of the goods subject to the security interest need not be specified unless the description given would, without such specification, include farm products to which the security interest does not apply.²⁴⁹

The indirect notification method of protecting a security interest has the advantage for the secured party of requiring that he give only one notice, by filing one EFS with the filing officer designated by state law, rather than sending notices to all potential buyers of the collateral.²⁵⁰ However, it has the disadvantage that the filing is only the

name as well, *i.e.*, that a simple claim to "proceeds" of collateral will not do if the proceeds are themselves farm products.

242. 9 C.F.R. § 205.206 (1987). Oddly, this list appears in an "Interpretive Opinion," rather than in a "Regulation."

243. 7 U.S.C. § 1631(c)(2)(C)(ii)(III) (Supp. IV 1986).

244. 9 C.F.R. § 205.103(a)(3) (1987) (regulation).

245. 7 U.S.C. § 1631(c)(2)(C)(ii)(IV) (Supp. IV 1986).

246. 9 C.F.R. § 205.103(a)(1) (1987) (regulation) (emphasis in original). *See also id.* § 205.107 (regulation defining "crop year").

247. *Id.* § 205.103(a)(6) (regulation).

248. *Id.* § 205.207(c) (interpretive opinion). For further discussion of the location-description requirement see Sanford, *supra* note 138, at 15.

249. *See* 9 C.F.R. § 205.207(b) (1987) (interpretive opinion).

250. Furthermore, the filing remains effective for a period of five years and its effectiveness can be continued by refiling or by filing a continuation statement. 7 U.S.C. § 1631(c)(4)(F) (Supp. IV 1986).

first step toward protection of the security interest, for the filing does not, of itself, operate as notice to any buyer who has registered with the central filing officer. Its effectiveness against a registered buyer depends on the buyer's having been notified of the filing by the central filing officer, either by sending to him, and the buyer's "receipt"²⁵¹ of, a copy of the portion of the master list which shows the particular filing or by informing the buyer of the filing in response to an inquiry from the buyer.²⁵² Since copies of the master list are required to be distributed to registered buyers only "regularly as prescribed by the State,"²⁵³ the secured party must accept the risk that a sale may occur before the buyer receives his notice of the secured party's filing and that the buyer will therefore take the goods free of the security interest despite the filing.²⁵⁴ Another risk for the secured party arises from the possibility that the central filing officer will fail to list the filed financing statement in his master list, or will record it incorrectly. The secured party, rather than the buyer, apparently bears the burden of such errors.²⁵⁵

251. "What constitutes receipt, as used in this section, shall be determined by the law of the state in which the buyer resides." 7 U.S.C. § 1631(f) (Supp. IV 1986). It follows that if a buyer who registers with a state's central filing officer lives in another state, his "receipt" of a notification from the central filing officer will depend on the definition of "receipt" embodied in the law of the buyer's state, not that of the state of the central filing system with which he has registered. For a discussion of potential problems arising from this rule, see Sanford, *supra* note 138, at 22-23.

252. See *supra* text accompanying notes 116-17. This feature of the "clear title" section of the Food Security Act differs notably from the effect of filing a financing statement under the U.C.C. A properly drawn and filed Code "financing statement" perfects the security interest and gives the secured party the benefits that flow from perfection, whether the rival claimant is aware of the filing when his interest in the goods arises or not. It is the *filing* that perfects the security interest. On the other hand, a Code filing which is made in good faith in an improper place or not in all places required by Article 9 is nevertheless "effective with regard to collateral covered by the financing statement against any person who has knowledge of the contents of such financing statement." U.C.C. § 9-401(2) (1978).

253. 7 U.S.C. § 1631(c)(2)(E) (Supp. IV 1986). An Agriculture Department interpretive opinion asserts that "distribution must be timely to serve its purpose" and that the "frequency of such distribution must be a consideration in review for certification" but recognizes that the states have "discretion to choose the interval between distributions." 9 C.F.R. § 205.208(f) (1987).

254. The Agriculture Department interpretive opinion cited in the preceding note observes that "whatever interval a State chooses will inevitably make possible some transactions in which security interests are filed in the system but registrants are not subject to them." *Id.* See also Note, *Clear Title*, *supra* note 100, at 91 (suggesting that "pre-notification will be an ideal alternative" in the interim, a suggestion not likely to be of much comfort to a secured party who is unaware of an impending sale).

255. An Agriculture Department interpretive opinion observes that, "Legislative history of the Section shows that buyers, commission merchants, and selling agents are not intended to be liable for errors or other inaccuracies generated by the system," citing Senate and House debates. 9 C.F.R. § 205.208(g) (1987). See also Note, *Clear Title*, *supra* note 100, at n. 164.

Additional risks for the secured party seem to lurk in the Federal Act's provisions regarding amendment of EFS filings to reflect "material changes."²⁵⁶ The Act includes in the definition of "effective financing statement" a requirement that the statement "be amended in writing, within [three] months, similarly signed and filed, to reflect material changes."²⁵⁷ The Act does not define "material changes." The Department of Agriculture interprets the phrase as referring to "whatever change would render the master list entry no longer informative as to what is subject to the security interest in question."²⁵⁸ An example might be a case where, under the terms of the security agreement, the secured party was granted a security interest in "all livestock now or hereafter owned by debtor." Suppose the debtor's only livestock at the time of the filing by the secured party of his EFS consisted of cattle, which were adequately described in the EFS, and the debtor subsequently acquired some hogs as well; presumably, an amendment of the EFS would have to be filed, describing the hogs as security for the debt, in addition to the debtor's cattle.²⁵⁹ A problem that might arise here is that the secured party might be unaware of the change in the character of the collateral and therefore would fail to make timely filing of an amendment. Would a registered buyer of the new collateral take subject to the security interest? The Department of Agriculture's interpretations hedge on the question, pointing out that "the Section is silent as to the consequences,"²⁶⁰ but suggesting that legislative history points in the direction of placing the burden of this risk on the secured party.²⁶¹

Another question is whether, if the secured party does file an amendment within three months after the change occurs, his security interest in the collateral described in the amendment (but not described in the EFS originally filed) is enforceable against a registered buyer who buys the new collateral before the amendment has been filed, or before he is notified by the filing officer of that filing.²⁶² Given

256. 7 U.S.C. § 1631(c)(4)(E) (Supp. IV 1986).

257. *Id.* "Similarly signed" evidently requires that both the secured party and the debtor sign the amendment, a requirement that could cause trouble for the secured party. *See* Sanford, *supra* note 138, at 15-16.

258. 9 C.F.R. § 205.209(a) (1987).

259. Mr. Sanford, *supra* note 138, at 16, suggests that amendments would also be required where locations of collateral change or collateral is transferred to a new owner.

260. 9 C.F.R. § 205.209(b) (1987).

261. *See id.*

262. The published regulations and interpretive opinions of the Department of Agriculture do not deal with this question.

the general pro-buyer orientation of the "clear title" rules,²⁶³ it seems unlikely that the intent of the rule on amendment of filed financing statements was to subject the buyer to the security interest in these circumstances. It would give the amendment a retroactive effect which the original financing statement did not have.

Assuming that is so, what is the effect of a late filing of an amendment? To read the Act as meaning merely that the buyer does not become subject to the security interest unless he receives notice of the amendment before he buys ignores the fact that the Act sets a specific three-month deadline for such a filing. To give that time limit effect, the Act seemingly must be read as meaning that the amendment never becomes effective as notice to registered buyers, if it is filed more than three months after the material change occurs; or, more drastically, that the original financing statement becomes ineffective at the expiration of three months after a material change occurs unless an amendment reflecting the change has been filed within that time. (The same problem arises in connection with direct notifications of security interests, for identical language requiring amendments to reflect material changes appears in the subsection dealing with such direct notifications.)²⁶⁴

On the other hand, the Act seems to subject the *buyer* to one type of risk, which develops when farm products collateral moves from its state of origin to another state, where it is sold by the debtor. If the state in which the farm products were "produced" has a "central filing system" certified as complying with the Federal Act, and if the secured party has properly filed an EFS in that state, but the buyer has not registered with the central filing officer of that state prior to his purchase of the collateral, it appears that he "takes subject to [the] security interest."²⁶⁵ It is entirely possible that the buyer will be unaware of the state of origin of the collateral, and thus not able to register with the filing officer of that state, prior to the sale.²⁶⁶ Despite the fact that one of the stated reasons for Congressional enactment of the "clear title" section of the Food Security Act was to correct the injustice produced by subjecting a buyer to a security interest when the buyer "lacks any practical method for discovering the existence of the

263. See *supra* text accompanying note 261.

264. 7 U.S.C. § 1631(e)(1)(A)(iii) (Supp. IV 1986). See Meyer, *Agricultural Credit*, *supra* note 150, at 497.

