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The Uniform Commercial Code and the Farmer

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THE UNIFORM COMMERCIAL CODE AND THE FARMER

BY WILLIAM M. GOEBEL*

THE UNIFORM COMMERCIAL CODE, "An Act relating to certain commercial transactions and contracts and other documents concerning them,"¹ became effective in Illinois at midnight, July 1, 1962.

Many areas of commercial law embraced by the Code may seem remote from the ordinary commercial transactions of the farmer. However, the use of a letter of credit, for example, may furnish the financing for substantial shipments of agricultural commodities in foreign commerce, and this can be of great importance to Illinois farmers.²

Other areas of the Code will clearly have an effect upon certain of the day-to-day farming operations in much the same manner as any other business operation.

"The farmer, also, is continuously engaged in commerce, as a buyer and seller of goods and a borrower of money. Thus he, too, has an interest in the clarification and improvement of the law of sales, bank deposits and collections and security devices. Moreover, he will benefit particularly from provisions of the Code which liberalize and simplify security interests in farm equipment, feed, livestock and crops."³

Certain provisions of the Code are particularly applicable to farm transactions. This article will discuss those provisions of the Code.⁴

ARTICLE 2 — SALES

Article 2, Sales,⁵ has now superseded the Illinois Uniform Sales Act.⁶ Unless the context otherwise requires, article 2 applies to sales of "goods" as

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¹ ILL. REV. STAT. c. 26, § 1—101 (1961). The full title of the act is informative and reasonably concise.

² The 1960-61 figures place Illinois agricultural exports for that period at approximately \$320,000,000. U.S. Dep't of Agriculture Release 647-62, February 19, 1962.

³ ILLINOIS UNIFORM STATE LAW COMMISSION, ILLINOIS ANNOTATIONS TO THE UNIFORM COMMERCIAL CODE 31 (1960). (Published in pamphlet form, as a public service, by Burdette Smith Company, these annotations are very helpful.)

⁴ While this review is limited in scope, farming transactions like other commercial transactions must be reviewed in light of the Code generally and particularly article 1, which contains the rules of construction, general definitions, and principles of interpretation applicable generally to the Code.

⁵ ILL. REV. STAT. c. 26, §§ 2—101 to —725 (1961). For a review of article 2, see Weeks, *The Illinois Uniform Commercial Code: Article 2—Sales*, 50 ILL. B.J. 494 (1962).

⁶ ILL. REV. STAT. c. 121½, §§ 1—77 (1959).

defined by the act. It does not apply to transactions intended to operate only as security transactions.⁷ It does not disturb those cases involving sales of goods when the seller retains a security interest for the price.⁸ Also, article 2 does not impair or repeal any statute regulating sales to consumers, farmers or other specified classes of buyers.⁹

Section 2—105(1) defines “goods” as follows:

“‘Goods’ means all things, including specially manufactured goods, which are movable at the time of identification to the contract for sale other than money in which the price is to be paid, investment securities (Article 8) and things in action. ‘Goods’ also includes the unborn young of animals and growing crops and other identified things attached to realty as described in the section on goods to be severed from realty (Section 2—107).”¹⁰

The Illinois Uniform Sales Act definition of “goods” included “industrial growing crops.”¹¹ This concept of “industrial” growing crops has been abandoned because present day commercial practices require the inclusion within the scope of article 2 of fruit, perennial hay, nursery stock and the like.¹² Unborn animals were not, as such, mentioned in the definition of “goods” or “future goods” in the Illinois Uniform Sales Act. They are expressly included in the Code in subsection (1) of section 2—105. Unborn animals are frequently intended to be sold and are contracted for before birth.

As to certain goods to be severed from realty, section 2—107(1) provides:

“A contract for the sale of timber, minerals or the like or a structure or its materials to be removed from realty is a contract for the sale of goods within this Article if they are to be severed by the seller but until severance a purported present sale thereof which is not effective as a transfer of an interest in land is effective only as a contract to sell.”

⁷ ILL. REV. STAT. c. 26, § 2—102 (1961). This section continues the rule of the Illinois Uniform Sales Act, ILL. REV. STAT. c. 121½, § 75 (1959). According to ALI & NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS, UNIFORM COMMERCIAL CODE 1958 OFFICIAL TEXT WITH COMMENTS 40 (1959) [hereinafter cited UCC], “security transaction” is used in the same sense in § 2—102 as in Article 9, Secured Transactions, of the Illinois Commercial Code, ILL. REV. STAT. c. 26, §§ 9—101 to —507 (1961).

⁸ *In re Halferty*, 136 F.2d 640 (7th Cir. 1943) (conditional sale); *Julius Levin Co. v. Rosenfield*, 230 Ill. App. 126 (1st Dist. 1923) (Sale plus pledge).

