CALIFORNIA PRODUCER'S LIENS: A PRIMER

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I. INTRODUCTION

"The United States was once largely an agrarian society and farmers continue to be beneficiaries of special legislation mitigating some of the harshness of the usual rules applicable to commercial transactions."[1] The special legislation includes tax provisions for cancellation of indebtedness where farmers are excluded from the group of persons for whom debt cancellation is taxable[2] and preferential treatment under the California Commercial Code which distinguishes "farm products" from other types of goods.[3] The Bankruptcy Code also includes special provisions that provide powerful remedies for those who qualify as a "Family Farmer."[4]

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[1] Riley C. Walter, *A Case for the Avoidance of Secret Farmer Liens: The California Producer's Liens*, 4 SAN JOAQUIN AGRIC. L.R. 37, 37 (1994).

[2] 26 U.S.C.S. § 108(a)(1)(C) (2009).

[3] CAL. U. COMM. CODE § 9102(34) (Deering 2009).

[4] *See* 11 U.S.C. 101(18), (19) (family farmer defined and special payments provided for under chapter 12); *see generally* 11 U.S.C.S. §§ 1201 – 1231 (2009).

California remains the Nation's number one state in agricultural production.[5] California provides protection to agriculture in the form of specialized statutes such as "producer's liens" which provide that any producer of farm products that are sold to any food processor shall have an automatic lien on that product for the agreed upon sale price.[6] The producer's lien is unique in that there is no formal "perfection" or notice required and the lien is perfected upon delivery of the agricultural products to the processor.[7] This Article serves as a primer on the requisite elements for asserting a producer's lien, a review of the case law interpreting producer's liens, a discussion of remedies for violation of the lien, and statutory requirements for termination of the lien.

II. IMPORTANCE OF AGRICULTURE IN CALIFORNIA'S ECONOMY AND TO THE CENTRAL VALLEY

The productivity and variety of California's agriculture positions the state as the nation's agricultural leader with $38 billion in agricultural production.[8] The state's Central Valley produces over 63% of that production and supplies nearly one fourth of America's food.[9] The region's farming operations "contribute more than twenty-two billion dollars a year in commodity value, and additional billions in associated activities to the state's diverse economy."[10] Six of the nation's top ten counties for agricultural production are in the Central Valley.[11]

The diversity of California's agricultural output is unmatched and encompasses 350 different crops and commodities.[12] Over fifty percent of the country's fruits, nuts and vegetables and more than 400 different

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[5] AMY MOFFAT, THE STATE OF THE GREAT CENTRAL VALLEY OF CALIFORNIA: ASSESSING THE REGION VIA INDICATORS, THE ECONOMY 21 (3RD ed. 2009), http://www.greatvalley.org/art,am2/uploads/1/ecoinidcators09_final.pdf.

[6] CAL. FOOD & AGRIC. CODE §§ 55631, 55632, 55633 (Deering 2009).

[7] *See generally* CAL. U. COM. CODE § 9312 (Deering 2009) (code section describes what is required to preserve and protect a security interest, such as filing, giving notice, obtaining possession the interest is "perfected").

[8] MOFFAT, *supra* note 5 at 22.

[9] *California's Central Valley*, (Nat'l Public Radio broadcast Nov. 11-14, 2002) California's central valley produces approximately $27 billion in revenues, approximately 63% of the state's entire agricultural production of $63 billion, *available at* http://www.npr.org/programs/atc/features/2002/nov/central_valley/

[10] ALVIN D. SOKOLOW, FARMLAND POLICY IN CALIFORNIA'S CENTRAL VALLEY: STATE, COUNTY, AND CITY ROLES, http://www.ucop.edu/cprc/documents/sokolow.pdf.

[11] California Farm Bureau Fed.com, Central Valley Land Use Report, http://www.cfbf.com/issues/landuse/report3.cfm (last visited March 6, 2009).

[12] The Great Valley Center.com, Productivity and Diversity of California's Agriculture, http://www.greatvalley.org/indicators/econ00/ag_div.aspx (last visited March 6, 2009).

crops and commodities are grown in California.[13] The state's agriculture contributes more than twelve billion dollars in agricultural products to U.S. exports.[14] Three of the most popular agricultural products sold in Europe - almonds, prunes and raisins - are grown nearly exclusively in California.[15] China is projected to quadruple its agricultural imports from California over the next fifteen years.[16] Such exports create additional jobs for Californians at a ratio of 27,000 jobs for every one billion dollars in agricultural exports.[17]

"About thirty percent of the Central Valley's total personal income derives from agriculture."[18] Agriculture-related industries provide jobs in food processing, transportation, equipment sales and support businesses.[19] The importance of agriculture to California, the Nation, and beyond cannot be over emphasized.

In recent years, the value of agricultural output has continued to increase in spite of the ongoing loss in total cropland to urbanization.[20] Currently, projections for California's economic health are disturbing and farmers are feeling the financial squeeze as they are caught in declining crop prices, drought, restricted water allotments[21] and rising production costs.[22] Many farm operations have slipped into the red and additional loss, such as a default from an insolvent processor, may grease the slide into growers' bankruptcies.[23] There are also increasing pressures on processors due to such factors as relative unavailability of commercial financing and a growing demand for secured collateral on loans as lend-

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[13] MOFFAT, *supra* note 5 at 26.

[14] California Farm Bureau Fed. *supra* note 11.

[15] The Great Valley Center.com, *supra* note 12.

[16] Jim Holland, *Banker Puts Caveats on Farms' Futures,* THE MODESTO BEE, May 12, 2007 (reporting speech by Ken McCorkle).

[17] California Farm Bureau Fed. *supra* note 11.

[18] *Id.*

[19] Julia Hollister, *The Central Valley: Heartland of Bountiful Harvests*, CAL. JOB JOURNAL, Aug. 20, 2006, *available at* http://jobjournal.com/article full text.asp?artid=1784.

[20] California Farm Bureau Fed. *supra* note 11 (the value of agricultural out put increased by approximately 6-7% annually in 1996 and 1997).

[21] Jim Carlton, *Shrinking Water Supplies Imperil Farmers*, WALL ST. J., Feb. 10, 2009, at 13, *available at* http://online.wsj.com/article/SB123423167165366189.html?mod+article-outside-box.

[22] Jock O'Connell, Opinion, *Globalization and the Perils of Farming in California's Central Valley*, THE SACRAMENTO BEE, July 29, 2001, *available at* http://jockoconnell.tripod.com/CVag.html.

[23] Walter & Wilhelm Law Group.com, *Farmers Should be Proactive Concerning Loan Default Notices, http://w2lg.com/Articless/Farmers%20should%20be%20proactive.pdf.*

ers lose confidence in the economy.[24] Farm product producers and processors will be better prepared to cope with the current economic challenges by having a thorough understanding of producer's liens law.

III. OVERVIEW OF SECURED STATUTORY LIENS IN CALIFORNIA AGRICULTURE

Given the size and economic importance of California's agricultural industry, the California legislature has been particularly active in adopting and enacting what has been called "secret" agricultural liens. This section reviews examples of some agricultural liens, their priority and status as secret liens.

A. Examples of Various Liens

California has a suite of statutory lien laws that mitigate the risk of financial loss to agricultural growers and ranchers from processors who are often subject to dual pressures from insolvency and secured loans from financial lenders.[25] Although the purposes of these regulations are similar, they vary in their requirements for lien creation, asserting the lien, continued possession by the processor, and prioritization among other liens.[26]

1. Agricultural Laborer's Lien (Civil Code Sections 3061.5-3061.6)

The Agricultural Laborer's Lien provides that "any person employed related to harvesting or transporting harvested farm products that were owned and grown or produced by a limited partnership shall have a lien on the severed farm products or sale proceeds."[27] The liens attach whether the work was done at the direction of the owner, owner's agent, contractor or any other person in charge of the harvesting or transporting of the severed crops.[28] The liens provided for under section 3061.5 are "preferred liens, prior in dignity to all other liens, claims, or encumbrances."[29] Part (c) provides that there is a "maximum liability for sev-

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[24] *See generally,* Frazier Nuts v. American Ag Credit, 46 Cal. Rptr.3d 869, 871-75 (Cal. Ct. App. 4th 2006).

[25] *See generally,* Richardson v. Wells Fargo Bank (*Churchill Nut*), 251 B.R. 143 (Bankr. N.D. Cal. 2000).

[26] Walter, *supra* note at 39.

[27] CAL. CIV. CODE § 3061.5(a) (Deering 2009).

[28] *Id.*

[29] *Id.* § 3061.5(b).

ered crops of the lesser among of actual proved claims or twenty-five percent of the fair market value of the crops."[30]

2. Lien for Service of Stallion, Jack or Bull (Civil Code Section 3062)

Also called the Livestock Breeder's Lien, section 3062 provides that "every owner or person having in charge a stallion, jack or bull, used for propagating purpose, has a lien for the agreed price of its service upon the mare or cow and upon the offspring of such service."[31] "The lien rights could be challenged where there was a willfully false representation concerning the breeding or pedigree has been made."[32]

3. Livestock;" "Meatpacker". Commencement of lien; Rights of buyer in ordinary course of business; Duration of lien; Filing of statement by lien claimant. (California Food & Agricultural Code Sections 55701, 55702)

The definitions of "Livestock" and "Meatpacker" are provided in section 55701.[33] A livestock seller's lien is not dependent upon possession and attaches where any person sells or furnishes livestock to a meatpacker.[34] The lien attaches on transfer of possession to the meatpacker and has priority over all other liens and security interest in the livestock and identifiable proceeds.[35] However, the Livestock Lien will cease to be in force after twenty-one days from the date of delivery of the livestock unless notice of the lien is filed with the Secretary of State.[36] Cal. Food and Agric. § 55702 provides for a lien where livestock is delivered to a meat packer but also provides for a lien on identifiable proceeds and products.[37]

4. Dairy Cattle Supply Lien (Food & Agriculture Code Sections 57401-57414)

The Dairy Cattle Supply Lien ("Dairy Lien") sets forth that a person who provides feed or material to aid in the raising or maintaining of dairy cattle has a lien upon the proceeds of the milk or milk products produced from the dairy cattle, for the reasonable or agreed charges for

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[30] *Id.* § 3061.5(c).
[31] *Id* § 3062.
[32] *Id.*
[33] CAL. FOOD & AGRIC. CODE § 55701 (Deering 2009).
[34] *Id.* § 55702 (a).
[35] *Id.*
[36] *Id.* § 55702(c).
[37] *Id.* § 55702(a).

the feed or material provided and for the costs of enforcing the lien.[38] Recovery under this section is limited to the reasonable or agreed upon charges for feed or material.[39] Dairy liens must be perfected and become effective upon filing of the standard financing statement form under the California Commercial Code.[40] A dairy lien that is perfected prior to the filing of a bankruptcy petition is insulated from lien avoidance under the bankruptcy code.[41]

5. Poultry and Fish Supply Lien (Food & Agriculture Code Sections 57501-57545)

Similar to the dairy lien, section 57510 establishes that a person who provides feed or materials to aid the raising or maintaining of poultry or fish, or for the production of eggs has a lien upon the proceeds of the sale of the eggs, poultry, fish, or other derived products, for the reasonable or agreed charges for the feed or material provided.[42] The poultry and fish lien includes the costs of enforcing the lien.[43] Recovery is limited to the cost of materials provided within a forty-five day period, and only two providers of feed or materials shall have an enforceable lien at any time.[44]

6. Agricultural Chemical and Seed Lien (Food & Agriculture Code Sections 57551-57595, 57700)

In order for a provider of agricultural chemicals or seeds to establish a lien under this section's subdivision (a), the person must first send by certified mail a written notice to the lien debtor that sets forth: (1) that payment of the agricultural chemicals or seeds are more than thirty days overdue; (2) stating that the reasonable or agreed charges are overdue; and (3) providing the lien debtor with three alternatives.[45] Generally the alternatives are either to allow the lien to be filed, enter into a consensual

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[38] *Id.* § 57405.