265. 7 U.S.C. § 1631(e)(2) (Supp. IV 1986).

266. The buyer may also have a problem of determining where particular farm products were "produced," even if he knows all of the relevant facts. See Sanford, *supra* note 138, at 21.

security interest,"²⁶⁷ the wording of the statute seems to compel the result that the buyer takes subject to the security interest in these circumstances.²⁶⁸

5. *Effect on U.C.C. Rules Other Than Section 9-307(1)*

One point that is clear from the statutory text and its legislative history²⁶⁹ (but which may not be so clear to financiers of agricultural operations) is that, despite the use of confusingly similar terminology in both statutes, a filing conforming to the "clear title" section of the Food Security Act is *not* the equivalent of a filing under Article 9 of the Uniform Commercial Code. It does not "perfect" a security interest, within the meaning of that term in Article 9, nor does it give the secured party as protected a status as he would have if he did perfect his security interest under Article 9. The Federal Act's filing system is superimposed on the Article 9 system for perfection of security interests and has the limited purpose of enabling the secured party to enforce his security interest against buyers of farm products from his debtor (and against commission merchants and selling agents who sell the products for the debtor).

When collateral takes the form of any type of property that is not within the definition of "farm products," as the Federal Act defines that term, the Federal Act does not alter the operation of Article 9 of the U.C.C. at all. Even if "farm products" are involved, the secured party must "perfect" his security interest in accordance with Article 9 in order to gain rights against persons other than *buyers* of those products, such as "lien creditors"²⁷⁰ and other secured parties claim-

267. 7 U.S.C. § 1631(a)(1) (Supp. IV 1986) (the statement of findings prompting the enactment of the "clear title" section, *quoted supra* note 152).

268. See 9 C.F.R. § 205.210(b) (1987) (interpretive opinion); Note, *Clear Title*, *supra* note 100, at 94-95.

269. See HOUSE REPORT, *supra* note 135, at 110 (commenting on the House bill which ultimately became the Food Security Act of 1985):

The bill is intended to preempt state law (specifically the so-called "farm products exception" of [U.C.C.] Section 9-307) to the extent necessary to achieve the goals of this legislation. Thus, this Act would preempt state laws that set as conditions for buyer protection of the type provided by the bill requirements that the buyer check public records, obtain no-lien certificates from the farm products sellers, or otherwise seek out the lender and account to that lender for the sale proceeds. By contrast, the bill would not preempt basic state-law rules on the creation, perfection or priority of security interests.

(Although the bill was considerably amended before its final passage, none of the changes made after this House Report was filed suggests an intent that would invalidate the final sentence of the passage quoted.)

270. A "lien creditor" is "a creditor who has acquired a lien on the property involved by attachment, levy or the like;" the term also includes "an assignee for benefit of creditors from

ing rights in the same collateral.²⁷¹ That may require filing, but it will

the time of assignment, and a trustee in bankruptcy [a secured party's *bete noire*] from the date of the filing of the petition or a receiver in equity from the time of appointment." U.C.C. § 9-301(3) (1978). As a general rule, "an unperfected security interest is subordinate to the rights of . . . a person who becomes a lien creditor before the security interest is perfected." *Id.* § 9-301(1)(b). An exception is made in favor of a secured party who has a "purchase money security interest;" such a secured party can gain priority over a lien creditor who has become such while the security interest was unperfected if the secured party files within a certain period after the debtor receives possession of the collateral. Under the 1978 Official Text this period is ten days. *Id.* § 9-301(2). Under the Arkansas Code, as a result of a 1983 amendment, the period is 21 days. Act of March 21, 1983, No. 561, 1983 Ark. Acts 1190 (codified at ARK. CODE ANN. § 4-9-301(2) (1987)).

271. U.C.C. § 9-312 contains an elaborate set of rules governing priorities among conflicting security interests in the same collateral. Arkansas amendments have produced some departures from the Official Text. *See, e.g.*, Act of April 2, 1987, No. 560, 1987 Ark. Acts 1565 (Adv. Leg. Ser.) (codified at ARK. CODE ANN. § 4-9-312 (Supp. 1987)); *supra* note 270.

One commentator has found a circular-priority problem in the interaction between the Food Security Act and the U.C.C. *See Note, Clear Title, supra* note 100, at 93-94. Assume that First Bank makes a loan to Farmer and takes a security interest in his farm products. First Bank perfects its security interest under the U.C.C. but fails to protect its security interest against buyers under the Federal Act. Second Bank then makes a loan to Farmer, taking a security interest in the same farm products, failing to perfect its security interest under the U.C.C. but giving Buyer direct notification of its security interest under the "clear title" section of the Food Security Act. Farmer sells his products to Buyer, who is a buyer in ordinary course of business; the sale violates the terms of both security agreements, and neither bank receives any of the proceeds. Under the Federal Act Buyer would take the goods subject to Second Bank's security interest but not subject to First Bank's security interest. However, under the U.C.C., §§ 9-301(1)(a) and 9-312(5)(a), First Bank's security interest is entitled to priority over that of Second Bank. The writer of the Note concludes that First Bank has priority over Second Bank but Buyer has priority over First Bank, and Second Bank has priority over Buyer. *See Note, Clear Title, supra* note 100, at 94. The commentator suggests that there are a number of possible solutions but recommends that secured parties avoid the problem by protecting themselves fully under both acts. *See id.* No doubt that is good advice, and there is a vexing problem in this fact situation, but it does not seem to be a problem of circular priorities in claim to the goods sold, if the Federal Act can be taken literally. As far as the goods are concerned, Second Bank has a good claim to them, unless the buyer satisfied the "payment obligations" shown in Second Bank's direct notification of security interest, but First Bank has no claim to the goods, against Buyer or Second Bank, for the Federal Act provides that the buyer takes "free of" First Bank's security interest. 7 U.S.C. § 1631(d) (Supp. IV 1986). The problem relates to the *proceeds* of the collateral. Both banks probably have security interests in the proceeds under U.C.C. § 9-306(2), and First Bank may well have priority over Second Bank in claim to the proceeds. (Under the U.C.C. § 9-306(3) First Bank's security interest in the proceeds is treated as perfected, at least temporarily, and possibly permanently, since its security interest in the original collateral was perfected. Under U.C.C. § 9-312(5)(a) First Bank's perfected security interest has priority over Second Bank's, if Second Bank's interest in the proceeds was unperfected.) Yet, to take the goods free of Second Bank's security interest under the Federal Act, Buyer must satisfy the "payment obligations" imposed by Second Bank in its notification of its security interest. 7 U.S.C. § 1631(e)(1) (Supp. IV 1986). Since such payment obligations are likely to call for payment to Second Bank, could Buyer safely comply with them if First Bank had the prior claim to the proceeds of the collateral? And if Buyer paid First Bank instead, would he take the goods free of Second Bank's security interest under the Federal Act?

be filing of a "financing statement" complying with the requirements of Article 9 of the Code,²⁷² and filing in the place or places specified by the Code.²⁷³

On the other hand, the Federal Act clearly nullifies the "farm products" exception of section 9-307(1) of the U.C.C. almost entirely, and it appears also to alter the operation of section 9-301(1)(c).²⁷⁴ In the discussion of that provision above,²⁷⁵ it was observed that the operation of the rule is to immunize buyers of goods from "unperfected" security interests in those goods, even if they are not buyers in ordinary course of business, if the buyers both give value and receive delivery of the goods without knowledge of the security interest. However, the "clear title" section of the Food Security Act, in its subsection (e), provides that, "[a] buyer of farm products takes subject to a security interest created by the seller" in the circumstances described in that subsection, none of which requires that the buyer actually know of the security interest. And, nothing in the wording of the

272. An "effective financing statement" under the Federal Act differs from a "financing statement" which satisfies the requirements of Article 9 of the Uniform Commercial Code in at least the following respects:

(1) An EFS must be signed by both the secured party and the "debtor." 7 U.S.C. § 1631(c)(4)(B), (C) (Supp. IV 1986). A Code financing statement must be signed by "the debtor" but not by the secured party, as a general rule. U.C.C. § 9-402(1) (1978). In some circumstances it can be signed by the secured party instead of the debtor. *Id.* § 9-402(2).

