# The Uniform Commercial Code and Real Estate Law: Problems for Both the Real Estate Lawyer and the Chattel Security Lawyer

by

Peter F. Coogan & Albert J. Clovis

Originally published in INDIANA LAW JOURNAL
38 IND. L.J. 535 (1963)

# INDIANA LAW JOURNAL

Volume 38 SUMMER 1963 Number 4


## THE UNIFORM COMMERCIAL CODE AND REAL ESTATE LAW: PROBLEMS FOR BOTH THE REAL ESTATE LAWYER AND THE CHATTEL SECURITY LAWYER*


PETER F. COOGAN† and ALBERT L. CLOVIS‡


One does not ordinarily associate the Uniform Commercial Code[1] with real estate law. All of its nine articles deal primarily, and seven out of the nine practically exclusively, with non-real estate. In fact, the majority of the articles deal with property so far removed from realty that it is tangible only in the sense that a piece of paper is necessarily involved.[2] Article 2 (the sales article) does, however, deal exclusively with tangible personal property ("goods"), and sometimes the goods have a recent real estate past, *e.g.*, lumber cut and sold is personalty, but

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* This article will appear as a chapter in a forthcoming second volume of SECURED TRANSACTIONS UNDER THE UNIFORM COMMERCIAL CODE by the senior writer and associates.

† Lecturer, Harvard Law School 1957-63; Visiting Lecturer, Yale Law School 1957-60, 1963-64; member of Massachusetts Bar. The senior author is a member of the national sponsors' subcommittee on article 9. Any opinions are, of course, those of the authors only. For Indiana law the authors have relied on the editors to a considerable degree.

‡ Member of the Ohio Bar.

1. Indiana adopted the Code during the 1963 session of the State Legislature, to become effective on July 1, 1964. The Code has been adopted in 28 states. The adoption of the Code has come at an accelerated pace in recent years. See UNIFORM COMMERCIAL CODE (Uniform Laws Annotated) IX, XXXIII. All references here are to the 1962 version of the Code, which differs slightly from the 1958 official text and comments. Of the sections discussed herein, there is no substantial change between the 1962 and earlier versions; the filing provisions of § 9-401 were restated in the 1962 version for clarity only. The Code as adopted by California (S.B. 118, 1963) differs materially in its treatment of crops and fixtures in several respects. Ohio originally adopted the sponsors' version of U.C.C. 9-313 but with a different numbering system. The 1963 legislature drastically changed the fixture section by a revision of Ohio's R.C. 1309.32(b) which will become effective on October 8, 1963. (Ohio House Bill 565.)

2. *E.g.*, negotiable instruments, documents of title, letters of credit, stock certificates. Article 3 covers commercial paper; article 4 on bank collections, deals with commercial paper and to some extent with documents of title, which is the subject matter of article 7. Article 5 deals with letters of credit, and article 8 with stocks, bonds and other longer term paper. Article 1 sets out many general principles and definitions, some of which affect substantive law. Only articles 2 (sales of goods), 6 (bulk transfers) and 9 (secured transactions) are likely to deal directly with tangible property. Only articles 2 and 9 are likely to touch realty interests.

when it was standing timber it was realty. And article 9 on secured transactions deals with security interests[3] in many kinds of collateral—some, such as secret processes and other "general intangibles,"[4] some of which may not even be represented by pieces of paper and some of which is extremely tangible. Section 9-104, in several subsections, seems to disavow contact with realty, but article 9 nonetheless covers crops and minerals, and also approaches the other end of the personal property scale in its regulation of security interests in goods which, whatever their past, have a real estate present but coupled with the fear of a chattel future—goods which have been or will be affixed to, or otherwise closely associated with particular real estate. For want of a better name, article 9 applies to this class of property the traditional if imprecise catchall label of "fixtures."[5]

One can scarcely conceive of anything more in the nature of land or real estate than clay soil or the solid stone underneath it. Yet the stone may be cut and removed from the land, and the clay may be made into bricks and stored in a building supply house, and thus both may become chattels, but are unlikely to remain chattels for long. They are almost sure to be incorporated into a building and thus reconverted into real estate and returned to the domain of real estate law—and so completely so that the person who was the true owner or mortgagee of them as personal property cannot ever get them back or retain any interest in them.[6]

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3. The defininition of "security interest" is essential. It is defined in § 1-201(37) as follows:

> "Security interest" means an interest in personal property or fixtures which secures payment or performance of an obligation. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer (Section 2-401) is limited in effect to a reservation of a "security interest." The term also includes any interest of a buyer of accounts, chattel paper, or contract rights which is subject to Article 9. The special property interest of a buyer of goods on identification of such goods to a contract for sale under Section 2-401 is not a "security interest," but a buyer may also acquire a "security interest" by complying with Article 9. Unless a lease or consignment is intended as security, reservation of title thereunder is not a "security interest" but a consignment is in any event subject to the provisions on consignment sales (Section 2-326). Whether a lease is intended as security is to be determined by the facts of each case; however, (a) the inclusion of an option to purchase does not of itself make the lease one intended for security, and (b) an agreement that upon compliance with the terms of the lease the lessee shall become or has the option to become the owner of the property for no additional consideration or for a nominal consideration does make the lease one intended for security.

4. See UNIFORM COMMERCIAL CODE § 9-106 and comments thereto.

5. Whether this term should have been abandoned in article 9, as it was done in article 2, is discussed *infra*, beginning at page 557.

6. See, *e.g.*, the Massachusetts court's discussion in Pierce v. Goddard, 39 Mass. (22 Pick.) 559, 562 (1839): "The materials used in . . . construction [of the new house] ceased to be personal property, and the owner's property in them was divested as effectively as though they had been destroyed.

Harder problems arise where both personal property law and real estate law govern simultaneously. Growing crops, in the absence of notice to the buyer of the real estate, may become the property of that buyer.[7] But if the proper filings have been made, one who has bought or taken a security interest in the crops prior to their severance from the land will prevail over a subsequent purchaser of the realty.[8]

Where standing timber is to be cut or minerals are to be mined, or growing crops are sold, there is a period of time in which personal property law (the Code) and real estate law govern simultaneously. That period of time is likely to be short; when severance has been completed, the law relating to goods takes sole command.[9] On the other hand, in the case of "fixtures," goods used so as to become part of the realty for some purposes, while retaining their chattel identity for other purposes, the dual realty-personalty character is permanent, unless and until the goods are removed from the realty.

It is obvious that where personalty become realty, or realty becomes personalty, or personalty becomes part-realty and part-personalty, conflicts are bound to arise between those whose interests are primarily in the land and those whose interests are primarily in the goods. Two sets of equally deserving and equally legitimate goals may come into sharp conflict and competition. One who has bought a farm or a woodlot may reasonably expect to get the crops[10] or the standing timber[11] growing on it unless given warning that rights in this property have been transferred to a mortgagee or other purchaser. One who has bought a house may legitimately expect that he has bought the furnace and the bathtub along with it, and the purchaser of a factory should be able to ascertain whether he is also buying the industrial furnace in it. The mortgagee who finances the farm owner, the home owner or the factory owner has, if anything, a greater interest in knowing that a stranger cannot remove crops, timber, minerals or the domestic or industrial furnace. But one who has made loans against the crops, or enabled the former owner of the house or factory to buy the new furnace "on time," has an equally

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7. Se, for example, the English Bills of Sale Act, 41 Vict. ch. 31, § 7 (1878).

8. UNIFORM COMMERCIAL CODE §§ 2-107(2), (3), 9-105, -301, -303. Compare English Bills of Sale Act, 41 Vict. ch. 31, § 7 (1878). For pre-Code law, see 1 WALSH & NILES, CASES ON PROPERTY 34, 37, 41, 45, 49 (1939).

9. *Compare* UNIFORM COMMERCIAL CODE § 2-103 *with* § 9-313.

10. UNIFORM COMMERCIAL CODE § 2-107. See Heavilon v. Heavilon, 29 Ind. 509 (1868); Turner v. Cool, 23 Ind. 56 (1864); Pool v. Rutherford, 336 Ill. App. 516, 84 N.E.2d 650 (1949); BROWN, PERSONAL PROPERTY § 162 (2d ed. 1955).

11. UNIFORM COMMERCIAL CODE §§ 2-107(1), (3). See Armstrong v. Lawson, 73 Ind. 498 (1881).

strong interest in being able to get a good security interest in these goods-associated-with-realty and remove them if he is not paid.

Public policy should encourage the financing by real estate mortgagees of fixtures (and possibly of other goods used along with land) and it should also encourage secured financing which makes it feasible for non-real estate mortgagees to finance crops or supply fixed assets used with the land. The Code's draftsmen attempted to achieve both of these aims and to reconcile the conflicts between them. Their solution—at least in principle—probably comes closer to resolving what are by nature almost unresolvable conflicts than anything which has yet been achieved. And since they were attacking one of the most difficult and complex areas of the law—the area where real estate and personal property collide and coalesce—it should not be too surprising that their language and mechanics do not always perfectly effectuate their principles.

The most difficult problems in the realty-personalty area under non-Code law will remain the most difficult under the Code—the fixture problems. No statute which adequately handles the fixture area, even if it is perfect to the last detail, can be simple to understand and utilize. And the Code's fixture provisions, though unassailable in principle, fail to achieve their objectives in some important practical respects.[12] The upshot is that, as the Code comes into force across the country, both the lawyer who represents real estate mortgagees and the chattel security lawyer will be confronted with a series of problems. Some of these will be old friends, carry-overs from the prior law, and others will be new. Some are inherent in the nature of things while others could be eliminated by a perfect fixture law. But in every case the most immediate concern of the working lawyer will be the practical solution of the particular problem confronting him.

But even where realty remains realty, and personal property retains its character as personalty, one sales contract or one mortgage may cover everything from general intangibles, like trade or utility franchises,[13] to land. The combination chattel realty mortgage is sufficiently common to merit attention. Railroads and other public utilities, as well as some industrial corporations, quite regularly mortgage both personal and real

12. See generally Coogan, *Security Interests in Fixtures Under the Uniform Commercial Code,* 75 HARV. L. REV. 1319 (1962).

13. Public utility fronchises are often subjected to utility mortgages, even where the purchaser at a foreclosure sale would be able to use the franchise only after approval by appropriate regulatory authority.

property in the same instrument.[14]

It is the purpose of this article to offer suggestions for solving some of the problems which are bound to confront both the real estate lawyer and the chattel security lawyer as the newly enacted Uniform Commercial Code comes into contact with the old, non-uniform real estate law of his state. We shall occasionally refer by way of example to the fixture law of Indiana and of some neighboring states, but the discussion is intended to be much wider than the law of any one state. Perhaps this purpose can best be achieved by first determining the effect of the Code upon real estate transactions generally, with a minimum attention to fixtures, and secondly exploring some of the Code's fixture problems.

## I. Effect of the Uniform Commercial Code on Realty Transactions, with Emphasis on Non-Fixture Aspects

We may begin our discussion with property usually thought of as real estate which, on severance and to some extent before severance, may be treated as personalty.

