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An Agricultural Law Research Article

A Commerce Focus on Secured Transactions

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A COMMERCE FOCUS ON SECURED TRANSACTIONS

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The subject of this discussion is Article IX[1] of the Uniform Commercial Code. For those who are not lawyers, Article IX deals with secured transactions. Basically, Article IX gives the lender the power to go after particular property that is the subject of what is called a security interest.

There are many controversial problems in this area. Let me make it clear what I am not going to cover. I am not going to discuss a lot of the problems with default in terms of repossession; I think that is simply a subject to be covered on another day. I am going to talk about the following things: how a lender creates a security interest in property; how to go about perfecting it, and what perfection is; who prevails if there is more than one party claiming the same collateral; and how a secured party can defeat a trustee in bankruptcy, if a fellow were to get in to bankruptcy.

A. *Scope*

I am going to start with the question of scope, specifically "Does Article IX of the Uniform Commercial Code apply to your problem?" If you are a lender, that is crucial because the lender has to decide, "Do I have to comply with the formal requirements of Article IX?" If you are a trustee in bankruptcy, and you're dealing with somebody who did not comply with Article IX, obviously your concern is whether Article IX applies with that transaction. If it does apply, and the lender has not done what he is supposed to do, the trustee is going to be able to knock that secured creditor down to what is called a general creditor. General creditors get virtually nothing in bankruptcy these days.

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1. U.C.C. §§ 9-101 (1977).

The first text under Article IX is § 9-102. This section says that any transaction in which the parties intended to create a security interest must comply with Article IX. A security interest in what? That's the key. Personal property is what Article IX applies to. Personal property only; it does not apply to pure real estate transactions. Those of you from Washington have an interesting case in *Freeborn v. Seattle Trust and Savings Bank*[2] For a long time it was the only case that had specifically addressed the issue that I am now going to talk about. Suppose a land owner sells property on a land contract. The buyer then promises to pay on an installment basis. Whether it's on a six-month basis, yearly basis, or a monthly basis, you have a flow of payments coming in from the buyer to the land owner. A typical situation would be that the land owner would sell off an acreage or the homesite to keep up the flow of payments. Now suppose the former land owner goes to a Production Credit Association (P.C.A.), wishing to borrow money. P.C.A. would ask, "What do you have to put up for collateral?" The land owner would answer "I've got this contract I entered into with B." The question is what does the P.C.A. have to do as far as having an interest in the flow of payments? I had taken the position before the *Freeborn* case was decided that the flow of payments here is personal property. It is not real estate; it is personal property interest in the flow of payments. If there were to be a bankruptcy on the part of land owner, the payments ought to be in compliance with the rules of Article IX. According to *Freeborn* the flow of payments is personal property; it is either a general intangible or it is accounts receivable under the terminology of the Code. Because it is personal property, the P.C.A. must comply with Article IX. If the P.C.A. would also take whatever interest this land owner had on the real estate, they would also have to file estate records. However, if the only interest they were taking was in the flow of cash payments—personal property—only Article IX would have to be complied with.

I have mentioned several times the need to comply with Article IX. What does this mean? Quite simply it means that you have

2. Freeborn v. Seattle Trust and Savings Bank, 94 Wn.2d 336, 617 P.2d 424, (1980); *see also In re* Bristol Assoc. Inc., 505 F.2d 1056 (3d Cir. 1974); Landmark Land Co. v. Sprague, 529 F. Supp. 971 (S.D.N.Y. 1981); *rev'd on other grounds*, 701 F.2d 1065 (2d Cir. 1983).

a written security agreement granting to the P.C.A. an interest in the flow of payments. Also, there must be a financing statement filed in the appropriate Article IX records. There were a number of lenders that simply had not thought about this issue. They were treating the entire flow of payments as a real estate interest and recording them in the real estate records with no reference to Article IX. So take a look at the *Freeborn* case carefully, those of you who practice in Washington. It doesn't make any difference what side of the coin you are on, if you represent a debtor, or represent a lender, or a trustee in bankruptcy; all the things I have been talking about have equal application.