[39] *Id.*§ 57401.

[40] *Id.*§ 57405.

[41] McGranahan v. Gilbert (*In re* Mendonca) (*Mendonca),* 2007 Bankr. LEXIS 485,*12 (Bankr. E.D. Cal. 2007).

[42] CAL. FOOD & AGRIC. CODE § 57510 (Deering 2009).

[43] *Id.*

[44] *Id.*

[45] CAL. FOOD & AGRIC. CODE § 57561 (Deering 2009) (*provides additional detail,* the notification must be in ten point type or bolder, notify the lien debtor that the debtor has ten days from receipt of the notice to select an alternative, notify the lien claimant of the alternative selected, and satisfy all the requirements of the selected alternative, and that the lien claimant may file the notice of claim of lien at any time after the lien debtor does not comply with the requirements of the code section).

security interest in the proceeding under the California Commercial Code, or pay the reasonable or agreed charges that are overdue.[46]

Once a person has complied with the terms of subdivision (a), then there is a lien upon the proceeds of the crop for the reasonable or agreed charges and for the costs of enforcing the lien.[47] The lien attaches to the proceeds of the crops that existed at the time of the application of the agricultural chemicals on the land - if no crops were planted, then the attachment is on the next production of crops following the last date on which the chemical was applied - or on the crops produced from the agricultural seed.[48] The lien would not exceed the reasonable or agreed charges for agricultural chemicals furnished within a sixty day period and within a forty-five day period for agricultural seeds.[49]

B. Priority of Agricultural Liens

Agricultural laborer's liens are preferred liens and have superior priority over all other liens, claims or encumbrances.[50] If there are multiple producers' lien claims with equal standing then the payment is to be prorated among the claimants.[51] Generally, the remaining agricultural liens are prioritized according to the time the notice of the lien claim was filed.[52] Thus, these producers' liens have preferred priority to all claims except laborer's claims for wages and salaries earned in connection with production of agricultural products and Uniform Commercial Code ("UCC") warehouse liens.[53]

C. Statutory Liens as "Secret" Liens

The statutory liens discussed above become effective upon some action by the lienholder and arise automatically with no formal perfection requirements.[54] Action such as delivering the livestock or agricultural crops to a processor is sufficient to create a lien right.[55] Because these liens do not have formal perfection requirements they are referred to as

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[46] *Id.*§ 57561.
[47] *Id.*
[48] *Id.*
[49] *Id.*
[50] CAL. CIV. CODE § 3061.5 (Deering 2009).
[51] U.S. Bank v. Deseret Farms (*In re* Sargent Walnut Ranches) (*Sargent Walnut*) 219 B.R. 880, 883 (Bankr. E.D. Cal., 1998).
[52] *See generally* CAL. FOOD & AGRIC. CODE § 57406, 57575, 57525 (Deering 2009).
[53] *Id.* § 55633 (Deering 2009).
[54] Valley Farm v. Andrew (*In re* Loretto Winery) (*"Loretto Winery"*), 898 F.2d 715, 719 (9th Cir. 1990).
[55] *Id.* at 718.

"secret liens".[56] As discussed in *Valley Farm v. Andrew* (*In re* Loretto Winery), 898 F.2d 715, 719 (9th Cir. 1990) ("*Loretto Winery*"), a bankruptcy case considering "secret liens" and "bona fide purchasers", a bankruptcy court will apply the state's "theoretical bona fide purchaser" test to determine if the particular lien is good and look to the words of the state statute.[57] A producer's lien is "good against a bona fide purchaser without possession under California law when the proceeds are not used to satisfy the lien."[58] However, where both title and physical possession had passed to the bona fide purchaser prior to bankruptcy the trustee may be able to avoid the lien.[59] Questions on whether a lien is enforceable against a bona fide purchaser are answered by applying the requirements of the state law.[60] Changes in the California Commercial Code impacting "agricultural liens" do not appear to impact the producer's lien. The reasoning is that the debtor in an "agricultural lien" is a farmer, grower, rancher or other producer of farm products whereas the "producer's lien" is limited to situations where the debtor is a processor.[61]

IV. THE FEDERAL PERISHABLE AGRICULTURAL COMMODITIES ACT ("PACA") SIMILARITIES AND DISTINCTIONS TO CALIFORNIA PRODUCER'S LIENS

The federal Perishable Agricultural Commodities Act ("PACA") provides that a floating trust is created for the benefit of unpaid growers of the produce and the buyer of perishable agricultural commodities is the trustee.[62] Congress enacted PACA in 1930 to prevent unfair business practices and promote financial responsibility in the fresh fruit and produce industry.[63] A PACA trust automatically goes into effect at the time the produce is delivered but, in contrast to a producer's lien, the seller must comply with the strict notice requirement or the PACA trust rights will be lost.[64]

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[56] Walter, *supra* note 1 at 39.

[57] Valley Farm v. Andrew (*Loretto Winery*), 898 F.2d at 721-722.

[58] *Id.* at 724.

[59] *Id.* at 719.

[60] *Id.* at 718.

[61] CAL. U. COMM. CODE § 9102(a)(5) (Deering 2009).

[62] Norton Enterprises v. TKO Farms, Inc., 1996 U.S. Dist. LEXIS 22649, at *2 (N.D. Cal. 1996).

[63] *See* Boulder Fruit Express v. Transportation Factoring, 251 F.3d 1268, 1270 (9th Cir. 2001).

[64] Flores v. DDJ (*In re* Enoch Packing Company), 2007 U.S. Dist. LEXIS 40010, at *20 (Bankr. E.D. Cal. 2007).

7 U.S.C. § 499 e(c)(2)[65] provides that "the receipt of the first shipment of produce by a commissioned dealer creates a PACA trust, and any receivables or proceeds derived from the produce are held in trust for the benefit of all unpaid suppliers."[66] The PACA trust continues until full payment for the transactions has been received.[67] Commodity producers are protected against secured lenders in that use of an account receivable derived from the sale of the agricultural commodity as collateral to secure a loan is generally considered a breach of trust.[68] For example, in *Norton Enterprises v. TKO Farms,* 1996 U.S. Dist. LEXIS 22649 (N.D. Cal. 1996), Comerica Bank held a security interest in TKO Farms' business assets, including accounts receivable and their proceeds.[69] TKO acknowledged that the assets in the bank account were subject to payment of PACA liens against the assets of TKO.[70] Comerica Bank argued that although PACA gives growers priority over the bank's security interest, it could retain the proceeds until the PACA claims are proven.[71] The District Court established a procedure for resolving the conflict over the PACA assets and appointed a special master to collect the PACA assets and administer the claims.[72] A plaintiff establishing a PACA trust must show: (1) the commodities sold were perishable agricultural commodities; (2) the buyer was a commission merchant, dealer, or broker; (3) the transaction occurred in interstate commerce; (4) the seller has not yet received full payment; and (5) the seller preserved its trust rights by giving proper notice to the buyer.[73] In a dispute over whether a PACA buyer's assets are subject to a PACA trust, the burden of proof is on the party opposing the claim.[74] Generally, a court will presume that the as-

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[65] 7 U.S.C. § 499e(c)(2)(2009) provides, in part: "Perishable agricultural commodities received by a commission merchant, dealer, or broker, and all transactions, and all inventories of food or other produces derived from perishable agricultural commodities, and any receivables or proceeds from the sale of such commodities or products, shall be held by such commission merchant, dealer, or brother in trust for the benefit of all unpaid suppliers or sellers of such commodities or agents involved in the transaction, until full payment of the sums owing in connection with such transactions has been received by such unpaid suppliers, sellers or agents."

[66] Callaway Produce v. Bear Kodiak (*In re* Bear Kodiak Produce), 283 B.R. 577, 583 (D.C. Az. 2002).

[67] *Id.*; 7 U.S.C. § 499e(c)(2).

[68] Boulder Fruit Express v. Transportation Factoring, 251 F.3d at 1271.

[69] Norton Enterprises v. TKO Farms, 1996 U.S. Dist. LEXIS 22649, at *2.

[70] *Id.* at *3.

[71] *Id.* at *4.

[72] *Id.* at *5.

[73] C.H. Robinson Co. v. Marina Produce, 2007 U.S. Dist. LEXIS 3098, at *5 (N.D. Cal. 2007).

[74] Callaway Produce v. Bear Kodiak, 283 B.R. at 583.

sets of a PACA buyer are part of the PACA trust unless: (1) no PACA trust existed when the asset in question was purchased; or (2) the asset was not purchased with PACA trust assets; or (3) subsequent to purchasing the asset, the buyer paid in full all suppliers, thereby terminating the trust.[75] PACA trust assets that are expended in violation of the trust may be traced to the PACA trust even if substantially changed in form.[76] So, third parties could be forced to disgorge funds that are traceable to a PACA trust.[77] However, the Ninth Circuit has held that third-party transferees of PACA assets are not guarantors of the PACA trust and are liable only if they had some role in causing a breach of a trustee's fiduciary duty or dissipation of the trust.[78]

In a bankruptcy proceeding, a PACA trust beneficiary, who has given timely, written notice of intent to preserve PACA benefits, will have priority over all other creditors.[79] One example of a court establishing PACA trust claims procedure and appointing a special master can be found in *Norton Enterprises v. TKO Farms*.[80] PACA provides that "shareholders, officers or directors of a corporation may be held personally liable for the corporation's PACA debts when those individuals are in a position to control PACA trust assets and the individuals have breached their duty to preserve the assets."[81] *C.H. Robinson,* 2007 U.S. Dist. LEXIS 3098 (N.D. Cal. 2007) involves Robinson as a wholesale supplier of perishable agricultural commodities and defendants Montalbano and Rodriguez as the sole owners of Marina Produce.[82] Here, the plaintiff prevailed in his efforts to have defendants Montalbano and Rodriguez held personally liable for PACA funds where he showed that: (1) Montalbano and Rodriguez exercised exclusive control over the PACA assets as sole owners of Marina; (2) Montalbano and Rodriguez were solely responsible for ensuring that Marina's liability to plaintiff was satisfied out of the PACA trust assets; (3) and Plaintiff specifically alleged that Montalbano and Rodriguez's failure to pay plaintiff out of the PACA trust created a breach of the trust which then made them individually liable to plaintiff.[83]

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[75] *Id.*

[76] *Id.* at 585.