A. *Crops and Real Estate Which Become Goods Upon Severance.* Under section 2-102, the sales article "applies to transaction in goods"; and might appear to have no relation to realty. But goods are defined in section 2-105 to mean

> all things . . . which are movable at the time of identification to the contract of sale. . . . "Goods" also includes . . . growing crops and other identified things attached to realty as described in the section on goods to be severed from realty (Section 2-107).

This section, together with section 2-107, is consistent with the idea that crops may be realty for some purposes.[15] The term "crops" and the phrases "other identified things attached to realty" and "goods to be severed from realty" are of more than passing interest. In comment 1 to section 2-105, the draftsmen say:

> Growing crops are included within the definition of goods since they are frequently intended for sale. The concept of "industrial" growing crops has been abandoned, for under modern practices fruit, perennial hay, nursery stock and the

14. The typical public utility mortgage covers both personalty and realty under the same instrument. Double filing is often required, but some states have special filing provisions for utility mortgages.

15. See notes 10 & 11 *supra,* and accompanying text. *Cf.* English Bills of Sale Act, 41 Vict. ch. 31, § 7 (1878).

> like, must be brought within the scope of this article. . . .
>
> The use of the word "fixtures" is avoided in view of the diversity of definitions of that term. This Article in including in its scope "things attached to the realty" adds the further test that they must be capable of severance without material harm thereto. As between the parties any identified things which fall within the definition becomes "goods" upon the making of the contract for sale.

It should be noted in passing that until the revisions made in 1956 the draftsmen of article 9 had likewise avoided the use of the term "fixtures."

The substantive provisions with regard to this kind of goods are contained in section 2-107, which is sufficiently important to be reproduced here in its entirety:

> Goods to be Severed from Realty: Recording
>
> (1) 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.
>
> (2) 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 the seller, even though it forms part of realty at the time of contracting, and the parties can by identification effect a present sale before severance.
>
> (3) 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.

Section 2-107 largely speaks for itself—the rights of the parties may be governed in part by the Code and in part by the state's realty law. But some points may be noted. The material harm test obviously does not apply under subsection (1) of section 2-107 but does under (2). Interesting questions may arise as to what categories are included in each.

Subsection (1) does not apply unless severances are to be made by the seller, and presumably he will not sever if too much harm is to be done thereby. If a real estate mortgagee is involved, presumably the mortgagee must look to real estate law for his protection, if any.

Apparently the kind of items referred to in the first sentence of section 9-313(1)[16]—goods incorporated into the realty—are covered by subsection (1) of section 2-107, and what article 9 calls "fixtures" are covered by subsection (2) of section 2-107. One who so desires is free to buy a fixture without purchasing the land itself—and here article 2 applies a severance-without-material-harm test. No such test applies to a fixture secured party's right of removal under section 9-313(5), but since the secured party must reimburse the holders of realty interests for all physical damage caused by removal, he is unlikely to remove unless he believes that he can be made whole in no other way. Finally, subsection (3) of section 2-107 confirms the impression given by subsections (2) and (1)—the Code does not say that goods to be severed may not be realty for some purposes.[17]

Under subsection (2) of section 2-107, the sale of growing crops is subject to the Code, and regardless of who is to sever them. But filing of the contract in the land records might well be required under subsection (3).[18] Note that here the filing with respect to sales of crops is

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16. The first sentence of § 9-313(1) reads: "The rules of this section do not apply to goods incorporated into a structure in the manner of lumber, bricks, tile, cement, glass, metal work and the like and no security interest in them exists under this Article unless the structure remains personal property under applicable law."

17. Section 2-107 is largely consistent with pre-Code law. It was held in Indiana, under the UNIFORM SALES ACT § 76, IND. ANN. STAT. § 58-606 (Burns 1961) that growing crops raised annually by labor (*fructus industriales*) were personalty, and could be the subject of an oral contract of sale. Ax v. Schloot, 116 Ind. App. 366, 64 N.E.2d 668 (1946).

It has been held that a contract for the sale of standing timber is a sale of an interest in realty, and must comply with the statute of frauds, Cool v. Peters Box & Lumber Co., 87 Ind. 531 (1887), but that a parol contract for the sale of timber to be severed by the purchaser gives a revokable license to the purchaser to enter on the land to make such severance. *Ibid.* Note that § 2-107(1) provides that only if the timber is to be removed by the *seller* is there a contract for the sale of goods. This was the majority view before the Code. See BROWN, PERSONAL PROPERTY § 164, at 829-30 (2d ed. 1955).

Under pre-Code law in Indiana a sale of minerals in the land is a sale of an interest in realty. Cypress Creek Coal Co. v. Boonville Mining Co., 194 Ind. 187, 142 N.E. 645 (1924). An Indiana statute provides that interests in oil and gas in the ground are interests in realty. IND. ANN. STAT. § 46-1803 Burns 1952). The statute was intended as declarative of the common law, IND. ANN. STAT. § 46-1805 (Burns 1952), and was not specifically repealed by § 10-102 of the Code or enacted by the Indiana Legislature.

18. There is some doubt as to whether Indiana realty law would require such a filing. The Indiana recording statute is IND. ANN. STAT. § 56-119 (Burns 1961), which provides: "Every conveyance or mortgage of lands *or of any interest therein,* and every lease for more than three [3] years shall be recorded in the recorder's office of the county where such lands shall be situated." (Emphasis added.) Do growing crops come within the phrase "or of any interest therein?" Clearly, at least, a sale of land, without

made in the real estate records, but a security interest in the same crops may or may not be recorded in that office, depending upon the version of section 9-401 adopted in a particular state.[19]

In other respects also the treatment of "things attached to the realty" or "crops" under article 2 is not on all fours with the treatment of their counterparts under article 9. Unlike article 2, article 9 in its present form does not "avoid" the use of the word "fixtures," though, on the other hand, it does not define them. Subsection (f) of section 9-105 reads as follows:

> "Goods" includes all things which are movable at the time the security interest attaches or which are fixtures (section 9-313) . . . . "Goods" also include . . . growing crops. . . .

The term "crops" is nowhere defined, but article 9 includes a new term "farm products" which is defined in subsection (3) of section 9-109 as follows:

> Goods are . . .
> (3) "farm products" if they are crops or livestock or supplies

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more, carries with it crops standing thereon. Heavilon v. Heavilon, 29 Ind. 509 (1868); BROWN, PERSONAL PROPERTY § 162 (1955). But, as stated in note 17 supra, fructus *industriales* are personalty under the Uniform Sales Act. And under the Indiana Chattel Mortgage Act of 1935, IND. ANN. STAT. §§ 51-501 to -521 (Burns (1951) *all* "crops," and even "forestry products" are subject to that act. See note 24 *infra*. Thus, while the Uniform Sales Act and the 1935 Chattel Mortgage Act were in effect, Indiana law was in accord with the majority view; contracts for the sales of *fructus industriales* and mortgages of all crops and forestry products would not have to be filed in the realty records. BROWN, PERSONAL PROPERTY § 164, at 824-25 (1955).

But what about contracts for the *sale* of *fructus naturales* or forestry products? And contracts for the sale of minerals in the ground? Under non-Code law these are realty interests. Further, the Uniform Sales Act and the Chattel Mortgage Act are repealed by the Code. What effect does the repeal of those acts have on Indiana law? Ar we thrown back to the law in effect prior to the adoption of those statutes?

The problems presented by § 2-107(3) are somewhat similar to those created by § 9-313(1), which looks to non-Code law for the definition of "fixtures." See note 70, *infra* and accompanying text. Under non-Code law the determining factor, in the absence of special statutory provision, as to whether realty law applied to an interest was whether the interest was "realty." The Code answers that question for some purposes, but does it answer it for all purposes? One way out of this dilemma is to interpret § 2-107(3) as recognizing an obligation to file a contract for the sale of growing crops, standing timber or minerals in the ground only where a non-Code statute specifically requires it, but the safer practice is to file on the assumption that without a filing a buyer of the land could take the crop.

19. Section 9-401 of the official text provides options for the legislatures. Under one option, all filing is done with the Secretary of State. Under the other and more commonly adopted option, local filing is specified for certain collateral. When the collateral is crops, the second option provides for double filing: the county of the debtor's residence, and the county where the land on which the crops are growing or to be growing is located. Often, of course, these two locations will coincide.

In Indiana, Illinois, Kentucky and Ohio the second option, providing for local filing, is in force. In Michigan, security interests in crops are filed with the Secretary of State.

> used or produced in farming operations or if they are products of crops or livestock in their unmanufactured state . . . 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 or inventory. . . .

Article 9's special statute-of-frauds provision of section 9-203 requires that the security agreement contain "a description of the collateral and in addition, when the security interest covers crops or oil, gas or minerals to be extracted, or timber to be cut, a description of the land concerned." Section 9-402 states: "When the financing statement covers crops growing or to be grown or goods which are or are to become fixtures, the statement must also contain a description of the real estate concerned."

Note that under section 9-401(b) fixture security interests are filed in the office "where a mortgage on the real estate concerned would be filed or recorded." But under one alternative left open to the adopting states there is no requirement whatsoever that filings for security interests in crops (as distinguished from sales of crops which may be required to be recorded with the realty records under subsection (3) of section 2-207) be filed in the same office as the realty records unless it so happens that chattel security and real estate security transactions are filed in the same office; and even where all filings are made in the same office, there may be three non-correlated sets of records; realty, fixtures and chattels.

Two sections of the Code indicate a paternalistic attitude toward the farmer which may seem strange in a state such as Indiana where the typical farmer is a very substantial citizen, and sometimes a corporation. The Code generally makes it easy to get an automatic security interest in after-acquired property. Section 9-204(4), however, severely limits the operation of this doctrine where crops are concerned. It provides

> No security interest attaches under an after-acquired property clause (a) to crops which become such more than one year after the security agreement is executed, except that a security interest in crops which is given in conjunction with the lease or land purchase or improvement transaction evidenced by a contract, mortgage or deed of trust may if so agreed attach to crops grown on the land concerned during the period of such real estate transactions. . . .[20]

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20. It is not clear under § 9-204(2)(a), as to whether a three year "crop" of alfalfa or a fifteen year crop of apples is to be treated the same as a one year crop of wheat or corn. Under that section no security interest can attach "in crops until planted

Section 9-312(2) is the other section which hinders, perhaps unduly, the ability of the farmer to mortgage future crops. It provides:

> 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 obligation 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 priority would seem so limited as to be of questionable practicable value to anyone, but would, nevertheless, cut down on the assurance that could be given to any person who relies upon getting a security interest in future crops. Thus, the combination of sections 9-204(4) and 9-312(2) would seem to severely limit the value of an after-acquired property clause with respect to crops.[21]

As has been noted, section 2-107(2) seems to recognize the fact that for some purposes crops constitute realty. Hence it may be that the Code allows the creation of a security interest in crops by way of a real estate mortgage but this subject to cut-off by a sale or the creation of a Code security interest.[22] However, there is no positive statement in

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or otherwise become growing crops." Does one planting of alfalfa produce a single crop, or one crop a year, or three crops a year for purposes of § 9-204? Apparently the security interest could attach when planting takes place, but the point is not too important because of the limitations to one year under § 9-204(4)(a) except as otherwise therein provided.