B. *Attachment*

I now turn to attachment, a key word under the code. Attachment means that the secured creditor has a right to claim particular collateral. Essentially, there are three requirements for attachment: (1) the written security agreement, granting to the lender a security interest in collateral properly described; (2) the debtor must have rights in the collateral; (3) the value must be given.[3] The agreement must meet the description requirement. The test under the Code is "reasonable identification." The agreement must reasonably identify whatever the collateral is. The question has become what is reasonable identification when you're dealing with crops, when you're dealing with livestock, or whatever it is you're dealing with in agriculture?

Take, for example, crops. First, what are crops? There is no definition of crops in Article IX. Second, what kind of crops do you have in the sense of possibilities (i.e., hay, wheat, barley, etc.)? What possibilities do you have with wheat (i.e., growing wheat, harvested wheat, stored wheat)? How do you describe all of that? Additionally, what could happen if you store that wheat in a commercial elevator? You could get a warehouse receipt or a scale ticket; a document of title.

Consequently, I am one that strongly believes that the security agreement should not use the terminology of the Code. For example, I do not think you ought to refer to something as "farm products" under Article IX. Instead, you should describe the collateral

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3. U.C.C. § 9-203 (1977).

as all harvested crops, wherever stored, all documents of title that represent stored grain, all growing crops, etc. The simple point here is to make sure you understand that "crops" covers a multitude of possibilities. Yes, you may use "crops" and get away with it, and there are some cases that have suggested that. However, I believe anyone representing a lender today must tell that lender to make sure they have crops in all their stages covered, as well as any documents of title.

What about livestock? Livestock presents some interesting problems. There are cases that firmly hold that a description like this, "all livestock, of every kind, presently owned or to be acquired," is enough to cover any additions to the herd by natural reproduction methods or by artificial insemination, for example, or purchased cattle.

There are some interesting differences of opinion with regard to how you identify livestock. Basically, there are two types of descriptions. One like I just talked about and the other which has, in addition to that general language, a list that provides for number of head, age of head, brand, and where they are located.

If there is a conflict, the importance of identifying the animals becomes obvious. A security agreement reflects whatever the parties intended. If all animals were to be covered, it seems to me that a general description is fine. But what if they did not intend for all of the animals to be covered? Also, what happens if you have replacements and you don't keep the specific list up to date? I think that a trustee in bankruptcy could argue, "you don't have all this cattle listed there, I don't care if you've got a general sort of blanket statement here; you have a specific list you will rely on and you didn't keep it up to date, therefore the only things covered are those on that list." That is the rub about any drafting; do you draft in a general way or do you draft in a more specific way? The minute you start making specific statements it seems you run the risk of leaving something out.

Regarding proceeds, Washington, Idaho, and Montana have all adopted the 1972 U.C.C. which means that the proceeds of all collateral—whether specifically mentioned or noted in the security agreement—are automatically covered. That was a change in the law for Montana because up until 1983 lenders had to specifically

refer to the proceeds in the security agreement or they were not covered. Consequently if you are involved in some litigation in Montana that originated prior to, or at least the documentation originated prior to 1983, you have different rules to deal with.

