

UNITED STATES BANKRUPTCY COURT  
FOR THE WESTERN DISTRICT OF TENNESSEE  
WESTERN DIVISION

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IN RE:

ANNIE MARIE C. RHEA,  
  
Debtor.

BK #91-30327-WHB  
Chapter 11

ANNIE MARIE C. RHEA,  
  
Plaintiff,

v.

Adversary Proceeding  
No. 91-0778

FARM CREDIT SERVICES OF  
MID-AMERICA, ACA,  
  
Defendant.

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MEMORANDUM OPINION AND ORDER ON COMPLAINT  
TO DETERMINE VALIDITY, EXTENT AND PRIORITY OF DEFENDANT'S  
CLAIMS AGAINST BANKRUPTCY ESTATE

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This cause is before the court on the complaint of the plaintiff, Annie Marie C. Rhea, requesting a determination of the extent, validity and priority of the claims of the defendant, Farm Credit Services of Mid-America ("FCS"), against the bankruptcy estate. This proceeding is core pursuant to 28 U.S.C. §157(b)(2)(K). The specific issue presented is whether FCS holds a properly perfected security interest in certain cotton gin equipment located on a 1.4 acre tract of land owned by the debtor.<sup>1</sup> FCS contends that the cotton gin equipment constitutes a fixture; and therefore, it holds a properly perfected security interest in it through the

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<sup>1</sup> The trial in this cause was held on September 29, 1992. Counsels for the parties presented evidence concerning the validity and priority of FCS's alleged security interest in the subject cotton gin equipment. No evidence was put forth regarding the value of FCS's claims against the bankruptcy estate; and therefore, the Court is not ruling on that issue.

recording of its deed of trust,<sup>2</sup> which refers to "fixtures." The debtor, on the other hand, argues that the cotton gin equipment is personal property that must be specifically covered in a security agreement and a recorded financing statement in order to be properly perfected and that FCS's filed financing statements do not cover said equipment.<sup>3</sup> The following constitutes findings of fact and conclusions of law pursuant to F.R.B.P. 7052.

### **SUMMARY OF FACTS**

The defendant, FCS, is the successor in interest to First Tennessee Production Credit Association ("PCA") which engaged in financial transactions with the debtor, including the following:

- (1) On February 25, 1982, a deed of trust was executed, which secured a loan to the debtor, her son and his wife, J. S. and Rebecca O. Rhea, in the sum of \$594,900.00. The deed of trust granted PCA a first mortgage lien on certain acreage owned by the debtor and was recorded in Fayette County, Tennessee on March 2, 1982. See Tr. Exh. 11.
- (2) On May 22, 1985, an "Agreement" was entered into by PCA and the debtor, her son and his wife. As part of a compromise and settlement of several debts owed to PCA, the debtor gave PCA both first and second mortgage liens on certain acreages in Fayette County, Tennessee. A first lien was also granted against all farm equipment owned by the parties. See Tr. Exh. 13.
- (3) On May 21, 1980, a financing statement (UCC-1) was filed by PCA covering certain equipment of the debtor.<sup>4</sup> See Tr. Exh. 48.

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<sup>2</sup> See Tr. Exh. 11.

<sup>3</sup> See Tr. Exh. 48.

<sup>4</sup> Continuation statements for PCA's financing statement were filed on May 22, 1985, and May 16, 1990. See Tr. Exh. 48.

Additionally, on July 31, 1986, the debtor, her son and his wife signed a promissory note to Richard P. and Rebecca D. Ozier in the amount of \$50,000.00.<sup>5</sup> The note was secured by a lien on certain cotton gin equipment. See Tr. Exh. 10. On August 1, 1986, the Oziers filed a financing statement (UCC-1) covering the subject cotton gin equipment.<sup>6</sup> See Tr. Exh. 17.

Finally, the debtor filed her voluntary Chapter 11 petition in this court on September 19, 1991.<sup>7</sup> The complaint of the debtor in this adversary proceeding was filed December 6, 1991.