21. The Indiana Chattel Mortgage Act of 1935, IND. ANN. STAT. §§ 51-501 to -521 (Burns 1951), which is superseded by the Code, is confusing in this respect. Section 51-501, which is perhaps too specific in its denotations of proper agricultural subjects for chattel mortgages, would seem to provide the following: There is no time limit on after-acquired livestock, poultry, "vertebrates" and bees [§§ 51-501(a), (b), (c), (f)]; future "crops" may not be mortgaged except those to be planted within one year from the date of the mortgage [§ 51-501(e)]; future fruits, nuts, berries, and "any and/or all horticultural, viticultural, and/and or forestry products" may not be mortgaged except those expected to *mature* within one year of the date of the mortgage.

The confusion is compounded by § 51-515, which provides that mortgages strictly on personalty must be refiled after three years, but that mortgages covering both realty and personalty are good for 20 years, and further "that such mortgage, deed of trust, or other indenture shall be a valid and continuing lien upon all property therein described or referred to, including, if . . . so provided, all after acquired personal property. . . ." What effect does this general provision have upon the earlier specific provisions relating to crops? Probably none, but an extension of the time limit as to crops mortgaged with the realty would not be inconsistent with the last part of § 9-204(4) of the Code.

22. Where the mortgagor of the realty is yet in possession, a purchaser or mortgagee of the crop may remove it over the objection of a prior mortgagee of the realty . . . unless the crop is specifically covered in the prior mortgage

article 9 with respect to obtaining a mortgage on crops under real estate law, as there is a statement in section 9-313(1) with respect to "fixtures." Apparently the security interest in crops given in conjunction with the lease or land purchase under section 9-204(4)(a) would not be a real estate crop mortgage but rather a Code security interest given along with a real estate mortgage.

We should note the difference between (i) security interests in next year's corn crop which can't be planted until next May and (ii) security interests in a crop of alfalfa hay which was planted two years ago but may be good for another two years. Section 9-204(2)(a) is not perfectly clear on this point, but it would seem that so far as subsection (2)(a) is concerned one can cause a security interest to attach when the alfalfa first becomes a growing crop but section 9-204(4) generally limits its interest to crops growing within the year. The problem here is not necessarily the same as that under section 2-401 where there must be a sufficient identification for a sale to become effective.

Even assuming that the Code goes less than all the way in validating security interests in after-acquired property so far as crops are concerned, its provisions will still be helpful: Under no circumstances should it be necessary to file a financing statement more than once in five years. The financing statement needs only to "indicate the types" of collateral to be covered and need not disclose whether future interests of any kind will be covered under an existing agreement, or any number of future agreements. A financing statement need not be tied to any particular security agreement or number of security agreements nor need it mention whether or not future property is to be covered. However, the secured party must insist that a new security agreement reasonably identifying the newly planted crops is executed and delivered to him by the debtor whenever new crops are planted.[23]

The principal rule of section 9-204(4) seems to be in accord with

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and a receiver has been appointed. . . . The problem varies according to the exact wording of the mortgage, the local statute . . . etc. See general annotation 47 A.L.R. 772-74; L.R.A. 1917-C. 49-52.

2 Walsh & Niles, Cases on Property 49 (1939). The Indiana Chattel Mortgage Act of 1935, § 2, Ind. Ann. Stat. § 51-502 (Burns 1951) seems to favor the crop chattel mortgagee, but it does not say that there could not be a real estate mortgage on crops. The case law is largely silent on the point. In one case, however, Lincoln Nat'l Bank & Trust Co. v. Nathan, 215 Ind. 178, 19 N.E.2d 243 (1938), the court indicated that the chattel mortgage statute and the realty recording statute were mutually exclusive. *Id.* at 186, 19 N.E.2d at 246. *Cf.* English Bills of Sale Act, 41 Vict. ch. 31, § 7 (1878).

23. See Uniform Commercial Code §§ 9-204(2), (4). *Cf.* English Bill of Sales Act, 41 Vict. ch. 31, § 7 (1877).

pre-Code chattel mortgage law of Indiana,[24] Illinois[25] and Wisconsin.[26] Why the laws of states where the typical farmer is a businessman who farms are so paternalistic is hard to understand. Perhaps some share-croppers in certain states do not show the judgment necessary to avoid mortgaging their future if permitted to do so, but this would not seem to be true of the majority of the farmers of states like Indiana, Illinois and Wisconsin. Is there greater need to protect an owner of a 100 acre farm from his folly than there is to protect the businessman who runs the village shoe repair shop? Must that "protection" apply to the 1,000 acre farmer? And should the farmer not be trusted to turn over the proceeds of a sale of his crops in the way the automobile dealer must be trusted to turn over the proceeds from the sale of cars "entrustde" to him?[27] Or is it that crops alone require special rules? The farmer seems to be classed with those individuals who are not businessmen—those who purchase consumer goods.[28] But the farmer, except to the

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24. See note 21 *supra.* Section 2 of the Indiana Chattel Mortgage Act of 1935, IND. ANN. STAT. § 51-501 to -521 (Burns 1951), probably gives more protection as to future advances than does § 204(5) of the Code. The Chattel Mortgage Act provides that the lien created by the mortgage is good against everybody except "the landlord's lien as now provided by law." Sections 9-204(3) and (5) of the Code recite that a mortgage may secure future advances but say nothing as to the priority. The secured party could count upon obtaining priority as to future crops only to the extent that he comes under the first-to-file rules of § 9-312(5)(a), and this is further limited by § 9-204 as well as by § 9-312(2) which gives priority to a subsequent advance given to enable the debtor to produce the particular crop—analogous to a purchase money security interest. At least so long as the crops are growing crops perfection under the Code can be achieved only through filing. If the crops had been severed, it is possible that one who made an advance on the basis of a warehouse receipt or other possessory lien could come ahead of the first filer as to subsequent advances made by the first filer. See UNIFORM COMMERCIAL CODE § 9-312(5)(b).

Section 9-205 is an expanded form of § 5 of the Indiana Chattel Mortgage Act, which provides that livestock which are mortgaged along with hay and other feed may eat such feed, and generally that mortgaged consumables may be used to preserve or fatten other mortgaged chattels. This would carry out the most recent legislative policy of the state. Nevertheless, section 9-205 expands this concept to allow the disposition of all collateral by the mortgagor.

25. See Annotations to ILL. ANN. STAT. ch. 26, § 9-204 (Smith-Hurd 1963).

26. For a good discussion on crop financing in Wisconsin, written with reference to an earlier draft of the Code, see COATES, LAW AND PRACTICE IN CHATTEL SECURED FARM CREDIT (1954). At p. 12 and following Coates discusses the Wisconsin prohibition against mortgages on future crops and the various attempts to circumvent it, most of which he thinks will be unsuccessful.

27. The usual rule of § 9-307(1) that one who buys in the ordinary course of business takes free even of a security interest he knows about does not apply to farm products. The financer of automobiles must look to the proceeds of the sale of his collateral, since he cannot reclaim the car from a buyer in the ordinary course of business. The rule applies to sales at wholesale as well as at retail. But theoretically one who buys a peck of appes at a farmer's roadside stand takes them subject to a security interest, of which he had no actual knowledge, in the apple crop. For the nature of present day "farmers," see the revealing analysis by Higbee in FARMS AND FARMERS IN AN URBAN AGE, TWENTIETH CENTURY FUND (1963).

28. Consumer goods become such only when they are bought for the use of the

extent of his "consumer goods," can "mortgage his future" as to other assets—his farm equipment and even his farm products other than crops. The Code's provisions in section 9-204 and 9-307 continue pre-Code law —but why was pre-Code law so backward on these points? Or can it be that the law allowing mortgages of after-acquired property other than crops is wrong? But we should be thankful for small favors. The Code does make it clear at least that a farmer can borrow against crops not yet planted if they will be planted within one year.

The application of the Code to interests in timber to be cut and minerals before severance has some similarities and some dissimilarities with its treatment of crops, and again the treatments under articles 2 and 9 have likenesses and differences. Under Section 2-107 the Code applies to a contract of sale if the seller is to sever, but no present sale takes place until severance unless there has been an effective transfer under real estate law. A purported security interest can "attack" prior to severance. A security agreement entered into prior to severance can, therefore, do no more than *provide for* a Code security interest to arise upon severance, unless, by complying with real estate law, the agreement is also a real estate mortgage. There can be no Code security interest in standing timber comparable to a Code interest in growing crops. The language of Section 9-203 which requires a "description of the land concerned" is not quite accurate in its reference to a security interest in standing timber, etc.,—by the time the security interest comes into being, the timber will no longer be standing. There likewise can be no Code security interest in minerals before extraction.

B. *The Combined Mortgage of Realty and Personal Property Including Crops and Fixtures.* Those who lend and those who borrow money on real estate have often found it advantageous to augment their basic land-and-buildings collateral with property which is or once was movable, but which has become somehow associated with particular land. This mutual advantage has given rise to the "combined" mortgage—one which may cover the spectrum of property classes: real estate, fixtures and other personal property, tangible and intangible.

The enactment of the Code has certain obvious consequences for the combined mortgage. Those which are created after the Code's effective date must comply with article 9 as well as with real estate law. This is so because article 9 governs every "transaction (regardless of its form) which is intended to create a security interest in personal property or

buyer or his family. The definition from § 9-109 reads: "Goods are (1) 'consumer goods' if they are used or bought for use primarily for personal, family or household purposes. . . ."

fixtures. . . ."[29] Fixtures may be used as security either through an "encumbrance" created under real estate law (*e.g.*, a real estate mortgage, mechanic's lien)[30] or a security interest created under the Code.[31] But if a post-Code mortgage which covers personal property as well as real estate is not perfected under article 9, it will not be perfected at all so far as the personal property is concerned.

The Code has other noteworthy, if somewhat less obvious, consequences for the combined mortgage. While its article 9 is generally not applicable to real estate, and while fixtures may be encumbered apart from it, the uncertainty involved in the classification of property is such that even mortgagees who feel that their mortgages cover only real estate and fixtures and no personal property would be ill-advised to disregard it. Further, while section 9-313(1) expressly preserves any non-Code law which allows a real estate mortgage to cover fixtures, the Code contains no comparable provision with respect to crops. Obviously safe practice calls for an article 9 filing whenever crops are to constitute part of the security, even where there is a real estate filing which covers crops. And, while the Code has no applicability prior to its effective date, article 9 may have important effects on combined mortgages which though created prior to its effective date, continue to exist after that date, if any of the collateral could be classified as either crops or fixtures. A detailed analysis is in order.

C. *Some General Conclusions.*

1. Real Estate Transactions, Whether Pre-Code or Post-Code, Are Not Affected by the Code If Neither Fixtures Nor Personal Property (Including Crops) Are Covered.