Moving on to "after-acquired property," there are some special problems here. While a complete discussion is beyond the scope of this talk, a few points must be made. For example, there were some substantial changes in bankruptcy law in 1978, one of the changes has an impact on after-acquired property. To illustrate, suppose a bank is financing the feedlot. The feedlot grants a security interest in all cattle, presently owned and after-acquired. Now suppose that this operator purchased cattle from someone else, using money out of the operating fund of the feedlot. In other words, there is no direct money obtained from the bank to finance the purchase of those animals. Now let's assume that they did that on March 1, 1984, and on May 1, 1984, there is a bankruptcy. The trustee will argue that there is a preferential transfer, under § 547(b) of the Bankruptcy Code. Under the 1978 Bankruptcy Code, inventory includes farm products. Yet that is the antithesis of the Uniform Commercial Code; inventory and farm products are separate categories of goods in the Uniform Commercial Code. However, cattle are covered in the Bankruptcy Code as inventory. Secondly, § 547(e)(3) says that a transfer is deemed to occur when the debtor obtains rights from the collateral. Under these facts, March 1 is when the debtor obtained rights in those new animals. The Bankruptcy Code says that is now the date of transfer. If there is a transfer on an account of the antecedent debt, which means a debt entered into prior to transfer, and that occurs within 90 days, the trustee can set it aside. Suffice it to say that if you represent the bank and the bank didn't provide the money, you've got a real problem because of § 547(b) of the Bankruptcy Act. However, there is an exception. Under 547(c)(5) you look at the value of the collateral 90 days before a bankruptcy, as well as the value of the collateral at the date of the bankruptcy. If there has been an improvement of the position in that 90 day period to the date of bankruptcy, the trustee can set aside only the improvement in position as a preferential transfer.

Another point that should be mentioned is that you do not have to execute a new security agreement every year under the

1972 version of the U.C.C. A security agreement, assuming you have the appropriate description, can cover future years. Under the 1962 version, a security interest could not attach to crops under an after-acquired property clause unless they became growing crops within one year of the execution of the security agreement.

I have mentioned that there are categories of goods under Article IX. There are four possibilities: inventory; farm products; equipment; and consumer goods. When dealing with agriculture, there are only two questions to ask: Do you have farm products or do you have inventory?[4] Focusing on farm products, there is a three part definition. First, you must have goods(whether crops or livestock or supplies) used or produced in farming operations or products of crops or livestock in their unmanufactured state. Generally speaking, that requirement is not hard to satisfy. The second requirement is that the goods must be in the possession of the debtor, and the debtor has to be engaged in raising, fattening, grazing, or other farming operations. As previously mentioned, the Uniform Commercial Code does not define crops, possession, or farming operations. Thus, the U.C.C. leaves it to the courts and lawyers to predict what is going to happen.

Turning to possession, there are two relatively recent Kansas cases, the only two cases that I know of that have even looked at possession at all. One of them is a bankruptcy decision, the other one is a federal district court judge's decision: *In re Roberts*[5] and *Garden City P.C.A International Cattle System*[6]. *In re Roberts* is the most recent case. In that case a lender took a security interest in growing crops. The crops were produced, harvested, and stored in the local elevator and a warehouse receipt was issued. The farmer got into difficulties and went bankrupt. The issue became, are the crops stored in the elevator "farm products", or are they "inventory?" In Kansas if they were inventory, at that time, a lender had to file with the secretary of state; if they were farm products, the lender had to file in the county where the debtor resided. The argument was made by the bank that there was constructive possession; that what you had was a bailee-bailor rela-

4. U.C.C. § 9-109(3) (1977).
5. 37 U.C.C. Rep. Serv. 1721 (Bankr. Kan. 1984).
6. 32 U.C.C. Rep. Serv. 1207 (D.D.C. Kan. 1981).

tionship between the farmer and elevator. While there was no physical possession, the Code did not require it; the Code used possession as the broader concept. Also, the wording of § 9.305 of the Code suggests that the drafters had a broad possession concept in mind. Another argument that can be made is that the drafters could have inserted the word "physical" if they wanted to restrict possession to physical possession. On the other side, the trustee argued that it was restricted to physical possession. Since the farmer did not have physical possession, the requirement was not met; therefore, there were no longer farm products and the bank was unprotected because they had filed in the wrong place. The court sided with the bank.

In *Garden City P.C.A.*, the farmer borrowed the money from the P.C.A., bought the animals, and the animals went directly to a commercial feedlot. They never were in the physical possession of the farmer. The feedlot operator then sold the animals, the P.C.A. was not paid, and the P.C.A. sued the purchaser of the animals. The question arose as to whether they were farm products. The federal district court judge held that the cattle were not in the physical possession of the debtor; therefore, they were not farm products.