⁹ ILL. REV. STAT. c. 26, § 2—102 (1961).

¹⁰ This is a modification of the definition of goods found in the Illinois Uniform Sales Act, ILL. REV. STAT. c. 121½, § 76(1) (1959).

¹¹ *Ibid.*

¹² UCC § 2—105 comment 1.

The foregoing subsection applies to the specified subject matter and only where removal or severance is to be performed by the seller. It does not purport to affect the well established decisions which hold that oil and gas leases granting the right to explore, drill for, mine, and remove oil, gas or other minerals are sales of interests in real property.¹³ Note that at least in one case the sale of standing timber and the right to enter and cut the same has also been held to be an interest in real estate.¹⁴ If instead of the seller the buyer is to remove or sever, the transaction will be considered one affecting real property, and the problems of recordation and the Statute of Frauds are involved.

Section 2—107(2) provides:

“A contract for the sale apart from the land of growing crops or other things attached to realty and capable of severance without material harm thereto but not described in subsection (1) is a contract for the sale of goods within this Article whether the subject matter is to be severed by the buyer or by the seller even though it forms part of the realty at the time of contracting, and the parties can by identification effect a present sale before severance.”

This section makes the determination of whether the subject matter is “goods” depend upon whether it can be severed or removed without damaging the real property. This provision appears contrary to one Illinois case¹⁵ in which it was held that whether a brick press bolted to a base in a brick yard was a chattel or a part of the realty depended on more than merely the ability to remove the press without causing damage to the realty.

On the other hand, it has been held that the lien of a seller of chattels subsequently attached to real estate is superior to rights of parties owning an interest in real estate where (1) the chattel may be removed without damage to the realty, and (2) the parties to the sale of the chattel intend the chattel should remain personalty.¹⁶ The Code drafters have not used the word “fixtures” in section 2—107 and thus have avoided many problems which might arise by use of this term. In its place they have substituted the “without material harm” test.¹⁷ This test is not without some problems, particularly in connection with machinery and equipment; however, few problems should arise with respect to severance of growing crops.

Subsection (3) of section 2—107 provides a method for protecting the buyer of goods under this section:

¹³ *Jilek v. Chicago W. & F. Coal Co.*, 382 Ill. 241, 47 N.E.2d 96 (1943).

¹⁴ *Pierce v. Coryn*, 126 Ill. App. 244 (2nd Dist. 1906).

¹⁵ *Simpson Brick Press Co. v. Wormley*, 166 Ill. 383, 46 N.E. 976 (1896).

¹⁶ *Hewitt v. General Electric Co.*, 164 Ill. 420 45 N.E. 725 (1896); *Thuma v. Granada Hotel Corp.*, 269 Ill. App. 484 (1st Dist. 1933).

¹⁷ UCC § 2—107(2) & comment.

"The provisions of this Section are subject to any third party rights provided by the law relating to realty records, and the contract for sale may be executed and recorded as a document transferring an interest in land and shall then constitute notice to third parties of the buyer's rights under the contract for sale."

The terms of this subsection suggest the necessity for a search of the records prior to any sales transaction covered by this section to make certain that the buyer will get "clear title."

Where the sales transaction involves unascertained or future goods such as crops to be grown or unborn animals, the problems of "existence" and "identification" come into play. Section 2—105(2) provides:

"Goods must be both existing and identified before any interest in them can pass. Goods which are not both existing and identified are 'future' goods. A purported present sale of future goods or of any interest therein operates as a contract to sell."¹⁸

Section 2—401(1) states that title to goods cannot pass under a contract for sale prior to their identification to the contract. Under Section 2—501(1), identification may be made at any time and in any manner explicitly agreed to by the parties, but in the absence of such explicit agreement the identification occurs:

"(a) when the contract is made if it is for the sale of goods already existing and identified;

"(b) if the contract is for the sale of future goods other than those described in paragraph (c), when goods are shipped, marked, or otherwise designated by the seller as goods to which the contract refers;

"(c) when the crops are planted or otherwise become growing crops or the young are conceived if the contract is for the sale of unborn young to be born within 12 months after contracting or for the sale of crops to be harvested within 12 months or the next normal harvest season after contracting whichever is longer."¹⁹

Thus, absent agreement to the contrary, a property interest passes under the Code when the crops are planted or otherwise become growing crops, and with respect to unborn animals, when conceived. This is contrary to some authorities who have maintained that property in planted crops and unborn animals cannot pass.²⁰ Early Illinois cases recognized that growing crops might be sold as personalty, but the courts were

¹⁸ Section 2—105(2) substantially follows the Illinois Uniform Sales Act, ILL. REV. STAT. c. 121½, § 17 (1959) (until goods are ascertained, no property therein passes to buyer).