Article 9 "applies so far as concerns any personal property and fixtures. . . ."[32] It "does not apply . . . except to the extent that provision is made for fixtures in Section 9-313, to the creation or transfer of an interest in or lien on real estate, including a lease or rents thereunder. . . ."[33] Thus the enactment of the Code will have no effect on mortgages which cover land and land alone, whether they were executed prior to the Code or thereafter. But if a note secured by a mortgage is

29. Uniform Commercial Code § 9-102(1)(a).
30. It has been held that a filing of a mechanic's lien is inconsistent with a claim that the goods are subject to removal by the vendor. Osborne, Mortgages § 217 n.53.
31. Section 9-313(1) seems to distinguish between a real estate law *encumbrance* and a Code *security interest.*
32. Uniform Commercial Code § 9-102(1).
33. Uniform Commercial Code § 9-104(j).

used as collateral in another transaction, the Code applies to the pledge of the note and the mortgage whether or not some recording under real estate law is required for the assignment of the mortgagee's interest in the mortgage.[34]

Though estates for years are for some purposes considered personal property, the Code would not seem to cover the mortgage of a lease on realty.[35] And the Code "does not apply . . . to a lien given by statute or other rule of law for service or materials. . . ."[36] Hence mechanic's and materialmen's liens may be obtained pursuant to the statutes which have always governed.

### 2. A Real Estate Lien Which Covers Fixtures, But No Personal Property, Can Be Created, Perfected and Enforced Under Ordinary Real Estate Mortgage Law or Under Mechanic's or Materialmen's Lien Statutes.

The Code "does not prevent creation of an encumbrance upon fixtures or real estate pursuant to the law applicable to real estate."[37] While the statutory language speaks only of the "creation" of an encumbrance under real estate law, it must mean creation, perfection and enforcement under real estate law.[38] Consequently, when the same secured party is claiming both fixtures and realty, he may well choose to have his rights as to fixtures determined under real estate law. And even where the person claiming an interest in fixtures is not a real estate mortgagee, he may, under certain unusual circumstances, prefer to bring himself under the protection of his state's mechanic's or materialmen's lien statute.[39] There may be occasions where a fixture supplier who did not make a timely filing under the Code may be able to file or record under the state's mechanic's lien statute and get some advantage which section 9-313 would not give him.

But since both a real estate mortgage and a mechanic's lien normally create interests in the property as a whole and ordinarily do not allow removal by the secured party of the property added by him, whether or not a fixture, they would seldom seem adaptable to creating effective security interests in fixtures where one person is claiming an interest in

34. See Uniform Commercial Code § 9-102(3) and comment 4 thereto.
35. Uniform Commercial Code § 9-104(j).
36. Uniform Commercial Code § 9-104(c).
37. Uniform Commercial Code § 9-313(1).
38. Coogan, *Security Interests in Fixtures Under the Uniform Commercial Code*, 75 Harv. L. Rev. 1319, 1349 (1962).
39. The Indiana mechanic's lien statutes are Ind. Ann. Stat. §§ 43-601 to -603, 43-701 to -709 (Burns 1952).

the real estate generally and a different person is claiming an interest in fixtures. Ordinarily where a security interest in fixtures alone is claimed, resort will and should be made to the Code. There is particularly good reason for this where the collateral is close to the nebulous dividing line between fixtures and personal property and might be held not to be a fixture but personal property instead. If the purported "fixture" is ultimately held to be personal property, a security interest perfected only under real estate law may be ineffective against a trustee in bankruptcy.[40] Morover if the secured party does not perfect his interest under the Code, he will not have the choice of enforcing his remedies separately against the fixtures, a choice which in many cases would provide a complete remedy without resort to the generally slower mechanics of real estate enforcement.

### 3. The Code Will Not Apply to Pre-Code Mortgages, Even Though They Cover Personal Property and/or Fixtures, Unless, After the Code's Effective Date, New Debt Is Created or New Personal Property (Including Crops or Fixtures) Are Added.

The official draft of the Code is concluded by article 10, "Effective Date and Repealer." This contains section 10-102(2), which is entitled "Provision for Transition" and which provides:

> Transactions validly entered into before the effective date . . . [of the Code] and the rights, duties and interests flowing from them remain valid thereafter and may be terminated, completed, consummated or enforced as required or permitted by any statute or other law amended or repealed by this Act as though such repeal or amendment had not occurred.

In adopting the Code, a number of states have seen fit to vary the content and numbering of this section.[41]

Apart from the confusion and problems created by the variations from the official text, section 10-102(2) makes it fairly clear that pre-Code transactions which involve no subsequent advances and no subsequent additions of property are completely outside the Code. This is so despite the use of the word "may." Although this might appear to suggest some power in the parties to elect to be covered by the Code rather than by pre-Code law, this is not a permissible construction. Such a

40. Coogan, *supra* note 38, at 1338.
41. Ohio's attempt on this score is discussed by Auerbach & Goldston, *Variations in the Ohio Enactment of the Uniform Commercial Code,* 14 W. Res. L. Rev. 22 (1962).

right of election would create serious practical problems. Had the draftsmen intended it, they would have expressly provided for it.[42] The parties can, of course, execute and file a new instrument which makes this a "transaction" under section 9-102, and this new transaction would be subject to the Code.

There is, however, an important exception to the generally valid proposition that pre-Code mortgages are not affected by the Code so long as no transactions creating a security interest thereunder in personal property or fixtures occur after the effective date of the Code. Where the old chattel security law under which the mortgage was created called for refiling at specified intervals and one of the refiling dates falls after the Code's effective date, the refiling is impliedly required to be done under the mechanics of the Code, rather than under the no longer existent mechanics of the old law.[43] But the fact that a refiling required by the old law is done under the Code should not mean that the Code's enforcement provisions will thenceforth govern the mortgage. In such circumstances, the Code should be viewed as a mere amendment to the old law, which, pursuant to section 10-102(2), continues to govern the enforcement of mortgages created under it.[44] And, when problems of enforcement are under consideration, it should not be forgotten that section 9-501(4) allows a mortgagee whose mortgage covers real estate and personal property to enforce the whole thing under real estate law.

### 4. Where, After the Code Becomes Effective, New Debt Is Added Under a Pre-Code Mortgage Whose Coverage Includes Personal Property (Including Crops or Fixtures), or New Personal Property Is Added. The Only Safe Procedure Is to Comply with the Code.

The post-Code creation of new debt or coverage of new personal property under a pre-Code instrument would seem to constitute a section 9-102(1)(a) "transaction . . . which is intended to create a security interest in personal property" and therefore to fall under the Code. An argument can be made that if pre-Code law covered present and future fruit or other products of trees, or plants, *with no new planting*,[45] old law

42. Coogan & Bok, *The Impact of Article 9 of the Uniform Commercial Code on the Corporate Indenture,* 69 Yale L.J. 203, 210-12 (1959).

43. *Ibid.* See, *e.g.*, Ind. Ann. Stat. § 51-515 (Burns 1951).

44. Coogan & Bok, *supra* note 42.

45. Compare the twelve month's limitation under § 2-501(1)(c) with that of subsection (4)(a) of 9 9-204. It may be that each annual apple crop or each of the three annual harvestings of alfalfa is to be considered a separate crop for purposes of article 9 as well as for purposes of article 2.

would continue to govern. If new plantings are made, the Code would seem to take over as to that collateral, and reliance upon an after-acquired property clause of a pre-Code mortgage would be unwise in any event. If the collateral involved in the transaction consists only of realty and fixtures, and both the language of the instrument and the non-Code law are adequate to cover security interests in the fixtures, the Code may be disregarded. But since, as noted above, in most states there is, as a matter of practice if not as a matter of theory, a great deal of uncertainty as to what constitutes a fixture, caution would seem to dictate bringing the transaction under the Code if the collateral includes anything in addition to straight and obvious realty. This precaution applies, of course, to crops.

Perhaps the Code's bearing on post-Code transactions under pre-Code mortgages can best be understood in terms of an example. Suppose that prior to the effective date of the Code, Mortgagor gave Real Estate Mortgagee a mortgage covering existing real estate, existing fixtures and existing personal property (including crops) and property in any of these three classes which may thereafter be acquired. The mortgage secures both present debt and debt which may be contracted in the future. In other words, the mortgage contains both an after-acquired property clause and a future advance clause. After the effective date of the Code either (i) Real Estate Mortgagee makes an advance or (ii) Mortgagor plants a new crop (section 9-204) or purchases a new hot water heater or some other item which under applicable law is either a fixture or personal property. In either event, one of section 9-102(1)(a)'s "transactions" has occurred and Real Estate Mortgagee, to be safe, should insist upon the execution and Code filing of a supplemental mortgage.

Such a supplemental mortgage may be a one-page instrument which "reasonably identifies" the collateral as required by section 9-110 and 9-203, contains the filing data required by section 9-402 and reaffirms the after-acquired property and future advance clauses of the original mortgage. If desired, it may of course be longer and contain additional parts of the old mortgage, though this is not necessary for Code purposes.

If such a mortgage is executed in accordance with the Code, it will pick up future advances and after-acquired personal property of the kinds described, subject only to the necessity for later confirmations as to future crops and after-acquired consumer goods (see section 9-204). If an adequate financing statement has been filed, no future filing will be necessary until the expiration of the five year period provided for in section 9-403.

Unless the Code and the pre-Code state law make it clear that the collateral in question is, or is not, a fixture, the only safe procedure is to file the new financing statement in the place or places specified in section 9-401(1)(a) on the assumption that the property is straight chattels and again in the place specified in section 9-401(1)(b) ("the office where a mortgage on the real estate concerned would be filed") on the assumption that the property is a fixture. If the collateral added is later held to be realty (*i.e.*, not a chattel and not a fixture) neither filing will be effective. If new real estate is to be covered, additional filing or recording as a real estate mortgage may also be required. Whether or not that recording is required will depend on the real estate law of the state in question, which, insofar as it relates to straight real estate, will not be changed by the enactment of the Code.[46]

D. *Difficulties in the Mechanics of Filing Under the Code.* Nothing in the Code prevents the inclusion in one instrument of security interests in both real estate and either fixtures or chattels (including crops) or all three. And a single instrument could be drawn in such a manner that, if properly filed, it would create perfected security interests in all classes of property. Such an instrument would follow the basic form of the traditional real estate mortgage, but would also describe chattels and fixtures, and comply with the formal requisites of a financing statement, as set forth in section 9-402 (signatures and addresses of both parties, etc.). But no single filing could fully perfect such an instrument. Double filing—as a real estate mortgage and as a security interest in chattels—would be the minimum; and, should the secured party desire to have the right to enforce as to the fixtures alone, without foreclosing the basic real estate mortgage, triple filing—as a fixture as well—will be necessary. Thus, many combination mortgages may be filed (or recorded) three times: (i) in the real estate office in accordance with the requirements of real estate law, including, of course, the payment of the applicable real estate recording or filing fee, (ii) in the same office, but in accordance with the Code, as a fixture, including the payment of the Code's filing fee, (iii) in the proper office or offices in which Code chattel filings must be made, including the payment of another Code filing fee. And depending upon the filing provisions adopted by particular states, additional filings may be required as well under the Code, *e.g.*, in one office

46. It has been stated that in Indiana a mortgage of realty may properly provide for coverage of after-acquired property. See INDIANA LAW ENCYCLOPEDIA *Mortgages* § 64 (1959). The only case cited in support thereof, however, was an 1898 case which dealt with the inclusion of after-acquired *personalty* in a mortgage of realty. Mortgage Trust Co. v. Moore, 150 Ind. 465, 50 N.E. 72 (1898).

for crops ("farm products") and in another for other chattels, or in a local and in a central filing office.[47]

The necessity for multiple filing may be an inescapable result of the parties' including under one instrument property governed by differing laws, or of their inability to determine what a future judge or jury will decide is a fixture; or it may be the result of trying to give the most effective form of notice to parties likely to be interested, or it may be attributable only to incomplete correlation between real estate and code filing systems.

