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An Agricultural Law Research Article

## **United State Agriculture Production Financing: Sources, Legal Rules, and Controversies**

by

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# UNITED STATES AGRICULTURE PRODUCTION FINANCING: SOURCES, LEGAL RULES, AND CONTROVERSIES

Keith G. Meyer\*

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## I. INTRODUCTION

Credit is essential to America's business world and very important in agriculture operations.<sup>1</sup> The broad distribution of goods and services in the United States is made possible by the plentiful supply of secured credit provided by financial institutions and sellers of goods. This belief is supported by the fact that the position of the unsecured creditor is very weak.<sup>2</sup> If a debtor fails to pay for goods purchased on credit, or fails to pay a loan when due, the unsecured creditor must file a lawsuit against the debtor, obtain a civil judgment, and collect the judgment by seizing and selling non-exempt property.<sup>3</sup> This is a slow, expensive, and inefficient process. The secured creditor,

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1. Farmer debt can be divided into two broad categories: real estate and non-real estate. The Appendix to this Article provides tables showing a breakdown of real estate and non-real estate farm debt.

2. See Theodore Eisenberg & Shoichi Tagashira, *Should We Abolish Chapter 11? The Evidence from Japan*, 23 J. LEGAL STUD. 111, 112 (1994).

3. See 15 U.S.C. §§ 1671-1677 (1994). When the debtor is an individual, states and Congress conclude that the public interest is not served by allowing the creditor to make the debtor a pauper. *Id.* § 1671. Accordingly, both state and federal law recognize that certain property of an individual debtor is protected from the claims of a creditor seeking property without the consent of the debtor, i.e., the property is exempt from seizure. *Id.* § 1672(b). Probably the most important property of debtors is their wages, which is protected under federal law. *Id.* § 1673. Except for wages and situations in which bankruptcy is involved, state law defines the property that can be seized by a creditor in the judicial debtor collection process. While state exemptions vary widely, most states exempt the following categories of property: the family residence and household furnishings, the clothing and personal effects of the debtor and the debtor's family, the family car, and the tools and other personal (movable) property used in the debtor's occupation.

however, contracts for an interest in specific property of the debtor and can often obtain the collateral without the expense of a lawsuit.<sup>4</sup> Further, an unsecured creditor's debt will be lost in bankruptcy, whereas a properly perfected secured creditor's security interest survives a debtor's bankruptcy.<sup>5</sup>

In 1940, the idea of a single, comprehensive commercial code covering all aspects of commercial transactions (contract, payment, and credit) was conceived.<sup>6</sup> By 1951, it became a reality when the Uniform Commercial Code (UCC) was created by the American Law Institute (ALI) and the National Conference of Commissioners on Uniform State Laws (NCCUSL).<sup>7</sup> Uniform rules are needed for a variety of reasons. Each state is independent in matters of legislation and judicature, and commerce knows no state boundaries. A lawyer dealing with a client in Kansas City who makes a contract with a person in San Francisco cannot advise the client without an extensive investigation of the relevant law of each state to determine what law governs the contract and what conflicts may arise. Section 1-102(2), which is applicable to all articles of the UCC, sets forth the basic premises of the UCC:

- (a) to simplify, clarify and modernize the law governing commercial transactions;
- (b) to permit the continued expansion of commercial practices through custom, usage and agreement of the parties;
- (c) to make uniform the law among the various jurisdictions.<sup>8</sup>

Transaction costs are minimized if parties in different states can rely on a known body of law when entering into a transaction. Thus, the resolution of problems between parties becomes easier if the outcome of litigation is reasonably predictable.

Commercial matters in the United States are traditionally governed by state law, not federal law. Accordingly, NCCUSL, a group of state governments organized in 1892 to draft and secure enactment of uniform state laws on a wide variety of subjects, became interested in designing a uniform com-

4. See U.C.C. § 9-503 (1996).

5. 11 U.S.C. § 544(a) (1994). The goal of bankruptcy is equal treatment for all creditors. The debtor's ability to make preferential transfers to creditors is considerably limited. After the filing of a bankruptcy petition, a creditor cannot improve its position vis-à-vis other creditors by seizing assets of the debtor. For individual debtors, bankruptcy provides the prospect of significant relief. This relief may take the form of relief from further personal liability for debts created prior to bankruptcy. A primary purpose of bankruptcy is to relieve honest debtors from oppressive debt and permit a fresh start. While a debtor's debt will be discharged, a properly created security interest will remain and can be enforced against the property subject to the security interest after bankruptcy.

6. RAY D. HENSON, HANDBOOK ON SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE 1 (2d ed. 1979).

7. U.C.C. GEN. CMT. OF NAT'L CONF. ON UNIF. STATE LAWS AND THE AM. LAW INST. xv (1989).

8. U.C.C. § 1-102(2) (1996). While many provisions of the UCC may be varied by agreement, some cannot. *Id.* § 1-102(3). For example, obligations of good faith, reasonableness, diligence, and care requirements cannot be changed. *Id.*

mercial code.<sup>9</sup> The ALI also played an instrumental role in the development of the UCC.<sup>10</sup> Since 1944, NCCUSL and the ALI have co-sponsored the UCC, working each year to preserve and update it.<sup>11</sup> The development process is designed to develop a national consensus that (1) the proposed statute is worthy of enactment by state legislatures and (2) uniformity is more important than refinements by individual state legislatures.<sup>12</sup>

Uniformity is dependent upon state legislatures adopting a uniform act without major changes, and state courts' construction in a manner consistent with the UCC's purpose. The UCC was enacted with local variations in all fifty states.<sup>13</sup> In general, Article 9 is conceptually the same in all states, but great variation exists as to where to file the financing statement.<sup>14</sup> Furthermore, fifty different state supreme courts construe and add their own unique

9. HENSON, *supra* note 6, at 1-3. NCCUSL drafts two types of proposed legislation: uniform acts and model acts. *Id.* at 3-5. Both types of legislation involve legal problems common to all states. Uniform acts are used when uniformity of treatment is very important; model acts are used when uniformity is not important. Members of this conference are called commissioners, and they come from the 50 states plus the District of Columbia, Puerto Rico, and the Virgin Islands. Most are practicing lawyers, but some are judges or law professors. Each state normally sends four commissioners, however, each state's delegation has only one vote. Commissioners must try to persuade their state legislatures to adopt NCCUSL proposals.

10. Unlike NCCUSL, the ALI is a private nonprofit corporation. *Bylaws*, 1996 A.L.I. ANN. REP. 591, app. I, §1.01. Its purpose is "to promote the clarification and simplification of the law and its better adaptation to social needs, to secure the better administration of justice, and to encourage and carry on scholarly and scientific legal work." *Id.* It has about 2500 members (professors, judges, and practicing lawyers), who are elected for life. *Rules of the Council*, 1996 A.L.I. ANN. REP. 63, app. I, §1.02; Marianne B. Culhane, *The UCC Revision Process: Legislation You Should See in the Making*, 26 CREIGHTON L. REV. 29, 43 (1992). The work of the ALI is funded by gifts, dues, receipts from the sale of publications, and returns on investments. *Revenues and Expenses July 1, 1994 through June 30, 1995*, 1996 A.L.I. ANN. REP. 51, annex 1. NCCUSL conceived the idea of a uniform commercial code and sought the help of the ALI, which has a wider membership, greater prestige, and more financial support.