¹⁹ The phrase "next normal harvest season" is intended to include nursery stock raised for normally quick "harvest" but excludes timber to which a "harvest season" is inapplicable. UCC § 2—501(1)(c) comment 6. Note also the function of § 2—501 in establishing rules for determining insurable interests in goods.

²⁰ WILLISTON, SALES §§ 135, 136 (1948).

quick to protect the rights of creditors and subsequent purchasers.²¹ In the case of contracts to sell growing crops, it would seem prudent for the buyer to utilize the Code provisions for recordation.²²

The provision on unborn animals is new to Illinois law. It would appear that the rights of parties to any contract for sale of unborn animals should be subject to properly perfected liens afforded by breeding laws, but this may not be the result. Title to unborn animals will pass when identified to the contract, which means, in the absence of an agreement, when conceived. Under section 27 of the Illinois Animals Act,²³ a properly perfected lien of the owner of a sire will attach at the birth of the get, and lasts for one year thereafter. Under section 51 of the same act, the owner's claim for lien for service of a stallion or jack cannot be filed as to the mare or progeny until service is rendered. In the latter case, title may pass before any lien can be perfected, and in the former, the creation of a lien and conception may occur at the same time, even though the one year lien period commences at birth.

Under section 2—105(4), an undivided share in an identified bulk of fungible goods, such as grain, is sufficiently identified for the purpose of sale even though the quantity of the bulk is not determined. The buyer becomes an owner in common. The quantity of the share may be designated either in terms of proportion of the bulk or specific number, weight, or measure.²⁴ Note that "fungible" as defined by section 1—201(17) is a broadened concept and expressly includes the idea of fungibility by agreement.²⁵

Farming transactions have given rise to numerous cases involving warranties, particularly in connection with the sale of livestock.

Section 2—313 contains provisions relating to express warranties.²⁶ Under these provisions, a statement becomes an express warranty when it constitutes part of the basis for the bargain.²⁷ The Illinois cases do not appear to follow any well defined pattern in establishing standards for deciding when a statement amounts to a warranty or merely an opinion.²⁸

²¹ *Davis v. Shepherd*, 87 Ill. App. 467 (1899); *Meinke v. Nelson*, 56 Ill. App. 269 (1894).

²² ILL. REV. STAT. c. 26, § 2—107(3) (1961).

²³ *Id.* c. 8.

²⁴ This generally continues the rule of the Illinois Uniform Sales Act, ILL. REV. STAT. c. 121½, § 6 (1959).

²⁵ UCC § 1—201(17) & comment. Compare with the definition of "fungible" in the Illinois Uniform Sales Act, ILL. REV. STAT. c. 121½, § 76 (1959).

²⁶ This section incorporates Illinois Uniform Sales Act, ILL. REV. STAT. c. 121½, §§ 12, 14, 16 (1959), and is completely rewritten.

²⁷ This is the equivalent of the "reliance" requirement under the Illinois Uniform Sales Act, ILL. REV. STAT. c. 121½, § 12 (1959).

²⁸ *VanHorn v. Stautz*, 297 Ill. 530, 131 N.E. 153 (1921) (seller's statement that hogs were sound held opinion, not warranty); *Reed v. Hastings*, 61 Ill. 266 (1871) (seller's

However, when affirmations of fact about goods are made by the seller during the making of the bargain, "clear affirmative proof" is required to take such affirmations out of the agreement, and the issue is ordinarily one of fact.²⁹

Section 2—314 deals with implied warranties of merchantability.³⁰ The Illinois Uniform Sales Act did not contain any definition of merchantability. Under section 2—314(1), merchantability of goods is implied if the seller is a merchant with respect to goods of the particular kind. A person making an isolated sale would not be a "merchant" as the term is used in the Code.³¹ Section 2—314(2) purports to enumerate standards for merchantability. They are not intended as exhaustive.³² The principal warranty created by this section is in subsection (2)(c), providing that goods, to be merchantable, must at least be "fit for the ordinary purposes for which such goods are used."

In the case of implied warranties in fungible goods, subsection (2)(b) of section 2—314 provides they must be of "fair average quality within the description." "Fair average" is appropriate to agricultural bulk products and means goods about "middle" quality, not the worst or best but that which will pass in the trade without objection. The Illinois cases follow this principle.³³ In cases of doubt, the price at which a merchant closes a contract is a good index as to the scope of the obligation in the particular transaction.³⁴ One selling corn implies that it will be fair and merchantable.³⁵ Paragraphs (a) and (b) of subsection (2) must be read together, for both refer to the standards used in the particular trade with respect to the transaction in question.