A number of non-Code statutes have devised means of allowing combination mortgages to be completely perfected through single filings. Some such statutes have been general,[48] and others have been specifically concerned with public utility company mortgages.[49] All have had the obvious advantage of eliminating filing detail and expense. And this can be done at virtually no cost; if such statutes make proper provision for the cross-indexing of their single filings, they can give notice to everyone who might be interested. Such special filings break the theoretical symmetry of the law, but usually the class of debtors affected is sufficiently specialized that no real harm is done. It would seem clear that some sort of cross-indexing single filing scheme should be worked into the Code. Some states, in different ways have attempted to do this.[50] In Ohio, however, the enactment of the Code was unfortunately accompanied by the repeal of the state's old single filing statute.[51] This oversight, together with other problems of the nature discussed herein, led Ohio to throw out the baby with the bath water. R. C. 1309.32(b) as it will be amended effective October 8, 1963 makes it practically impossible for a vendor to sell on secured credit anything which might be held to be a fixture unless he obtains the consent of all holders of any interest in the real estate. Particularly where publicly held bonds are outstanding, such consents may well be in fact unobtainable.

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47. Section 9-401 specifies the same filing office for most collateral likely to be used by a farmer. There could, however, be some non-farm assets included in an overall farm mortgage which would require filing in a different office; in addition it may be necessary to file as to crops in the realty records.

48. *E.g.*, 121 Ohio Laws 374 (1945), former codification, OHIO REV. CODE 9 1309.03.

49. These are fairly numerous. See, *e.g.*, CONN. GEN. STAT. REV. § 16-217 (1958); ILL. ANN. STAT. ch. 95, § 51 (Smith-Hurd Supp. 1962); N.Y. LIEN LAWS § 231.

50. In 1960 Massachusetts added a new § 9-401 and made some adjustments in other sections. See also, New York's version of § 9-302, which saves N.Y. LIEN LAW § 231, which provides for joint filings of combination mortgages of corporations. The Indiana provision is § 9-401(1)(c), which provides for filing "when the debtor is a corporation in all cases except . . . [fixtures], in the office of the Secretary of State." Multiple filing as to realty, fixtures, and chattels is not eliminated thereby, but the possibility of double filing by a corporation when the collateral is crops is precluded by that provision.

51. 121 Ohio Laws 374 (1945), former codification, OHIO REV. CODE § 1319.03.

Another noteworthy aspect of the Code's filing mechanics is the absence of any directions to filing officers on how fixture filings should be handled. Section 9-401(1)(b) simply provides that fixture filings must be made "in the office where a mortgage on the real estate concerned would be filed or recorded." There is no assurance that fixture filings made in the appropriate registry of deeds or record's office will find their way into indices usable by real estate title searchers. In some instances, they have not been properly indexed. In fact, it has been reported that for a short time after the Code became effective in different states some county recorders followed the practice of placing fixture filings in shoe boxes, making no index whatsoever with respect to them. A clarifying amendment containing specific indexing provisions (including special provisions where registered land is concerned) is clearly needed. Pending such an amendment, the real estate title searcher should acquaint himself with the filing practice followed in his locality and proceed accordingly.[52]

And, regardless of his location, the searcher should note that the sponsors' text of section 9-402 requires only that a fixture financing statement contain the names of the debtor and the secured party and "a description of the real estate concerned." There is no requirement that it contain the name of the record owner of the "real estate concerned," though several states have followed Massachusetts in adding such a requirement.[53] Often the debtor and the record owner will be one and the same person, but in cases where this is not so (*e.g.*, where the debtor is a tenant), a search in the name of the record owner would give no notice of a properly filed security interest in a fixture on the premises concerned. While the tenant's possession should serve as a red flag in such situations, there is still need for legislative correction. Fixture financing statements should be required to contain the name of the record owner as well as the name of the debtor where the two are different. Until such an amendment can be made, real estate title searchers should search fixture records in the name of all persons whom they know to have had possession of the premises as well as in the name of the record owners. And those giving opinions on real estate titles should include appropriate qualifications in their opinions.

52. Parenthetically, it should be noted that the real estate searcher may have to look in non-real estate records for crop mortgages. The applicable version of § 9-401(1)(a) may provide for filing "in the office of the [County Recorder] in the county where the land on which the crops are growing or to be grown is located," but that does not mean that such filings are necessarily correlated with realty records.

53. Some of these states are listed in the comments to UNIFORM COMMERCIAL CODE (Uniform Laws Annotated) § 9-402.

## II. Effect of the Code on Chattel Type Security Interests in Fixtures

Thus far, the Code has been viewed largely from the standpoint of the real estate bar. The focus has been on the combination mortgage—an umbrella security instrument under which basic real estate collateral is augmented by personal property and fixtures. Now the focus shifts to the fixture security instrument, which covers fixtures separately from the land to which they are affixed, and thus to the province of the chattel security bar. But this does not mean that the lawyer who represents real estate mortgages should stop reading. Quite the contrary. He may find that his problems are best illuminated in the indirect light of a discussion addressed primarily to the chattel security man.

A. *Some Code Sources of Confusion With Respect of Fixtures.* The Code's fixture provisions are necessarily complex. But they are also unnecessarily confusing—and particularly so if read in chronological order. The Code's first reference to fixtures may be found in its general definitional section, 1-201, whose subsection (37) defines "security interest" as "an interest in personal property *or fixtures* which secures payment or performance of an obligation."[54] This suggests that all security interests in fixtures fall under the Code, and this suggestion is reinforced by the language of section 9-102(1).[55] As has been seen, however, this is not so. Security interests in fixtures may be created and enforced outside the Code, under real estate law.[56]

The next reference to fixtures appears in section 9-104(j). It and the references which appear in sections 9-105(f), 9-302(1)(c) and (d), and 9-307(2) suggest that 9-313 is a comprehensive and all inclusive fixture section, containing a complete law of fixture security interests. On the other hand, section 9-313's title, "Priority of Security Interests in Fixtures" suggests that it deals only with priorities, and section 9-312(1) suggests that it is even narrower than that, dealing only with priorities between fixture security interests and interests in real estate. In fact, the truth lies somewhere between these conflicting suggestions. While section 9-313 is more than a priorities section, it by no means contains a comprehensive law of fixture security interests.

A number of other Code sections relate to fixture security interests. Section 9-204, for example, determines the time of attachment and 9-303 the time of perfection; 9-401 specifies the place of filing; 9-402 the requirements of a fixture financing statement; 9-312 the priorities be-

54. Emphasis added.
55. See note 29 *supra* and accompanying text.
56. See Uniform Commercial Code §§ 9-313(1), 9-501(4).

tween different fixture security interests; and part 5 of article 9 relates to remedies generally.

But even if one struggles through a reading of section 9-313 in conjunction with all of these other sections, he will not emerge with a comprehensive picture of the Code's rules as to fixture security interests. This is so because, with respect to fixtures, the Code has sharply departed from its general practice of identifying its subject matter and delimiting its scope through the rather complete definition of terms. Instead, section 9-313(1) provides that: "the law of this state other than this Act determines whether and when . . . goods become fixtures."

While this kind of provision is unhandy in that it requires the lawyer to lay aside his statute book and search for case law, it would not be seriously objectionable if a fairly clear body of case law, the rules of which were compatible with the Code's general design, existed. Unfortunately, however, the law of fixtures is a tangle of confusion and inconsistencies. Anyone who attempts to analyze it will come to appreciate the frustration which was expressed by the Supreme Court of Washington in *Strain v. Green*:[57]

> We will not undertake to write a treatise on the law of fixtures. Every lawyer knows that cases can be found in this field that will support any position that the facts of his particular case require him to take. . . .
>
> There is a wilderness of authority. . . . [Fixture cases] are so conflicting that it would be profitless to undertake to review or harmonize them.

Not only is non-Code law a poor place to find a usable definition of a fixture;[58] in a number of states its underlying principles are ir-

57. 25 Wash. 2d 692, 695, 172 P.2d 216, 218 (1946).

58. A quotation from the standard English work on the subject is in point:

> The term *fixtures* is used by writers with various significations; but it is always applied to articles of a personal nature which have been affixed to land. Very frequently no further idea is intended to be conveyed by the term than the simple fact of annexation to the freehold; and hence have arisen the popular expressions of landlord's fixtures and tenant's fixtures; of removable and irremovable fixtures. The name of fixtures is also sometimes applied to things expressly to denote that they *cannot* legally be removed; as where they have been annexed to a house, &c., and the party who has not affixed them is not at liberty afterwards to sever and take them away. Thus, it has been said that an article shall fall in with the lease to the landlord, or descend to the heir with the inheritance *bcause* it is a fixture.
>
> The term *fixtures*, however, may, it is thought, be most accurately defined as denoting those personal chattels which have been annexed to land so as to become part of it, but which *may* be afterwards severed and removed by the person who has annexed them . . . against the will of the owner of the freehold. But, it should be observed, that the term has been used by the Courts

reconcilable with the Code's fixture scheme. Central to the Code's fixture provisions is the right to remove: If a secured party with a pre-affixation interest fully satisfies the conditions set forth in section 9-313, he may, on the debtor's default, sever the fixture from the real estate to which it has been attached, and this notwithstanding the objections of third parties who hold mortgage or other interests in the real estate.

But, under the non-Code law of some of the most important states which have enacted the Code, one version or another of the view that was expressed in *Teaff v. Hewitt*[59] (which is generally considered the leading American case on the law of fixtures) prevails: "A removable fixture as a term of general application, is a solecism—a contradiction in words."[60] The court said further: "A fixture is an article which was a chattel, but which by being physically annexed or affixed to the realty, became accessory to it and part and parcel of it."[61]

The import of this can perhaps best be grasped in terms of an example. Let us take the problem of creating a security interest in a furnace. Suppose that Furnace Dealer wishes to sell a hot air furnace to Home Owner, the furnace to be installed in Home Owner's house, which is mortgaged to Local Savings and Loan. Home Owner cannot conveniently pay cash, and his credit does not justify a sale on open credit; so Furnace Dealer proposes to take a security interest in the furnace. To have any real value, such a security interest must do what the Code contemplates; it must entitle Furnace Dealer to remove the furnace if he is not paid. And the right to remove will depend on the furnace's property classification. If, on affixation, the furnace becomes straight real estate, it cannot be removed over the objections of Local Savings and Loan. If instead it only becomes a fixture, its removability will depend on Furnace Dealer's having made a proper fixture filing. If it remains straight

and amongst text writers without much precision; and it is difficult to determine in which of the above senses it is most frequently employed. On the whole it will be found that, in cases which do not immediately involve the question of removability, the term is generally used as denoting merely articles which, on account of their annexation to the freehold, have ceased to be chattels.

The above definition divides itself into two branches; first, a consideration of what is meant by annexation; secondly, what is intended by a right of removal against the will of the owner of the freehold.