[77] Flores v. DDJ (*In re* Enoch Packing), 2007 U.S.Dist. LEXIS 40010 at *13.

[78] Boulder Fruit v. Transportation Factoring, 251 F.3d at 1272.

[79] Flores v. DDJ (*In re* Enoch Packing), 2007 U.S. Dist. LEXIS 40010 at *13.

[80] *See generally* Norton Enterprises v. TKO Farms, 1996 U.S. Dist. LEXIS 22600 at *4.

[81] C.H. Robinson v. Marina Produce, 2007 U.S. Dist. LEXIS 3098 at *7-8.

[82] *Id.* at 1-2.

[83] *Id.* at 7-8.

V. PROVISIONS AND PURPOSE OF PRODUCER'S LIENS

California provides statutory safeguards for the financial protection of producers who sell farm products to processors.[84] A producer's lien arises where a grower, the "producer," delivers that farm product to another entity for processing.[85] Examples of such a sale and delivery of an agricultural product include: a tomato grower delivering tomatoes to a tomato canner; a nut grower delivering unshelled or partially shelled nuts to a processor for processing and preparation for sale; and a grape grower delivering grapes to a winery. The importance of producer's liens manifests when the grower is not paid because the processor's lender asserts a senior security interest in accounts and proceeds to the detriment of the grower.

A. California's Producer's Liens: The Statue and Purpose

1. Statute

The Producer's Lien can be found at Cal. Food & Agric. Code, Division 20, Chapter 6, section 55631 and provides, "Every *producer* of any *farm product* that *sells* any product which is grown by him to any *processor* under contract has a lien upon such product and upon all processed or manufactured forms of such farm product for his labor, care and expense in growing and harvesting such product."[86]

2. Statutory Definitions

Definitions – for the purposes of the Cal. Food & Agric. Code sections the following definitions are applicable.

Farm Product: Section 55403 defines "*Farm product*" to include ever agricultural, horticultural, viticultural, or vegetable produce of the soil, honey and beeswax, oilseeds, poultry, livestock product, and livestock for immediate slaughter.[87] It does not include timber or any timber product, milk or any milk product, any aquacultural product, or cattle sold to any person who is bonded under the federal Packers and Stockyards Act.[88]

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[84] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 882.

[85] *Id.*

[86] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 882.; CAL. FOOD & AGRIC. CODE § 55631 (Deering 2009).

[87] CAL. FOOD & AGRIC. CODE § 55403 (Deering 2009).

[88] *Id.*

Producer: Section 55408 provides that a "*producer* means any person that is engaged in the business of growing or producing any farm product."[89]

Processor: Section 55407 provides that a "*processor* is any person that is engaged in the processing or manufacturing of any farm product, that solicits, buys, contracts to buy, or otherwise takes title to, or possession or control of, any farm product from the producer of the farmed product for the purpose of processing or manufacturing it and selling, reselling, or redelivering it in any dried, canned, extracted, fermented, distilled, frozen, eviscerated, or other preserved or processed form."[90] It does not include any retail merchant that has a fixed or established place of business in the state and does not sell at wholesale any farm product which is processed or manufactured by him.[91] Section 55521 provides that a person shall not act as a processor or a cash buying processor unless the person has obtained a processor's licenses provided for in Section 56574.[92]

3. "Lien" Definition

The Producer's Lien statute does not provide a definition of the term "lien" or "producer's lien."[93] Absent an express statutory definition in the statue, the Fifth Appellate adopted a definition that the term "lien" is defined as a "legal right or interest that a creditor has in another's property, lasting until a debt or duty that is secured is satisfied."[94] Applying this definition of "lien," the California Fifth District Appellate Court concluded that a grower/producer's legal interest in the sale proceeds of the product delivered to the processor is appropriately classified as a lien.[95] Further, the Fifth District Appellate Court considered that the grower's right to be paid from the proceeds was not terminated in *Frazier Nuts v. American Ag. Credit*, 46 Cal. Rptr.3d 869, 871 (Cal. Ct. App. 4th 2006) ("*Frazier Nuts*"), where the processor was no longer in posses-

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[89] *Id.*§ 55408.

[90] *Id.*§ 55407.

[91] *Id.*

[92] *Id.*§ 55521.

[93] Frazier Nuts v. American Ag Credit, 46 Cal. Rptr.3d 869, 879 (Cal.Ct. App. 4th 2006).

[94] *Id.* (where the Fifth Appellate applied the definition of "lien" that can be found in Black's Law Dictionary p.933 and the definition found in the Uniform Fraudulent Transfer Act, *Cal. Civ. Code § 3439.01*).

[95] *Id.* at 879.

sion of the product.[96] Thus, extending the growers' rights beyond inventory to include the proceeds of the inventory.[97]

4. Purpose

The purpose of producer's liens is to afford protection to growers against insolvent processors by providing the grower a lien on the product they delivered to the processor.[98] The California legislature has discussed that a "grower has the risk of producing the crop and it would be inequitable and contrary to the public interest in a viable agricultural industry to leave the grower vulnerable to insolvent processors."[99] During insolvency, the processor may be pressured by various lenders to apply crop proceeds to meet demands of other debt.[100] In contrast to other agricultural liens that have a statutory limitation on the lien's life, the California legislature intended to eliminate any statutory limitation on a producer's lien's life since a grower may not know that a processor is in financial straits until long past the previously set sixty day limitation.[101]

B. Producer's Lien as "Secret Lien"

1. Producer's lien not avoidable where processor had possession when bankruptcy case filed

In *Loretto Winery*, the producer of grapes, Valley Farm, sold grapes to the Loretto Winery.[102] The Loretto Winery filed for Chapter 11 bankruptcy eight days after Valley Farm's last delivery.[103] After the case was converted to a Chapter 7, the bankruptcy trustee sued in bankruptcy court to avoid Valley Farm's producer's lien on the partially processed grapes.[104] The bankruptcy court and the bankruptcy appellate court allowed that 11 U.S.C. § 545(2) would permit the trustee to avoid the California producer's lien.[105] 11 U.S.C. § 545(2) provides that a trustee can avoid a lien that "is not perfected or enforceable on the date of the filing

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[96] *Id.* at 871.
[97] *Id.* at 882.
[98] *Id.* at 878-79.
[99] *Id.* at 879.
[100] *Id.*
[101] Alvarez Farms v. Bank of California (*In re* T.H. Richards), 910 F.2d 639, 644-645 (9th Cir. 1990).
[102] Valley Farm v.Andrew (*Loretto Winery*), 898 F.2d at 717.
[103] *Id.*
[104] *Id.*
[105] *Id.*

of the petition for bankruptcy as against a bona fide purchaser that purchases such property on the date of the filing of the petition, whether or not such a purchaser exists."[106] The Ninth Circuit overturned and held that the California producer's lien was not voidable where the processor had possession of the grapes when it filed for bankruptcy. [107]

Justice Beezer's dissent in *Loretto Winery* argued that federal preemption makes section 545(2) superior to any state scheme of creditor priorities and enforcing the California statutory producer's liens reorders federally created priorities according to the state scheme.[108] Congress's perception of state statutory liens has been that they are "thinly disguised attempts" to impose state ordered priorities in federal bankruptcy.[109] Further criticism of the *Loretto Winery* holding focuses on the absence of notice to subsequent purchasers.[110] Absent a recorded instrument a subsequent bona fide purchaser lacks constructive notice of the lien.[111] The dissent observes that California courts have not considered the enforceability of the producer's liens against bona fide purchasers (at the time of the *Loretto Winery* decision) and state policy would be adverse to upholding liens where subsequent purchasers did not have notice.[112]

2. Tension between the Bankruptcy Code and "Secret" statutory liens

The tension between federal preemption and absence of notice is recognized in the *Loretto Winery* majority opinion, which acknowledged a tension where creditors will not be treated equally in federal bankruptcy court when state law establishes priorities for state statutory liens.[113] Notwithstanding the principle of uniformity in the Bankruptcy Code, Congress has deferred to local policy expressed in the state's statutory liens.[114] Under the Bankruptcy Code the statutory lien's validity is determined under state law.[115] In *Loretto Winery,* the court found that particular lien held by Valley Farm was good under the laws of the state against a bona fide purchaser.[116] So, the trustee or debtor-in-possession,

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[106] *Id.* at 725.
[107] *Id.* at 724-725.
[108] *Id.* at 725 (Beezer,C.J., dissenting).
[109] *Id.* at 718.
[110] *Id.* at 726 (Beezer,C.J., dissenting).
[111] *Id.* (Beezer,C.J., dissenting).
[112] *Id.* (Beezer,C.J., dissenting).
[113] *Id.* at 718.
[114] *Id.* at 718-19.
[115] *Id.* at 720.
[116] *Id.* at 724.

standing in the place of the hypothetical bona fide purchaser, could not avoid the lien.[117]

VI. AREAS OF DISPUTE IN PRODUCER'S LIEN

Producer's lien law cases arise in state court and frequently in federal bankruptcy court as well. This section will discuss issues that arise as to priority of lien rights, validity of subordination and waiver of priority, disputes over co-mingled agricultural products and survivability of a grower's rights once the processor no longer has possession of the product. This body of law continues to develop with state and federal courts handing down holdings that, at times, appear to be quite divergent.[118]

A. Determining what is a Producer; what is a Processor

The definitions of "producer" and "processor" are provided in Cal. Food & Agric. §§ 55407 and 55408.[119] Examples of how case law interprets "processor" includes some of the following:

- a processor carrying out a stage in processing or readying the agricultural for sale, such as polishing rough rice and then selling it;[120]
- processing almonds for sale;[121]
- taking partially processed walnuts and performing additional processing; and
- processing raw tomatoes into a canned product.