### **DISCUSSION**

In order for this court to decide whether FCS holds a properly perfected security interest in the cotton gin equipment, a determination must be made as to whether the gin constitutes a fixture.<sup>8</sup> According to Tennessee Code Annotated §47-9-313(1)(a), "[g]oods are 'fixtures' when they become so related to particular

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<sup>5</sup> The Court has permitted the debtors' creditors, the Oziers, who are Rebecca O. Rhea's parents, to intervene in this adversary proceeding. See Order Allowing Intervention (April 21, 1992).

<sup>6</sup> An amendment and a continuation statement for the Oziers' financing statement were both filed on March 28, 1991. See Tr. Exh. 17.

<sup>7</sup> On January 23, 1987, the debtor's son and his wife, J.S. and Rebecca O. Rhea, Jr., filed a Chapter 12 petition in the Western District of Tennessee. See Tr. Exh. 14. They were discharged on September 4, 1992. In addition, on January 23, 1987, the debtor also filed a Chapter 12 petition in this district. See Tr. Exh. 14. She voluntarily dismissed her case on October 24, 1991.

<sup>8</sup> The Court notes that the cotton gin is made up of numerous interlocking pieces of equipment. See Tr. Exh. 9. However, all parties have treated the gin as one object for the purposes of a fixture determination; and therefore, this Court will also accept that position.

real estate that an interest in them arises under real estate law." Courts have developed a three-part fixture test. "Whether an article is a fixture depends on (1) annexation to the realty, (2) whether the article was intended to be permanently attached to the freehold, and (3) whether the article can be removed without substantial injury to the freehold." Still v. Cal-Maine Foods, Inc. (In re Mayfield), 31 B.R. 900, 903 (Bankr. E.D. Tenn. 1983); see also Still v. City Bank & Trust Co. (In re Belmont Ind.), 1 B.R. 608, 610-12 (Bankr. E.D. Tenn. 1979).

#### **A. ANNEXATION**

The "annexation test" is generally a threshold test which depends on whether the goods are so sufficiently attached as to be considered a permanent improvement. In re Hammond, 38 B.R. 548, 551 (Bankr. E.D. Tenn. 1984). "The degree to which the article must be fastened to the property depends on its size, weight, shape, and function." Belmont Ind., 1 B.R. at 610 (quoting Comment, 42 Tenn. L. Rev. 354, 359 (1975)). "The court need only find that the items do not fall in the category of those clearly not fixtures." Id.

In the present case, the debtor's son testified that<sup>9</sup> the Rhea gin is attached to a concrete slab floor by 50 to 250 anchor bolts. The gin is of a sufficient size and weight that a crane, forklift and chain hoists would be necessary to remove it. See Tr. Exh. 20. In addition, the removal might take approximately four, forty-hour weeks. Id. The cotton gin cannot be moved without great effort and cannot clearly be deemed a non-fixture. Therefore, the cotton gin is annexed to the real property and passes the threshold test.

#### **B. INTENTION**

The second part of the fixture test is "whether the article was intended [by the parties] to be permanently attached to the freehold." Mayfield, 31 B.R. at 903; see Hammond, 38 B.R. at 551. The contract between the parties provides some evidence of the intent. Hammond, 38 B.R. at 551. However, when a third party is included, the court may also look to more objective criteria such as the perspective of an "innocent

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<sup>9</sup> The debtor did not testify.

realty mortgagee." Mayfield, 31 B.R. at 903; Belmont Ind., 1 B.R. at 610. If the "innocent mortgagee" could have expected the item to be included in its mortgage, then the intention requirement will be met.<sup>10</sup> Id. In addition, "a consideration of all the individual facts and circumstances" of the particular case must be made. Id.

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<sup>10</sup> Any pre-UCC cases referenced by the parties "are relevant only as indicators of what the courts have thought realty purchasers or mortgagees should reasonably expect to be included as part of realty . . . . [However], since then reasonable expectations may have changed." Belmont Ind., 1 B.R. at 612.