AMOS & FERARD, ON THE LAW OF FIXTURES AND OTHER PROPERTY PARTAKING OF A REAL AND PERSONAL NATURE (3d ed. 1883) (Citation omitted.) Some of the meanings in which the learned English authors are using fixtures have no bearing on chattel security law; a security interest in a fixture without the right to remove is practically meaningless.

59. 1 Ohio St. 511 (1853).
60. *Id.* at 524.
61. *Id.* at 527.

personal property, Local Savings and Loan will have nothing to say about its removal, whether or not a filing has been made.

Suppose that our hypothetical furnace is installed in a Massachusetts home. Furnace Dealer's lawyer must then examine the Massachusetts non-Code law to determine "whether and when" the furnace becomes a fixture. In doing so, he will come upon *General Heating & Appliance Co. v. Goodwin*,[62] which held that a hot air furnace, even though practically all of it could be removed without injury to the realty, had become part of the realty and could not be removed without the consent of the holder of a prior real estate mortgage. The opinion does not use the word "fixture," but simply holds that the furnace had become real estate. In fact, this seems to be the position of all Massachusetts case law. It recognizes only two classes of property—real estate, which cannot be removed over the objection of one with an interest in the realty, and personal property, which can always be removed, notwithstanding failure to file or record. This rigid all-or-nothing approach gave considerable difficulty to chattel security lenders, and out of this difficulty arose a Massachusetts statute[63] which allowed the removal of a list of specified articles, providing that filings with respect to them had been made in the real estate records. The list included furnaces. But the statute has been interpreted to permit removal only as against *subsequent* mortgages of the real estate.[64] And, more important, it was expressly repealed by the Massachusetts act which enacted the Code.

The situation would be no better if Home Owner were an Ohio resident. The *Teaff v. Hewitt* idea that a removable fixture is a contradiction in terms has already been observed. Ohio law regards fixtures as a species of the genus realty. And it has been held that a furnace is this kind of a fixture. In *Holland Furnace Co. v. Trumbull Sav. & Loan Co.* the court refused to allow an unpaid conditional vendor to remove his furnace over the objections of a holder of an earlier real estate mortgage.[65]

62. 316 Mass. 3, 54 N.E.2d 676 (1944). See Wedge v. Butler, 136 Me. 189, 6 A.2d 46 (1939). *Compare* Central Lithograph Co. v. Eatmor Chocolate Co., 316 Pa. 300, 175 Atl. 697 (1934); Clary v. Owen, 81 Mass. (15 Gray) 522 (1860). Massachusetts is not thought of as a state which accepts either the industrial plant mortgage doctrine of Pennsylvania, or the "institutional" doctrine of New Jersey, but the reasoning of the Massachusetts court in *Goodwin* would seem natural to a Pennsylvania or a New Jersey lawyer. See note 67 *infra*.

63. Mass. Acts 1912, ch. 245, former codification, as amended, MASS. ANN. LAWS ch. 184, § 13.

64. Gar Wood Indus. v. Colonial Homes, 305 Mass. 41 (1940).

65. 135 Ohio St. 48, 19 N.E.2d 273 (1939). The 1963 amendment to the fixture section of the Code may go further than did this case in making it difficult for a vendor to sell a furnace on secured credit.

If our hypothetical furnace were in New Jersey, the situation would at first appear to be more propitious. New Jersey was among the first states to reject the Massachusetts rule that once a chattel had been sufficiently attached to realty, it could never again be severed without the consent of all holders of security interests in the real estate, including prior mortgagees, who could not have relied on the after-affixed property's being a part of their collateral.[66] New Jersey was one of the earlier states to adopt the Uniform Conditional Sales Act which codified the doctrine that under some circumstances the fixture conditional vendor could remove it, unless its removal resulted in material injury to the real estate. Most courts interpreted this to mean physical injury.[67] But in the 1930's the New Jersey courts enunciated the institutional doctrine: If an affixed article is essential to the operation of the realty building, it cannot be removed even though its removal causes no physical injury, and regardless of how the security interest in it has been perfected.[68]

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66. Campbell v. Roddy, 44 N.J. Eq. 244, 14 Atl. 279 (1888).

67. The New Jersey cases are discussed in an excellent report entitled, *Communication From the Law Revision Commission to the Legislature Relating to Conditional Sales of Fixtures,* LEG. DOC. No. 65(M), in 1942 N.Y. LAW REVISION COMM'N REP. 673. The report was written by Professor William Farnham of the Cornell Law School. Farnham states on p. 12 (1942 REP. at 682) that "the Court of Errors and Appeals in October 1932 first adopted the Institution Doctrine in Domestic Elec. Co. v. Mezzaluna, 109 N.J.L. 573, 162 A. 722."

This apparently is strictly correct, but the seeds of the Institutional Doctrine may well have been sown in the pre-Uniform Conditional Sales Act cases of New Jersey which applied the test of whether or not the security of the realty interest was diminished by subsequent action of the conditional vendor and the debtor. See the excellent article by Ralph N. Kleps entitled *Uniformity versus Uniform Legislation: Conditional Sales of Fixtures,* 24 CORNELL L.Q. 394 (1939): "The New Jersey cases followed the great case of *Campbell v. Roddy,* and they held that the security interest of the conditional vendor would be protected so long as removal would not diminish the security to which the holder of the realty interest was entitled." *Id.* at 398.

The Uniform Conditional Sales Act, § 7 of which deals with fixtures, was adopted by New Jersey in N.J. Laws of 1919, ch. 210, §§ 1-32. Under that act the right to remove fixtures was conditioned upon the lack of material injury to the real estate. Courts in other states had held that this meant physical injury to the land. *E.g.,* Harvard Fin. Corp. v. Greenblat Constr. Co., 261 N.Y. 169, 184 N.E. 748 (1933). See also Peoples Sav. & Trust Co. v. Munsert, 212 Wis. 449, 249 N.W. 527 (1933). The New Jersey courts, however, probably building upon their own equitable doctrine that the conditional vendor could remove if the interest of the mortgagee of the realty was not diminished, and quite possibly influenced by the industrial plant doctrine of the integrated plant mortgage doctrine of Pennsylvania, held that the material injury included economic injury to the realty. See generally Kratovil, *Fixtures and the Real Estate Mortgagee,* 97 U. PA. L. REV. 180 (1948); Robinson, McGough & Scheinholtz, *The Effect of the Uniform Commercial Code on the Pennsylvania Industrial Plant Doctrine,* 16 U. PITT. L. REV. 86 (1955); Leary, *Financing New Machinery for Mortgaged Pennsylvania Industrial Plants,* 4 VILL. L. REV. 498 (1959).

68. Professor Grant Gilmore, reporter for article 9 from 1946 until 1952, and a member of the national sponsors subcommittee on article 9 from its inception, is himself certain that § 9-313 was intended to abolish the institutional doctrine of New Jersey and

It should by now be apparent that the non-Code law of Massachusetts, Ohio and New Jersey as to the meaning of the term "fixture" is fundamentally out of harmony with the Code's fixture scheme. The same is to some extent true of Pennsylvania and its integrated plant mortgage doctrine. That law denies what under the Code is the most important attribute of a fixture: removability. Obviously, the bases on which such law determines "whether and when . . . goods become fixtures" have no functional relationship whatsoever to the Code's fixture provisions.[69] Accordingly, a choice must be made. Either the old law

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the plant mortgage doctrine of Pennsylvania. See his *The Purchase Money Priority,* 76 HARV. L. REV. 1333, 1360-63, 1397-98 (1963). But this intention, so clear to the chief draftsman of article 9, is not so obvious to others. Professor Ferguson, of Rutgers School of Law, in his annotations to § 9-313 published by the New Jersey Commission to Study and Report upon the Uniform Commercial Code, states the belief that the institutional doctrine is abolished as to the test of the secured party's right to remove, but that it may still be applicable in determining what is a fixture. Robinson, McGough & Scheinholtz, *supra* note 67, seem to have made the same assumption as to the effect of the Code on Pennsylvania law. The difficulty is that if the Code does not abolish the institutional doctrine and the plant mortgage doctrine, courts may be misled into holding that the hot air furnace in Massachusetts or the New Jersey oil burner is neither personal property nor the kind of fixture which the Code makes removable by the secured party who has seasonably filed, but it is realty and not affected by the Code's fixture provisions. See nn. 62, 64, 67.

69. Of course, in most states it was recognized, before the Code, that certain chattels, although affixed to realty, could be removed under certain circumstances. Thus, wherever the Uniform Conditional Sales Act was in force there could be removal of certain fixtures under § 7, which provided in part:

> If the goods are so affixed to realty at the time of a conditional sale or subsequently as to become a part thereof and not to be severable wholly or in any portion without material injury to the freehold, the reservation of property as to any portion not so severable sholl be void after the goods are so affixed as against any person who has not expressly assented to the reservation. If the goods are so affixed to realty at the time of a conditional sale or subsequently as to become part thereof but to be severable without material injury to the freehold, the reservation of property shall be void after the goods are so affixed as against subsequent purchasers of the realty for value and without notice of the conditional seller's title, unless the conditional sale contract, or a copy thereof, together with a statement signed by the seller briefly describing the realty and containing the name of the owner thereof and stating that the goods are or are to be affixed thereto, shall be filed before such purchase in the office where a deed of the realty would be recorded or registered to affect such realty.

But this statute is repealed by the Code whenever the Code is enacted. Is the case law thereunder still relevant when determining the existence of a "fixture" under state law, as required by § 9-313(1)? Probably not.

It would be necessary, then to turn to case law prior to the enactment of the Uniform Conditional Sales Act. Even here, in some states, the courts recognized that certain chattels affixed to realty could be removed. The cases are inconsistent, however, as to whether such a chattel is a "fixture" or not. Thus, an Indiana case, Citizens Bank v. Mergenthaler Linotype Co., 216 Ind. 573, 25 N.E.2d 444 (1940), stated that "fixtures" were "part of the real estate" and not removable. It held, however, that linotype machines were "personalty" and could be removd by a conditional vendor as against a subsequent realty mortgagee with notice. An earlier case, New Castle Theater Co. v. Ward, 57 Ind. App. 473, 104 N.E. 526 (1919), involving the right to certain property as between a lessor and a lessee, did recognize that "fixtures" may be removed if certain of fixtures must be partially disregarded and the Code's basic philosophy effectuated, or the Code's fixture sections must be reduced to little more than an absurdity by the rigid and literal application of the old law. The enlightened choice, and the choice which the courts should make, is to read 9-313 so that it makes sense, and then read its sense into non-Code law.

B. *How to Make Sense Out of the Code's Fixture Provisions.* Difficulties in interpreting a complex and technical statute can often be alleviated by considering the general problems to which it is addressed and determining the basic policies that it adopts toward them before attempting to ascertain its application to particular fact situations. If this sort of approach is taken with respect to the Code's fixture provisions, it will soon become apparent that they have a design and that, in general, it is a sensible and salutary one. When this has been apprehended, their application to particular situations will be far easier to grasp.