1. Determination of who is a producer

In *Linida Ranches v. Minturn Nut Company,* 2002 Cal. App. Unpub. LEXIS 5897, at *3 (2002) ("*Linida*"), the plaintiff, Linida Ranches, was a grower of almonds.[122] Linida Ranches entered into a purchase contract to sell almonds to Amtrade.[123] Minturn was not a party to the purchase contract.[124] Amtrade entered into an oral agreement with Minturn that Minturn would serve as a "handler of record" for the almonds since Am-

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[117] *Id.* at 719.
[118] Frazier Nuts v. American Ag Credit, 46 Cal. Rptr. 3d at 877.
[119] CAL. FOOD & AGRIC. CODE §§ 55407, 55408 (Deering 2009).
[120] *In re* Cal. Pacific Rice Milling, 265 B.R. 237, 238 (Bankr. E.D. Cal. 2002).
[121] Frazier Nuts v. American Ag Credit, 46 Cal. Rptr. 3d at 872.
[122] Linida Ranches, Inc., v. Minturn Nut Company, (2002) 2002 Cal. App. Unpub. LEXIS 5897, *2.
[123] *Id.* at *4.
[124] *Id.* at *4-5.

trade was not licensed as a handler.[125] Minturn's tasks were to (1) arrange for recordation and payment of almond inspection by USDA; (2) provide assessment payment to the Almond Board; and (3) arrange for shipment of inedible nuts to an oil processor.[126] Minturn never acquired possession of the almonds and was not licensed as a processor.[127] The processing of the almonds was carried out by Almond Tree Hulling, Inc.[128]

Linida filed a cause of action against Amtrade, Gallegos (sole shareholder of Amtrade) and Minturn.[129] The allegations against Minturn included: (1) foreclosure of producer's lien and violations of processor's licensing law; (2) conversion; and (3) injunction.[130] The Fifth Appellate District upheld that Minturn was not liable as either a processor or under a theory of agent liability for Amtrade's action.[131] Minturn was not a processor for the purposes of the Cal. Food & Agric. Code § 55638, and held that the plain meaning of the section was that it is the removal of farm product subject to a producer's lien.[132] Minturn established that it did not act as a processor since it did not solicit, buy, contract to buy, or take title to, or possession or control of, Linida's almonds for the purpose of processing or manufacturing them.[133] The agreement between Amtrade and Minturn did not require Minturn to purchase, or take title to, or possess or control Linida's almonds.[134] The *Minturn* court held that performing tasks such as arranging inspections, paying assessments, arranging for disposition of inedibles, and submitting reports did not make Minturn the processor of the almonds.[135] Further, Minturn was not liable under the theory that Minturn was the processor's agent, where Minturn performed its tasks for Amtrade independently of Amtrade; Amtrade offered no instruction, supervision, or direction of Minturn's work.[136] Finally, the *Linida* court held that none of the acts performed by Minturn were violations of Cal. Food & Agric. Code § 55607 or 55609, because Linida did not sell or deliver any of the almonds to Minturn.[137]

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[125] *Id.* at *7.
[126] *Id.*
[127] *Id.* at *10.
[128] *Id.* at *5.
[129] *Id.* at *3.
[130] *Id.*
[131] *Id.* at * 36-38
[132] *Id.* at *39
[133] *Id.* at *35
[134] *Id.* at *35-36
[135] *Id.*
[136] *Id.* at *9, 38.
[137] *Id.* at *39-40.

2. Determination of who is a processor

A "processor" is defined under Cal. Food & Agric. Code § 55407 as any "person engaged in the processing ... or manufacturing of any farm product ... that buys ... or takes possession of or control of the farmed product for the purpose of processing or redelivering the product in any dried, canned, extracted, fermented, distilled, frozen, eviscerated, or other preserved or processed form." [138] The agricultural product is generally in its raw form or it may be partially processed and the "processor" readies the product for final sale.[139] For example, a walnut grower may deliver "partially processed" walnuts and the processor further processes the walnuts for sale to third-party buyers.[140] A person may not act as a processor or a cash buying processor unless the person has first obtained a license as provided in Cal. Food & Agric. Code § 56574.[141] The only specific requirements for obtaining a food processor's license are that the applicant show "character, responsibility, and good faith" and a sound financial status.[142] The producer's lien only applies where the sale of farm products is made to a buyer who has a processor's license.[143] Producer's liens do not attach to an intermediary who does not take possession or the product, nor has other involvement in the sale or processing; an intermediary who coordinates inspection of product, pays assessments, and arranges for disposition of rejected product is not considered a processor as defined in section 55407.[144]

B. Commingled Products

In re California Pacific Rice Milling, 265 B.R. 237 (E.D. Cal. 2001) *("Rice")*, held that a processor may commingle agricultural products and the producers will retain a lien over the commingled crop inventory.[145] However, the producer does not have a lien over all agricultural products that are in the processor's inventory.[146] The processor in *Rice* acquired rough rice from various purchases and various California farmers.[147]

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[138] CAL. FOOD & AGRIC. CODE § 55407 (Deerings 2009).
[139] *See id.*
[140] U.S. Bank v. Deseret Farms (*Sargent Walnut)* 219 B.R. at 882.
[141] CAL. FOOD & AGRIC. CODE § 55521 (Deerings 2009).
[142] San Benito Foods v. Veneman, 58 Cal. Rptr. 2d 571, 573-574 (Cal.Ct. App. 4th 1996).
[143] CAL. FOOD & AGRIC. CODE § 55521 (Deering 2009).
[144] Linida Ranches v. Minturn Nut Company, 2002 Cal. App. Unpub. LEXIS 5897 at *36.
[145] *In re* Cal. Pacific Rice Milling, 265 B.R. 237, 240 (Bankr. E.D. Cal. 2002).
[146] *Id.*
[147] *Id.* at 238.

Typically a rice processor will commingle rice from various producers only if the rice is the same variety and from the same year of production.[148] In *Rice,* the processor commingled the 1999 M401 variety rice purchased from the producer with 1999 M401 rice purchased from other producers.[149] In January, 2001, the producer filed for foreclosure on its producer's lien.[150] The processor also had inventories of sweet rice, long grain rice and Calrose rice in addition to the M401 variety.[151] The processor filed for Chapter 11 bankruptcy in May, 2001.[152] The producer argued that the producer's lien attached to a processor's entire inventory of rice.[153] The *Rice* court discussed that Cal. Food & Agric. § 55634 modified Cal. Food & Agric. § 55631 so that the producer's lien extends beyond the specific product of the producer and attaches to other commingled products from other farmers; as a result that which is not segregated is commingled.[154] The purpose of section 55634 is to ensure that the producer's lien is not extinguished by a processor who commingles the crops from different farmers.[155] The *Rice* court is careful to distinguish that the clear language of section 55631applies the lien only to farm products grown by the producer and section 55634 extends the lien to commingled products.[156] One example would be that liens from Producer 1 and Producer 2 would attach to a commingled inventory of Producers 1 & 2 agricultural product but where Producer 3's product was segregated then Producer 3 would not have a lien on the commingled product of Producers 1 & 2 and the first two producers would not have a lien on Producer 3's segregated product.[157]

The producer further argues in *Rice* that segregating the rice by year of production was an artificial and unfair limitation on crops available for lien attachment.[158] Here, the court discounts this argument and points out that the custom and practice of rice processors is to segregate rice crops by year because the product is perishable and the quality varies annually.[159]

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[148] *Id.*
[149] *Id.*
[150] *Id.*
[151] *Id.*at 238-39.
[152] *Id.* at 238.
[153] *Id.* at 239.
[154] *Id.* at 240.
[155] *Id.*
[156] *Id.*
[157] *See id.* at 240-41.
[158] *Id.* at 241.
[159] *See id.*

C. Producer's Lien Rights in Regards to other Secured Interests

California agricultural producer's liens provide that the producer's lien has preferred priority to all claims except laborer's claims for wages and salaries and UCC warehouse liens.[160] The lien covers the full amount owed to the producer or the value of the farm product on the date of delivery and attaches to all raw and processed forms of the farm product that include co-mingled farm products from various growers.[161] The lien remains attached while the product is in possession of the processor but does not extend to any product in excess of the amount owed to producers.[162]

1. Priority of interest where multiple creditors hold an interest in the proceeds

In *Bank of Stockton v. Diamond Walnut Growers*, 244 Cal. Rptr. 744, 745 (Cal. Ct. App. 3d 1988), the issue does not involve a producer's lien but the case provides a useful discussion of priorities between competing secured creditors.[163] The producer was Bella-Farms Partnership, a grower who operated a walnut and chestnut ranch.[164] Bella-Farms became a member of Diamond Walnut Growers ("Diamond"), a nonprofit agricultural marketing cooperative, in 1982.[165] The agreement provided that Bella-Farms would sell all walnuts grown during a five year period to Diamond.[166] Diamond was obligated to market the walnuts and pay Bella-Farms its pro rata share of the member proceeds.[167]

In advance of the receipt of proceeds, Diamond made several loans to Bella-Farms pursuant to written agreements.[168] Diamond filed a financing statement pertaining to the loan agreements with the Secretary of State in 1982.[169] Previously, Bella-Farms had borrowed money from the Bank of Stockton ("Bank") in 1981 and the loan was originally unsecured by crop proceeds.[170] Bella-Farms did not repay the loan on January 31, 1983, as originally obligated and at that time Bella-Farms gave to the

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[160] CAL. FOOD & AGRIC. CODE § 55633 (Deering 2009).
[161] Frazier Nuts v. American Ag Credit, 46 Cal. Rptr. 3d 869, 874-75.
[162] *Id.*
[163] *See* Bank of Stockton v. Diamond Walnut Growers, 244 Cal. Rptr. 744, 745 (Cal. Ct. App. 3d 1988).
[164] *Id.* at 745.
[165] *Id.* at 745-46.
[166] *Id.*
[167] *Id.*
[168] *Id.*
[169] *Id.*
[170] *Id.* at 746.

Bank a "valid, insurable lien on certain equipment ... and a valid insurable first lien on all crops grown on the property and a first assignment of all proceeds from the sale of all crops grown on the property..."[171] Neither the Bank nor Diamond had actual notice of each other's interest at the time they filed their financing statements with the State.[172] The member proceeds from sale of Bella-Farms 2003 walnut crop was approximately $220,000: Bella-Farms owed in excess of $500,000 to the Bank and about $135,000 to Diamond.[173] The California Third Appellate Court decided on appeal the priority between competing security interests between the Bank and Diamond.[174]

Generally, the priority of a security interest depends upon its being "perfected."[175] This happens when the security interest has attached and all applicable steps required for perfection under Cal. Com. Code §§ 9302, 9304, 9305 and 9306 have been taken.[176] An interest is perfected when:

a) the debtor has rights in collateral (§ 9203(1)(c));

b) the security interest has "attached," i.e. has become "enforceable against the debtor" (§ 9203(2)); and

c) a "financing statement" has been filed (§ 9302 (1)(b) and 9306(3)).[177]

Where there are conflicting security interests the usual rule is that the interests are ranked according to priority in time of filing or perfection.[178] The task of determining the priority interest was complicated by the different security interests that Diamond and Bank held. Diamond's security interest was on the "member proceeds" which had status as an account as defined in UCC 9106.[179] One issue was whether Diamond's interest was perfected at the time it filed the financial statement or at some later point, such as when the walnut crop was delivered or when member proceeds were earned.[180] The California Third Appellate Court held that the security interest attached in 1982 when Diamond gave value, Bella-Farms signed the security Agreement, and Bella-Farms had