(2) An EFS must contain not only the "name and address of the person indebted to the secured party" but also the social security number or taxpayer ID number of the "debtor." 7 U.S.C. § 1631(c)(4)(D)(ii), (iii) (Supp. IV 1986). The U.C.C. requires only the name and mailing address of the debtor in a financing statement. U.C.C. § 9-402(1) (1978).

(3) An EFS must contain "a description of the farm products subject to the security interest." 7 U.S.C. § 1631(c)(4)(D)(iv) (Supp. IV 1986). This means a description adequate to identify the particular goods subject to the security interest. *See supra* text accompanying notes 240-49. A U.C.C. financing statement may describe the collateral specifically, but it is enough for it to indicate "the types . . . of collateral." U.C.C. § 9-402(1) (1978).

(4) An EFS "must be amended . . . within 3 months . . . to reflect material changes." 7 U.S.C. § 1631(c)(4)(E) (Supp. IV 1986); *see supra* text at notes 256-64. The U.C.C. permits amendment of a filed financing statement "by filing a writing signed by both the debtor and the secured party" but does not require amendment within any particular time after changes occur, and apparently the only penalty for failure to file such an amendment is that a security interest in collateral not described in the original filing is not perfected by filing until an amendment containing such a description is filed. U.C.C. § 9-402(4) (1978). *See also* Note, *Clear Title*, *supra* note 100, at 82.

273. The place of filing for farm products under the Arkansas U.C.C. is a county office, or perhaps more than one county office (*see supra* text accompanying notes 50-52), whereas filing of an EFS under the Food Security Act must be with the "Secretary of State" of the state in which the farm products have been or are to be produced. 7 U.S.C. § 1631(c)(4)(B), (e)(2), (3) (Supp. IV 1986).

274. *See Meyer, Congress's Amendment*, *supra* note 153, at 7; Note, *Section 1324 of the Food Security Act*, *supra* note 74, at 471.

275. *See supra* text at notes 42-44.

subsection suggests that the security interest must be "perfected" under Article 9 to be effective against the buyer.²⁷⁶ The subsection refers to "[a] buyer," and since the preceding subsection speaks of "a buyer who in the ordinary course of business buys," subsection (e) presumably means "any buyer." Furthermore, the subsection subordinates a buyer to "a security interest created by his seller," without express limitation to perfected security interests, and there is no reason to believe that the omission was inadvertent, since the immediately preceding subsection shows awareness of the concept of perfection. Where "farm products" collateral is concerned, then, it appears that by operation of subsection (e) of the Federal Act, the holder of an unperfected security interest will sometimes be able to enforce that interest against a buyer who was entirely unaware of the security interest when he took possession of and paid for the goods.

There is also a question regarding the effect of the Federal Act on section 9-306(2) of the U.C.C. The earlier discussion of this Code section²⁷⁷ brought out that the Code rule operates to divest a security interest in collateral when the debtor sells or otherwise disposes of the collateral, if the disposition has been "authorized by the secured party in the security agreement or otherwise." The question of when a disposition of collateral has been so "authorized" has provoked a good deal of litigation, particularly with regard to farm products collateral. Does the Federal Act change the operation of this rule?

To some extent, it appears that it does. As previously suggested,²⁷⁸ the provisions of paragraph (e)(1) of the "clear title" section of the Food Security Act—those dealing with the direct notification device for protection of a security interest—seem to nullify prohibitions of sale of the collateral which may appear in a security agreement, as well as some conditions imposed on the debtor's freedom of sale by the secured party, when the secured party elects to employ the direct notification method of protecting his security interests. The only conditions which can remain effective against a buyer in ordinary course of business to whom such notification is given, it seems, are conditions regarding payment which can be complied with by the buyer.²⁷⁹ The Federal Act thus overrides, to a substantial degree, the

276. 7 U.S.C. § 1631(e) (Supp. IV 1986).

277. See *supra* text accompanying notes 13-39.

278. See *supra* text accompanying notes 157-62.

279. The statement probably needs qualification in a case where the secured party has not only given direct notification but also made a proper central filing and the buyer has either failed to register with the central filing officer or has received notice of the filing from the central filing officer after registering. By operation of paragraphs (2) and (3) of subsection (e)

affirmative rule of U.C.C. section 9-306(2) that a security interest "continues in collateral notwithstanding sale . . . thereof by the debtor," when the sale has *not* been "authorized."

Does the Act go further and nullify, wholly or partially, the implication of U.C.C. section 9-306(2) that if the buyer's disposition of the collateral *was* "authorized in the security agreement or otherwise," the security interest is divested by the disposition? One commentator on the "clear title" section of the Food Security Act has argued that it does, or at least that it causes a security interest in farm products to continue in the collateral and makes the interest enforceable against a buyer of the collateral despite an authorization for the debtor's sale which is found in an "implied waiver" arising from the secured party's dealings with the debtor.²⁸⁰ The basis for this conclusion is the declaration of subsection (e) of the Federal Act that, "[a] buyer of farm products takes subject to a security interest created by the seller if" the direct notification or indirect notification rules of the subsection have been satisfied, without providing that this rule applies only to "unauthorized" sales.²⁸¹ While the wording of subsection (e), standing alone, may suggest such a reading, it is hard to accept when the "clear title" section is read as a whole and in the light of its history. The section itself shows that Congress was concerned about the plight of a buyer who buys without knowledge "that the sale of the products violates the lender's security interest in the products."²⁸² Legislative history indicates that Congress meant to displace Code rules only to the extent necessary to give some protection to such a

of the "clear title" section, the buyer would probably take the goods "subject to a security interest created by his seller" in any case where the sale was unauthorized unless he negotiated a release of the security interest from the secured party, since paragraphs (2) and (3) do not require that the financing statement or any notice given to the buyer by the central filing officer inform him of conditions with which he must comply in order to obtain the goods free of the security interest. See discussion of this difference between direct and indirect notifications in the text *supra* following note 206.

280. See Sanford, *supra* note 138, at 9-10.

281. *Id.* The argument is that the direct notification provisions of paragraph (e)(1) state the exclusive method by which a buyer can be freed from a security interest of which he has been given direct notification (namely, by complying with the payment obligations set forth in the notice), and that, although the parts of subsection (e) dealing with central filing systems are more ambiguous, they can be read as meaning that the only way a buyer who has received indirect notification of a security interest can take free of the interest is by obtaining an explicit waiver or release of the security interest from the secured party. Furthermore, Mr. Sanford argues, "Unless the conflicting results under Section 9-306(2) are preempted, the [Food Security Act] will not have accomplished its presumed goal in creating order, certainty, and simplicity in this area of the law." *Id.* at 10.