11. Article 9 was changed in 1972 and is currently being reviewed for possible changes. See HENSON, *supra* note 6, at 316. Article 2 is also being revised.

12. Both the NCCUSL and the ALI have worked on revisions, and both must approve changes. Culhane, *supra* note 10, at 53. NCCUSL directs the effort to get states to adopt the new version of the UCC. *Id.* While the ALI revision process typically starts with a study committee and a group of advisors, if changes are needed, a drafting committee is appointed. *Id.* at 46. The drafting committee includes academics, representatives of the various industries affected, and consumer advocates. *Id.* at 47-48. An attempt is made to develop a code which has broad appeal so special interest groups will not derail states from adopting it. *Id.* at 51. Currently, the American Bar Association also plays an important role in the development process. See Edward L. Rubin, *Thinking Like a Lawyer, Acting Like a Lobbyist: Some Notes on the Process of Revising UCC Articles 3 and 4*, 26 LOY. L.A. L. REV. 743 (1993).

13. LEN YOUNG SMITH & G. GALE ROBERSON, *BUSINESS LAW* 25 (4th ed. 1977); DAVID G. EPSTEIN ET AL., *BASIC UNIFORM COMMERCIAL CODE TEACHING MATERIALS* 5 (3d ed. 1988); ROBERT BRAUCHER & ROBERT A. RIEGERT, *INTRODUCTION TO COMMERCIAL TRANSACTIONS* xxxvii (1977).

14. See U.C.C. § 9-401 (1996). The drafters of Article 9 chose not to resolve the conflict between those arguing for one statewide filing and those supporting local filing, in which filing is made in the county where the debtor resides. Thus, the possibility that local filing officers would try to prevent all of Article 9 from being adopted was eliminated.

interpretations.<sup>15</sup> Of course, true uniformity could be achieved by Congress enacting the UCC pursuant to the Commerce Clause.<sup>16</sup>

In order to facilitate an understanding of the conflict between traditional agricultural lenders and credit sellers of agricultural production inputs, it is necessary to first discuss the basics of Article 9. Next, the specific priority rules applicable when multiple creditors claim the same agricultural products will be considered. This Article concludes by focusing on a few of the suggested changes of Article 9 rules affecting agriculture credit.

## II. ARTICLE 9 OF THE UCC

The UCC is currently divided into eleven articles.<sup>17</sup> Article 9 deals with secured transactions in personal or movable property in fifty-five succinctly

15. See generally Harold A. Hintze, Note, *Disparate Judicial Construction of the Uniform Commercial Code—The Need for Federal Legislation*, 1969 UTAH L. REV. 722, 726-27, 744-50.

16. U.S. CONST. art. I, § 8, cl. 3. Congress has the power to regulate commercial transactions under the Commerce Clause because financing the sales of goods or loans is within the definition of interstate commerce.

In general, Congress has not exercised its power. Bankruptcy and certain consumer legislation, however, are the exceptions. See, e.g., Bankruptcy Reform Act of 1978, 11 U.S.C. §§ 101 et seq. (1994); Fair Debt Collection Practices Act, 15 U.S.C. § 1692 (1994); Truth in Lending Act, 15 U.S.C. § 1601 (1994). Litigation would be in federal courts, and it would probably require more judges. Special courts, however, could be created solely to handle commercial law matters. Parts of Articles 3 and 4 dealing with check collection are already federalized due to the need for uniformity. See U.C.C. §§ 3-102(c), 4-102 cmt. 1. Yet many critics oppose federalization of Article 9 for a variety of reasons including creditor rights which is a state law issue. Others argue for federalization of Article 9, noting that financing today is not confined to one state, and large businesses operate in more than one state. Furthermore, proponents of the federalization of Article 9 argue that planning and transaction costs would be substantially reduced and revisions could be made more quickly.

17. General provisions affecting all parts of the UCC are in Article 1. U.C.C. §§ 1-101 to 1-209 (1996); see, e.g., *id.* §§ 2-103(4), 9-105(4). Article 2 applies to "transactions in goods." *Id.* § 2-102. It de-emphasizes the title concept and includes a number of novel provisions dealing with the formation of sales contracts and creating different standards of conduct for merchants and nonmerchants. See *id.* §§ 2-104, 2-204, 2-401. Article 2A regulates all facets of leases. *Id.* § 2A-102. A lease is "a transfer of the right to possession and use of goods for a term in return for consideration, but a sale, including a sale on approval or a sale on return, or retention or creation of a security interest is not a lease." *Id.* § 2A-103(j). Article 3 deals with payment methods concentrating on negotiable instruments, checks, and other drafts. *Id.* § 3-102. Article 4 deals with bank deposits and collections of checks, and Article 4A deals with funds transfers. *Id.* §§ 4-101 cmt. 1, 4A-102. Article 5 deals with letters of credit. *Id.* § 5-101 cmt. Bulk sales of the inventory of a business are covered in Article 6. *Id.* § 6-103. Documents of title including warehouse receipts and bills of lading are the subject of Article 7. *Id.* § 7-101 cmt. Article 8 articulates rules relating to investment securities such as stocks and bonds. *Id.* §§ 8-101, 8-102(15). Article 9, of course, governs secured transactions. *Id.* § 9-102. Articles 10 and 11 are essentially administrative in nature, dealing with effective dates and repealing old commercial laws. See, e.g., *id.* §§ 10-102, 11-102.

It is important to note that the drafters were mindful of the role of courts. Official Comment 1 to § 1-102 states in part: "[The Act] is intended to make it possible for the law embodied in this Act to be developed by the courts in the light of unforeseen and new

stated sections and is the most novel part of the UCC. In the late 1940s, when the UCC was drafted, the leading commercial states had separate and very distinct laws on chattel mortgages, conditional sales, trust receipts, factors' liens, and assignments of accounts receivable. The law of chattel security was as provincial and nonuniform then as the law of real estate mortgages is today. The most radical innovation in Article 9 is its substitution of a unitary security device for the many security devices previously in use. The terms such as "mortgagee," "pledgee," and "conditional sale" do not appear in Article 9. Instead, the unitary security device is formulated in terms of four basic concepts: "secured party," "debtor," "collateral," and "security interest."