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[171] *Id.*
[172] *Id.* at 746.
[173] *Id.*
[174] *Id.* at 752-53.
[175] Royal Pigments & Chemicals v. Bomanite Corporation, 2009 U.S. Dist. LEXIS 28569, at *11 (E.D. Cal. 2009).
[176] *Id.*
[177] Bank of Stockton v. Diamond Walnut Growers, 244 Cal. Rptr. 744, 747; Royal Pigments & Chemicals v. Bomanite Corporation, 2009 U.S. Dist. LEXIS at *11.
[178] Bank of Stockton v. Diamond Walnut Growers, 244 Cal. Rptr. 744, 749.
[179] *Id.* at 747.
[180] *Id.* at 748-49.

rights in the account.[181] In contrast, the Bank obtained a security interest in both the crop and the proceeds in 1983.[182] The Court considered that as to the crop, the Bank was the secured creditor and Diamond was an unsecured creditor.[183] However, as to the rights to receive the "member proceeds," both parties were perfected secured creditors and Diamond's interest was in first priority because it had filled its UCC statement prior to the Bank.[184] "Priority is assigned as to the particular collateral in issue."[185] If the crop had been marketed to anyone but a secured creditor with a higher priority interest, here Diamond, then the Bank would have been the sole secured creditor to the funds which were the proceeds of the transaction.[186] The Bank's security interest in the walnuts continued after the transfer of possession to Diamond.[187] However, the court held that the Bank's security interest was extinguished when Diamond sold the walnuts.[188] The court awarded the "member proceeds" to the cooperative and considered that the cooperative's security interest had priority in that it was filed earlier in time.[189]

2. A Bankruptcy Court has interpreted the producer's lien law and held that the producer's lien was extinguished when the processor was no longer in possession of the product

The Producer's Lien law does not provide an express lien on the proceeds derived from the sale of the farm products.[190] At issue in *U.S. Bank v. Deseret Farms,* 219 B.R. 880 (E.D. Cal. 1998) (*"Sargent Walnut"*), was whether the secured loan from U.S. Bank or Deseret's producer's lien had the superior claim over the proceeds in Sargent Walnut Ranch's account and if the producer's lien shifts from the product to the sale proceeds.[191] Sargent Walnut Ranch ("SWR") was a walnut "processor" who obtained a loan from U.S. Bank that was secured by inventory, accounts

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[181] *Id.*
[182] *Id.* at 749.
[183] *Id.* at 749-50.
[184] *Id.*
[185] *Id.* at 750.
[186] *Id.*
[187] *Id.* at 752.
[188] *Id.*
[189] *Id.* at 750.
[190] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. 880, 883 (Bankr. E.D. Cal. 1998).
[191] *Id.* at 881.

receivable, sale proceeds and the personal property of SWR; the loan was initially perfected on January 30, 1987 and restated on April 10, 1995.[192]

During August, 1996, Deseret, a "producer" of walnuts, sold and delivered multiple shipments of partially processed walnuts to SWR.[193] SWR further processed the walnuts and sold them to a third party without paying Deseret for the walnuts.[194] SWR deposited the sale proceeds into a Wells Fargo account.[195] SWR filed for Chapter 7 bankruptcy on August 27, 1997, and the sale proceeds were deposited in the court registry.[196] The Court held that U.S. Bank had a perfected security interest in SWR's inventory, accounts and proceeds, and Deseret had a producer's lien from the time that Sargent Walnut first took possession of the walnuts until the time they were sold to third party buyers. [197] The Court was critical of Deseret for failing to take back a purchase money security interest in the walnuts at the time of their sale to SWR and then failing to enjoin SWR from the continued transfers of Deseret's walnuts.[198]

The court held that the proceeds were the collateral of the U.S. Bank and Deseret's producer's lien was extinguished when Sargent Walnut was no longer in possession of the walnuts. [199] The *Sargent Walnut* analysis and holding is criticized by the Fifth District Appellate Court in *Frazier Nuts v. American Ag. Credit*, 46 Cal. Rptr. 3d 869, 877 (Cal. Ct. App. 4th 2006) *("Frazier Nuts")*, which arrived at a contrary holding as to the continuation of a producer's lien over sale proceeds.[200]

3. State court held that the producer's lien extended to the proceeds derived from the sale of the product

In what is considered the most important producer's lien decision in recent years, the Fifth District Appellate Court considered the issue in *Frazier Nuts*[201] whether California's producer's lien statute grants a producer priority to the proceeds from a processor's sale of farm products

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[192] *Id.*
[193] *Id.* at 882.
[194] *Id.*
[195] *Id.*
[196] *Id.*.
[197] *Id.* at 881-82.
[198] *Id.* at 883, 886.
[199] *Id.* at 886.
[200] Frazier Nuts v. American Ag. Credit, 46 Cal. Rptr. 3d 869, 877 (Cal. Ct. App. 4th 2006).
[201] *See infra* note 267 (*Frazier Nuts* is a closely related state court case to the bankruptcy case of *In re* Central Valley Processing).

over the secured lender.[202] The plaintiffs in *Frazier Nuts* were almond growers and Central Valley Processing was a processor with facilities located in Merced, California.[203] The defendant was American Ag Credit, a production credit association and a secured lender to Central Valley.[204] The plaintiff growers delivered almonds to Central Valley from 2002-2003 and each grower received a promise of payment from Central Valley.[205] Central Valley had a lending relationship with American Ag and its predecessor in interest that dated to 2000.[206] After a series of renewed loans, American Ag established a maturity date of November 1, 2002, for the principal of approximately $4 million.[207] The collateral securing the loan was Central Valley's inventory of almonds, accounts receivable, and the processing equipment located in Merced, and the loan was further secured by the personal guarantees of Central Valley's five shareholders.[208] The personal guarantees motivated the managers of Central Valley to resolve the debt owed to the secured lender over the debt owed to the growers.[209] When Central Valley failed to fully meet the maturity date for the $4 million loan the lender communicated its intent to obtain full payment of the loan.[210] Central Valley filed for Chapter 11 bankruptcy on February 21, 2003, and the bankruptcy was later converted to a Chapter 7.[211] The Bankruptcy Court ordered additional funds paid to the American Ag in June, 2003, subject to valid claims by the growers.[212]

The growers filed complaints against American Ag based on multiple legal theories: (1) intentional interference with economic relations; (2) money had and received; (3) conversion; (4) unjust enrichment; and (5) unfair business practices in violation of Cal. Bus. & Prof. Code § 17200.[213] The fundamental dispute between the growers and the secured lender concerned the grower's claim to the proceeds generated by the processor's sale of almonds to third parties.[214] The Superior Court held that (1) the secured lender's "mere acquiescence" in Central Valley's

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[202] Frazier Nuts v. American Ag. Credit, 46 Cal. Rptr. 3d at 871.
[203] *Id.*
[204] *Id.* at 872.
[205] *Id.*
[206] *Id.*
[207] *Id.*
[208] *Id.*
[209] *Id.*
[210] *Id.*
[211] *Id.* at 873.
[212] *Id.*
[213] *Id.*
[214] *See id.*

decision not to pay the growers did not create a triable issue of fact in regards to the lender's intent to interfere with contractual relations, and (2) the grower's producer's lien did not extend to the accounts receivable or sale proceeds arising out of the sale of the 2002 almond crop.[215] The grower's appealed and argued that they were "entitled to recover the wrongfully diverted proceeds of the sale of their almonds."[216] The grower's argument was based on their contractual rights and on the rights arising under the producer's lien statute that address sale proceeds.[217] American Ag argued that the growers' had no lien or other right in the almond sale proceeds and American Ag's priority right as a secured lender entitled it to the sale proceeds.[218]

Important in *Frazier Nuts* is that it contains a review by the state court of the bankruptcy courts' findings in *Sargent Walnut* and *Loretto Winery*.[219] The *Frazier Nuts* Court considered and declined to follow the holding in *Sargent Walnut* and the position argued by American Ag, and found that *Sargent Walnut*'s holding would undermine the legislative purpose of protecting producers.[220] Interpreting the last sentence of Cal. Food and Agric. Code § 55638 to deny a producer priority to sale proceeds would eviscerate the producer's protection intended under the section at a time when the producer is most at risk - from a processor having financial difficulties and an inability to pay both a creditor with a security interest in the proceeds and the producer.[221]

The *Frazier Nut* Court reasoned that denying the secured lender a right to the proceeds derived from sale of the crop does not eliminate all avenues of securing a loan.[222] Nor does it "profoundly alter the risk of lending to processors...so that agricultural lending is thrown into disarray."[223] The Court's holding eliminated the risky option of securing a loan with the portion of the crop proceeds already subject to a producer's lien, but there remains other options, such as securing a loan with real property, equipment and/or the balance of the crop proceeds beyond that obligated to pay the growers.[224]

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[215] *Id.* at 873-74.
[216] *Id.*
[217] *Id.*
[218] *Id.*
[219] *Id.* at 877 (The Fifth Appellate notes that a state court it is not bound by either the federal court's holding in *Sargent Walnut* or in *Loretto Winery*.)
[220] *Id.* at 877-78.
[221] *Id.* at 880-81; CAL. FOOD & AGRIC. CODE § 55638 (Deering 2009).
[222] Frazier Nuts v. American Ag Credit, 46 Cal. Rptr. 3d 869, 882 (Cal. Ct. App. 4th 2006).
[223] *Id.* at 882-83.
[224] *Id.* at 882.

In conclusion, the Fifth District Appellate Court held that the grower's claims to the sale proceeds derived from their crops are liens upon the proceeds and the grower's liens have priority over a processor's secured lender's security interest in the proceeds.[225] The holding provided that "Cal. Food & Agric. § 55638 imposes a legal obligation on processors to use the proceeds of farm products to pay producers and further creates a correlative right in producers to the sale proceeds."[226] How far this superior lien extends remains to be determined, but it is now clear it extends beyond product in the possession of the processor.