In this case, the deed of trust, executed on February 25, 1982, and securing a loan from PCA to the debtor, her son and his wife, grants PCA a first mortgage lien on real property described as: "Tract Number Two . . . on which is located a cotton gin owned and operated by J.S. Rhea." See Tr. Exh. 11. In the introduction "Witnesseth" paragraph, the deed of trust also refers to "fixtures . . . thereon" the realty. Id. The "Agreement" entered into by the debtor on May 22, 1985, awards PCA a first mortgage lien on 3.4 acres of land identified as Parcel 4B, "upon which there is situated a cotton gin and other improvements, . . ." See Tr. Exh. 13. A first lien is also granted against all farm equipment. See id. Finally, on May 21, 1980, PCA filed a financing statement covering "[a]ll farm equipment and/or [i]nventory and proceeds including, but not limited to, tanks, tractors, combines, cotton pickers, tilling and harvesting equipment." See Tr. Exh. 48.<sup>11</sup> Although the deed of trust and the "Agreement" do not specifically list each individual piece of equipment that makes up a cotton gin and do not state specifically that the gin is to be a fixture included as security, they both do mention a cotton gin in the descriptions which could put third parties on notice as to that possibility. The contracts thus provide some evidence, albeit ambiguous, of an intention to include the cotton gin as a fixture.

The court may also look to other evidence reflecting on the parties' intentions. The debtor's son never testified that neither he nor the debtor intended to give PCA a security interest in the cotton gin as a fixture. Furthermore, the debtor herself did not testify in court, in deposition, or otherwise regarding her intentions. On the other hand, several exhibits were referred to in testimony and introduced by PCA, which included appraisals, loan documents, financial summaries, field reports, internal memoranda and letters. These exhibits all contain references, direct and indirect, by PCA to the cotton gin as collateral, with some providing valuations of the gin as a whole. See Tr. Exh. 16, 23-33, 35-38, 40-45. An insurance policy was also introduced, which was taken out by the debtor and her son on the cotton gin as a whole, including both the

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<sup>11</sup> See supra, at 2 n. 4.

building and the equipment. See Tr. Exh. 39. PCA is listed as the first loss payee on the policy while the Oziers, the debtor's other creditors with an alleged lien on the cotton gin equipment, are listed as the second loss payee, but for "applicable equipment only." See id. This policy therefore tends to indicate that PCA has a first mortgage and lien on both the gin building and equipment. In addition, previous Chapter 12 petitions of both the debtor and her son were introduced. See Tr. Exh. 14, 21. Their schedules are identical; Schedule A-2 lists Richard P. Ozier, Jr., as holding a security interest on "cotton gin equipment" while FCS (formerly PCA) is shown as having a first lien on the "cotton gin and two acres" as opposed to "on the cotton gin building" only. Id. Moreover, Somerville Bank & Trust is shown as having a "2nd on cotton gin and 2 acres behind PCA." Id. The debtor's son testified that he did sign his petition and did give his counsel some information and documents in order to complete the petition, but he was not positive where his counsel had obtained the information regarding the cotton gin.

Finally, the debtor introduced evidence including internal PCA memoranda, appraisals, balance sheets and loan classification memoranda which exclude the gin equipment and possibly indicate that the cotton gin was not intended as a fixture. See Tr. Exh. 1-7. However, this evidence only covers the years 1988 to 1990. The debtor alleges that FCS changed its position regarding the cotton gin around 1988 and took a more conservative approach on whether the gin was included in its mortgage. This alleged change in FCS's position would then account for the gin equipment's exclusion in the exhibits introduced. However, if FCS did indeed change its viewpoint in 1988, the exhibits would not reflect what the intentions of the parties were at the time the deed of trust and the "Agreement" were executed. Rather, the change would be explained by FCS's proof that it understood Tennessee's law may have changed subsequent to the execution of the Rhea's loan documents. Therefore, the above-mentioned exhibits are of minimal relevance in determining the parties' intent. The evidence presented by both parties leaves the court with an imperfect view of the parties' intentions; however, the proof leans toward FCS's position that the cotton gin was intended to be permanently attached as a fixture and to be included in its security. Furthermore, the objective evidence, such as the

"innocent mortgagee's" expectations based on the parties' actions and the industry as a whole, supports this position too.