Article 9 has its own distinct language. The person granting credit may become a secured party by contracting for a security interest in property called collateral to secure an obligation of the debtor.<sup>18</sup> The contract is a security agreement.<sup>19</sup> Security interest is defined to be "an interest in personal property or fixtures which secures payment or performance of an obligation."<sup>20</sup> Consider the following illustration: Farmer wants to borrow \$40,000 from Bank to buy a new combine; however, Bank will loan the money only if the combine is security for the loan. In Article 9 language, Bank is the secured party, Farmer is the debtor, the combine is the collateral, Bank's interest in the combine to secure payment is a security interest, and the agreement creating the security interest is the security agreement.<sup>21</sup> Because Bank is loaning Farmer the money to obtain the combine, the Bank's security interest is a special kind of security interest called a purchase money security interest (PMSI).<sup>22</sup>

Article 9 is basically divided into five parts: Scope,<sup>23</sup> Attachment,<sup>24</sup> Perfection,<sup>25</sup> Priorities,<sup>26</sup> and Default.<sup>27</sup> All but default will be briefly discussed in this Article.

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circumstances and practices. However, the proper construction of the Act requires that its interpretation and application be limited to its reason." *Id.* § 1-102 cmt. 1.

18. *See id.* § 9-203.

19. *See id.* §§ 9-201, 9-203(1)(a).

20. *Id.* § 1-201(37).

21. *See id.* §§ 1-201(3), 9-105(1)(l).

22. *See infra* text accompanying notes 78, 85, 88. A security interest is a purchase money security interest (PMSI):

to the extent that it is (a) taken or retained by the seller of the collateral to secure all or part of its price; or (b) taken by a person who by making advances or incurring an obligation gives value to enable the debtor to acquire rights in or the use of collateral if such value is in fact so used.

§ 9-107(a)-(b). A PMSI holder in many instances is given special priority. *Id.* § 9-312(3)-(4).

23. *Id.* §§ 9-102, 9-104.

24. *See id.* §§ 9-203 to 9-204.

25. *See id.* §§ 9-302 to 9-306.

26. *See id.* §§ 9-201, 9-301, 9-304(2), 9-306(2), 9-307, 9-312.

27. *See id.* §§ 9-501 to 9-507.

### A. Scope

Article 9 applies to any voluntary transaction, regardless of form, which is intended to create a security interest in personal property or fixtures *and* to the sale of accounts receivable or chattel paper.<sup>28</sup> It does not apply to interests in property obtained involuntarily by a creditor such as liens given by statute or obtained through the court system.<sup>29</sup> Personal or movable property includes: goods (e.g., consumer goods, farm products, equipment, and inventory),<sup>30</sup> documents of title (e.g., warehouse receipts),<sup>31</sup> instruments (e.g., promissory notes and certificates of deposit),<sup>32</sup> accounts receivable, general intangibles (e.g., contract rights or a future interest),<sup>33</sup> and investment property (e.g., stocks, bonds, and commodity futures contracts).<sup>34</sup> While security interests in real estate are not covered by Article 9,<sup>35</sup> security interests in unsevered crops, crops to be grown, and harvested crops are covered.<sup>36</sup> If a transaction is covered, the attachment,<sup>37</sup> perfection,<sup>38</sup> priority,<sup>39</sup> and default rules<sup>40</sup> of Article 9 apply.

### B. Attachment

The drafters of Article 9 chose the term attachment to denote the creation of a security interest.<sup>41</sup> Attachment means that the security interest can be enforced against specific property of the debtor.<sup>42</sup> Attachment occurs when three facts are established.<sup>43</sup> First, a proper security agreement must

28. *Id.* § 9-102(1)(a) ("Except as otherwise provided in Section 9-104 on excluded transactions, this Article (a) applies to any transaction (regardless of its form) which is intended to create a security interest in personal property or fixtures including goods, documents, instruments, general intangibles, chattel paper or accounts . . ."). Section 9-102(1)(b) covers sales of accounts and chattel paper. *Id.* § 9-102(1)(b).

29. *Id.* § 9-104(c); *see also infra* note 77 and text accompanying notes 89-99. *But see id.* § 9-310.

30. *See* §§ 9-109, 9-102(1)(a).

31. *See id.* § 9-102(1)(a).

32. *See id.* § 9-309.

33. *See id.* §§ 9-102(1)(a), 9-106.

34. *See id.* §§ 9-102(1)(a), 9-115.

35. *Id.* § 9-104(j). Article 9 does not apply to the creation or transfer of an interest in or lien on real estate, except to the extent that provision is made for fixtures under other articles of the U.C.C. *See id.* § 9-313.

36. *Id.* § 1-201(37) (defining the term "security interest"); § 9-109(3) (defining what is intended as a "farm product"); § 9-105(1)(h); § 9-203(1)(a).

37. *Id.* § 9-203.

38. *Id.* § 9-304.

39. *See generally id.* §§ 9-301 to 9-318.

40. *See generally id.* §§ 9-501 to 9-507.

41. *See id.* § 9-203 (stating that attachment occurs when the events denoted in subsection (1) of the section have taken place unless the time of attachment is explicitly agreed upon).

42. *See id.*

43. *See id.* § 9-203 cmt. 1.

exist.<sup>44</sup> Unless the secured creditor has possession of the collateral, the agreement must be in writing, signed by debtor, and contain a collateral description which reasonably identifies what property is subject to a security interest.<sup>45</sup> A security agreement can create a security interest in debtor's current property as well as in property debtor obtains in the future.<sup>46</sup> In addition to a proper security agreement, the secured party must give value<sup>47</sup> and the debtor must have rights in the collateral.<sup>48</sup> Once these three requirements are satisfied, the security interest has attached and is enforceable against the collateral described in the agreement upon debtor's default.<sup>49</sup>

### C. Perfection

To protect against third parties (other creditors, buyers of the collateral, and the bankruptcy trustee), the secured party must perfect its security interest.<sup>50</sup> When a conflict exists between the debtor and a secured party, a security interest is enforceable even if the secured party is unperfected.<sup>51</sup> Section 9-303 states "a security interest is perfected when it has attached and when all of the applicable steps required for perfection have been taken."<sup>52</sup> The applicable steps refer to acts by the secured party that will give notice of the security interest.<sup>53</sup> The three principal methods of perfection are the secured creditor taking possession of the collateral, the filing of a financing statement in a designated public office, or the notation of the security interest on a certificate of title.<sup>54</sup>

The key to perfection is the correct classification of the collateral. The possibilities are: fixtures,<sup>55</sup> goods,<sup>56</sup> documents of title,<sup>57</sup> instruments,<sup>58</sup>

44. *Id.* § 9-203(1)(a).

45. *Id.* § 9-203(1)(a) cmt. 1.

46. *Id.* § 9-204(1). This section provides that a security agreement may make clear "all obligations covered by the security agreement are to be secured by after-acquired collateral." Additionally, a recent case raises some questions about the effectiveness of these "dragnet" clauses. *See Western Farm Credit Bank v. Auza*, 181 B.R. 63, 71 (B.A.P. 9th Cir. 1995) (holding that under Arizona law these clauses will not be automatically upheld).