D. Waiver of Rights

A number of processors, caught between the demands of a bank to collateralize a loan and the lien rights of the producer, have pressured producers to subordinate their lien rights to the lending bank.[227] Growers may agree to subordinate their liens and waive their priority.[228] Waiver is understood to be an intentional or voluntary relinquishment of a known right and at least one court has applied the "knowingly waived" requirements in regards to a grower agreeing to subordinate its' producer's lien rights.[229] Cal. Food and Agric. Code § 55639 limits waivers of producers liens to five ways: (1) paying the agreed value; (2) deposits of a surety bond for the value with the director of agriculture; (3) depositing cash with the director; (4) depositing as a public warehouse receipts to the director; and (5) obtaining a release from the director after payment in full for the farm product.[230]

1. Principles of waiver apply to subordination of producer's lien rights

Silva Farms v. Wells Fargo Bank (In re GVF Cannery), 202 B.R. 140 (N.D. Cal. 1996) ("*GVF*"), was a tomato cannery that borrowed working capital from Wells Fargo Bank in order to complete its annual pack of processed tomatoes, sell its inventory and collect receivables.[231] The loan was secured with the inventory and receivables.[232] GVF sought to provide to Wells Fargo the first priority creditor position and to accomplish

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[225] *Id.*
[226] *Id.* at 871.
[227] *See generally* Silva Farms v. Wells Fargo Bank (*In re* GVF Cannery) ("*GVF Cannery*"), 202 B.R. 140, 2 (N.D. Cal. 1996).
[228] *Id.* at 9.
[229] *Id.*
[230] CAL. FOOD & AGRIC. CODE § 55639 (Deering 2009).
[231] Silva Farms v. Wells Fargo Bank, 202 B.R. 140, 1-2, (N.D. Cal. 1996).
[232] *Id.* at 1.

this, GVF asked all growers to sign subordination agreements at the time they executed sales contracts with GVF.[231] Silva was a grower who was approached to sell tomatoes to GVF.[234] Brooks, a GVF representative, was introduced to Silva by an old friend of Silva.[235] Silva was asked to sign an agreement that would subordinate his producer's lien first priority rights to Wells Fargo.[236] Silva was illiterate and Brooks represented that the terms of the subordination agreement, "would do Silva no harm...that the bank has guaranteed the money's going to be there for the tomato crop" and that Silva would be paid.[237] Silva sought additional reassurance from Brooks and was repeatedly told that GVF was doing fine."[238] However, GVF was not on sound financial ground and when its assets were liquidated under Chapter 7 bankruptcy Silva was owed approximately $1.1 million.[239] Silva brought an adversary proceeding in bankruptcy court and argued that his waiver of his producer's lien was invalid and GVF obtained the subordination through fraud.[240] Following the Bankruptcy's Court's ruling, the District Court heard Wells Fargo's appeal and affirmed that waiver principles applied to subordination of the producer's lien.[241] The District Court held that in order for a grower to effectively subordinate its producer's lien the following is required:

> (1)The grower be informed that it had a statutory first priority lien on its product;
>
> (2)That by subordinating its producer's lien the grower was giving up its right to first priority;
>
> (3)The waiver would place the grower in a subordinate position behind a secured lender bank; and
>
> (4)If the processor went bankrupt and the processor's assets were not sufficient to cover its debts to the secured lender holding first priority position then the grower would not receive payment or, depending on the processor's assets, would not receive full payment."[242]

Although the Bankruptcy Court's decision relied heavily upon Silva's ignorance of the facts and the effect of subordination, the District Court

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[233] *Id.* at 2.
[234] *Id.*
[235] *Id.*
[236] *Id.* at 3.
[237] *Id.* at 4.
[238] *Id.* at 3-4.
[239] *Id.* at 5.
[240] *Id.* at 6.
[241] *Id.* at 9.
[242] *Id.* at 13-14.

emphasized that the effectiveness of the waiver should be determined based on the four factors identified above.[243]

2. In order for waiver of producer's lien rights to be effective it must be in accord with § 55639

Recently, the Fifth District's decision in *Frazier Nuts* was expanded in *Wells Fargo HSBC Trade Bank v. Sun Valley Nut,* No. 625050 (Cal. Super. Ct. Stanislaus County June 25, 2009)("*Sun Valley*").[244] In *Sun Valley*, grower Robert Martelli ("Martelli") delivered his 2005 almond crop to Sun Valley Nuts ("Sun Valley") which was valued at $880,010.27.[245] By June 2006, Sun Valley had paid Martelli $295,000 on account.[246] On July 26, 2006, when it could not pay the balance, Sun Valley executed a one year note to Martelli for $585,010.27.[247] Over time, Sun Valley made interim payments but by March, 2009, a balance remained unpaid of $347,262.72.[248]

Sun Valley had a revolving line of credit with Wells Fargo HSBC Trade Bank ("Wells Fargo") where Sun Valley deposited all accounts receivables payments in its accounts at the Wells Fargo, which then swept those accounts nightly, applying the funds collected to Sun Valley's loan balance.[249]

When Sun Valley defaulted on its loan to Wells Fargo in August, 2008, Wells Fargo had a receiver appointed.[250] The receiver sold the inventory of almonds.[251] In March, 2009, almost five years after Martelli delivered his crop to Sun Valley, the receiver moved the court for an order permitted him to distribute approximately $350,000 of the

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[243] *Id.* at 14.

[244] *See generally* Wells Fargo HSBC Trade Bank v. Sun Valley Nut, No. 625050 (Super. Ct. Stanislaus County June 25, 2009) (order Denying Pl. Mot. Instr. & Distr. Funds);*and* Martelli Opp'n to Pl. Mot. For Instr. & Order Re. Interim Distr. Funds at 2, Wells Fargo v. Sun Valley Nut, (Cal. Super. Ct. Stanislaus County, opp'n filed June 10, 2009) (No. 625050).

[245] Martelli Opp'n to Pl. Mot. For Instr. & Order Re. Interim Distr. Funds at 2, Wells Fargo v. Sun Valley Nut, (Cal. Super. Ct. Stanislaus County, opp'n filed June 10, 2009) (No. 625050).

[246] *Id.*

[247] *Id.*

[248] *Id.*

[249] *Id.*

[250] Resp. of Wells Fargo Bank to Martelli Opp'n at 1, Wells Fargo v. Sun Valley Nut, (Cal. Super. Ct. Stanislaus County, resp. filed June 18, 2009) (No. 625050).

[251] *Id.*

$750,000 on hand from the sale of inventory to Wells Fargo which claimed to have a perfected first lien on the funds.[252]

Martelli objected to the motion, contending that under *Frazier Nuts* he had a lien prior to Wells Fargo's.[253] Wells Fargo replied that (1) Martelli had waived his right to a producer's lien by accepting Sun Valley's tender of its note, and (2) that Martelli had no interest in the funds in the hands of the receiver, which constituted the proceeds of sale of crops delivered to Sun Valley years after Martelli delivered them.[254] Martelli contended that he had not waived his lien, because Cal. Food & Agric. Code §55639 sets forth five exclusive methods for waiver of a producer's lien none of which had occurred in that case.[255] Second, Martelli argued that because the Bank wrongfully took the proceeds of Martelli's crop sales by sweeping the bank account, Martelli had a prior equitable right to the funds the receiver proposed to pay over to Wells Fargo.[256]

After the hearing, the Superior Court denied the receiver's motion.[257] Effectively, the Court ruled that under *Frazier Nut*, Martelli had a producer's lien which was prior in time to that of the Bank, that no novation or waiver had occurred when Martelli accepted Sun Valley's note, and that the receiver held the funds due the Bank subject to a constructive trust in Martelli's favor.[258] The matter was thereafter settled.[259]

E. Non-Profit Cooperatives

There are exceptions under producer's lien law for non-profit cooperative associations.[260] In particular, Chapter 6 does not apply to nonprofit cooperative associations.[261] However, the Legislative intent of Cal. Food and Agric. Code § 55461 was not to prevent or prohibit a qualified association of producers from asserting the rights of a producer under either

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[252] *Id.* at 2.

[253] Martelli Opp'n to Pl. Mot. For Instr. & Order Re. Interim Distr. Funds, *supra* note 245, at 2-3.

[254] Resp. of Wells Fargo Bank to Martelli Opp'n, *supra* note 250, at 2-3.

[255] Martelli Opp'n to Pl. Mot.for Instr. & Order Re. Interim Dist. Funds, *supra* note 245, at 3.

[256] *Id.* at 5.

[257] Wells Fargo HSBC Trade Bank v. Sun Valley Nut, No. 625050, slip op. at 2 (Super. Ct. Stanislaus County June 25, 2009) (order Denying Pl. Mot. Instr. & Distr. Funds).

[258] *See generally id.* (The court denied the receiver's motion, confirmed the prior tentative ruling for Martelli's Opposition (which argued that Martelli had a superior claim than the Bank under his Producer's Lien right) and the court held that *Frazier Nuts v. American AG Credit* is controlling, at 2).

[259] *Id.*

[260] CAL. FOOD & AGRIC. CODE § 55461 (Deering 2009).

[261] *Id.*

Chapter 6 (commencing with § 55401) or Chapter 7 (commencing with Section 56101) of Division 20, in connection with any product produced by its members.[262] In *Allied Grape Growers v. Bronco Wine*, 249 Cal. Rptr. 872, 885-86 (1988), the Fifth District Appellate Court denied Cal. Food and Agric. Code § 55881 damage provisions to Allied in that Allied was a nonprofit cooperative association formed under Cal. Food and Agric. Code § 54001 *et seq.*[263] Since Cal. Food and Agric. Code § 55881 is part of Chapter 6, division 20, the Court held that the express terms of Cal. Food and Agric. Code § 55461 precluded Allied from collecting damages under Cal. Food and Agric. Code § 55881.[264] Under Cal. Food and Agric. Code § 55631.5, "a nonprofit cooperative association acting as a producer bargaining association may assert a producer's lien for, or on behalf of, its members."[265] This allows the producer's lien law to be applied to the activities of the organization in dealing with farm product of non members of the organization and activities which involve acting as a producer bargaining association asserting the lien rights of its members.[266]

F. Producer's Liens in Bankruptcy

1. Potential for conflicting interests in bankruptcy between growers, debtor and trustee

McGranahan v. Christian (In re Central Valley Processing), 2007 Bankr. Unpub. LEXIS 926, (E.D. Cal 2007) [267] was a large complex bankruptcy involving many growers with "producer's liens" where the interest of the growers was in conflict with the debtor, the trustee, and the committee of unsecured creditors; so that consolidating the growers representation into a Growers' Committee provided effective representation of the growers' interests.[268] Central Valley, the Debtor, was in the business of processing and selling almonds that it had acquired from approximately sixty-four persons and entities who were produc-

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[262] *Id.* at Note at 2.

[263] Allied Grape Growers v. Bronco Wine, 249 Cal. Rptr. 872, 885-86 (Cal. Ct. App. 3d 1988).

[264] *Id.*

[265] CAL. FOOD & AGRIC. CODE § 55631.5.

[266] *See id.*

[267] McGranahan v. Christian (*In re* Central Valley Processing) *(Central Valley)*, 2007 Bankr. LEXIS 926, 17 (E.D. Cal 2007) *unpublished.* (*Frazier Nuts v. American Ag.* is a closely related state court case to *In re* Central Valley Processing.)

[268] *Id.*

ers/growers of almonds.[269] Central Valley filed for a voluntary Chapter 11 bankruptcy on February 21, 2003.[270] Following the debtor's motion to use accounts receivable and to continue selling the almond inventory in order to generate funds for operating expenses, the court appointed *sua sponte* the "Growers' Committee" to protect the growers' rights under the California Food and Agriculture Code.[271] The Court had observed in the bankruptcy proceeding that the growers, as a group, had priority lien rights based on Cal. Food and Agric. Code § 55631 in regards to the almond inventory then in the possession of the debtor.[272] The Court was concerned that the debtor was not recognizing, honoring or protecting those rights.[273] Although the growers occupied the position of a secured creditor with each grower holding an undivided equal priority claim on the almond inventory, there was not sufficient inventory to meet the grower's claim.[274] Pursuant to 11 U.S.C. § 1102(a)(2) and the court's inherent authority under 11 U.S.C. §105(a) the Bankruptcy Court ordered the appointment of the Growers' Committee and authorized employment of the Committee's attorney.[275]

Subsequently, the Court allowed "the Debtor to process and sell the Almond Inventory" and the proceeds were segregated with the statutory Grower Liens attached to the Grower Proceeds.[276] The Growers' Committee and its appointed counsel continued to protect the growers' rights after the defendant's bankruptcy was converted to a Chapter 7.[277] The record provides that the available almond proceeds were collected and distributed to the growers with net proceeds of nearly $3.1 million.[278] The amount of the proceeds recovered was estimated to be 85% plus, of the growers' claims, plus payment of fees and expenses to legal counsel.[279]

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[269] *Id.* at 3.
[270] *Id.*
[271] *Id.* at 16-17.
[272] *Id.* at 16.
[273] *Id.*
[274] *Id.* at 16-17.
[275] *Id.* at 17-18.
[276] *Id.* at 18.
[277] *Id.* at 20.
[278] *Id.* at 18.
[279] *Id.* at 21.