The *Garden City P.C.A.* case sent shockwaves through lenders in Kansas; they had to start filing everywhere. It resulted in Kansas changing to central filing, the same central filing system used in Washington; you have to file with the Department of Licensing. In Idaho and Montana, you have to file farm products locally. You have to file in the county of the debtor's residence, so you still have this problem.

What happens if you file the financing statement and you describe the grain that is stored in a warehouse as farm products? One of the requirements of perfection is that you file in the right place, which is with the secretary of state or the Department of Licensing (for inventory or farm products in Washington). However, one other requirement is that the financing statement must have an adequate description of the goods. It can be a fatal error if you call the grain "farm products" and it is held to be "inventory." The way you get around this in Washington is very simple—you describe the goods generically and do not use the Code terminology. Also, the description in the security agreement and the financ-

ing statement should be the same. Consequently, you describe the collateral as "all grain wherever stored", and any document of title representing it, in your security agreement, and financing statement. You will not have a problem in Washington since financing statements are filed in the same place for inventory and farm products.

However, you have a different problem in Idaho and Montana; you must file in two places. Prudent insurance is to file a U.C.C.-1 (financing statement) locally and centrally and again, do not describe the collateral as "farm products" or "inventory." Describe them in a way in which any lay person would understand what collateral covered that loan.

The third requirment for farm products is that the debtor be engaged in raising, fattening, grazing, or other farming operations. If the feedlot operator is involved in fattening animals, you have "farm products." However, if that feedlot operator is feeding some and is in the business of marketing some, it is not fully clear. The Illinois case of *Farmers State Bank v. Webel*[7] suggests that you might have two types of goods. This case involved a broker who had a bad market and he decided to keep some hogs to feed out. Consequently, when the bankruptcy occurred, he was feeding the animals. The court held they were not farm products and the only reason he had the hogs essentially was because the market was bad. Because he had kept them for market reasons and could not market them, his prime operation was marketing, not feeding.

Another interesting case is the *K.L. Smith Enterprises v. the United Bank of Denver.*[8] There was a loan of over two million dollars made by the United Bank of Denver. A man wanted to start an egg business; he went to the United Bank of Denver and was sent to the agricultural loan department of that bank, where they worked out an agreement. The security agreement described the collateral as all inventory and equipment; likewise, the financial statement described the collateral as all inventory and equipment. When the business went bankrupt, there was a question as to what kind of collateral he had. The only land involved in the business was that required for a building for the egg producing hens. There

7. 112 Ill. App. 3d. 87, 446 N.E. 2d 525 (1983).
8. 28 U.C.C. Rep. Serv. 534, 2 Bankr. 28 (Bankr. D. Colo. 1980).

was no traditional farming in the sense of working the land or someone living on the land; it was a mechanized egg production business. The bank argued that it was not a farming operation, but a pure business; that it was not farming in the sense of traditional farming. On the other hand, the trustee relied on a statement in the comments to the Uniform Commercial Code § 9.109 which defines "farm products" and says the livestock "includes hens." Thus, since hens are livestock, and eggs are products of livestock, eggs are farm products. These animals are associated traditionally with farming. The court held for the trustee. The lesson here: file both ways and describe the collateral in a generic way.

In all fairness to the bank, there are some cases that suggest that a farming operation is going to be defined narrowly. But a lender cannot run the risk today in terms of the planning; if you have a litigation situation, then you have something to argue.