47. *Western Farm Credit Bank v. Auza*, 181 B.R. at 71.

48. *See* U.C.C. § 9-203(1)(c).

49. *Id.* § 9-203(1).

50. *See generally id.* § 9-302.

51. *See generally id.* §§ 9-201, 9-203; *cf. id.* § 9-301.

52. *Id.* § 9-303(1).

53. *See id.* §§ 9-115, 9-303, 9-304 to 9-306.

54. *Id.* §§ 9-304, 9-305.

55. *Id.* § 9-313.

56. *Id.* § 9-105. Goods are articles of personal property which are movable at the time the security interest is established. *See id.* § 9-109. There are four types of goods: consumer goods, equipment, farm products, and inventory. *Id.*

57. *Id.* § 1-201(15). Document means a document of title and includes warehouse receipts for goods in storage (e.g., grain stored in a public warehouse) and bills of lading for goods in transit. *Id.* The document must purport to be issued by or addressed to a bailee and purport to cover goods in the bailee's possession. *Id.*

58. *Id.* § 3-104. Instrument means a negotiable instrument (such as a note, draft, or

accounts,<sup>59</sup> chattel paper,<sup>60</sup> general intangibles,<sup>61</sup> investment property,<sup>62</sup> and proceeds.<sup>63</sup> The most common way to perfect is to file. Once it is determined what type of collateral is involved, a secured creditor knows in what public office to file the financing statement.<sup>64</sup> In most states the financing statement is filed either in the county where the debtor resides or in the Secretary of State's office in the city where the state capital is located.<sup>65</sup> A financing statement, or UCC-1 as it is often called, is a written document containing the names and addresses of the debtor and secured party, a description indicating the types or describing the items of collateral, signed by the debtor, and is effective for five years.<sup>66</sup>

The function of the financing statement is to provide public notice to other potential creditors of the debtor that some or all of the debtor's personal property may be subject to a security interest.<sup>67</sup> The description of the property need not be as specific as the one in the security agreement, merely indicating the types of collateral is sufficient.<sup>68</sup> Secured creditors normally will not make loans until they have searched the filed financing statements to determine if the property in which they are contemplating taking a security interest is already subject to a security interest. The name of the debtor is important because filed financing statements are indexed according to the name of the debtor. This system is key to giving notice to other creditors.

#### D. Priorities

Often, different individuals claim the same collateral or the proceeds of the original collateral. To resolve a priority conflict, potential claimants must

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check) or any other writing which evidences a right to the payment of money, and is not itself a security agreement or lease and is of a type which is in the ordinary course of business transferred by delivery with any necessary endorsement or assignment. *Id.* § 9-105(1)(i).

59. *Id.* § 9-106. Account means the right to payment for goods sold or leased or for services, whether or not earned by performance, and this right is not evidenced by an instrument or chattel paper. *Id.*

60. *Id.* § 9-105(1)(b). Chattel paper means a writing which evidences both a monetary obligation and a security interest in or a lease of specific goods. *Id.*

61. *Id.* § 9-106. General intangibles means any personal property other than goods, accounts, chattel paper, documents and instruments. This is a catch-all category. The goodwill of a business is an example. *Id.*

62. *Id.* § 9-115(f). Investment property includes such things as stocks, bonds, commodity futures contracts, and commodity accounts. *Id.*

63. *Id.* § 9-306(1). Proceeds includes whatever is received when collateral (of any description) is sold, exchanged, collected, or disposed of otherwise. *Id.* Insurance payments for destroyed collateral are included. *Id.* Money, checks, and the like are "cash proceeds;" all other proceeds are "noncash proceeds." *Id.* A security interest in collateral continues in the proceeds of the collateral, subject to various filing requirements set forth in § 9-306(3). *Id.* § 9-306(3).

64. *See id.* § 9-401.

65. A small fee is charged for filing each financing statement.

66. *Id.* §§ 9-402, 9-403.

67. *See* § 9-402 cmt. 2.

68. *See id.*

be identified. Article 9 governs six groups of competitors: (1) unsecured creditors;<sup>69</sup> (2) lien creditors;<sup>70</sup> (3) unperfected secured parties;<sup>71</sup> (4) perfected secured parties (purchase money and nonpurchase money);<sup>72</sup> (5) purchasers (buyers in the ordinary course of business, nonbuyers in the ordinary course, and buyers of farm products);<sup>73</sup> and (6) the debtor's trustee in bankruptcy.<sup>74</sup> Once the parties are identified, the analysis begins with section 9-201.<sup>75</sup> It provides: "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."<sup>76</sup> The sections providing the exceptions are: 9-301 (contests between unperfected secured creditors and others and rights of the lien creditor), 9-307,<sup>77</sup> 9-308, 9-309 (contests between secured creditors and certain purchasers), 9-310 (statutory liens),<sup>78</sup> 9-312

69. *See id.* § 9-312(5)(b).

70. *See id.* § 9-301(1), (3); *see also* Bankruptcy Code § 544(a)(1) (1994).

71. *See* U.C.C. § 9-312(5)(b).

72. *See id.* § 9-312(5)(a); *see also id.* §§ 9-312(3)-(4).

73. *See id.* §§ 9-301(1)(a), 9-307.

74. In every Chapter 7 (liquidation), Chapter 13 (consumer reorganization), Chapter 12 (farmer reorganization), and in some Chapter 11 cases, a bankruptcy trustee will be involved. *See, e.g.*, 11 U.S.C. §§ 704, 1202, 1302 (1994). The trustee is created by federal law through the bankruptcy code and is given broad powers. *See id.* While the powers and duties of the trustee vary from chapter to chapter, the trustee can avoid or repudiate certain transfers of the debtor including those made to creditors. *See id.* § 544. This person may sue on behalf of the bankruptcy estate and be sued. *See id.* § 323(b).

75. U.C.C. § 9-201 (1996).

76. *Id.*

77. In 1986, Congress in effect repealed section 9-307(1) as it applied to the sale of farm products subject to a perfected security interest. 7 U.S.C. § 1631 (1994). Under the uniform version of section 9-307(1), the purchase of farm products from a person engaged in farm operations did not take free of a perfected security interest unless the secured party authorized the sale. U.C.C. § 9-307(1) (1996). Conversely, the general rule under section 1631 of Title 7 is that the buyer takes free of a perfected security interest created by his seller even though the buyer knows of its existence and state law provides otherwise, unless buyer has received appropriate notice under section 1631(e). 7 U.S.C.A. § 1631(d) (1994). For a general discussion of section 1631, see Drew L. Kershen & J. Thomas Hardin, *Congress Takes Exception to the Farm Products Exception of the UCC: Retroactivity and Preemption*, 36 KAN. L. REV. 1 (1987); Drew L. Kershen & J. Thomas Hardin, *Congress Takes Exception to the Farm Products Exception of the UCC: Centralized and Presale Notification Systems*, 36 KAN. L. REV. 383 (1988); Keith G. Meyer, *Congress's Amendment to the U.C.C.: The Farm Products Rule Change*, 55 J. KAN. BAR 17 (1986).