Section 2—315³⁶ provides for an implied warranty of fitness for a particular purpose,³⁷ which arises if at the time of the sale the seller has

statement that sheep were not with lamb and had not been with buck held a warranty); *Ender v. Scott*, 11 Ill. 35 (1849) (statement that horse was sound not warranty unless reliance thereon shown); *Towell v. Gatewood*, 3 Ill. 22 (1830) (bill of sale recited that tobacco was good first and second rate held opinion, not warranty); *Keller v. Flynn*, 346 Ill. App. 499, 105 N.E.2d 532 (2nd Dist. 1952) (statement that hogs were "long time treated" held a warranty).

²⁹ UCC § 2—313 comment 3.

³⁰ This section incorporates Illinois Uniform Sales Act, ILL. REV. STAT. c. 121½, § 15(2) (1959) but is broader and is completely rewritten. (Note that serving of food and drink is expressly included. This is new.)

³¹ UCC § 2—314 comment 3.

³² UCC § 2—314(2) comment 6.

³³ *Fuchs & Lang Mfg. Co. v. R. J. Kittredge & Co.*, 242 Ill. 88, 89 N.E. 723 (1909) ("merchantable" means fair, average quality, not the best).

³⁴ UCC § 2—314(2) comment 7.

³⁵ *Babcock v. Trice*, 18 Ill. 420 (1857).

³⁶ See Illinois Uniform Sales Act, ILL. REV. STAT. c. 121½, § 15(1), (4), (5) (1959).

³⁷ This is similar to Illinois Uniform Sales Act, *id.* § 15(1) (1959).

reason to know the buyer's requirements, and the buyer relies on the skill or judgment of the seller to furnish suitable goods.³⁸ The seller's defense to an action on such warranty that the buyer bought goods bearing a "patent or trade name" is no longer available. This is a major extension of the warranty.³⁹ As farming has become more and more specialized and dependent upon sophisticated products and services, this section will grow in importance.

Exclusions and modifications of warranties are controlled by section 2—316, and as to express warranties, specific rules of evidence apply as provided by section 2—202. Implied warranties may be excluded from a sale by "as is" or words of similar import, or if the buyer has reasonable opportunity to inspect the goods, or by course of dealing.

ARTICLE 6—BULK TRANSFERS

Article 6, Bulk Transfers,⁴⁰ is the shortest substantive article of the Code. Section 6—102 sets out the enterprises to which the article applies⁴¹ and the types of transactions⁴² involving those enterprises which are covered. The scope of the Code provisions as to transactions covered and protection afforded creditors is substantially the same as the former act with respect to sales of chattels in bulk.⁴³ Farming, however, is not included within those covered enterprises as defined in article 6.⁴⁴ Thus the cases holding bulk sales by farmers to be within the provisions of the bulk transfer laws are now superseded.⁴⁵ The rationale for excluding farming, and also contracting, professional services, and the like lies in the fact that the bulk sales risk is considered not as great as in the case of an enterprise selling merchandise from stock.⁴⁶ The kinds of transfers covered by the act are believed to be those that carry the major bulk sales risks.

³⁸ For Illinois law, see *Green v. Ryan*, 242 Ill. App. 466 (3rd Dist. 1926) (implied warranty that cow is fit for breeding arises from her purchase at sale of breeding cattle. The bull in the case, named Master of Arts, was obviously vulnerable to a suit on express warranty).

³⁹ UCC § 2—315 comment 5.

⁴⁰ ILL. REV. STAT. c. 26, §§ 6—101 to —110 (1961). For a review of article 6, see Cation, *The Illinois Uniform Commercial Code: Article 6—Bulk Transfers*, 50 ILL. B.J. 292 (1961).

⁴¹ ILL. REV. STAT. c. 26, § 6—102(3) (1961).

⁴² *Id.* §§ 6—102(1), (2), (4).

⁴³ ILL. REV. STAT. c. 121½, §§ 78-80 (1959); Trumbull, *The Uniform Commercial Code in Illinois*, 8 DE PAUL L. REV. 1 (1958).

⁴⁴ UCC § 6—102(3) & comment 2.

⁴⁵ *Coon v. Doss*, 361 Ill. 515, 198 N.E. 341 (1935) (sale of livestock and implements); *Weskalnies v. Hesterman*, 288 Ill. 199, 123 N.E. 314 (1919) (sale of livestock and machinery); *Tipsword v. Doss*, 273 Ill. App. 1 (3rd Dist. 1934) (where seller engaged in farming sold in bulk all his livestock and equipment, noncompliance with act rendered sale void as to creditors).

⁴⁶ UCC § 6—102(3) comment 2.

Article 6 also applies to bulk transfers effected by auction. However, by definition, the sale by auction of farm implements, livestock, equipment and the like does not constitute a bulk sale.

ARTICLE 9 — SECURED TRANSACTIONS

The provisions of Article 9, Secured Transactions,⁴⁷ make significant changes in the law of security in Illinois.⁴⁸ The article prescribes a comprehensive scheme for the creation and regulation of security interests in personal property and fixtures.