C. *Perfection*

Perfection is what a creditor needs to do to be protected against third parties. What perfection means is that the secured creditor must file a financing statement in the appropriate place, with the appropriate description of the collateral. However, there is a particular problem for those of you who are practicing, or lending, in Washington. The Washington Legislature, along with some of the midwestern legislatures, has changed the rules with regard to purchase money security interests, and the time required to perfect them. A "purchase money security interest" is when the lender provides the money to purchase the goods. John Deere was instrumental in getting these things changed. In essence, what happens here is the farmer goes to a John Deere dealer and they sell him a tractor or a combine, and the farmer gives back a security interest. This is a "purchase money security interest," that I like to call P.M.S.I. Under the uniform version of the Code, John Deere has ten days from the time the farmer received possession of that tractor to get the paperwork done and get the financing statement filed. John Deere argued ten days was not enough time to get the paperwork done, the documentation in order, and get it filed with the appropriate office. Thus, Washington changed the ten days to

twenty days.[9] However, the ten-day requirement in the uniform version was built into the 1978 Bankruptcy Code.[10]

Importantly, if you are giving advice to a client, you should tell him or her to operate on the ten-day framework, not the twenty-days. I will stress that the only time lenders are going to get in trouble is if that farmer goes bankrupt *within* 90 days of the filing of that financing statement. If he gets *beyond* that 90 days, you do not have a problem. Therefore, in Washington, my advice is to ignore the change in the statute; do not run the risk for that particular problem.

Now, assuming we have farm products: where do you file the financing statement? I have mentioned that in Washington you file with the Department of Licensing; in Idaho and Montana you file in the county of the debtor's residence. There are a few notes of caution for those from Idaho and Montana—there is a special requirement with regard to growing crops. In Idaho, when growing crops are involved, there must be a legal description of the land in the security agreement.[11] Also, in Montana you need a real estate description, but it does not have to be legal description. In addition, if the growing crops are located in a county other than the debtor's residence you must file a finance statement in that county as well. Thus, there is double filing for a farmer that is operating in more than one county in Idaho and Montana. This is also true if you have a corporate entity involved. Corporate entities' offices are where their principal place of business are, and if the land where they are farming is in another county, you must file in that county as well.

Montana also has a special law with regard to security interest in livestock. If the secured party wants to be protected against the world, it must also file the livestock market notice.[12]

To have perfection, there must be attachment. An attachment issue involves debtors who are farming leased land. Many farmers lease farmland and a farmer generally says that he is, "farming a section and a half or farming four-hundred or two-hundred acres."

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9. Wash. Rev. Code §§ 9-312(4), 9-301(2) (1983).
10. 11 U.S.C. (b), (e)(1983.
11. Idaho Code §§ 554.1101-.11109 (1966).
12. Mont. Code Ann., §§ 30-1-101, 30-9-511 (1965).

A bank must understand that the debtor (farmer) does not have rights to all of the crops being produced, if there is a crop-share lease involved. The farmer only has his percentage of the crop. For illustration, let us assume that this farmer is leasing some of his land and there is a 50-50 crop split. This farmer only has rights in 50 percent of the crops being produced, since that is all the crops he/she has rights in. Thus, if the bank believes it is getting more than that, they are wrong. The debtor can only give whatever he/she has rights in. In a crop-share lease, that is whatever the crop percentage is. If it is a straight cash lease, the farmer has all of the crop to put up because he has rights in *all* of the crops.

Additionally, many states have landlord liens. A sad situation happened in Iowa when an older couple leased their land to a tenant who eventually went into bankruptcy. The land had been leased on a cash lease agreement. The couple relied on the landlord's lien in bankruptcy. They lost. It was a statutory lien, and avoidable under § 545 of the Bankruptcy Code which has a specific provision for rents in distress. They were a general creditor. Therefore, if you are representing land owners today who are cash leasing land to others, create a security interest. Perfect it the same way any security interest in crops would be.

Note, however, that there are some risks in creating the security interests in the sense of the "first in time" rule.[13] For example, if you have a landlord-tenant relationship that is not new, the land owner or the lawyer representing the land owner should get a Subordination Agreement from the P.C.A. or the bank so that if something were to happen they would have priority over the first to file. If you have a bank that is financing a farmer with an ongoing relationship, it will have already filed and will be first in time; thus, a Subordination Agreement is needed. If it is a new arrangement, the first time for the land owner and the tenant, then the perfected landlord will be alright because it is clear that the lender would have no claim to the crops on the new land inasmuch as its security agreement and financing statement would not have covered this new land.