78. No uniform definition of liens exists. Liens give the person, who provided goods or services on credit, an interest in specific property to assure payment for the goods or services. A lien on specific property may be obtained in a variety of ways. In general, there are three categories of liens: judicial liens, statutory liens, and consensual liens. U.C.C. § 9-301(1) (1996). Liens can exist in either real estate or personal property. Only personal property liens are covered here. Judicial liens are normally created in the litigation process when the creditor seeks a money judgment on an unpaid debt and then enforces the judgment by properly taking control of nonexempt property.

Statutory liens are not consensual and do not depend upon judicial action by the creditor. They are status liens that arise by operation of law due to the status of a particular creditor. Statutory liens give the creditor an interest in specific goods to assure payment for goods,

(contests between secured creditors claiming an interest in the same collateral), and 9-306 (proceeds). Lien creditors defeat unperfected secured creditors.<sup>79</sup> Section 9-301(3) defines lien creditor to be “a creditor who has acquired a lien on the property involved by attachment, levy or the like . . . and a trustee in bankruptcy from the time of the filing of the petition.”<sup>80</sup> This means that unperfected secured creditors’ claims to specific property are unenforceable in bankruptcy.<sup>81</sup> The exceptions to section 9-201 are the rule.

When the conflict is between two perfected secured creditors, the first to file will win, unless the second to file has a purchase money security interest.<sup>82</sup> Article 9 adopts a “pure race” filing system with the system based on notice filing.<sup>83</sup> It is not unfair to the second filing creditor because this creditor could have discovered the first creditor’s security interest if it had searched the filed financing statements. The second creditor can either pay off the first creditor, obtain a subordination agreement from the first creditor,<sup>84</sup> refuse to make a loan, or make a loan knowing the first creditor has priority. Consider this example: On January 2, Debtor executes a proper security agreement covering existing equipment in favor of Bank A, and a financing statement is filed in the proper place but no money is advanced. On March 1, Bank B lends Debtor \$5,000, obtains a properly created security interest in equipment, and files a proper financing statement covering the equipment in the appropriate place. Bank A learns Bank B has a properly perfected security interest in the equipment, but, on April 1, loans Debtor \$5,000 secured by the January 2 security agreement. Debtor defaults on both loans. If the collateral will bring only \$5,000 on foreclosure, Bank B’s security interest is ineffective against Bank A because Bank A filed first with respect to the collateral, and the subsequent perfection will relate back to the date of filing.<sup>85</sup> It makes no difference that Bank B technically perfected the loan first (attachment plus filing). The test is who filed first.<sup>86</sup>

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services, land, labor, or whatever was provided by the person entitled to the lien. Statutory lien holders are given the rights of a secured creditor even though they did not bargain for security. *See, e.g.*, § 9-310. Finally, these liens are normally given to creditors who sold goods on credit or who performed some service or otherwise had given some value that preserved or enhanced the value of the property subject to the lien. *See infra* notes 93-102 and accompanying text.

Consensual liens are obtained pursuant to agreement and are covered by Article 9 of the UCC. It must be noted that under Article 9, the term lien is used as a contradiction to a security interest. A security interest is considered to be a consensual interest as opposed to a lien which is not created by contract. *See, e.g.*, U.C.C. § 9-310(b).

79. *Id.* § 9-301(1)(b).

80. *Id.* § 9-301(3).

81. *Id.* § 9-301(1)(b) (the unperfected secured creditor is not entitled to get any specific property in bankruptcy even though the debtor contractually gave the creditor an interest in the specific property).

82. *Id.* § 9-312(5)(a); *see also id.* §§ 9-107, 312(4); *see infra* notes 85, 88, 102, and accompanying text.

83. *Id.* § 9-312(5)(a); *see also id.* § 9-312(4).

84. *See id.* § 9-316.

85. *See id.* § 9-312(5)(a).

86. *See id.*

If Bank B had a purchase money security interest, the result would be different. For example, on January 2, Debtor, a newspaper, borrows \$100,000 from Bank for working capital and grants a security interest in all equipment now owned or hereafter acquired.<sup>87</sup> Bank perfects by filing a financing statement on January 2. On February 10, Debtor takes delivery of a new printing press from ABC Manufacturing Company, which retains a purchase money security interest<sup>88</sup> in the equipment and files a proper financing statement in the proper place on February 10. If Newspaper defaults, ABC has priority even though it filed later because it retained a purchase money security interest.<sup>89</sup>

### E. Current Agricultural Credit Issues

With this background, it is appropriate to turn to current controversies involving agriculture credit. Credit plays a large role in agricultural operations. For example, Farmer grants a perfected security interest in crops and livestock to Bank who supplies a loan to be used for production expenses (seed and fertilizer). Farmer then buys fertilizer and seed from a supplier on an open account, which means credit is extended but no promissory note or security agreement is signed. At harvest, Farmer hires a custom cutter to harvest the crops, which were produced on leased land. Problems arise when Farmer does not pay the Bank, the supplier, the harvester, or the landlord, and all of these parties subsequently assert they have a prior claim to Farmer's crops and livestock. Does Article 9 resolve this conflict? It clearly does, so long as none of the creditors are statutory lien holders.<sup>90</sup> If the supplier, the harvester, and landlord are unsecured creditors, Bank, as a perfected secured creditor, wins because perfected secured creditors defeat unsecured or general creditors.<sup>91</sup> Bank also wins if any of the creditors are subsequent lien creditors (a judgment is rendered and docketed, and the sheriff seizes crops or livestock).<sup>92</sup> The negative inference of section 9-301(1)(b) is that a lien creditor will lose to a prior perfected secured creditor.<sup>93</sup> A more difficult question is presented if any of the creditors have statutory liens.

Statutory liens are not consensual and do not depend upon judicial action.<sup>94</sup> They are status liens that arise by operation of law.<sup>95</sup> Statutes grant

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87. Such an agreement is contained in an after-acquired collateral clause. *See id.* § 9-204(1).

88. *See id.* § 9-107; *see supra* note 21 and accompanying text.

89. *See id.* §§ 9-312(4), 9-312(5)(a); *see also supra* note 78.

90. *See id.* §§ 9-301, 9-102(3), 9-104(b)-(c), 9-310.

91. *Id.* §§ 9-301(1), 9-312(5).

92. *Id.* § 9-301(1)(b), (4).

93. *Id.* § 9-301(3) (stating that "[a] 'lien creditor' means a creditor who has acquired a lien on the property involved by attachment, levy or the like . . . and a trustee in bankruptcy from the date of the filing of the petition or a receiver in equity from the time of appointment"); *see also id.* § 9-301(1)(b) (stating that "an unperfected security interest is subordinate to the rights of a person who becomes a lien creditor before the security interest is perfected").