282. 7 U.S.C. § 1631(a) (Supp. IV 1986).

buyer.²⁸³ The sounder interpretation of subsection (e) thus seems to be that the subsection makes a buyer "subject to" a security interest only where there would *be* a continuing security interest under U.C.C. rules, and therefore that neither the divesting effect of section 9-306(2) nor the courts' determinations of what constitutes an authorization of sale under that subsection are overridden by the Federal Act.²⁸⁴

6. *Protection of Commission Merchants and Selling Agents*

The foregoing analysis of the "clear title" section of the Food Security Act has centered on its operation in favor of or against *buyers* of encumbered farm products, because the primary focus of this article is on the effect of the Federal Act on Arkansas' Uniform Commercial Code. Neither the Official Text of the U.C.C. nor the Arkansas U.C.C., as it read prior to 1986, had anything to say about the potential liability of persons who act as agents for owners of goods in conducting sales which violate the rights of secured parties. A number of cases decided prior to the advent of the Food Security Act have involved suits brought against such agents to hold them liable for the value of the goods or the value of the proceeds of the sales on a theory of conversion; such suits have succeeded at times.²⁸⁵ A person acting as agent for the owner of the goods for the purpose of sale, no matter how innocently he may act, is not a "buyer" of the goods and hence cannot be a "buyer in the ordinary course of business," nor does any other Article 9 rule explicitly protect such an agent. To hold intermediaries of this sort liable to the secured party for their participation in unauthorized sales of collateral, even when they have acted in good faith and without reason to know of the impropriety of the sales, may seem particularly unjust.²⁸⁶ A few states had legislation protecting these intermediaries, or some of them, prior to the enact-

283. See *supra* note 269.

284. Mr. Sanford also raises the question whether the "clear title" section of the Food Security Act changes the operation of U.C.C. § 9-318(3), which permits an assignee of an account or other payment right to notify the obligor that direct payment is to be made to the assignee and requires the obligor to comply with such notification. He concludes that § 9-318 is unaffected because the Federal Act deals only with security interests in goods, not with such interests in payment obligations resulting from their sale. See Sanford, *supra* note 138, at 10-11. That reading appears correct.

285. See *supra* note 40. See also Meyer, *The 9-307(1) Farm Products Puzzle: Its Parts and Its Future*, 60 N.D.L. REV. 401, 426 (1984).

286. See Uchtmann, Bauer & Dudek, *The UCC Farm Products Exception—A Time to Change*, 69 MINN. L. REV. 1315, 1331-32 (1985).

ment of the Food Security Act.²⁸⁷

The extension of the "clear title" section of the Food Security Act to protect "commission merchants" and "selling agents" from liability to holders of security interests in farm products they sell for farmers (if those interests were created by the sellers)²⁸⁸ is thus understandable, even though such agents are not mentioned in the congressional findings explaining the reasons for the enactment of the section.²⁸⁹ The rules applicable to commission merchants and selling agents, defining the circumstances in which they will or will not be "subject to" a security interest in farm products, almost exactly duplicate those applicable to buyers and present the same problems of interpretation and application,²⁹⁰ with one additional element of ambiguity. To merit protection against a security interest under the rule of paragraph (g)(1), the agent must be one who "sells, *in the ordi-*

287. See *id.* at 1330-31 (citing Georgia and Nebraska as having done so by amendments to their U.C.C.s and Louisiana in its own law dealing with security interests in livestock).

288. 7 U.S.C. § 1631(g) (Supp. IV 1986).

289. *Id.* § 1631(a).

290. The general rule protecting commission merchants and selling agents, as well as the exceptions to it, all appear in a single subsection of the "clear title" section of the Food Security Act, subsection (g). See *id.* § 1631(g) (Supp. IV 1986).

The first paragraph of subsection (g) is in substance much the same as subsection (d), which is the general rule protecting buyers who in ordinary course of business buy farm products from persons engaged in farming operations. Under subsection (d) such a buyer "shall take free of a security interest created by the seller, even though the security interest is perfected; and the buyer knows of the existence of such interest." *Id.* § 1631(d). Under paragraph (1) of subsection (g) the general rule is that

a commission merchant or selling agent who sells, in the ordinary course of business, a farm product for others, shall not be subject to a security interest created by the seller in such farm product even though the security interest is perfected and even though the commission merchant or selling agent knows of the existence of such interest.

Id. § 1631(g)(1).

Paragraph (2) of subsection (g) is the counterpart, with respect to commission merchants and selling agents, of subsection (e), applicable to buyers. Paragraph (2) sets forth the exceptions to the rule of paragraph (g)(1), just as subsection (e) provides exceptions to the general rule of subsection (d). Whereas subsection (e) begins, "A buyer of farm products takes subject to a security interest created by the seller if . . .", paragraph (g)(2) begins, "A commission merchant or selling agent who sells a farm product for others shall be subject to a security interest created by the seller in such product if . . ." *Id.* § 1631(e) & (g)(2). What follows in paragraph (g)(2) tracks what follows the introductory language of subsection (e) virtually word for word, except that the phrase "commission merchant or selling agent" is substituted for "buyer" wherever "buyer" appears in subsection (e). Thus, for example, paragraph (2)(A)(v) of subsection (g) requires that a direct notification of a security interest given by a secured party or seller to a *commission merchant or selling agent* show "any payment obligations imposed on the *commission merchant or selling agent* as conditions for waiver or release of the security interest." *Id.* § 1631(g)(2)(A)(v) (emphasis added). Further, paragraph (2)(B) requires that the *commission merchant or selling agent* have performed the payment obligations in order to avoid being subject to the security interest. *Id.* § 1631(g)(2)(B). In subsection

nary course of business, a farm product for others."²⁹¹ Does this imply, not merely regularity of the form and circumstances of the transaction, but also that the agent must have been acting in good faith and without knowledge that the sale violates the rights of the secured party? There is less basis in the language of the Act or its history for determining the intended meaning of the phrase "ordinary course of business," as applied to the conduct of agents for purposes of sale, than there is for reading the Act as requiring that a buyer, to qualify as a "buyer in the ordinary course of business" be acting in good faith.²⁹² But if, as has been argued,²⁹³ such a requirement is implied by the latter definition, it seems probable that Congress meant a similar requirement to apply to commission merchants and selling agents.

Another potential problem affecting commission merchants and selling agents is raised by the Federal Act's provision that "[w]hat constitutes receipt, as used in this section, shall be determined by the law of the State in which the buyer resides."²⁹⁴ That this rule is intended to apply to notifications sent directly or indirectly to commission merchants and selling agents is apparent from its inclusion in the subsection dealing with such agents.²⁹⁵ The commission merchant or selling agent for whom a notification is intended may reside and do business in a state other than the state in which the buyer of the goods resides (in fact, there may be no identifiable buyer at the time the notification is sent). Yet the question of whether the agent has "received" the notification is governed by the law of the state where whoever turns out to be the buyer resides, or so the Act seems plainly to mean.²⁹⁶ An Agriculture Department interpretive opinion takes this bull by the horns, by declaring that "buyer," in this context, means "intended recipient of the notice."²⁹⁷ The courts may not agree with this reading.²⁹⁸

(e) exactly the same wording appears, except that "buyer" appears in place of the italicized words above.

Paragraph (3) of subsection (g) duplicates the rule of subsection (f), declaring, "What constitutes receipt, as used in this section, shall be determined by the law of the State in which the buyer resides." *Id.* § 1631(g)(3).

291. *Id.* § 1631(g)(1) (emphasis added).

292. Compare discussion *supra* text accompanying notes 151-54.

293. *Id.*

294. 7 U.S.C. § 1631(g)(3) (Supp. IV 1986).

295. An identical rule appears in subsection (f), which immediately follows the subsection dealing with when buyers take subject to security interests. See *id.* § 1631(f).

296. See Sanford, *supra* note 138, at 22.

297. 9 C.F.R. § 205.210(c) (1987).