We have already examined priorities. The general rule is "first to file." There are, however, two major exceptions. The first is the

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13. U.C.C. § 9-312(5)(a) (1977).

purchase money security interests in non-inventory.[14] Suppose the bank is financing the farmer and the farmer is given back a security interest in all equipment presently owned and after-acquired, and is properly filed. The farmer then goes to the John Deere dealer and buys a new tractor giving it a perfected security interest for the tractor. That is a purchase money security interest, and under the U.C.C. 9-312(4), John Deere will come ahead of the bank when this farmer defaults on both loans. The key is that the "first to file" rule will not give the bank protection because there is a super priority that is given to properly perfected purchase money security interest holders.

The second exception concerns "the buyer in ordinary course rule." There are two distinct situations: the buyer of inventory, or the buyer of farm products. Looking first at inventory, suppose we have a bank that finances an appliance dealer and the appliance dealer has given the bank a perfected security interest in all inventory presently owned and after-acquired. Suppose this appliance dealer sells to Mr. X a refrigerator and Mr. X gives a perfected security interest or Mr. X pays cash. The appliance dealer defaults on its loan from the bank and the bank wants to "go and get what ever they can get since Mr. X just bought a new refrigerator." They try to repossess Mr. X's refrigerator. Can the bank do this? The answer is No. Under 9-307(1) a buyer in the ordinary course [1-201(9)] takes free of a prior perfected security interest created by his seller. Because Mr. X is a buyer in the ordinary course and the appliance dealer created the security interest, Mr. X wins.

There is a special rule dealing with farm products. If we assume we have farm products subject to a perfected security interest, what happens when the farmer sells to an elevator or a processer? If the farmer fails and has not remitted the proceeds to the bank, the farm products rule says the bank can sue the elevator in conversion, or it can repossess the grain. The reason being that the security interest of the lender flows right down to that purchaser. There have been some recent cases in Iowa and Washington addressing the reasons behind the farm products rule. First, however, there is one section that we need to address besides the so-called farm products rule of 9-307(1). That section is called 9-

14. U.C.C. § 9-312(4) (1977).

306(2), and says "except as otherwise provided in the code, the security interest continues in the collateral unless the security agreement specifically authorized the sale or otherwise." All the litigation is centered on the "otherwise." Quite simply, the question is "has the farm lender authorized the sale?" If the farm lender is found to have authorized the sale, then it has given up its interest.

Thus, once the bank has perfected security interest in farm products, the question becomes "has the bank in some way authorized the sale?" In Washington, the court in *Southwest Washington P.C.A. v. Seattle National Bank*[15] rejected what is called the "prior course of dealing rule" to show authorization. In that case, there was a term loan of one year; each year it was renewed, and there had been a ten year relationship with the farmer and the P.C.A. The budget was prepared and the P.C.A. knew that the farmer had to sell the crops to pay on the debt. However, the key point was that the agreement provided that there was to be prior written consent for the sale and that was never given. For ten years the P.C.A. allowed the farmer to sell and remit the proceeds. In the eleventh year, the farmer sold it and did not give the proceeds back. He had sold to a processor and the processor went bankrupt. The question was whether the P.C.A. still had a perfected security interest or whether it was cut off. The court held that a prior course of dealing without more did not show authorization; therefore, the P.C.A. still had a perfected security interest and had not authorized the sale.[16]

In *First National Bank v. Iowa Beef Producer*[17], the tenth circuit rejected a conditional authorization argument. The secured party had argued that it did not consent to the sale inasmuch as the debtor did not remit the proceeds of the sale and the consent to allow the debtor to sell in his own name was conditioned upon the debtor remitting the proceeds by his own check. The court appeared to treat this as actual consent.