Some permanent improvements were made to the real property due to the gin's location there. The debtor's son testified that the cotton gin equipment was not custom-made for the gin building. However, the majority of the larger pieces of equipment were replaced in the early 1970's. When the press was replaced, one wall of the gin building was removed so that the building could necessarily be enlarged to hold the new press. See generally Tr. Exh. 9. In addition, the metal gin building standing today had been erected around the old 1942 gin building, which was covering the gin equipment and which old building was then torn down. Finally, the seed house, which stores seed, and the shed, which can store up to six cotton trailers, were both built after the gin equipment was installed. An "innocent mortgagee" could certainly view these permanent improvements to the real property as an indication that the gin was intended to remain "permanently attached." The factors of the gin's size and the number of years it has been operated also lend themselves to that conclusion. See Tr. Exh. 15 (pictures of the Rhea gin); see also Tr. Exh. 20 (cost, equipment and time required to remove gin).

The court may also look to the general industry expectations of an "innocent mortgagee." Both the debtor's son and William B. Cowan, Jr., a farmer and ginner since 1963, testified that a gin building's primary use is as a weather protector for the gin. There was no testimony that an empty gin building could be used for anything. Therefore, the gin building might not be viewed as an independent asset by the farming industry. Mr. Cowan also testified that a market for gin equipment does exist. However, he knew of only one gin in the area which had been moved, but was familiar with other gins which had closed while leaving the gin equipment in the building. Nevertheless, Mr. Cowan was the only witness to testify regarding a market for used gins, and this court was left with an ambiguous view of the size of markets for used gin equipment for reinstallation or for scrap. The court therefore questions whether an "innocent mortgagee" would be aware of a used gin market in the area of the Rhea gin or the fact that gins may be moved from one location to another.

In summary, the court finds that the parties, that is the Rheas and PCA, intended for the cotton gin and its equipment to be permanently attached and to be treated as a fixture. Although some evidence presented is ambiguous as to intent, the court finds that the proof as a whole weighs in FCS's (PCA's) favor that the gin be deemed a fixture. An "innocent mortgagee" would reasonably have expected this particular cotton gin to be included as a fixture in its mortgage. The "intention test" is therefore met, and the court now moves to the "removability test."

### C. REMOVAL

"Generally, an article annexed to realty will be held to be a fixture if it cannot be removed without material physical injury to the freehold." Still v. City Bank & Trust Co. (In re Belmont Ind.), 1 B.R. 608, 612 (Bankr. E.D. Tenn. 1979). Therefore, the court must hear and analyze evidence such as the damage to the property after removal and the steps required to remove the article, the use of the building and property for other purposes once the article is removed, and the economics of disassembling, moving, and reassembling a used article. See In re Hammond, 38 B.R. 548, 552 (Bankr. E.D. Tenn. 1984); Still v. Cal-Main Foods, Inc. (In re Mayfield), 31 B.R. 900, 904 (Bankr. E.D. Tenn. 1983); Belmont Ind., 1 B.R. at 612; Harry J. Whelchel Co. v. King, 610 S.W. 2d 710, 714 (Tenn. 1980).

In this case, the Rhea gin building is made of metal with iron trusses and a concrete floor. As previously described, the gin itself is attached to the concrete slabs by between 50 to 250 anchor bolts. Some pieces of equipment have been removed before without dismantling the building. However, when the press was replaced, one wall was removed so that the building could be enlarged to hold it.<sup>12</sup>

Three witnesses testified regarding the ability to remove the gin. The debtor's son alleged that the gin could be disassembled and moved out the door piece by piece, but no further details were given. Mr. Cowan testified in the context of a generic gin. He stated that gin equipment may be removed part by part using

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<sup>12</sup> See Tr. Exh. 9 (list of gin equipment).

mostly farm labor. However, a crane is needed for some larger pieces. Finally, Glen C. Jordan, a consultant with Continental Murray Ginning and with fifty-two years of experience with cotton gins, appraised the effort and cost which would be required to remove the specific Rhea gin. See Tr. Exh. 20. He estimated that five workers and one supervisor would be needed and would take approximately four, forty-hour weeks. One crane, one forklift and chain hoists would also be needed. Approximately four hundred square feet of the metal roof would have to be taken off in order to remove the gin. Id. The roof could be replaced without permanent damage, except for some dents in the metal.