298. See Sanford, *supra* note 138, at 22.

III. THE ARKANSAS LEGISLATION

A. *Summary of the Legislation*

The Federal Act invites the states to enact their own laws setting up "central filing systems." The Arkansas General Assembly accepted this invitation in 1986. Act 16 of the Second Extraordinary Session of that year²⁹⁹ amended sections 9-307³⁰⁰ and 9-407³⁰¹ of Arkansas' Uniform Commercial Code, with the declared intent of complying with the "clear title" section of the Food Security Act of 1985.³⁰² These Arkansas amendments became effective December 1, 1986.³⁰³

Section 1 of Act 16 amended section 9-307 of the U.C.C. by adding three subsections. The new subsection (4) provides:

A secured party may enforce a security interest in farm products against a buyer who, in the ordinary course of business, purchases farm products from, or a commission merchant or selling agent who, in the ordinary course of business, sells farm products for, a person engaged in farming operations only where the secured party has signed and filed with the Secretary of State a form containing [specified information].³⁰⁴

The form must contain essentially the same information that is required by the Food Security Act to appear in an "effective financing statement,"³⁰⁵ and which is signed by the "debtor" as is also required by the Federal Act.³⁰⁶

The new subsection (5) of section 9-307³⁰⁷ defines the terms "commission merchant" and "selling agent" identically with the Federal Act.³⁰⁸ The new subsection (6) of section 9-307,³⁰⁹ requiring amendment of a filing in the event that "a material change occurs," is

299. Act of May 19, 1986, No. 16 (2d. Ext. Sess.) (codified at ARK. CODE ANN. §§ 4-9-307, -407 (1987) (amended 1987)).

300. ARK. STAT. ANN. § 85-9-307 (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307 (1987 & Supp. 1987)).

301. *Id.* § 85-9-407 (current version at ARK. CODE ANN. § 4-9-407 (1987)).

302. Act of May 19, 1986, No. 16 (2d Ext. Sess.) (short title).

303. *Id.* § 5 (effective date).

304. ARK. STAT. ANN. § 85-9-307(4) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307(4) (1987 & Supp. 1987)).

305. 7 U.S.C. § 1631(c)(4) (Supp. IV 1986). *See also supra* text accompanying notes 118-25.

306. 7 U.S.C. § 1631(c)(4)(C) (Supp. IV 1986).

307. ARK. STAT. ANN. § 85-9-307(5) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307(5) (1987 & Supp. 1987)).

308. 7 U.S.C. § 1631(c)(3), (8) (Supp. IV 1986); *see supra* note 94.

309. ARK. STAT. ANN. § 85-9-307(6) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307(6) (1987 & Supp. 1987)).

in substantial accord with the Food Security Act³¹⁰ but adds that "[t]he effectiveness and continuation of the form is to be treated as if it were a financing statement."

The second section of Act 16 amended section 9-407 of Arkansas' U.C.C. by adding five new subsections, all dealing with the duties of the Secretary of State in the administration of the central filing system. Subsection (3) of amended section 9-407³¹¹ calls for recordation of the date and time of filing of each financing statement covering farm products and compilation of a "master list" of the filings (substantially in accord with the requirements of the Food Security Act³¹²). The new subsection (4) of section 9-407³¹³ mandates maintenance of a list of buyers, commission merchants and selling agents who have registered to indicate interest in receiving the master lists or portions thereof (as is required by the Federal Act³¹⁴). New subsection (5) of section 9-407³¹⁵ requires distribution "on a regular basis as determined by the Secretary" of copies of the master list or portions of it to registered buyers, commission merchants and selling agents who have requested such distributions (as is required by the Federal Act³¹⁶). New subsection (6) of section 9-407 calls for the Secretary of State, "[u]pon the request of any person [to] provide to such person, within 24 hours, an oral confirmation followed by a written confirmation of the filing of any effective financing statement filed [under section 9-307(4)] and relating to the debtor or seller upon whom such information has been requested."³¹⁷ This is similar to the language of the Federal Act, though the Federal Act requires such a "confirmation" to be given only "to those not registered" as wanting to receive copies of the master list.³¹⁸ The new subsection (7) of section 9-407³¹⁹ prescribes fees to be charged for the several services to be rendered by the Secretary of State.

310. 7 U.S.C. § 1631(c)(4)(E) (Supp. IV 1986).

311. ARK. STAT. ANN. § 85-9-407(3) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-407(3) (1987 & Supp. 1987)).

312. 7 U.S.C. § 1631(c)(2)(B)-(C) (Supp. IV 1986).

313. ARK. STAT. ANN. § 85-9-407(4) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-407(4) (1987 & Supp. 1987)).

314. 7 U.S.C. § 1631(c)(2)(D) (Supp. IV 1986).

315. ARK. STAT. ANN. § 85-9-407(5) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-407(5) (1987 & Supp. 1987)).

316. 7 U.S.C. § 1631(c)(2)(E) (Supp. IV 1986).

317. ARK. STAT. ANN. § 85-9-407(6) (Interim Supp. 1986), (current version at ARK. CODE ANN. § 4-9-407(6) (1987 & Supp. 1987)).

318. 7 U.S.C. § 1631(c)(2)(F) (Supp. IV 1986).

319. ARK. STAT. ANN. § 85-9-407(7) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-407(7) (Supp. 1987)).

A 1987 Arkansas act supplemented and modified Act 16 of 1986. It created positions for additional personnel in the office of the Secretary of State to administer the central indexing and reporting system,³²⁰ appropriated funds for the operation of the system,³²¹ regulated disposition of funds collected in the course of the operation of the system,³²² set up reporting requirements regarding expenditures,³²³ and increased the allowable fees to be charged for services rendered.³²⁴ The 1987 Act also provided, "Livestock buyers and livestock sale barns are hereby exempted from the provisions of Act 16 of the Second Extraordinary Session of the Seventy-Fifth General Assembly."³²⁵

The Arkansas central filing system was certified by the Department of Agriculture as being in compliance with section 1324 of the Food Security Act "for all farm products produced in [Arkansas]" on December 22, 1986.³²⁶ The certification was amended to exclude most livestock on February 23, 1987.³²⁷

B. Analysis of the Arkansas Legislation

For one accustomed to the straight-forward style of Article 9 of the U.C.C., the new Arkansas version of section 9-307 sets subtle traps. Unless the Code language is read with care, and in tandem with another statute to which it makes no reference, a reader is likely to come away with a most erroneous impression of the law dealing with the relation between a holder of a perfected security interest in farm products and a buyer of those products from the farmer-debtor who makes an unauthorized sale of the collateral.

The reader is likely to notice, first, that the wording of subsection (1) of section 9-307 has not been altered. It lays down, as it always has, a general rule that a buyer in ordinary course of business takes

320. Act of Mar. 3, 1987, No. 108, §§ 1, 2, 1987 Ark. Acts 267 (Adv. Leg. Ser.) (codified at ARK. CODE ANN. § 4-9-307, -407 (Supp. 1987)).

321. *Id.* §§ 3, 4, 9, 10, 1987 Ark. Acts 268-70 (Adv. Leg. Ser.).

322. *Id.* §§ 7, 8, 9, 1987 Ark. Acts 269-70 (Adv. Leg. Ser.) (codified in part at ARK. CODE ANN. § 4-9-407(7) (Supp. 1987)).

323. *Id.* § 5, 1987 Ark. Acts 269 (Adv. Leg. Ser.).

324. *Id.* §§ 7, 11; ARK. CODE ANN. § 4-9-407(2), (7) (Supp. 1987).

325. Act of Mar. 3, 1987, No. 108, § 6, 1987 Ark. Acts 269 (Adv. Leg. Ser.). This provision is codified in ARK. CODE ANN. § 4-9-307(7) (Supp. 1987) as: "Livestock buyers and livestock sale barns are exempted from the provisions of subsections (4)-(6) of this section."

326. 51 Fed. Reg. 46,887 (1986).

327. 52 Fed. Reg. 6,040 (1987) (giving notice of amended approval "to cover all farm products produced in the State of Arkansas except: Cattle & Calves, Goats, Horses, Hogs, Mules, Sheep & Lambs").

free of any security interest created by his seller, but it excepts from the operation of that rule, as it always has, "a person buying farm products from a person engaged in farming operations."³²⁸ Knowing that the Code in the past has contained no other provision that would render the secured party vulnerable to the buyer's claim to the goods, the reader is likely to conclude that the security interest is enforceable against the buyer even if he is a buyer in ordinary course of business.