94. *United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 240 (1989).

the appropriate creditor rights in specific property of the debtor.<sup>96</sup> Many state legislatures created statutory liens to give special protection to individuals and economic groups involved in the production or financing of agricultural products.<sup>97</sup> There is neither intrastate nor interstate uniformity with regard to statutory agricultural liens and no model or uniform lien laws exist. Such liens vary depending on how the lien is created, perfected, enforced, and the priority of the statutory lien holder vis-à-vis other creditors and purchasers of the goods subject to the lien. Moreover, neither of them are found in the statutes nor are they cross referenced in Article 9.

In general, disputes concerning claims to personal property are governed by Article 9 of the UCC. Most agriculture liens, however, are not covered by Article 9. Section 9-102<sup>98</sup> declares that Article 9 applies to all transactions<sup>99</sup> regardless of form, intended by the parties to create a security interest in personal property. Sections 9-102(2) and 9-104 exclude certain types of transactions. The last sentence of section 9-102(2) states that "[t]his Article does not apply to statutory liens except as provided in section 9-310."<sup>100</sup> Also, section 9-104 excludes certain liens from coverage.<sup>101</sup> Section 9-104(b) excludes landlord's liens from coverage,<sup>102</sup> and section 9-104(c) provides that Article 9 does not apply "to a lien given by statute or other rule of law for services or materials except as provided in section 9-310 on priority of such liens."<sup>103</sup>

95. *Id.*

96. *See supra* note 77.

97. *See, e.g.*, CAL. CIV. CODE § 3061.5 (West 1996); FLA. STAT. ANN. § 697 (West 1996); IOWA CODE § 570A.2 (1995).

98. U.C.C. § 9-102(1) (1996) (stating in part: "Except as otherwise provided in § 9-104 on excluded transactions, this Article applies (a) to any transactions (regardless of its form) which is intended to create a security interest in personal property or fixtures including goods, documents, instruments, general intangibles, chattel paper or accounts . . .").

99. These transactions must be consensual in nature and all contracts and agreements regardless of form are covered. *Id.* § 9-102 cmt. 1. These agreements need not be in writing if the secured party has possession of the property. *Id.* § 9-203(1)(a). *See* section 1-201(3) for the definition of agreement; and *see* section 1-201(37) which defines in more detail when a document entitled a lease is really a security interest, and thus a transaction covered by Article 9. If a transaction is covered by Article 9, all of the rules (attachment, perfection, priority, and default) apply.

100. *Id.* § 9-102(2).

101. *Id.* § 9-104(b)-(c).

102. Professor Gilmore in his treatise indicated that landlord liens were excluded for two reasons. 1 GRANT GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY § 10.7(b) (1965). First, Article 9 is designed to apply to consensual security interests, and, secondly, the landlord's lien does not create an interest in personal property. *See id.* Yet, it should be noted that in many states a landlord's lien for unpaid rent of farm land attaches to crops produced on the rented land when rent is not paid. *See, e.g.*, KAN. STAT. ANN. § 58-2524 (1994). Crops are clearly considered personal property under Article 9. *See, e.g.*, U.C.C. §§ 9-105(1)(h), 9-203, 9-402(1) cmt. 1.

103. U.C.C. § 9-104(c).

Liens are either possessory or nonpossessory. Section 9-310 only applies to possessory liens.<sup>104</sup> The creditor claiming the protection of section 9-310 must have possession of the goods, whose value has been enhanced or preserved by services or materials supplied by the creditor, and a statutory or common law lien must exist.<sup>105</sup> The only situation in which Article 9 applies is when the qualified possessory lien holder defeats a prior perfected secured creditor.<sup>106</sup> This priority rule is very similar to the "super priority" given to purchase money security interest under section 9-312(4).<sup>107</sup>

Conflicts between a perfected secured party and lien holders other than those covered by section 9-310 or section 9-301 are resolved by the application of non-UCC rules.<sup>108</sup> There are numerous agriculture liens not covered by the UCC. Examples include: liens for stud service; commission merchant selling farm products; livestock feeders or stable keepers; shoeing animals; unpaid pasture rent; unpaid rent of crop land (landlord lien); veterinarian services; labor and machines used to harvest farm products; processing of farm products; production supplies such as feed, fertilizer, seed, and chemicals; and bovine brucellosis treatment.<sup>109</sup> In short, most of these liens are statutory and differ from state to state as to substance, creation, perfection, enforcement, and priority as to other creditors or purchasers of farm products subject to statutory liens. It is very difficult to determine what liens exist. These uncertainties cause a variety of problems. Creditors and lawyers advising them have no firm basis for planning decisions. Both state and federal courts, particularly bankruptcy courts, have difficulties resolving priority disputes involving agriculture liens.<sup>110</sup>

104. *Id.* § 9-310.

105. *Id.*

106. *Id.*

107. *Id.* § 9-312(4) cmt. 2:

A purchase money security interest in collateral other than inventory has priority over a conflicting security interest in the same collateral or its proceeds if the purchase money security interest is perfected at the time the debtor receives possession of the collateral or within ten days thereafter.

*Id.*

This rule is an exception to the "first to file" rule which normally determines priority under Article 9 when there is a conflict between two perfected secured creditors. *See id.* § 9-312(5)(a). Significantly, section 9-310 does not require any public notice. *Id.* § 9-310. Apparently, the drafters believed that possession was all the public notice that was required. This is consistent with how Article 9 treats perfection in that possession by the creditor of a good can amount to perfection under section 9-305 so long as attachment has occurred under sections 9-203 and 9-303(1). *See id.* §§ 9-305, 9-203, 9-303(1). Remember, section 9-203 requires an agreement between creditor and debtor, and it need not be in writing if the creditor has possession of the collateral. *Id.* §§ 9-203(1), 1-201(3).

108. *Id.* § 1-103.

109. Keith G. Meyer, *Should the Unique Treatment of Agricultural Liens Continue?*, 24 IND. L. REV. 1315, 1324 (1991).

110. *See id.*; *see also* Steven C. Turner, *Nebraska's Adoption of Statutory Provisions for the Creation, Perfection and Enforcement of a Security Interest in Real Estate Rents*, 27 CREIGHTON L. REV. 181 (1993).