VII. ENFORCEMENT MECHANISMS AND REMEDIES

"The producer's lien attaches upon delivery to the processor of the entire farm product inventory of the processor."[280] Generally "a producer's lien on farm products that are in the possession of a processor is superior to a prior perfected security interest in the farm products."[281]

A. Enforcement Mechanisms

It is imperative that a producer not sit on its rights when faced with a potentially insolvent processor. A producer may sue to enforce a lien and "may get an injunction to restrain the doing of any acts on the part of the processor that would have the effect of removing the product from the processor's possession."[282] Further, a producer may have causes of action against a third party/secured lender who has received the sale proceeds of the product in conflict with the priority interest held by the producer, including: conversion, unfair business practices, intentional interference with economic relations, money had and received, and unjust enrichment.[283]

1. Lien rights may be lost or compromised once the product is no longer in possession of the processor

The Court in *Sargent Walnut* decided that the right of a producer to attach a producer's lien to the proceeds derived from the sale of the farm products was lost where the processor no longer possessed any inventory of the product.[284] The *Sargent Walnut* case involved Deseret Farms as a producer of walnuts who delivered to Sargent Walnut for processing approximately 139,072 pounds of walnuts during August of 1996.[285] The total amount that Deseret Farms invoiced Sargent Walnut for was approximately $310,034.[286] Sargent Walnut completed processing on the walnuts and sold them to a third party buyer receiving $303,580 in pro-

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[280] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 882; CAL. FOOD AGRIC. CODE § 55632.

[281] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 882.

[282] Valley Farm v. Andrew (*Loretto Winery*), 898 F.2d at 722.

[283] *See* Frazier Nuts v. American Ag. Credit, 46 Cal. Rptr. 869, 882-831 (Cal. Ct. App. 4th 2006) (although the *Frazier Nut* court rejected some of the causes of action the court allowed that there were sufficient facts to state causes of action for conversion and unfair business practices).

[284] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 882.

[285] *Id.* at 882.

[286] *Id.*

ceeds.[287] On August 27, 1997, Sargent Walnut filed for Chapter 7 bankruptcy and the remaining proceeds of $295,361 from Deseret Farms' walnuts were turned over to the bankruptcy trustee.[288] At the time that Sargent Walnut filed for bankruptcy the processor no longer possessed any of Deseret Farms' walnuts.[289] The Court discussed that while the producer's lien law provides a variety of rights, there is no express provision granting a producer's lien on the proceeds from the sale of farm products.[290]

In the 2006 case, *Frazier Nuts*, the Fifth District Appellate Court held that the legislature intended that a producer's lien attaches not only to the farm products sold by that producer, but also attaches to the processor's entire farm product inventory.[291] If the producer is not paid then a suit may be filed to foreclose on the producer's lien.[292] During the adjudication of the suit the producer may obtain an injunction against the processor to restrain the processor from selling or transferring the product out of the possession of the processor.[293] A creditor faced with a bankrupt processor could file an adversary proceeding in bankruptcy court to enforce their producer's liens.[294] Additionally, a processor that transfers processed farm product without paying the producer would be subject to mandated civil and criminal penalties.[295] Financial relief is available to an unpaid producer for farm products grown or produced in California.[296] Cal. Food and Agric. Code § 56701 created the Farm Products Trust Fund, which may compensate up to fifty percent of any claim for unpaid farm creditors upon default by licensed produce sellers, but not more than fifty thousand dollars against any one licensee.[297]

However in contrast to the state court's holding in *Frazier Nuts*, the Bankruptcy Court found that a producer's lien could be extinguished

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[287] *Id.*

[288] *Id.*

[289] *Id.*

[290] *Id.* at 883.

[291] Frazier Nuts v. American Ag Credit, 46 Cal. Rptr. 869, 871-72 (Cal. Ct. App. 4th 2006).

[292] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 883.

[293] *Id.*

[294] Alvarez Farms v. Bank of California (*T.H. Richards Processing*), 910 F.2d at 642.

[295] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 883; CAL. FOOD & AGRIC. CODE §§ 55901, 55922 (Deering 2009).

[296] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 883; CAL. FOOD & AGRIC. CODE § 56708 provides that money deposited in the products fund shall only be used to pay for farm products grown or produced in California. Under section 56701 the producer may receive up to 50% of its claim, with a limit of $50,000 per year to be paid on claims against any one processor.

[297] CAL. FOOD & AGRIC. CODE § 56701, 56707 & 56708 (Deerings 2009).

where the product is transferred out of the possession of the processor.[298] In *Sargent Walnut,* the transfer of the walnuts from the processor to a third party buyer, and entirely out of the possession of Sargent Walnut, was pivotal to the Court's determination that Deseret's producer's lien was extinguished.[299] The District Court considered that its holding was consistent with Cal. Com. Code § 2403, which recognizes that a bona fide purchaser for value acquires good title from a seller even though the seller violated the law.[300] Deseret Farms, the producer, was criticized by the District Court for relying upon its producer's lien where Deseret could have obtained a purchase money security interest in its walnuts at the time of sale to Sargent Walnut.[301] Although not extensively discussed, the Court observed that Deseret was aware that Sargent Walnut was having solvency issues and did not attempt to protect its interest in the product for over a year, and until the walnuts were entirely out of the possession of the processor.[302]

This Article suggests that the *Sargent Walnut* decision appears inconsistent with other courts' willingness to trace proceeds derived from the sale of goods subject to liens. Relying upon Cal. Com. Code § 2403, the District Court, in *Sargent Walnut,* discussed that liens predicated on possession are "not uncommon" in California law and a bona fide purchaser for value acquires good title even where the seller had sold the product in violation of the law.[303] Applying the *Sargent Walnut* reasoning that "the producer's lien does not attach to the proceeds derived from the total liquidation of the product,"[304] is inconsistent with the protection afforded producer's liens in Cal. Food and Agric. Code § 55638 which permits the sale of the subject goods to satisfy the lien obligations.[305] If the sale of the producer's goods is permitted under the code section, then how can the proceeds *received* from sale not be subject to the producer's lien? Particularly when the provisions of the California Food and Agricultural Code are to be liberally interpreted to provide for their purpose and the purpose of the producer's lien laws is to protect of the financial viability of farmers and growers.[306]

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[298] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 886.
[299] *Id.*
[300] *Id.* at 885-86.
[301] *Id.* at 886; Cal. U. Comm. Code § 9312.
[302] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 883.
[303] *Id.* at 886.
[304] *Id.*
[305] Alveraz Farms v. Bank of California (*T.H. Richards*), 910 F.2d at 647.
[306] U.S. Bank v. Deseret Farms (*Sargent Walnut*), 219 B.R. at 883-884.

A producer faced with facts similar to *Sargent Walnut* may find a more advantageous outcome could be realized by including the third party purchaser in the suit. The District Court commented in dicta that voiding the contract to a bona fide purchaser was a remote possibility under the *Sargent Walnut* facts; however, the Court suggested that a completed contract is unlikely to be voided.[307]

Frazier Nuts was a state court case, decided in 2006 case by the Fifth Appellate District, and the state court was not constrained by the rulings of the Ninth Circuit in *Loretto Winery* nor the Bankruptcy Court in *Sargent Walnut*.[308] As discussed, the *Sargent Walnut* holding may be distinguished from *Loretto Winery* and other cases where possession has not actually been transferred to a third party buyer. In *Loretto Winery,* the processed farm product inventory had been sold, but had not left the possession of the processor prior to the bankruptcy petition date.[309] Similarly, in *Alvarez Farms v. Bank of California* (*In re T.H. Richards Processing*), 910 F.2d 639, 649 (9th Cir. 1990), possession was found to still be with the processor even where the products had been transferred to a field warehouseman.[310] Likewise, in *Richardson v. Wells Fargo (In re Churchill Nut Company)*, 251 B.R. 143 (N.D. Cal. 2000) ("Churchill Nut"), a sheriff's possession of the products pursuant to a levy did not transfer actual possession of the products, but the products remained in the constructive possession of the debtor.[311]

2. Court finds that possession of product has not left the possession of the processor where the product is in control of levying officer

The Churchill Nut Company was a walnut, almond, and cherry processor and in 1997 entered in to a series of purchase contracts with Boeger Family Farms ("Boeger") for the delivery of walnuts.[312] Churchill Nut was already in financial difficulty and under pressure from its secured lender, Wells Fargo, and sought agreements from various growers to subordinate their priority liens to the bank's interest.[313] However, Boeger

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[307] *Id.* at 885-86.

[308] Frazier Nuts v. American Ag. Credit, 46 Cal Rptr. 3d 869. 877 (Cal. Ct. App.4th 2006).

[309] Valley Farm v. Andrew (*In re* Loretto Winery). 898 F.2d 715, 717 (9th Cir. 1990).

[310] Alvarez Farms v. Bank of California, (*In re* T.H. Richards), 910 F.2d 639, 649 (9th Cir. 1990).

[311] Richardson v. Wells Fargo Bank (*Churchill Nut*), 251 B.R. 143, 151 (N.D. Cal. 2000).

[312] *Id.* at 145.