That assumption would be incorrect, and perhaps unforgivable, because simply by reading on in the same section the reader would discover that the Code *now does* contain another provision impairing the security. The new subsection (4) of section 9-307 provides, "[a] secured party may enforce a security interest in farm products against a buyer who, in the ordinary course of business, purchases farm products from . . . a person engaged in farming operations *only* where the secured party has signed and filed with the Secretary of State a form" containing specified information and signatures.³²⁹ This rule sets up conditions for enforceability of the security interest against the buyer which are different from the steps required by the Code for "perfection" of the security interest, since the filed form must contain information and a signature not required in a "financing statement" by section 9-402,³³⁰ and the filing must be with the Secretary of State, rather than locally, as section 9-401 requires for a Code "financing statement."³³¹

Having found this new rule, our reader is likely to deduce that if the secured party has made a central filing of the sort required by section 9-307(4) before the sale, he may enforce his security interest against the buyer. Isn't that the natural reading of the subsection? It may be, but the conclusion is wrong. It is wrong because the federal Food Security Act of 1985 provides that "notwithstanding any other provision of . . . State . . . law, a buyer who in ordinary course of business buys a farm product from a seller engaged in farming operations *shall take free* of a security interest created by the seller," *except as otherwise provided in the next subsection*;³³² and under the next subsection a central filing suffices to give the secured party enforceable rights against the buyer only if the buyer has failed to register with the

328. ARK. STAT. ANN. § 85-9-307(1) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307(1) (1987 & Supp. 1987)).

329. ARK. CODE ANN. § 4-9-307(4) (Supp. 1987) (emphasis added).

330. *Id.* § 4-9-402 (1987). See also *supra* note 272.

331. ARK. CODE ANN. § 4-9-401 (1987).

332. 7 U.S.C. § 1631(d) (Supp. IV 1986) (emphasis added).

Secretary of State prior to the purchase.³³³ If the buyer has registered, the security interest is not enforceable against him unless the buyer has received direct or indirect notification of the security interest.³³⁴ The Arkansas U.C.C. makes no reference to this Federal Act; the reader must know of it to avoid a misunderstanding of the law.

Assuming that our reader avoids that trap, he is likely to reason that, at the very least, subsection (4) of section 9-307 of the Code teaches that the secured party cannot preserve his rights against a buyer in ordinary course without filing with the Secretary of State. Right? Wrong! True, that subsection of the Code says that such a filing is the "only" way the secured party may preserve his rights,³³⁵ but the "clear title" section of the Food Security Act says otherwise. It makes the buyer "subject to a security interest created by the seller if . . . within 1 year before the sale . . . the buyer has received from the secured party or the seller written notice of the security interest" in proper form.³³⁶ This rule operates whether or not the state in which the farm products were produced has established a central filing system, and whether or not the secured party has made a central filing.³³⁷

333. *Id.* § 1631(e)(2).

334. *Id.* § 1631(e)(3). Although subsections (5) and (6) of § 9-407 of the Arkansas U.C.C., as amended in 1986, require the Secretary of State to supply information about filings with respect to farm products to registered buyers, commission merchants and selling agents and to persons who request information about filings as to particular debtors or sellers, neither that section nor § 9-307 conditions enforceability of the security interest on such information having been received by the person against whom enforcement is sought. *See* ARK. STAT. ANN. §§ 85-9-307, -407(5), -407(6) (Interim Supp. 1986) (current version at ARK. CODE ANN. §§ 4-9-307, -407(5), -407(6) (1987 & Supp. 1987)).

335. ARK. STAT. ANN. § 85-9-307(4) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307(4) (1987 & Supp. 1987)).

336. 7 U.S.C. § 1631(e)(1) (Supp. IV 1986).

337. The new subsection (4) which was added to § 9-307 of the Arkansas U.C.C. by Act 16 of 1986 may have been drafted on the assumption that the "clear title" section of the Food Security Act gave the State the right to "opt out" of the direct notification provisions of the Federal Act by adopting the indirect notification machinery (*i.e.*, by setting up a "central filing system" complying with the Federal Act), in its place. Indeed, some early commentators on the Federal Act so read it. *See, e.g., Meyer, Agricultural Credit, supra* note 150, at 491; Richards, *supra* note 17, at 417; Note, *Federal Legislation Provides Protection, supra* note 74, at 766. That reading, however, is not consistent with the text of the Act, which provides:

A buyer of farm products takes subject to a security interest created by the seller if—
 (1) . . . within 1 year before the sale . . . , the buyer has received from the secured party or the seller written notice of the security interest . . . , or (2) in the case of a farm product produced in a State that has established a central filing system . . . the buyer has failed to register . . . and the secured party has filed an effective financing statement . . . ; or (3) in the case of a farm product produced in a State that has established a central filing system, the buyer . . . receives from the Secretary of State of such State written notice [of a filed financing statement covering the farm products].

The federal law thus flatly contradicts section 9-307(4) of the Arkansas U.C.C. and overrides the contrary state law.³³⁸

Another layer of deception lurks in the fact that Arkansas' Act 108 of 1987 exempts "livestock buyers and livestock sale barns" from the operation of Act 16 of 1986.³³⁹ This type of exemption is presumably permissible under the Food Security Act without invalidating the entire central filing system. The Department of Agriculture has issued an interpretive opinion that declares:

A State may establish a system for specified products and not for all. A State establishing a system for specified products and not for all will be deemed to be "a State that has established a central filing system" as to the specified products, and will be deemed not to be such a State as to other products.³⁴⁰

But where does this take us when the collateral is livestock? Subsection (4) of section 9-307 is inapplicable, since it was added to the Arkansas U.C.C. by Act 16 of 1986.³⁴¹ The "central filing system" rules of the Federal Act³⁴² are irrelevant, since there is no Arkansas "central filing system" applicable to security interests in livestock.³⁴³ The relevant rule that remains in the Arkansas U.C.C. is section 9-

7 U.S.C. § 1631(e) (Supp. IV 1986) (emphasis added). The three paragraphs of the subsection are stated as complete alternatives, and there is no language in the Act suggesting that by electing to establish a central filing system, the state in which the farm products are produced nullifies the direct notification provisions of paragraph (1). See Clark, *supra* note 157, at 1336-39 (treating the direct notification provisions as applicable whether or not the state in which the farm products are produced has a central filing system). See also Sanford, *supra* note 138, at 26 (asserting that a state law which prohibited direct notification when the state implemented a central filing system would be void but suggesting, without further explanation, that a state "might . . . validly restrict direct notice once a security interest is listed in a master list").

It is apparently true that a Senate amendment to the House bill which ultimately became the Food Security Act of 1985 would have given the states such an option, but the Conference Committee adopted the wording that appears in the enacted statute, without describing it as an adoption of the Senate's amendment. See H.R. CONF. REP. NO. 447, 99th Cong., 1st Sess. 485-86, 490-91 (1981).

338. See Meyer, *Congress's Amendment, supra* note 153, at 8.

339. See ARK. CODE ANN. § 4-9-307(7) (Supp. 1987).

340. 9 C.F.R. § 205.206(c) (1987).

341. The exclusion has been codified in the Arkansas Code of 1987 as subsection (7) of § 9-307, providing: "Livestock buyers and livestock sale barns are exempted from the provisions of subsections (4)-(6) of this section." ARK. CODE ANN. § 4-9-307(7) (Supp. 1987).

342. 7 U.S.C. § 1631(e)(2) and (3) (Supp. IV 1986).

343. A "central filing system," under the Federal Act, is a system certified by the Secretary of Agriculture as complying with the Act's requirements for such a system. *Id.* § 1631(c)(2). The latest certification relating to the Arkansas central filing system excepts from the approval coverage of cattle, calves, goats, horses, mules, hogs, sheep and lambs. See *supra* note 327 and accompanying text.