As has been seen, whenever a security interest is taken in essentially movable property which has become closely associated with particular land, there arises a potentiality for conflict—conflict between the holder of the security interest and holders of interests in the real estate. And no one can say that the interest of one is less worthy than the interest of the other. It is proper and desirable for real estate purchasers (whether or not they be mortgagees) to purchase not only the bare land itself, but also property which is closely associated with and used along with the land. And it is equally proper and desirable for non-real estate mortgagees to supply and retain security interests in fixed assets used along with the land. Consequently, the conflict cannot be intelligently resolved by eliminating or unduly restricting either of the two competing interests; what is instead needed is an accommodation between them. This is what the Code has attempted to achieve.

The Code's accommodation is built around a special class of property: "Fixtures." And despite section 9-313(1)'s express definitional abdication, when the Code speaks of fixtures, it refers to what is at least a partially defined legal concept, a class of property which functions in a particular and unique way. In other words, the Code's provisions do contain, albeit indirectly, something of a definition of a fixture. Sec-

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legal standards are met. But cases involving contests between lessors and lessees are not generally helpful in determining priorities of secured creditors.

But in those cases, the end result was not really affected by whether the chattel was a "fixture" or not. The central issue was removability. The Code, on the other hand, has already determined the issue of removability. It wants something different from non-Code law, but it cannot in the end, hope to receive it. Non-Code law was preoccupied with removability. When that is taken away, non-Code law becomes of little value.

tion 1-201(37) says that a Code security interest may exist in either "personal property or fixtures." This suggests that personal property and fixtures are two different classes of property. This suggestion is reinforced by section 9-105(f) which distinguishes fixtures from movable goods. And article 9 repeatedly provides that fixtures are to be treated differently from "personal property." Sections 9-401 and 9-402 require that fixture filings be made in both a different place and a different manner from those prescribed for personal property filings. Section 9-313 speaks of goods "becoming" fixtures, implying that on affixation they are transformed, changed in legal character.

And not only are the Code's fixtures separate and different from personal property, they are also separate and different from real property. In either case fixtures are subject to special rules different from those applicable to realty or personalty. Thus, our analysis is helped by treating fixtures as a class by themselves.

The Code contains an express delineation of the boundary line between fixtures and real property. The first sentence of section 9-313(1) provides: "The rules of this section do not apply to goods incorporated into a structure in the manner of lumber, bricks, tile, cement, glass, metal work and the like and no security interest in them exists under this Article unless the structure remains personal property under applicable law." Thus, when goods are incorporated into a structure, they become straight real estate. No Code security interest can exist in them; they can be encumbered only under real estate law. And, in accordance with the second sentence of section 9-313(1), which speaks of "*other* goods becom[ing] fixtures" (emphasis added), they are the *only* goods which become real estate. Goods which are merely attached to a structure in some manner short of incorporation into it do not become real estate; they either remain non-fixture personal property or become fixtures.

As has already been observed, the second sentence of 9-313(1) reads:

> The law of this state other than this Act determines whether and when other goods become fixtures.

So has the fact that the non-Code law of many states views a fixture as a non-removable part of the real estate and is consequently out of harmony with the Code.[70] Under the Code, removability is of the very essence of a fixture. Subsection (5) of 9-313 provides:

> When under subsections (2) or (3) and (4) a secured party has priority over the claims of all persons who have interests in

70. See note 69 *supra* and accompanying text.

> the real estate, he may, on default, subject to the provisions of part 5, remove his collateral from the real estate but he must reimburse any encumbrancer or owner of the real estate who is not the debtor . . . for the cost of repair of any physical injury, but not for any diminution in value of the real estate caused by the absence of the goods removed or by any necessity for replacing them.

In other words, if under section 9-313(2), (3) and (4) a fixture secured party achieves priority over holders of interests in the real estate, he may, on the debtor's default, remove his fixture collateral. Rightly or wrongly, a fixture secured party is given full priority over *existing* interests in the realty, provided only that his security interest has *attached* prior to affixation, even if his interest is never perfected; he may achieve priority over subsequent realty interests by making a timely fixture filing. Sections 9-401(1)(b) and 9-402(1) describe a fixture filing. It is made by means of a financing statement which contains all of the provisions necessary for a straight chattels financing statement and which, in addition, describes the real estate concerned. And it is filed "in the office where a mortgage on the real estate concerned would be filed or recorded." In other words a fixture filing is one which will give constructive notice of a fixture security interest to future purchasers—including mortgagees—of the real estate.

At this point, the Code's structure and the nature of its accommodation between real estate claimants and movable property claimants should have emerged. For the purpose of determining rights of those who claim under security arrangements respecting personal property associated closely with real estate, the Code divides the world of collateral into three separate classifications. On the one hand, there is real estate—property incorporated into a structure—which is non-removable and which can only be encumbered under real estate law. On the other hand, there is personal property—property which has not been appropriated to particular real estate in such a manner that real estate purchasers can reasonably expect to purchase it along with the land—which is freely removable notwithstanding the objections of holders of interests in the real estate on which it happens to be situated. In the middle, there are fixtures, and their unstated but nevertheless real Code definition can now be apprehended. We might call the first two categories "straight" realty and "straight" personalty, to distinguish them from fixtures which have some characteristics of each, but are different from both in some respects. Fixtures are removable, if not freely movable property; they have not been incorporated into a structure in the manner of bricks and mortar.

But they have been so affixed to particular real estate that, absent proper notice to the contrary, a future purchaser (including a mortgagee) of the real estate may reasonably expect to, and in fact does, purchase them along with the land. If, however, a chattel security man gets a good security interest in a fixture and properly perfects it—that is, he files so as to give notice to real estate purchasers (and does so at the right time) —he retains his interest, and with it the right to remove, as against such purchasers.

C. *A Practical Example.* For the last few pages the discussion has been proceeding on a perhaps uncomfortably theoretical level. Accordingly, a concrete example would now seem appropriate. Suppose the Debtor operates a building supply business on land mortgaged to Savings Bank. To obtain a loan, he gives Finance Company a security interest in all of his inventory. The inventory collateral includes 100,000 bricks stacked in his yard, 1,000 bags of cement and 500 bags of mortar piled in his warehouse, a portable electric heater, and the component parts of a hot air furnace. At this point, all of this collateral is normal inventory—personal property—and it may be encumbered under a normal inventory lien, perfected under the Code's provisions applying to personal property. And, of course, Savings Bank as real estate mortgagee has no interest in the inventory. Movable goods, although they may be destined to become realty or to become fixtures, do not become such until they are appropriated for use with particular real estate. Prior to such appropriation, chattel filing rules—not realty recording nor the special fixture filing rules of section 9-401 and 9-402—apply.

But now an additional development. Suppose the bricks, mortar and cement are used to build another warehouse on Debtor's land, and that the hot air furnace is installed in this warehouse. Though they are the self-same goods, the bricks, mortar and cement are now related to real estate in a drastically different manner. In legal terms—both those of the Code and of the law generally—they have lost their character as movables and become part of a particular piece of real estate by accretion or something akin thereto. The closeness of the association between the realty involved and the bricks, mortar and cement, together with the disproportionate relationship between the extent of the damage to the realty which removal would occasion and the comparatively small value of the goods when removed is such that social policy requires that the chattel security man be forbidden to remove the former chattels which were once his collateral—and this regardless of the kind of security interest he may have had in them and regardless of how it may have been perfected.

The parts of the furnace, however, are in a different category. While affixed to and closely associated with the new warehouse and thus with the real estate, they have not been "incorporated" into it as have the bricks and mortar. Unlike the bricks and mortar, the furnace could be removed with little damage to itself or to the warehouse. Consequently, under the Code the furnace should be considered a fixture, the sort of property in which a chattel type security interest and right to remove may exist. And if the furnace is considered a fixture, the Code would allow Finance Company to remove it if Debtor did not pay—and this notwithstanding the fact that Finance Company made no fixture filing. Sections 9-313(2) and (4) provide that when a security interest attaches to goods before they become fixtures, it prevails over all interests in the real estate that existed prior to affixation. This arrangement is sensible. Since the furnace was movable personal property of another when Savings Bank acquired its mortgage on the real estate, Savings Bank could not have counted on it as being a part of its collateral. Consequently, Savings Bank would not be hurt if Finance Company removes it. (Whether it is injured by the removal of the old furnace is a different question, only indirectly affected by the Code's rules.)

The furnace is not only different from the bricks and mortar; it is also different from the portable electric heater, which, let us suppose, is now being used in the original warehouse. Unlike the furnace, this heater has no particularly close association with the real estate. While it is now customarily used there, its only physical connection is through an electric cord and plug. By its very nature, it is freely transferable to a different location and service with different realty. Thus, the heater falls into the straight personal property category, as did the bricks and mortar when they were inventory. Because it is personal property, Savings Bank has no interest in it as real estate mortgagee. And, even if after Debtor had begun to use the heater to keep the warehouse warm Insurance Company were to take a second mortgage on the real estate, it would not thereby acquire an interest in the heater, nor would it expect to; in accordance with long established custom and practice, real estate purchasers do not expect to acquire the personal property which happens to be situated on the real estate purchased. If they want to buy such property, they know they must make special arrangements.

It is in this respect that the hot air furnace differs from the portable heater. While not actually integrated into the real estate, this furnace is a fixture; that is, it is so closely associated with the realty that a real estate purchaser would normally expect to buy it along with the land. For example, Insurance Company would expect its mortgage to cover the furnace as well as the warehouse itself. The Code recognized this expectation. In accordance with sections 9-313(2) and (4) a real estate purchaser can expect to prevail over the holders of security interests in fixtures then attached to his property unless he can find notice of these security interests in the real estate records. In other words, if a holder of a chattel type security interest in a fixture is to be able to remove his collateral over the objections of a subsequent purchaser (including a mortgagee) of any interest in the real estate, he must have perfected his interest by means of a fixture filing.

Another aspect of the Code's recognition of the natural expectations of those who hold interests in the real estate in general may be found in 9-313(3). This provides that a chattel type security interest that attaches to a fixture after it has been affixed to particular real estate will not give rise to a right to remove over the objections of those who held interests in the real estate at the time of its attachment. In other words, a holder of a general interest in the real estate has as an adjunct thereof an interest in the fixtures attached to it. This interest cannot be taken away or subordinated without his consent. This postaffixation security interest will be new in many states; basically it enables a fixture secured party to obtain consent of holders of existing interests in the real estate, and to come ahead of future holders by giving statutory notice to them.

D. *Prior Law and Some Suggestions as to Code Application.* The Code concept of fixtures—property which partakes of some of the aspects of personalty and some of the aspects of realty, basically removable and yet passing with the land unless there is notice to the contrary—is not original or even novel. The Code's fixture provisions are based upon section 7 of the Uniform Conditional Sales Act. This in turn was based upon the earlier statutes of four different states. While these statutes differ somewhat in content, and differ greatly in the manner in which they were applied, they all have the same central idea—which is the same as that of the Code: that there is a certain relationship between chattels and particular real estate in which the chattels become so affixed to and identified with the land that they pass with it unless there is agreement and notice to the contrary. These chattels do not merge into the real estate but remain removable if there has been such agreement and notice.