Under article 9, the distinctions among the various security devices are not retained. In their place, the article substitutes the term "security interest." The new terminology does not outlaw the old traditions. Section 9—102(2) makes this clear:

"This Article applies to security interests created by contract including pledge, assignment, chattel mortgage, chattel trust, trust deed, factor's lien, equipment trust, conditional sale, trust receipt, other lien or title retention contract and lease or consignment intended as security. This Article does not apply to statutory liens except as provided in Section 9—310."⁴⁹

All of these devices are for the primary purpose of securing the performance of some obligation such as repayment of a loan or the payment of a purchase price. The Code replaces these various forms with the security agreement. The terms of the agreement may vary depending upon the specific purpose and the kind of collateral involved. The agreement may be designed to fit the functional needs of the parties. It may cover many kinds of collateral and incorporate different kinds of security interests, including traditional devices, the creation of which, under pre-Code law, would have required separate documentation.⁵⁰ Subject only to the exclusions listed in section 9—104, article 9 permits an infinite variety of security interests which may be created and combined in a security agreement with reference to collateral as defined in the article. Classification problems, such as deciding whether an instrument is a chattel mortgage or a conditional sale, are

⁴⁷ ILL. REV. STAT. c. 26, §§ 9—101 to —507 (1961).

⁴⁸ A suggested Illinois bibliography would include the following: McGraw & Henson, *The Illinois Uniform Commercial Code: A Practical Review of Article 9—Secured Transactions*, 50 ILL. B.J. 112 (1961); Davenport, *An Introduction to the Illinois Uniform Commercial Code*, 50 ILL. B.J. 20 (1961); Henson, *Chattel Mortgages in Illinois v. Secured Transactions Under the Uniform Commercial Code*, 9 DE PAUL L. REV. 125 (1960); Trumbull, *The Uniform Commercial Code in Illinois*, 8 DE PAUL L. REV. 1 (1958); *Symposium on the Uniform Commercial Code and Illinois Law*, 53 N.W. U.L. REV. 315 (1958).

⁴⁹ Even though these various terms may be used, the rules of article 9 govern the transaction. UCC § 9—102 comment 2.

⁵⁰ Coogan, *Operating Under Article 9 of the Uniform Commercial Code Without Help or Hindrance of the "Floating Lien,"* 15 BUS. LAW. 373, 380 (1960).

avoided because such classification is immaterial. Purchase money security interests are specifically recognized in section 9—107.

Under the Code, it is unimportant whether title to the collateral is in the secured party or the debtor.⁵¹ Under prior law, title was sometimes material. The question of whether a chattel mortgage on cattle covered progeny has been decided on the basis of title,⁵² and conditional sales were based on the premise that the title remained in the seller.

Prior to the enactment of the Code, except for real estate mortgages and conditional sales agreements used in sales of equipment, the chattel mortgage, more than any other device, was used to secure farm loans for seed, feed, fertilizer, crops, livestock, and equipment. In a functional sense, the practice will probably continue, except that the terminology will not be the same and the document will bear a different title—security agreement instead of chattel mortgage. Some drafters are using both designations. This will not impair the validity of the agreement, but the use of chattel mortgage terms such as mortgagor and mortgagee may well lead to undesired results in that it may carry the implication that the prior law referable to chattel mortgages is to be used for the construction and interpretation of article 9 transactions. The Code drafters did not intend this result. The *1958 Official Text* indicates that for article 9 “a set of terms has been chosen which have no common law or statutory roots tying them to a particular form.”⁵³ It would seem most important to use, where applicable, the precise terminology provided by the Code. The borrower, thus, is designated the “Debtor”; the lender or one entitled to payment or performance is called the “Secured Party”; and the “Security Agreement” is the agreement which creates or provides for the “Security Interest” which is the interest of the secured party.

The security agreement, as provided in section 9—201, is effective according to its terms between the parties against purchasers of the collateral and against creditors. However, the security interest created thereby is not enforceable against the debtor or third parties unless the collateral is in the possession of the secured party or unless the debtor has signed a security agreement containing a description of the collateral.⁵⁴ According to section 9—204, a security interest cannot attach to collateral until (1) there is an agreement that it attach, (2) value is given by the secured party, usually by promising to furnish or by furnishing money or collateral, and (3) the debtor has rights in the collateral. All three must take place, but the order of events is not important. The perfection of the security interest as to third parties is accomplished by giving the public notice of the transaction

⁵¹ ILL. REV. STAT. c. 26, § 9—202 (1961).

⁵² *O'Brien v. First Galesburg Nat'l Bank*, 275 Ill. App. 176 (2nd Dist. 1934).

⁵³ UCC § 9—105 comment 1.

⁵⁴ ILL. REV. STAT. c. 26, § 9—203 (1961).

either by the secured party having possession or by filing in a public office, either locally or with the Secretary of State, or occasionally, out of caution, both. The place of filing is governed by section 9—401.