307(1),³⁴⁴ which operates to preserve the enforceability of the security interest against the buyer, since livestock still qualifies as a "farm product" under the Arkansas Code as long as it remains in the hands of a farmer.³⁴⁵ *But*, the federal Food Security Act reverses that rule by providing that "notwithstanding any other provision of . . . State . . . law, a buyer who in ordinary course of business buys a farm product from a seller engaged in farming operations *shall take free* of a security interest created by the seller"³⁴⁶ The only exception allowed by the Federal Act is the direct notification device.³⁴⁷ Thus, many, if not most, sales of Arkansas livestock to buyers in ordinary course of business will be sales free of the security interests created by the sellers. The Arkansas Code says just the opposite.

All of this discussion assumes that the phrase "buyer in the ordinary course of business" has the same meaning in both the Arkansas U.C.C. and the "clear title" section of the Food Security Act.³⁴⁸ If that is not so, the language of the Arkansas U.C.C. becomes even more misleading.

The 1986 amendments to the Arkansas U.C.C. provide some protection for "commission merchants" and "selling agents," as well as for buyers, since the new subsection (4) of section 9-307³⁴⁹ expressly includes them in its rule. However, the section is just as misleading as to the law that really governs where commission merchants and selling agents are concerned as it is with regard to that applicable to buyers. It should be noted also that the 1987 Act excluding "livestock buyers" from the provisions of the 1986 Act also excludes "livestock sale barns."³⁵⁰ That term is undefined, but it probably operates to place sales agents conducting sales of livestock in "sale barns" in the same nearly invulnerable position as "livestock buyers."³⁵¹

344. ARK. STAT. ANN. § 85-9-307(1) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307(1) (1987 & Supp. 1987)).

345. Neither the 1986 Act amending the U.C.C. (*see supra* text accompanying notes 299-319) nor the 1987 Act (*see supra* text accompanying notes 320-25) changes the definition of "farm products" that appears in ARK. STAT. ANN. § 85-9-109(3) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-109(3) (1987)). For that definition, *see* note 59 *supra*.

346. 7 U.S.C. § 1631(d) (Supp. IV 1986) (emphasis added).

347. *Id.* § 1631(e)(1).

348. *See supra* text accompanying notes 145-56.

349. *See* ARK. STAT. ANN. § 85-9-307(4) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307(4) (1987 & Supp. 1987)).

350. *See* ARK. CODE ANN. § 4-9-307(7) (Supp. 1987).

351. *See supra* text accompanying notes 339-47. The term "livestock" is undefined as well, and, as interpreted by the Arkansas Secretary of State, is apparently construed as not including all farm animals. *See* 52 Fed. Reg. 6,040 (1987) (indicating that the Secretary of State requested that Arkansas' central filing system be certified as covering all farm products except

The 1986 amendment of Arkansas' U.C.C. appears to change the operation of the Code in one area which is not touched by the Federal Act. The definition of "farm products" in the "clear title" section of the Food Security Act³⁵² does not include "supplies used or produced in farming operations," but the definition of "farm products" in the Arkansas U.C.C. does.³⁵³ Since the 1986 and 1987 Arkansas legislation did not amend the "farm products" definition of the Arkansas U.C.C., the term "farm products," as used in the new subsection (4) of section 9-307, presumably includes supplies used or produced in farming operations. That subsection declares,

A secured party may enforce a security interest in farm products against a buyer who, in the ordinary course of business, purchases farm products from, or a commission merchant or selling agent who, in the ordinary course of business, sells farm products for, a person engaged in farming operations *only* where the secured party has signed and filed with the Secretary of State a form containing [specified information].³⁵⁴

That rule, it seems, can be taken literally if the collateral is "supplies used or produced in farming operations" which are in the hands of a farmer. Thus, as to such collateral, a secured party, even if he "perfects" his security interest in those products by the local filing which Article 9 of the Code calls for, cannot be assured of being able to enforce his security interest against buyers or against agents who sell such collateral for the debtor but must file with the central filing officer for farm products. This is true despite the fact that the substantive provisions of the Federal Act are irrelevant to the security interest. However, if a central filing is made, that appears to be sufficient in itself to make the security interest enforceable against such

cattle and calves, goats, horses, mules, hogs, sheep and lambs). Fish raised on a fish farm, poultry and (perhaps) pigs are examples of animals that could be "farm products" but are within the scope of Arkansas' central filing system, as the Secretary of State and the Department of Agriculture envision it. It will be a question for the Arkansas courts whether the "livestock" exception of the 1987 Act is of such narrow scope. If not, another nice question of statutory interpretation arises: are the types of livestock which are not excepted from the scope of the Arkansas central filing system by the terms of the federal certification subject to the substantive rules of the "clear title" section of the Food Security Act, insofar as those rules relate to the operation of a central filing system, or are they outside the scope of those rules because the "State" has not "established" a central filing system for such products?

352. 7 U.S.C. § 1631(c)(5) (Supp. IV 1986). See *supra* text accompanying notes 142-44.

353. See ARK. STAT. ANN. § 85-9-109(3) (Supp. 1985) (current version at ARK. CODE ANN. § 4-9-109(3) (1987)).

354. *Id.* § 85-9-307(4) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307(4) (1987 & Supp. 1987)).

buyers and agents,³⁵⁵ whether or not the security interest has been "perfected" under Article 9.³⁵⁶ It seems unlikely that the Arkansas legislature had any actual intention to create such an anomalous rule, but it would take some highly creative judicial "construction" of the statute to avoid the conclusion that the amended version of section 9-307 calls for such a result.³⁵⁷

IV. CONCLUSION

If a camel is "a horse planned by a committee"³⁵⁸ the mind boggles at what two committees could accomplish. The combined efforts of the United States Congress and the Arkansas General Assembly to provide "clear title" for farm products may provide an analogy. Even

355. The Arkansas U.C.C., as amended, includes no rules conditioning the secured party's rights against buyers, commission merchants or selling agents on their having received notice of the filing of a statement in accordance with subsection (4) of § 9-307. See *supra* note 334.

356. Section 9-307(4) of the Arkansas U.C.C. is not, in express terms, limited in its application to holders of perfected security interests. See ARK. STAT. ANN. § 85-9-307(4) (Interim Supp. 1986) (current version at ARK. CODE ANN. § 4-9-307(4) (1987 & Supp. 1987)).

357. One commentator on the "clear title" section of the Food Security Act has suggested that the Federal Act overrides some state laws other than the states' Uniform Commercial Codes. As an example, he has pointed out that in Arkansas and some other states a landlord's lien on a tenant's crops for unpaid rent can be enforced against purchasers of the crops, but the writer asserts that "Congress reversed this rule as well when it provided in section 1324(d): 'Except as provided in subsections (e) and notwithstanding any other provision of Federal or local law' Meyer, *Agriculture Credit*, *supra* note 150, at 502 (citing, *inter alia*, *Holmes v. Riceland Foods, Inc.*, 261 Ark. 27, 546 S.W.2d 414 (1977)). That is a possible reading of the Federal Act but certainly not clearly correct. The rule which is laid down as applicable "notwithstanding any other provision Federal, State or local law" is that a buyer in ordinary course of business of farm products from a farmer "shall take free of a security interest created by the seller . . ." 7 U.S.C. § 1631(d) (Supp. IV 1986) (emphasis added). The question is whether a landlord's lien for rent is a "security interest." The Federal Act defines the term as "an interest in farm products that secures payment or performance of an obligation." *Id.* § 1631(c)(7). Except for being limited to interests in farm products, this is the same language that is employed in the Uniform Commercial Code to define the term "security interest." U.C.C. § 1-201(37) (1978). But the Code goes on specifically to exclude landlords' liens from the scope of Article 9, U.C.C. § 9-104(b) (1978), and the scope of the Article is affirmatively defined as being limited to "security interests created by contract," and "statutory liens" are specifically excluded. U.C.C. § 9-102(2) (1978). In Arkansas the landlord's lien on crops grown on the leased premises is statutory. ARK. STAT. ANN. § 51-201 (1971) (current version at ARK. CODE ANN. § 18-41-107 (1987)). The problem of interpretation is whether the Federal Act definition of "security interest" is meant to adopt the U.C.C. meaning of the term in Article 9. Since the Federal Act does not say, there is room for treating the Federal Act as having a broader application than Article 9 of the Code, but since the legislative history clearly indicates that the Act's target was U.C.C. § 9-307(1), the sounder reading of the Federal Act definition of "security interest" is that it refers to an interest created by contract and does not include statutory liens such as Arkansas' landlord's lien. See *supra* text accompanying note 135.