[313] *Id.*

was one of the growers that did not sign a subordination agreement.[314] Churchill Nut owed Boeger approximately $380,658 for the walnuts and had paid approximately $21,000 when Boeger filed a state court complaint in April, 1998, to foreclose on its producer's lien and to recover damages.[315] Boeger prevailed at trial and subsequently obtained a judgment for $421,298.73 and a writ of execution was issued.[316] The Sheriff seized approximately 166 tons of shelled walnuts, but before a Sheriff's sale could take place, Churchill Nut filed for bankruptcy and the sale was stayed.[317] Pursuant to a motion by the bankruptcy trustee the walnuts were turned over to the bankruptcy estate.[318]

At issue was whether the walnuts, which were physically in possession of the Sheriff at the time the bankruptcy was filed, were within reach of the other producer's unsubordinated liens or had the walnuts been transferred and become the property of Boerger.[319] Boeger relied upon *Del Riccio v. Superior Court of California*, 115 Cal. App. 2d 29 (1952), and argued that when a writ is properly issued and executed the money collected, while in the hands of the officer, is the property of the judgment creditor and not the debtor.[320] Thus, Boeger argued that case law and the language of Cal. Food & Agric. Code § 55634 provided that the grower's lien applies to the farm product which is in possession of the processor and, so, the growers would lose their Producer's Liens when a processor loses possession.[321] The Northern District Court of California found Boeger's argument flawed.[322] On the one hand, if the Sheriff's levy caused Churchill Nut to loss possession of the walnuts, then the transfer triggered the protections of the preferential transfer statute, 11 U.S.C. § 547(b), and the trustee could potentially avoid the transfer and reclaim the walnuts as property of the bankruptcy estate.[323] Alternately, policy underlying the producer's lien law would be undermined where the assertion of a producer's lien right by one grower allows the grower to gain a lien more senior to other growers.[324] As a result of such an action, the other equally positioned grower's rights would be pre-empted in the race

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[314] *Id.* at 146.
[315] *Id.* at 145.
[316] *Id.*
[317] *Id.* at 145-46.
[318] *Id.* at 146.
[319] *Id.* at 147.
[320] *Id.* at 147-48; (*citing* Del Riccio v. Superior Court of California, 115 Cal. App. 2d 29, 31 (1952).
[321] Richardson v. Wells Fargo Bank (*Churchill Nut*), 251 B.R. at 147-48.
[322] *Id.* at 148.
[323] *Id.*
[324] *Id.* at 150.

to the courthouse.[325] Further, the District Court in Churchill Nut considered that there was a distinction between the collection of tangible property and cash under a writ and held by a third party such as the sheriff.[326] "Where there are goods of uncertain value, so that the goods must be liquidated in a sale, then the goods remain constructively in the debtor's possession."[327] Here, the court held that the walnuts in the possession of the Sheriff were constructively in the possession of the debtor and were within the reach of the producer's lien held by the other unsubordinated growers.[328]

B. Remedies- Regulatory/Criminal

A processor that fails to pay a producer may be subject to civil penalties under Cal. Food & Agric. Code § 55922.[329] Further, a processor may be subject to criminal penalties where the processor has taken actions that would defeat a producer's lien rights, for example Cal. Food & Agric. § 55905 provides that a person has committed a misdemeanor if they defraud a producer or in any way places or attempts to place the produce beyond the control, reach or recovery of the producer.[330] Generally, the failure to comply with the terms of the producer's lien sections constitutes a misdemeanor.[331] "Such a violation not only subjects the processor to suspension or revocation of its processor's license, and civil penalties of up to $500 per violation, but also constitutes a misdemeanor punishable by a fine of not less than $500 and up to $2,000 and one year in the county jail."[332] When a processor fails to pay the producer for the product, the producer may file a state court complaint against the processor for damages and proceed to foreclose on its producer's lien.[333] Following a favorable judgment the producer could obtain a writ of execution and the Sheriff could seize the product pursuant to the writ.

However, the remedies provided for in Chapter 6 of the Food and Agricultural Code are not the sole remedies available to a producer of agri-

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[325] *Id.*

[326] *Id.* at 151.

[327] *Id.*

[328] *Id.*

[329] CAL. FOOD & AGRIC. CODE § 55922 (Deering 2009).

[330] CAL. FOOD & AGRIC. CODE §§ 55901, 55905, 55906 (Deering 2009) (provide for a misdemeanor punishable by a fine of not less than $500 and up to $2,000 and one year in a county jail.)

[331] CAL. FOOD & AGRIC. CODE § 55906; *Id.* § 55878 (Deering 2009).

[332] Frazier Nuts v. American Ag. Credit, 46 Cal. Rptr. 3d 869, 878 (Cal. Ct. App. 4th 2006).

[333] U.S. Bank v. Deseret Farms, 219 B.R. at 883.

cultural products.[334] Other remedies would be available and Cal. Food & Agric. Code § 55437 recognized that "breaches of contract or potential business torts would provide fuller remedies that what would be available in Chapter 6."[335] Potential theories for recovery include: money had and received; conversion; unjust enrichment; intentional interference with contractual relationships; and unfair business practices. Further, any remedies expressly provided for in the contract are enforceable.[336]

VIII. TERMINATION OF LIEN

Cal. Food & Agric. Code § 55639 provides that termination of the producer's lien may occur by one of five actions.[337] Any processor that desires to secure a release of any of all of such liens on any product or processed product may do so in any of the following ways:

> (1)By paying the agreed or actual value of any farm product which is purchased by such processor within twenty days from the date of delivery of the farm product unless the date of payment is otherwise agreed upon in writing or such payment is secured other than by lien.
>
> (2)By depositing with the director (of Food and Agriculture) a surety bond which is executed by such processor as principal and by surety company which is qualified and authorized to do business in this state as surety in an amount which equals the current market value of the product or processed product which is intended by such processor to be sold or otherwise disposed of, as such value may appear by the sworn statement of such processor in accordance with quotations from the federal-state market news service or other evidence which is satisfactory to the director. The bond shall be conditioned that if the processor fails to pay up to the amount of such bond the lawful claims of all producers whose liens have been released by the bond, within thirty-five days after the date of the bond, the surety shall be liable to and shall pay to the state on behalf of such claimants all such lawful claims as may be covered by the amount of the bond, together with costs of suit if an action if filed on the bond.
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> (3)By depositing with the director a cash sum in lawful money of the United States which is expressly set apart by an instrument in wiring that is signed by the processor for the purpose of guaranteeing to the extent of such sum, payment of all existing claims of producers whose liens are released by the deposit within thirty-five days from the date of such deposit. The director

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[334] Bronco Wine Company v. Logoluso Farms, 262 Cal. Rptr. 899, 905-06 (Cal. Ct. App. 3d 699, 1989).

[335] CAL. FOOD & AGRIC. CODE § 55437 (*provides* The rights, remedies, and penalties which are provided for in this chapter are in additions to any other rights, remedies, or penalties which are provided for by law, and any acts or parts of acts in conflict therewith are hereby repealed.); Bronco Wine Company v. Logoluso Farms, 262 Cal. Rptr. at 906.

[336] Bronco Wine Company v. Logoluso Farms, 262 Cal. Rptr at 906.

[337] CAL. FOOD & AGRIC. CODE § 55639 (Deering 2009).

> shall be named in such instrument as trustee to carry out the purpose and intent of the instrument.
>
> (4)By designating, setting apart, and depositing in a public warehouse a quantity of any processed farm products and indorsing over to the director and delivering to him the warehouse receipt for such products for the purpose of guaranteeing to the extent of the value of such deposit payment within thirty-five days from the date of such deposit, all existing claims of producers and labor claimants whose liens are released by it.
>
> (5)By securing a release from the director after payment in full for such farm product. [338]

The Ninth Circuit considered that the use of the term "may" in Cal. Food and Agric. Code § 55637 indicated a permissive release of the lien when "any producer may...release any lien...upon arrangements being made for ...payment which are satisfactory to the producer."[339] *In re T.H. Richards Processing* the lower courts were overturned in holding that the growers had released their liens where they had taken security interests in the processor's inventory or had entered into a demand-payment arrangement.[340] The Ninth Circuit rejected the argument that when a grower agreed to a satisfactory payment plan there was an *ipso facto* release of the producer's lien.[341] The holding of the *T.H. Richards* decision was that a producer's lien is not released by the agreement of the producer to a demand-payment plan and a court should not release a producer's lien in a fashion not expressly provided for in section 55639.[342]

IX. CONCLUSION

The California agricultural lien laws are designed to reduce the financial risk to farmers in consideration of their role as essential components of California's economy and producers of the basic food resources necessary in society.[343] Over time there have been some far ranging suggestions to further reduce risk to farmers, including: changes to the California Producer's Lien and federal bankruptcy law; developing state or federal statutory trusts; establishing state insurance funds; requiring high-

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[338] *Id.*

[339] Alvarez Farm v. Bank of California (*T.H. Richards Processing*), 910 F.2d at 645.

[340] *Id.* at 647-648.

[341] *Id.* at 644.

[342] *Id.* at 646-647.

[343] *See generally* Frazier Nuts v. American Ag Credit, 46 Cal. Rptr. 3d 869, 880 (Cal. Ct. App. 4th 2006).

coverage bonding of processors; and offering insolvency insurance.[344] More practically, during difficult economic times there are lessons that can be applied from the case law and precautions that a prudent grower should consider. As discussed in this Article case law has evolved the application of the producer's lien priority in state court to include liens on both the product in possession of the processor and the proceeds that are derived from the sale.[345]

A prudent grower would want to know the financial status of the processor that the grower is dealing with. A processor's ongoing unpaid debt owed to a producer coupled with undersecured loans or loans secured by the sale proceeds should send warning flags of financial trouble to come. Growers should determine whether their processors/buyers are financially capable of paying for the crop and may want confirmation from the processors lenders that the grower will get paid. A good contract is the first line of defense for a grower's rights. Of late, some growers have been presented with contracts that call for the grower to waive their producer's lien rights.[346] This is most frequently encountered when a processor is under pressure from a lending institution to secure a superior position for the bank loan and obtain agreements from growers to subordinate their interests. A waiver of these important rights will place the grower in the position of an unsecured creditor. [347] This is not favorable. There are few good reasons for a grower to relinquish their position as a priority secured creditor.

If a troubled processor is headed for bankruptcy, a grower should not sit on its rights but promptly take action. Some possible courses of action include seeking injunctions to prevent the disposal of the product and securing the sale assets. Once a processor is in bankruptcy, the grower will want to assert a claim in bankruptcy court against the debtor, and may seek a motion to lift the automatic stay to retake possession of the products or negotiate the terms for sale of the product. The interest of growers is not the same as the interest of an unsecured creditors' committee, unless the grower waived its producer's lien rights.[348] The bankruptcy courts have allowed the formation of a "Growers' Commit-

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[344] Dale Bratton, Ph.D., *The California Agricultural Producer's Lien, Processing Company Insolvencies, and Federal Bankruptcy Law: An Evaluation and Alternative Methods of Protecting Farmers*, 36 HASTINGS L.J. 609, 643 (1985).

[345] *See generally* Frazier Nuts v. American Ag Credit, 46 Cal. Rptr. 3d at 882-83.

[346] Walter & Wilhelm Law Group.com, *Grape Growers: "Protect Against Non Payment"*, http://w2lg.com/Articles/GRAPE%20GROWERS.pdf.

[347] *Id.*

[348] Walter & Wilhelm Law Group.com, *Be a Smart Marketer of Farm Products: Protect Against Non Payment by Processors*, http://w2lg.com/Articles/smart%20marketer.pdf

tee" in complex bankruptcies to look after the interests of the growers.[349] A growers' committee may be more effective in protecting the grower's mutual interest than a grower acting alone. Growers, as producers, are entitled to special protection afforded in California producer's lien laws and a prudent grower will want to be familiar with the available benefits and challenges of the lien laws.

[349] *Id.*