15. 92 Wn. 2d 301, 593 P.2d 167 (1979); *see also In re* San Juan Packers, 696 F.2d 707 (9th Cir. 1983); Western Idaho PCA v. Simplot, 106 Idaho 260, 678 P.2d 52 (1984); *In re* Cost Trading Co., 36 U.C.C. Rep. Serv. 1753, 31 Bankr. 670 (Bankr. Ct. D. Ore. 1983); *In re* Surviver Farms Inc., 36 U.C.C. Rep. Serv. 416, 27 Bankr. 655 (1982).

16. Southwest Washington PCA v. Seattle First Nat'l Bank, 92 Wn. 2d 30, 593 P.2d 167 (1979). The court did state, however, "any course of *performance* . . . or other conduct subsequent to the agreement can amount to a waiver." *Id.* at 593.

17. 626 F.2d 724 (10th Cir. 1978).

It is clear the agriculture community is having troubles. The agriculture community includes more than just farmers. The community includes implement dealers, elevators, and the banks. There are some questions that have been overlooked. If we change the farm products rule and take away a protection for the banks, what impact, first of all, is that going to have on the whole credit-availability issue? Second, I do not know about small banks here in Washington, but in Kansas there is a large number of rural banks that have some problems, and if we reverse this rule, there is a question as to how they are going to protect themselves.

A secured creditor may protect itself through borrower lists. What I mean by borrower lists, in this sense, is where the lender sends out to all known buyers of farm products a list of their debtors and says, "If you buy from any one of these people on this list, you should understand that unless you pay me with a joint-payee check, I am not waiving my security interest."

An interesting question is whether a bank would send out such a list. If the farm product rule is changed, we will see lenders asking permission from their borrowers. Banks could make the agreement to send this list out as a pre-condition for getting money. A lender can not normally find out who all the buyers are through a filing system. Interestingly enough, that was done in Delaware. Delaware changed the farm products rule. To buy free of a perfected security interest, the buyer must register with the Secretary of State.

Another thing I think you are going to see happen with this rule is now happening in California. In 1976 California did away with the farm products rule.[18] California has relatively few buyers, and lenders know who most of them are. Lenders have essentially said they will not lend unless: 1) you have a source to buy your products; 2) there is an assignment of proceeds executed; 3) the buyer agrees to send X percentage of the funds directly to the lender. The lenders have had a great deal of success with getting the buyers to sign those agreements. I think you are going to see banks coming up with some imaginative ideas if they lose their protection.

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18. CAL. COM. CODE § 1401 (West 1976).

Congress has had hearings on whether to federalize this rule because the livestock industry finds it is impossible to cope with. For example, filing officers will not give processors any information over the phone. They have got to go there. Packers do not know who is going to show up. Thus, if you are located in Spokane and buying from two or three states, you don't know who is going to show up at any given day. It is such a nightmare that the livestock industry has asked Congress to preempt the states and enact a federal rule. I personally am opposed to that for a variety of reasons. There is no doubt that we lack uniformity, and I don't know what is going to happen in Washington. I think the state of Iowa has the best system possible. It is computerized now, with a private search firm. For years, members of the Iowa agricultural community have been able to call up that private search firm and identify the farmer. It can check the records and indicate who the listed people are. A computer program allows it to get around the debtor name problems. The elevators and the livestock operators have been using it, but they still do not like it. They are asking the current Iowa legislature to change that rule. If you have a system like Iowa's and people are not happy, you know very well that in other states people will not be happy.[19]

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19. In December 1985, Congress changed the farm products rule. Section 1324 of the Food Security Act of 1985, 131 CONG. REC. H12249, H12388 (Daily ed. Dec. 17, 1985). The major purpose of § 1324 is to protect both commission merchants selling farm products subject to perfected security interests, and buyers of farm products subject to perfected security interests. The act permits individual states to choose between two alternative methods of dealing with the sale of farm products. It provides that buyers buy free of a perfected security interest unless the buyer receives written notice from the lender or the seller, *or*, in the alternative, the state adopts a new and different central filing system in which the secretary of state will provide buyers who register or request it with financing statement information.