358. A.K. ADAMS, *THE HOME BOOK OF HUMOROUS QUOTATIONS* 24 (1969), attributed to VOGUE MAG. (July 1958).

if one concedes that the Uniform Commercial Code, as it stood in most states (including Arkansas) before Congress stepped in, treated buyers of such products unfairly, and that a congressionally-imposed reform of the law was justified, the reform that materialized leaves much to be desired.³⁵⁹ Further, the attempt to adapt the Arkansas U.C.C. to this reform has added unnecessary confusion to that created by the Congress.

Clear gainers under the "clear title" section of the Food Security Act of 1985 are buyers of farm products.³⁶⁰ Buyers in ordinary course of business have gained a security of title which was previously denied them in most states, including Arkansas. It is not a complete security, but even the exceptions are more tolerable for buyers than was their position under prior law. They can now generally be assured of protection from security interests created by their sellers unless they have actually received notices of the security interests before they buy, as well as information that will enable them to locate the secured parties to obtain further information and negotiate lien-free purchases.

This protection comes at a price, however. In any case where the farm products involved have been produced in a state which has a federally-approved "central filing system," and it will be up to the buyer to find out whether that is so, the buyer will have to go to the trouble of registering with that state's central filing office and will have to pay for periodic distributions of copies of master lists of filed

359. One of the more vigorous published criticisms of the "clear title" section of the Food Security Act is that of Professor Charles W. Mooney, Jr., who was chairman of the Uniform Commercial Code Committee of the American Bar Association's Section on Corporation, Banking and Business Law in 1986. He wrote:

Although even the most pejorative hyperbole is inadequate to fully express what section 1324 deserves, the following is a frail attempt: Section 1324 is internally inconsistent, unintelligible, and unworkable. It was drafted and enacted without apparent knowledge or understanding of present and past systems of public notice and secured financing. It ignores the issues involved in multistate transactions. It does not draw upon, acknowledge, or include many matters that are adequately covered in the U.C.C. and in judicial decisions that treat such U.C.C. provisions. It is a disaster. No buyer or financier of farm products should tolerate such incompetence from its legal counsel, yet these disgraceful provisions have now been imposed upon agricultural commerce and finance. What is worse, in attempts to set up "central filing systems" under section 1324, some state legislatures may expand the harm by unnecessarily disrupting the existing U.C.C. article 9 filing systems and thereby interfering with secured transactions unrelated to farm products.

Mooney, *Introduction to the Uniform Commercial Code Annual Survey: Some Observations on the Past, Present, and Future of the U.C.C.*, 41 BUS. LAW. 1343, 1352 (1986).

360. *But see* Sanford, *supra* note 138, at 29 (arguing that "the Act does little for buyers, commission merchants, and selling agents who viewed the U.C.C. as an unfair collection device for bankers," because they had largely adapted to the U.C.C. "farm products" exception to § 9-307 before the enactment of the Food Security Act).

financing statements. Buyers will also have to adopt filing systems of their own, in order to keep track of master-list copies they receive, and will have to make their own searches of these lists before buying farm products.³⁶¹ Furthermore, buyers will have to file and examine any direct notifications of security interests which they receive from secured parties, and these may be voluminous.³⁶² These costs will undoubtedly affect willingness to buy farm products and have a tendency to hold down prices buyers are willing to pay for them, but this trade-inhibiting tendency may be considerably less than the effect of the prior law.

Commission merchants and selling agents are also gainers under the Federal Act,³⁶³ and the observations made in relation to buyers apply to them as well.

Clear losers are the financiers of agricultural operations. Their previous, nearly invulnerable, position *vis-à-vis* buyers of farm products collateral, when the sales have not been authorized, has been much eroded. The means left open to them for preserving the enforceability of their security interests have saddled them with costs and risks which are bound to affect their eagerness to make agricultural loans and to increase their charges for such credit.

Secured parties will have to continue to perfect their security interests under the Code, as they have been accustomed to doing. But they must now, in addition, employ the machinery of the Federal Act to preserve the effectiveness of their security interests against buyers of the collateral and agents for the debtors who participate in unauthorized sales. If they choose to employ the direct notification method, they will have to find out what persons are likely to buy the products and sell them for their debtors, and notices will have to be delivered to all of them. Even then, the secured parties must bear the risk of sales to undiscovered or unlikely buyers and sales by undiscovered or unlikely agents. Furthermore, the notices will have to be carefully drafted to comply with detailed but ambiguous statutory requirements, and secured parties, having given such notices, must remember the one-year time limit on their effectiveness and the need to deliver amendments in the event of "material changes."

A simpler procedure is to file an "effective financing statement" with the Secretary of State in the state where the farm products have been or are to be produced, but this alternative is not available if that

361. See Note, *Clear Title*, *supra* note 100, at 87; Fry, *supra* note 74, at 449.

362. See Meyer, *Agriculture Credit*, *supra* note 150, at 496; Fry, *supra* note 74, at 449.

363. But see *supra* note 360.

state does not have a federally-approved "central filing system," as is true in Arkansas where the collateral is "livestock." And, even if there is one (as in Arkansas with respect to other "farm products," as the Federal Act defines that term), the financing statement has to be carefully drafted to comply with statutory and regulatory requirements. Even after it is filed, the secured party is dependent upon the administrators of the central filing system to get accurate summaries of the contents of the financing statement into the hands of registered buyers, commission merchants and selling agents before they participate in sales of the collateral. Moreover, secured parties who have filed must remain alert to the possibility of "material changes" occurring which will require the filing of amendments to their filings.

The means for secured parties to protect their security interests under the Federal Act are so unreliable that secured parties will, as a practical matter, be compelled to select their farmer-borrowers with greater care and monitor their handling of farm-products collateral more closely than they have been accustomed to doing. That, in itself, may be quite desirable, but the need for such policing will also increase the cost of agricultural credit.

How do the farmers fare under this Federal Act? As sometime *buyers* of farm products they will share the advantages gained by other buyers, and conferral of such benefits was a part of the congressional motivation for enacting the law.³⁶⁴ As *sellers* of farm products, farmers gain no perceptible legal advantage. Any changes in the markets for their products, for good or ill, resulting from the Federal Act will affect all farmers, not merely those who cannot be trusted to play fair with their creditors. Whether farmers will now find it easier to market their products at more favorable prices and, if so, whether they will find that that benefit outweighs the probable increase in their costs of obtaining credit and the possible drying up of sources of credit remains to be seen.³⁶⁵

As to the Arkansas legislative reaction to the Food Security Act, the evident desire of the Arkansas legislature to give suppliers of agricultural credit the opportunity to take advantage of the grudging protections which Congress offered through the "central filing system" device cannot be faulted, though it is not clear why those who finance production of livestock deserve these protections less than others. However, the manner in which the adaptation to the new federal law was made seems almost designed to mislead those who are affected by

364. See *supra* note 136.

365. But see Note, *Federal Legislation Provides Protection*, *supra* note 74, at 773.

it. The new subsection (4) of section 9-307 of Arkansas' Uniform Commercial Code simply does not reflect the reality of the applicable law, and the exclusion of livestock sales from the central filing system mechanism has been handled in such a way as to hide, rather than reveal, the impact of the change. It would have been far better to set up a "central filing system" conforming to the requirements of the "clear title" section of the Food Security Act, plainly excluding livestock collateral from its scope and to amend the Arkansas U.C.C. only by adding cautions in sections 9-301 and 9-307 that the provisions of these sections are modified in their operation by that federal legislation.

The greatest gainers from this spate of federal and state legislation may be the members of the legal profession. Many new opportunities for employment in counseling and litigation have been opened to the practicing bar.