The reader who has an extra moment may find it interesting to place section 7 of the Conditional Sales Act alongside the Code's section 9-313 and compare the two. This exercise will reveal extensive similarity. One major difference is that the Code is more emphatic and more liberal with respect to the right to remove. Proper filing or no, section 7 denied the right to remove whenever goods were attached to real estate so as "not to be severable wholly or in any portion without material injury to the freehold." The Code, on the other hand, allows removal regardless of the extent of the resultant injury to the freehold, but requires the remover to pay for all such injury, whether it be great or slight.

This Code emphasis on the right to remove is extremely important. As has been seen, the idea that a fixture was a non-removable part of the realty was common in pre-Code law, and in some states succeeded in perverting the Conditional Sales Act. This perversion was accomplished by expanding the concept of non-removable real property into areas which should have been occupied by conditionally-removable fixtures. An example is New Jersey's use of the institutional doctrine to forbid removal whenever economic injury to the freehold would result. This thinking destroyed opportunities for chattel-type financing in a number of instances where it would have been commercially desirable and where the Conditional Sales Act's authors must have intended that it be available. Thus there exists an historical tendency toward overexpanding the non-removable realty classification. Our courts must take care lest this tendency run away with them and upset the balanced accommodation between realty claimants and chattel claimants that the Code is designed to accomplish.

Judges should not have undue difficulty in this regard. As has been seen, section 9-313(5) emphasizes the right of removal, providing for it even though substantial damage to the realty may result. And the first two sentences of 9-313(1) rather clearly establish the boundary line between fixtures and real estate. *Goods do not become non-removable parts of the real estate unless they are "incorporated into a structure in the manner of lumber, bricks, tile, cement. . . ." All goods which are not so incorporated into a structure remain either fixtures and conditionally removable or personal property and freely removable.* This is 9-313's cardinal rule, and fixture and chattel secured parties should be able to rely on it.

While the Code is not too clear, it is to be hoped that no court will hold that an ordinary hot air furnace, which simply has not been incorporated into a structure, constitutes realty. While the case of the furnace is rather clear, other cases will arise in which the application of the incorporation-into-a-structure test is difficult. In such circumstances, it would seem that any judicial error should be on the fixture side of the line rather than on the realty side. This is so because the fixture secured party loses everything if his collateral is wrongly held to be non-removable realty, whereas the holder of an interest in the real estate loses little or nothing if a part of the real estate is wrongly held to be a fixture. There can be no removal if the realty man really had a right to count the "fixture" a part of his collateral, and, in any event, the remover must pay for the physical damage to the remaining realty.

While the Code is fairly definite on the realty-fixture boundary line, it will be remembered that it leaves the fixture-chattel boundary line to the often inapposite vagaries of non-Code law. While this is unfortunate, it is not catastrophic, at least insofar as fixture and chattel secured parties are concerned. As long as they know their collateral is basically removable, they can protect themselves by means of multiple filing. Whenever there is any question, they should perfect as if their collateral were both a fixture and a chattel.

There can be little question but that the Code should be legislatively corrected with respect to the fixture-chattel boundary line. While fixture and chattel secured parties can adjust to the present situation by means of double filing, this is messy and wasteful. And real estate people may be seriously prejudiced. A court applying inapposite non-Code law might hold property which should be considered a fixture to be a chattel, and thus deprive a real estate mortgagee of property he had relied on. An amendment drawing the line in terms of the reasonable expectations of a real estate purchaser is definitely needed. Pending such an amendment, it would seem that the courts should exercise their ingenuity and try to work non-Code law into the Code's framework.[71] This should not prove impossible even in those states whose cases purport to recognize only two classes of property. Even in Massachusetts there are chinks in the judicial wall and something of a de facto if not a theoretical recognition of an intermediate class.

E. *Further Code Problems With Particular Reference to Bankruptcy.* Once the Code's tripartite property classification has been comprehended and the general location of the two boundary lines ascertained, the fixture rules are not too complicated. As has been seen, the Code recognizes two different types of security interests in fixtures—preaffixation interests and postaffixation interests.

Preaffixation security interests are by far the more important. They are the interests described in section 9-313(2): those which attach to goods before they become fixtures. Thus they include and in the main are composed of purchase money interests in fixture collateral, interests which prior to the Code would have been conditional sales. In this they

71. It should require no ingenuity to decide that many items called "fixtures," such as "fixtures" of a shoe store—have nothing to do with 9-313. The use of the word fixtures is not good. The English Bill of Sales Act at least carefully excludes from the fixture area certain "trade machinery." English Bills of Sale Act, § 7, 41 & 42 Vict. ch. 31 (1878).

differ from postaffixation interests, which are defined in 9-313(3) as those which "attach to goods after they become fixtures."

With respect to persons acquiring general interests in the real estate *after* they have attached, postaffixation and preaffixation security interests behave in the same way: their priority is determined by section 9-313(4). But with respect to persons already having interests in the real estate at the time of their attachment, postaffixation and preaffixation fixture security interests behave in radically different manners, as well they should. Section 9-313(3) provides that a postaffixation fixture security interest is:

> invalid against any person with an interest in the real estate at the time the security interest attaches to the goods who has not in writing consented to the security interest or disclaimed an interest in the goods as fixtures.

This is only sensible. Any other provision would allow fixture secured parties to confiscate property owned and relied upon by real estate claimants with neither compensation nor consent. But, for equally good reason, section 9-313(2) indicates that the opposite result will obtain for preaffixation security interests. They take precedence over all real estate interests existing at the time of their attachment—and this even if they are not then and never are perfected—as fixtures or in any other manner. This arrangement is generally unobjectionable because people who acquire their interests in real estate prior to the time that a particular fixture is appropriated for use with the land do not expect to obtain an interest in the fixture. They have not bought and paid for it, and any right they may obtain in it is in the nature of a windfall. Consequently, they have no real right to claim it as against the person who has supplied the money which has enabled the debtor to purchase it.[72]

Section 9-313(2) does, however, raise a problem with respect to a real estate mortgagee who supplies the money to construct a new house. Such a mortgagee might well find it disastrous to discover that shortly after the completion of the house (which, of course, had been accomplished principally with his money) a conditional vendor has removed the furnace, or the dishwasher, or the plumbing. Yet the construction mortgagee will encounter some difficulty in protecting himself against this

72. Massachusetts created a fixture class legislatively when it enacted Mass. Acts 1912, ch. 245, former codification, as amended, MASS. ANN. LAWS ch. 184, § 13. While this act was necessarily repealed by the enactment of the Code, expansion of the class to like terms will help fill the void as to what is a Code fixture.

eventuality.[73] There seems to be only one way that he can do this with any degree of completeness: Let him make sure that some of his advances are actually used to pay the vendor of the plumbing equipment, the furnace, the dishwasher, or any other fixture equipment which he considers an essential part of a salable house. It will no longer be sufficient, as it was under some pre-Code law, simply to see that the vendor has been paid. This because under section 9-107 it is perfectly possible for a purchase money security interest to be created in favor of a financer who did not supply the goods but who did furnish the money to pay for them to the person supplying them.

It is now time to consider the rights of fixture secured parties with respect to *subsequent* real estate purchasers. Here, the situation is the same whether the interest involved be preaffixation or postaffixation. In either event, the priorities are set out in section 9-313(4). In accordance with this section, fixture secured parties generally take priority over all subsequent real estate purchasers or lien holders. But a fixture security interest will not prevail over the following interests:

> (a) a subsequent purchaser for value of any interest in the real estate; or
>
> (b) a creditor with a lien on the real estate subsequently obtained by judicial proceedings; or
>
> (c) a creditor with a prior encumbrance of record on the real estate to the extent that he makes subsequent advances if the subsequent purchase is made, the lien by judicial proceedings is obtained, or the subsequent advance under the prior encumbrance is made or contracted for without knowledge of the security interest and before it is perfected.

Thus, if a fixture security interest is to prevail and permit removal over the objections of subsequent real estate purchasers, it must be perfected. Just how it must be perfected is not clear. Must there be a complete fixture perfection, or will any good faith effort to perfect suffice? For example, suppose there is a good faith error in classification: Property thought to be a chattel and with respect to which a chattel filing has been made is found by a court to be a fixture. Or suppose that a proper chattel perfection was made when the collateral was still a chattel and

73. A preaffixation security interest (under § 9-313(2)) in fixtures is very likely to be a purchase money security interest, as defined in § 9-107. A postaffixation security interest under § 9-313(3) is relatively unimportant, but gives an opportunity for a borrower to offer as security under the Code something which could otherwise be used only under the generally more cumbersome real estate law. He must, however, get the consent of present realty interst holders.

before it was possible to ascertain the location of the real estate to which it would eventually be affixed. Who loses in such cases, the subsequent purchaser of the real estate, or the person claiming the chattel-type security interest in the fixture?

It would at first seem that the chattel security man should lose. The real estate purchaser had no notice of his interest in the fixture and consequently should buy it along with the land. But when it is remembered that section 9-313(4) as it is presently written treats a creditor with a lien on the real estate in the same manner that it treats a real estate purchaser, this first impression may be abandoned. Whenever a security interest is vulnerable to a lien creditor, it may also be vulnerable to the debtor's trustee in bankruptcy under sections 60b, 70c and 70e of the Bankruptcy Act. And it would seem unlikely that the Code's draftsmen intended to weaken security interests which, though perfected, have not been completely perfected as fixture security interests to this extent, for vulnerability to a trustee in bankruptcy virtually destroys a security interest. Consequently, it would seem best to read 9-313(4)'s "perfected" as including not only fixture perfections but also chattel perfections where they were proper when made. However, there is considerable doubt as to whether courts will adopt this construction, and this doubt should serve to emphasize the need for double filings. Any chattel-type financer who conceives of a possibility that his collateral could be regarded as a fixture should file as if it were both a fixture and a chattel—that is if he wants to be safe against subsequent real estate purchasers and the debtor's trustee in bankruptcy.

Even if the suggested construction of section 9-313(4) is adopted, problems will remain, especially for real estate people. Consequently, it would seem that an amendment to 9-313 is definitely needed. It should be changed to provide that while a full-dress fixture filing is necessary to perfect as against subsequent real estate purchasers, any kind of perfection—any good faith guess as to the right manner of filing—will suffice as against lien creditors.[74] If this were done, and if fixtures are considered personalty[75] and not realty for purposes of section 60 of the Bankruptcy Act, so that preferences with respect to them are judged by the lien creditor test and not by the bona fide purchases test, all undesirable vulnerability in bankruptcy could be dispensed with. And at the same time real estate purchasers could rely on the realty records.

The Code's fixtures should be regarded as personalty and not realty for purposes of the Bankruptcy Act's section 60. They are specifically

74. See Gilmore, *Purchase Money Security Interests,* 76 Harv. L. Rev. 1333 (1963).

excluded from the realm of real estate by the first two sentences of 9-313(1) and they are basically removable.

## Conclusion

If there is one byword for the practicing lawyer which should emerge from this article it is "caution." Whenever movable property becomes associated with particular realty, caution is in order. Those holding or acquiring realty interests should exercise it. They should bear in mind the possibility that they may not be able to obtain notice of all fixture security interests from the real estate records.

Most important, both real estate claimants and chattel-type secured parties should exercise caution with respect to the classification of collateral. Double and even triple filing is in order. The cost and burden of such extra filing is unfortunate, but slight when compared with the dangers which accompany a mistaken single filing.