Currently, Article 9 is being evaluated and many proposed changes, including agricultural changes, are under consideration. A task force of the American Bar Association has made numerous recommendations.<sup>111</sup> One recommendation focuses on statutory liens.<sup>112</sup> Crops or livestock are produced with various types of inputs such as chemicals, seed, fertilizer, and feed.<sup>113</sup> Many times these inputs are purchased from a supplier on open account and, in some instances, the supplier is given a statutory lien on the crops or livestock to secure payment.<sup>114</sup> Many lending institutions, however, have extended credit to the farmer with the understanding that the money will be used to purchase input needs such as seed, fertilizer, and other chemicals<sup>115</sup>—relying on an Article 9 security interest in crops and livestock to secure payment. The task force recommended that Article 9 should govern perfection, priority, and enforcement of agricultural statutory liens on personal property such as growing crops, harvested crops, and livestock.<sup>116</sup> The creation of statutory liens, however, would be governed by non-UCC law.<sup>117</sup> Under the proposal, the holder of the lien must file a financing statement.<sup>118</sup> The holder could file without the debtor's signature<sup>119</sup> and pre-file with the debtor's authorization.<sup>120</sup> The priority rule suggested is the first-to-file rule unless the applicable lien statute specifically provides otherwise.<sup>121</sup> For example, if the statute creating a lien on livestock for unpaid veterinary bills provides that the lien has priority over a prior perfected secured party, the lien will prevail. Conversely, when the statute creating the lien is silent as to priority over a prior perfected secured creditor, the secured creditor will win. While not all members of the task force supported the blended priority rule proposal, the overall proposal does accomplish a major objective of including the liens in the filing system so all parties have notice, i.e., it eliminates the existing "secret liens."<sup>122</sup>

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111. ARTICLE 9 TASK FORCE OF THE SUBCOMM. ON AGRIC. & AGRI-BUS. FIN., AMERICAN BAR ASSOCIATION, REPORT ON AGRICULTURAL FINANCING UNDER ARTICLE 9 OF THE UNIFORM COMMERCIAL CODE & SUGGESTED CHANGES TO ARTICLE 9, at 5-7 (July 23, 1995) [hereinafter A.B.A. ARTICLE 9 REPORT].

112. *Id.*

113. *Id.*

114. *Id.*

115. *Id.*

116. *Id.*

117. *Id.*

118. *Id.* at 6-7, 19.

119. This is contrary to the current rule under section 9-402 which requires the debtor's signature except in very limited circumstances. U.C.C. § 9-402 (1996); *see also* A.B.A. ARTICLE 9 REPORT, *supra* note 111, at 20.

120. A.B.A. ARTICLE 9 REPORT, *supra* note 111, at 7.

121. *Id.* at 6-7.

122. *See* Steven C. Turner et al., *Agricultural Liens and the UCC: A Report of Present Status and Proposals for Change*, 44 OKLA. L. REV. 9 (1991). It must be pointed out that the issue of farm liens is complicated because of the way in which Congress has dealt with specific farm situations. For example, Congress specifically changed the farm products rule of U.C.C. section 9-307(1), *see* 7 U.S.C. § 1631 (1994), and enacted a special bankruptcy chapter to deal exclusively with farmers. *See* 11 U.S.C. §§ 1201-1208, 1221-1231 (1994). It also estab-

My preference is to make all creditors who want to be able to claim an interest in specific farm products subject to Article 9. Article 9 provides a complete set of understandable rules. All creditors can determine their status vis-à-vis other creditors, as well as the trustee in bankruptcy, if the debtor were to default. The default rules are also relatively straightforward, and courts and attorneys are far more familiar with them than with the enforcement procedure of lien laws. Furthermore, a new set of terms and rules would not need to be developed. Any creditor supplying goods, labor, land, or services to a person engaged in a farming operation would be subject to Article 9. Conflicts concerning a security interest in farm products or goods<sup>123</sup> would also be determined under Article 9.

Another problem area concerns purchase money security interests in farm products. Suppose in 1993, Bank loans Farmer \$30,000 for seed, fertilizer, chemicals, and fuel. In return, Farmer grants Bank a perfected security interest in the 1993 crop, as well as all crops to be grown in 1994, and all harvested crops. Farmer defaults on its loan to Bank, and Bank will not provide production financing for the 1994 crop. Farmer obtains financing from Credit Corporation for the 1994 crop and gives Credit Corporation a perfected security interest in the 1994 crop. Farmer defaults on the Credit Corporation loan. Both Bank and Credit Corporation claim priority to the 1994 crop. When two perfected secured creditors claim the same collateral, the first to file will win absent a specific rule to the contrary.<sup>124</sup> A limited purchase money security interest priority is given to crop production suppliers under section 9-312(2). To qualify for this priority, the following four conditions must be met: (1) the production crop lender must have a perfected purchase money security interest in crops for new value; (2) the purpose of the value must be to enable the debtor to produce the crops during the current production season; (3) the value must be given not more than three months before the crops become growing crops; and (4) the obligation owing to the earlier secured party must have been due more than six months before the crops were planted.<sup>125</sup> The principal issue is the meaning of the requirement that the previous obligation be due more than six months before the crops were planted.<sup>126</sup> Most courts interpret this requirement to mandate that payments be six months in default.<sup>127</sup> This gives very limited protection to

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lished trust funds to give unpaid sellers of livestock, poultry, and perishable commodities priority over perfected secured parties of the buyers. See 7 U.S.C. § 196 (1994). See generally *In re Gotham Provision Co.*, 669 F.2d 1000 (5th Cir. 1982). The United States Department of Agriculture, maintaining that Congress gave it the power to preempt state laws affecting government farm program payments, promulgated regulations specifically providing that the government payments made in the form of commodity certificates were not subject to state Article 9 rules. 7 C.F.R. § 1470.4(b)(2) (1996). Courts, however, are split as to the validity of the regulations. See, e.g., *In re George*, 119 B.R. 800 (Bankr. D. Kan. 1990); *In re Rutz*, 104 B.R. 128 (Bankr. S.D. Iowa 1989).

123. See U.C.C. §§ 9-105(h), 9-109, 9-203(1), 9-402(1) (1996).

124. *Id.* § 9-312(5)(a).

125. *Id.* § 9-312(2).

126. *Id.*

127. See, e.g., *Dennis v. Connor*, 733 F.2d 523, 525-26 (8th Cir. 1984); United States

production lenders. Prior secured parties can probably schedule payments to fall due within the six month period. This limitation is particularly important because the 1972 amendments to Article 9 changed the old rule which required a new security agreement every year in order for a security interest in crops to be created.<sup>128</sup> In other words, after-acquired property clauses did not apply to crops, and new suppliers of credit could obtain priority over a prior filed secured creditor if the prior creditor did not obtain a new security agreement because attachment could not occur.<sup>129</sup>

Some farmers have bitterly complained that section 9-312(2) and the broad after-acquired property clauses coupled with the first-to-file rule prevented them from receiving new financing. Unless a subordination is obtained or section 9-312(2) is applicable, a perfected secured creditor having a proper security agreement covering after-acquired property will have a prior claim to any new crops produced even if the creditor does not provide any financing.<sup>130</sup> Interestingly, the prior secured creditor's after-acquired property clause is probably ineffective in bankruptcy court if debtor plants the crops within ninety days of bankruptcy.<sup>131</sup> It should be noted, however, that the secured party's interest stems from the fact that the debtor still owed money. It is also interesting to note that farmers cannot be involuntarily forced into bankruptcy.<sup>132</sup> Unfortunately, not all farmers can and should be saved. Moreover, a complicated scheme under Article 9 should not be created just to save marginal farmers. If help is to be given, it would seem appropriate for the government, for social policy reasons, to provide financial help via a specific assistance program rather than by revising Article 9.