“Collateral,” as defined by section 9—105, means the property subject to a security interest. It is a general term embracing tangible and intangible property. Collateral which consists of tangible personal property is “goods.”⁵⁵ “Goods,” by definition in section 9—105(1)(f), includes unborn young of animals and growing crops.⁵⁶ Section 9—109 further classifies goods as follows:

“(1) ‘consumer goods’ if they are used or bought for use primarily for personal, family or household purposes;

“(2) ‘equipment’ if they are used or bought for use primarily in business (including farming or a profession) or by a debtor who is a non-profit organization or a governmental subdivision or agency or if the goods are not included in the definitions of inventory, farm products or consumer goods;

“(3) ‘farm products’ if they are crops or livestock or supplies used or produced in farming operations or if they are products of crops or livestock in their unmanufactured 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;

“(4) ‘inventory’ if they are held by a person who holds them for sale or lease or to be furnished under contracts of service or if he has so furnished them, or if they are raw materials, work in process or materials used or consumed in a business. Inventory of a person is not to be classified as his equipment.”

The classes of goods are mutually exclusive. The same property cannot, as to the same person, be both equipment and inventory at the same time. Generally, the primary use will determine the classification. Occasionally there will be a close case such as a farmer's jeep which could be either equipment or consumer goods.⁵⁷

It is clear from the scope of “farm products” and “equipment” that an article 9 security agreement may be drawn to cover all of the ordinary farming operations. Note, however, that “goods” are “farm products” only if they are in the possession of a debtor who is engaged in farming operations of one kind or another. “Farming operations” are not defined in the article; however, it seems clear that “farming operations” includes raising livestock

⁵⁵ UCC § 9—105 comment 3.

⁵⁶ Note that the definition in § 9—105(1)(f) appears similar to § 2—105(1). The sales article definition refers to the time of identification to the contract, while the article 9 provision refers to the time the security interest attaches.

⁵⁷ UCC § 9—109 comment 2.

as well as crops. The term "livestock" is apparently intended to include fowl because eggs are designated as "products" of livestock.⁵⁸

In the event crops or livestock or their products come into possession of one not engaged in farming, they cease to be "farm products." If they pass to one engaged in marketing for sale or a manufacturer or processor, they become "inventory."⁵⁹ This means that even though crops or livestock remain in the hands of one engaged in farming operations, if they are processed or subjected to manufacturing, they may lose their classification as "farm products." Just when this transformation occurs is unclear. Some processes are closely related to farming, such as pasteurizing or boiling sap. On the other hand, large scale canning operations are not farming, but manufacturing.⁶⁰

The Code does not solve the problems involved in describing collateral in the security agreement. Section 9—110 merely requires the collateral to be reasonably identified. The same test is applicable where a description of real estate is required.⁶¹ In describing equipment and livestock, familiar practices of using serial numbers, motor numbers, color, markings, ear tags, location and the like, together with the words "all . . . including . . ." will continue to be used. The use of the legal description of real estate, while desirable, is not required provided there is reasonable identification.

After-acquired property⁶² or proceeds of sale of farm products⁶³ should be specifically mentioned if intended to be included in the collateral.

Even though covered by the security agreement, a security interest will not attach as to unborn animals until conceived, or in growing crops until planted, until fish are caught, or until timber is cut.⁶⁴ In the case of increase in livestock, some authorities suggest that a security interest in livestock plus an after-acquired property clause will not cover all increase. The theory is that a security interest in a cow alone will not include presently conceived but unborn young because of the fact that the debtor has a present separate interest in the unborn young. An after-acquired property

⁵⁸ *Id.* comment 4.

⁵⁹ *Ibid.*

⁶⁰ *Ibid.*

⁶¹ UCC § 9—110 & comment. If growing crops, timber to be cut, or fixtures are to be included in collateral, the security agreement must contain description of the real estate involved. ILL. REV. STAT. c. 26, §§ 9—203(1)(b), —402(1) (1961).

⁶² ILL. REV. STAT. c. 26, § 9—204(3) (1961). Prior to the Code, a chattel mortgage on livestock covered progeny even though the mortgage did not so state. *O'Brien v. First Galesburg Nat'l Bank*, 275 Ill. App. 176 (2nd Dist. 1934).

⁶³ ILL. REV. STAT. c. 26, §§ 9—203(1)(b), —306 (1961). A problem develops under § 9—306(2) if proceeds are included in the collateral covered. The inclusion of proceeds may be held to have impliedly authorized sale free of the security interest; thus, in the security agreement and financing statement some indication could be made which, if intended, negatives waiver of any security interest.