The removal process would be expensive. Mr. Jordan testified that the cost would total approximately \$13,300.00, not including transportation expenses.<sup>13</sup> In addition, reinstallation in a different building would cost another \$13,300.00. A new concrete foundation would also need to be built along with electricity run to the new building. Removal of the gin would therefore necessitate a large degree of time and effort, along with significant expense.

Little evidence was presented regarding the gin building's suitability for other uses if the gin is removed. The court notes that a larger cotton gin is located less than five miles from the Rhea gin. See Tr. Exh. 35. This fact reduces the chances that another ginner would install a new gin at the Rhea location.<sup>14</sup> Nevertheless, the debtor's son did testify that the storage shed, near the gin building, could be used to store farm equipment.

In summary, the cotton gin may be removed from the building with minimal physical damage to that building. However, the difficulty, time and expense of removing the gin distinguishes it from other cases in which electrical and plumbing connections could simply be disconnected. See Still v. City Bank & Trust Co.

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<sup>13</sup> The Jordan appraisal was made on June 25, 1992.

<sup>14</sup> The Court notes that the information regarding the larger and nearby gin is contained in an appraisal which was made on October 24, 1985. See Tr. Exh. 35.

(In re Belmont Industries), 1 B.R. 608 (Bankr. E.D. Tenn. 1979). Questions also remain concerning the possible uses, if any, of the gin building and the other surrounding buildings after removal. No income-producing uses were suggested for the gin building. The court therefore concludes that the cotton gin should be considered a fixture under the "removability test."

### CONCLUSION

In summary, this court concludes that the cotton gin equipment located on the 1.4 acre tract of land owned by the debtor constitutes a fixture. The cotton gin is (1) annexed to the realty, (2) was intended to be permanently attached to the freehold, and (3) cannot be easily removed. FCS (formerly PCA) thus holds a first priority, properly perfected security interest in the cotton gin and its equipment through the recordation of its deed of trust covering the said 1.4 acre tract.<sup>15</sup> Richard P. and Rebecca Ozier therefore hold a second priority lien on the cotton gin equipment because their financing statement was recorded subsequent to FCS's deed of trust. See Tr. Exh. 17, 48.

Although the court has determined the cotton gin's fixture status, no proof was introduced concerning the amount of FCS's secured claim on the cotton gin and the extent, validity and priority of FCS's other claims against the bankruptcy estate.<sup>16</sup> Therefore, this court cannot make any final determinations regarding FCS's claims, including §506 valuations.

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<sup>15</sup> Because the cotton gin equipment is a fixture, not personal property, the issue of whether the gin equipment was specifically covered in PCA's (now FCS's) financing statement is now moot. See Tr. Exh. 48. In addition, the debtor never raised a question regarding the filing of FCS' deed of trust; and therefore, this court will assume proper perfection of FCS' mortgage. See Tr. Exh. 11.

<sup>16</sup> The complaint of the debtor and/or the plaintiff, Annie Marie C. Rhea, requests a determination of the extent, validity and priority of the claims of the defendant, FCS, against the bankruptcy estate. See Complaint at 4-5.

**IT IS THEREFORE ORDERED** that a status conference shall be set for Monday, January 11, 1993, at 10:00 a.m., in Courtroom 680, 200 Jefferson Avenue, Memphis, Tennessee. Prior to or at that time, the court will accept stipulations regarding the extent, validity and priority of FCS's claims, and at that conference, the parties will discuss the particular issues left for further adjudication at trial. If this date is not mutually agreeable for counsel, said counsel may consult with each other and Ms. Carol Smith, the courtroom deputy, for an alternate date. If the status conference reveals that the parties are unable to stipulate as to the remaining issues, the Court will set this proceeding for further trial. The Court will not enter a judgment until a final order is entered on all issues.

SO ORDERED this 10<sup>th</sup> day of December, 1992.

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WILLIAM HOUSTON BROWN  
UNITED STATES BANKRUPTCY JUDGE

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