One approach in dealing with these allegations that after-acquired clauses are too sinister is to go back to the approach of the 1962 Code which provided that attachment could not occur unless the crops became growing crops within *one* year of execution of the security agreement.<sup>133</sup> This approach is far superior to developing a complex statute to deal with the problem<sup>134</sup> or keeping the hodge-podge of lien laws that exist today. In any event, all input suppliers should be subject to the first-to-file rule.<sup>135</sup> Some suppliers of fertilizer, seed, and chemicals, like Credit Corporation in my example above, want to replace section 9-312(2) with a rule giving the creditor who supplies "new value" to produce the crop priority over the prior

v. Minster Farmers Coop. Exch., Inc., 430 F. Supp. 566, 570 (1977). For a further discussion of this proposition, see Steve H. Nickles, *Setting Farmers Free: Righting the Unintended Anomaly of UCC Section 9-312(2)*, 71 MINN. L. REV. 1135, 1186 (1987).

128. See U.C.C. § 9-204(4)(a) (1962).

129. *Id.*

130. See U.C.C. § 9-312(5) (1996). *But see id.* §§ 9-107(a)-(b), 9-312(3)-(4); *supra* text and accompanying notes 73, 81, 82.

131. See 11 U.S.C. §§ 547(b), (c)(5), (a)(1) (1994) (inventory for purposes of the Bankruptcy Code includes farm products); see also *id.* § 552 (providing that an after-acquired property clause is ineffective as to property obtained after the bankruptcy petition is filed).

132. See *id.* § 303(a).

133. See U.C.C. § 9-204(4) (1972).

134. See Nickles, *supra* note 127, at 1193-95.

135. U.C.C. § 9-312(5)(a) (1996).

perfected secured creditor like the Bank who filed first, but did not supply any value for the 1994 crop.<sup>136</sup>

Now suppose that in January 1996, Farmer grants a perfected security interest in the 1996 wheat crop and Bank loans money to be used for seed, fertilizer, and chemicals. Farmer, in February 1996, buys fertilizer and seed from a supplier on credit and grants the supplier a perfected security interest in the same 1996 wheat crop. Applying the first-to-file rule, Bank is entitled to priority in an amount of the crop that is necessary to satisfy Farmer's unpaid debt if default occurs. Some suppliers want Article 9 changed to provide a pro-rata distribution to all purchase money security interest holders inasmuch as both have supplied new value to the crop.<sup>137</sup> Other production suppliers have argued that purchase money security interest holders should be granted the super priority provided for under section 9-312(4).<sup>138</sup> Yet others believe that either one of these exceptions to the first-to-file rule will have an adverse impact on the availability of credit to farmers because traditional farm lenders will be reluctant to rely on crops or livestock as collateral if farmers could give priority to suppliers subsequent to a bank loan decision based in part upon a search of the records showing no filed financing statements. Section 9-312(4) provides: "A purchase money security interest in collateral other than inventory has priority over a conflicting security interest in the same collateral or its proceeds if the purchase money security interest is perfected at the time the debtor receives possession of the collateral or within ten days thereafter."<sup>139</sup>

Consider, however, the following example: On January 1, Farmer gives Bank a perfected security interest in all of its equipment (tractors, combines, drills, etc.) presently owned and acquired. On February 13, Farmer buys and takes possession of a new combine from a John Deere dealer who obtains a security interest and files properly on February 1. Farmer defaults on both loans. The dealer has priority under section 9-312(4).<sup>140</sup> This example is significantly different from two creditors both supplying purchase money financing for a crop and both claiming the same collateral. The effect of the new value added is quite different from the John Deere dealer whose value produced a specific identifiable piece of new collateral. Also, a pro-rata rule in which two perfected secured parties share in proportion to each one's contribution does not seem appropriate. A simple rule becomes complex in that it would be necessary to trace each creditor's contribution to the end product.

### III. CONCLUSION

When considering whether the basic priority rules of Article 9 should be changed, the genius of the drafters must be remembered. This genius is illus-

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136. See A.B.A. ARTICLE 9 REPORT, *supra* note 111, at 5-6.

137. *Id.*

138. *Id.*

139. U.C.C. § 9-312(4) (1996).

140. See *supra* note 78.

trated by the fact that the drafters condensed a conglomeration of complex, difficult-to-understand rules into fifty-five succinct sections containing relatively simple, understandable rules providing a clear and predictable framework for resolving conflicts.<sup>141</sup> Availability of credit is currently not a problem for most farmers. In fact, too much availability has been a larger problem. The real question is not whether the system should be changed to accommodate industries uncomfortable with the current rules or a few farmers who have been denied credit. The real question is what changes are necessary to make the legal system and the credit system work in a fair and efficient manner. Finally, most lawyers, creditors, and farmers can effectively deal with a system that has clear, simple, and certain rules, regardless of who is given priority. This is what Article 9 was designed to do, and this heritage must be continued.

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141. See *supra* note 16 and accompanying text.

## APPENDIX

Table 1<sup>a</sup>  
Real Estate Farm Debt

Year	Farm Credit System	Farmers Home Administration	Life insurance companies	All operating banks	Individuals and others	CCC storage and drying facilities loans	Total
Million Dollars							
1950	991	257	1,353	986	2,526	18	6,131
1960	2,539	723	2,975	1,592	4,992	48	12,868
1970	7,145	2,440	5,610	3,772	11,378	146	30,492
1980	36,196	8,163	12,928	8,571	30,180	1,456	97,495
1983	48,929	9,550	12,718	9,317	32,320	888	113,722
1985	44,584	10,427	11,836	11,385	27,200	307	105,739
1990	26,885	8,093	10,186	17,227	16,000	7	78,398

Table 2<sup>b</sup>  
Non-Real Estate Farm Debt (including operator households)

Year	All operating banks	Farm Credit System	Farmers Home Administration	Debts owed to individuals and others	Total	CCC crop loans
Million Dollars						
1950	2,524	513	329	2,760	6,126	794
1960	4,991	1,568	420	4,990	11,969	1,342
1970	11,102	5,515	795	4,850	22,262	1,730
1980	31,564	20,539	11,397	17,721	81,221	3,836
1983	39,026	20,164	14,608	18,945	92,744	10,576
1985	35,513	14,562	16,720	15,378	82,173	17,598
1990	32,913	10,103	10,652	13,000	66,669	4,377

a. ECONOMIC SEARCH SERV., U.S. DEP'T OF AGRIC., ECONOMIC INDICATORS OF THE FARM SECTOR, NATIONAL FINANCIAL SUMMARY 75 (1991).

b. *Id.* at 76.