⁶⁴ ILL. REV. STAT. c. 26, § 9—204(2) (1961).

clause by definition cannot include a present interest; thus, careful drafting requires the security agreement to specifically mention the cow, all unborn presently conceived and all increase not yet conceived.⁶⁵

A security agreement may provide that the collateral, whenever acquired, shall secure all obligations under the agreement. However, in the case of crops, no security interest attaches by reason of an after-acquired property clause as to crops which are planted more than one year after the security agreement is executed, except where the security interest in the crops is given in conjunction with a lease or land purchase agreement, in which case the security interest in the crops may by agreement continue for the life of the real estate transaction.⁶⁶

A security agreement may also provide for future advances whether or not given pursuant to commitment.⁶⁷ To assure flexibility, the agreement could secure additional loans made any time prior to the filing of record of a "Termination Statement,"⁶⁸ which constitutes the release of the security interest.

Prior to the Code, if a chattel mortgagee was permitted to consume mortgaged goods, or if the goods were such as could be used only by consumption and the mortgagee remained in possession, the mortgage was fraudulent as to third parties.⁶⁹ This rule was repealed as to agricultural products, thus permitting, for example, the use of a mortgaged crop for feed.⁷⁰ The Code has resolved the problem, as section 9—205 provides that a security interest is not fraudulent against creditors or invalid by reason of liberty in the debtor to use, commingle or dispose of all or part of the collateral, even without replacement, and to use or dispose of proceeds.

In order that a security interest will be valid as against third parties, the interest must be perfected. This is accomplished by filing either a financing statement as provided by section 9—302 or a security agreement as provided by section 9—402. If the latter course is adopted, the security agreement must also contain the formal requisites of a financing statement as prescribed by section 9—402.

In cases where the collateral is equipment used in farming operations, farm products or accounts, or contract rights or general intangibles arising from or relating to the sale of farm products by a farmer, a security interest is perfected by filing in the office of the Recorder of Deeds in the county of

⁶⁵ COATES, *LAW AND PRACTICE IN CHATTEL SECURED FARM CREDIT* 22 (1954).

⁶⁶ ILL. REV. STAT. c. 26, § 9—204(3), (4)(a) (1961).

⁶⁷ *Id.* § 9—204(5).

⁶⁸ *Id.* § 9—404 (1961).

⁶⁹ *Talty v. Schoenholz*, 323 Ill. 232, 154 N.E. 139 (1926); *Harris v. Wemple*, 63 Ill. App. 577 (3rd Dist. 1895).

⁷⁰ ILL. REV. STAT. c. 95, § 1(a) (1959).

the debtor's residence, or if a nonresident, in the county where the goods are kept. Where the collateral is crops, filing must, in addition, also occur in the county where the land on which the crops are grown is located.⁷¹

Perfection of the interest by such filing is required except in a few specific cases including a purchase money security interest in farm equipment having a purchase price not in excess of \$2,500. Filing would seem advisable even here, however. Under section 9—307(2), unless prior to purchase the secured party has filed a financing statement covering such farm equipment, a buyer takes free of the security interest, even though perfected, if he buys without knowledge of such interest, for value, and for his own farming operations. Also, under section 9—307(1), a buyer in the ordinary course of business, except a person buying farm products from a seller engaged in farming operations, takes free of a security interest created by the seller, even though the buyer is aware of the security interest.

With respect to other farm equipment, including all fixtures and motor vehicles required to be licensed, filing must take place in order to perfect the security interest.⁷² The inclusion in section 9—302(1)(c) of motor vehicles required to be licensed raises a somewhat troublesome problem. Security interests in automobiles and trucks, titled through the office of the Illinois Secretary of State, are perfected by notation of the lien on the face of the title, and this method is exclusive.⁷³ As used in section 9—302(1)(c), "vehicle" covers those farm motor vehicles, other than automobiles and trucks, which are required to be licensed.⁷⁴ This would not include those certain vehicles, including implements of husbandry, on which optional certificates of title may be issued, except when their use brings them within the licensing provisions.⁷⁵ Note also that the term "motor vehicle" by definition in the Illinois Motor Vehicle Law is very broad and includes trailers and other mobile equipment.⁷⁶

Most mobile farm equipment, other than trucks and automobiles, is exempt from title and license requirements as implements of husbandry.⁷⁷ Whether or not an item of such equipment is an implement of husbandry may depend not upon the fact that it is essentially farming equipment but upon the use of the equipment. Thus, for example, a farm tractor, farm wagon, or trailer operated on the highway other than incidentally could

⁷¹ *Id.* c. 26, § 9—401(a) (1961).

⁷² *Id.* § 9—302(1)(c).

⁷³ ILL. REV. STAT. c. 95½, §§ 3—201 to —210 (1961); ILL. REV. STAT. c. 26, § 9—302(3)(b) (1961).

⁷⁴ ILL. REV. STAT. c. 95½, § 3—402 (1961).

⁷⁵ *Id.* § 3—103.

⁷⁶ *Id.* § 1—133.

⁷⁷ *Id.* §§ 1—124, 3—102(6), 3—103, 3—402(2).

be non exempt, and required to be titled and licensed.⁷⁸ In such case, the perfection of a security interest would require the issuance of a title with the lien noted thereon. Under most circumstances, these items of mobile farm equipment will be properly classified as implements of husbandry, thus exempt from licensing. The fact that the character of the equipment may change in accordance with use does not impair the validity of a perfected security interest. Section 9—401(3) provides that a proper filing once made continues effective though the debtor's residence, place of business, the location of the collateral or its use, whichever controlled the original filing, is thereafter changed.

With respect to priorities, the Code contains the rules which will govern any given case.⁷⁹ The general rule is that where competing security interests are perfected by filing, priority is governed by time of filing of the financing statements. This is so, regardless of which interest attaches first, and in the case of a filed security interest, whether the security interest attaches before or after filing.⁸⁰ The lender thus, whenever possible, should file before the security interest attaches. This rule is the natural result of a system based on notice filing.⁸¹ Special rules are applicable to cases involving purchase money security interests.⁸² Section 9—312(2) provides for priority of a new value security interest in crops arising out of a current crop production loan:

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

The secured party under the foregoing provision thus has priority over earlier security interests in the particular crop which secured obligations such as rent, or principal, or interest payable on a mortgage.⁸³ Practitioners representing land owners should note the possible impact of this section on

⁷⁸ ILL. ATT'Y GEN. REP. & OPS. 167, at 170 (1960): “[I]f a farm wagon, wagon trailer or like vehicle is not used in connection with agricultural, horticultural, or livestock raising operations, it is like any other trailer or freight carrying vehicle for purposes of the Illinois Motor Vehicle Law.”

⁷⁹ ILL. REV. STAT. c. 26, § 9—312 (1961).

⁸⁰ *Id.* § 9—312(5) (a).

⁸¹ McGraw & Henson, *The Illinois Uniform Commercial Code: A Practical Review of Article 9—Secured Transactions*, 50 ILL. B.J. 112 (1961).

⁸² ILL. REV. STAT. c. 26, § 9—312(3), (4) (1961).

⁸³ UCC § 9—312(2) comment 2.

the customary landlord's lien upon crops,⁸⁴ and the ability of the tenant under this section to create security interests which may take precedence over the landlord's interest in any crop provided by the lease.

In case of doubt, the lease might be drafted to include a provision requiring the tenant to obtain an agreement from the lender subordinating any such lender's interest to that of the landlord, and providing that in the event of the failure on the part of the tenant to obtain such agreement the lease, prior to the execution of any security interest in favor of the lender, shall ipso facto be and become terminated as between the parties.⁸⁵ This lease provision could be one in the nature of a security interest in the crops which would be perfected by filing in the manner prescribed by the Code.⁸⁶ Of course, any provision seeking to prohibit the tenant from disposing of or encumbering his own interests is ineffective, and in all transactions under article 9, the debtor has an interest which may be reached by creditors.⁸⁷

Section 9—310 provides for priority of liens in favor of persons who furnish services or materials in the ordinary course of business, with respect to goods subject to a security interest where such lien is given by statute or rule of law and the goods are in the possession of such persons. Under this provision, stablekeepers have a prior lien on animals in their possession,⁸⁸ and threshermen have a prior lien on grain in their possession and processed by them. Retention of possession of the serviced animal may be the only way, however impractical, a breeder can adequately protect his interests under his statutory liens heretofore mentioned.

The Code also provides rules to govern problems of priorities in fixtures and accessories, but leaves to the law of Illinois, other than the Code, to determine whether and when goods become fixtures.⁸⁹ Similar rules are provided for accessions.⁹⁰ Also covered are priorities when goods are commingled and processed.⁹¹ Farm improvements, purchases of equipment and repairs and replacements on equipment, and the handling of fungible goods and other farm products are governed by these rules.

In general, with respect to secured transactions involving farming, the lenders, whether they are individuals or institutions, prefer to encumber as much personal property as possible to secure the loan. This fact is one of the reasons that procedures in farm lending must be sufficiently flexible to permit the farmer reasonable latitude in his operations. Crops must be sold

⁸⁴ ILL. REV. STAT. c. 80, §§ 31—33, 35 (1961).

⁸⁵ ILL. REV. STAT. c. 26, § 9—316 (1961).

⁸⁶ *Id.* § 1—201 (37).

⁸⁷ *Id.* § 9—311.

⁸⁸ ILL. REV. STAT. c. 82, § 58 (1961).

⁸⁹ ILL. REV. STAT. c. 26, § 9—313 (1961).

⁹⁰ *Id.* § 9—314.

⁹¹ *Id.* § 9—315.