

IN THE UNITED STATES DISTRICT COURT FOR THE
DISTRICT OF NEBRASKA

IN RE:

MAHLOCH FARMS, INC.,

Debtor.

IN RE:

HARVEY and ALICE MAHLOCH,

Debtors.

NORWEST LEASING, INC.,

Appellant,

v.

C. G. WALLACE, III, Trustee,

Appellee.

BK. 82-0-669

FILED
DISTRICT OF NEBRASKA

OCT 11 1984

BK. 82-0-670

William L. Olson, Clerk
By _____ Deput

CV. 83-0-838

MEMORANDUM OPINION

This matter comes before the Court on appellant's notice of appeal from an order of the bankruptcy court overruling appellant's motion requesting that the trustee surrender \$17,250 held in escrow on account of center pivot irrigation equipment sold by the trustee. After consideration of the findings made by the bankruptcy court, the briefs and oral argument of the parties, and the applicable law, the Court reverses the order of the bankruptcy court for the reasons hereinafter stated.

FINDINGS OF FACT

Mahloch Farms, Inc. [hereinafter referred to as Mahloch] entered a ten-year lease agreement with NBC Leasing Company [hereinafter referred to as NBC] for rental of eight center pivot irrigation sprinklers. Only one of the eight irrigation sprinklers, however, is the subject of this lawsuit.

Soon after entering the lease agreement, NBC filed an informational financing statement in Mahloch's county of residence (Saline County) and in the county where the irrigation equipment was located (Perkins County). The informational financing statement filed in connection with the lease agreement properly listed the underlying real estate for seven of the eight irrigation sprinklers. One of the center pivot sprinklers was, however, shown to be located on the southeast quarter section of property in Perkins County when in fact it was located on the southwest quarter of that particular section in an area not owned by Mahloch.

Mahloch transferred its interest in the lease agreement to Lease Northwest, Inc., which in turn, assigned its interest to appellant. Subsequently, Mahloch filed a petition for relief under Chapter XI of the bankruptcy code and discontinued making payments under the lease agreement. Appellee was made trustee in the Mahloch bankruptcy and, pursuant to an agreement with appellant, appellee sold the irrigation equipment along with the underlying real estate. The sum of \$17,250 was deposited in escrow pending a final determination of the rights of the parties to the proceeds.

Appellant made a motion requesting the bankruptcy court order the appellees surrender the \$17,250 held in escrow on grounds that the appellant retained ownership of the irrigation equipment under the lease agreement. The appellee argued, and the bankruptcy court found, that the lease agreement was a disguised security transaction and, therefore, the bankruptcy court denied appellant's motion. Thereupon, appellant brought this appeal.

The appellant and appellee agree that three issues are presented by this appeal: (1) whether the center pivot irrigation equipment is personal property or a fixture (2) whether the lease agreement is in substance a secured financing arrangement rather than a lease, and (3) whether the strong-arm powers of Section 544 give appellee priority regardless of whether the agreement is a lease or secured transaction. Because the Court finds the issue of whether the irrigation equipment was a fixture to be dispositive, the Court does not entertain the other issues raised on this appeal.

DISCUSSION

1. Standard of Review

Rule 8013 of the bankruptcy rules sets forth the governing standard for the district court when reviewing orders of the bankruptcy court. Rule 8013 provides in pertinent part:

On an appeal the district court . . . may affirm, modify or reverse a bankruptcy court's judgment [or] order . . . [F]indings of fact shall not be set aside unless clearly erroneous. . . . See *First Nat'l Bank of Clinton v. Julian*, 383 F.2d 329 (8th Cir. 1967).

The bankruptcy court did not specifically find that the irrigation equipment was a fixture, but such a finding was implicit in its judgment.¹ The general rule is that where facts which will support the bankruptcy court can be inferred from facts specifically found, the reviewing court will deem such inferences were made. *In re Brown*, 21 B.R. 701 (1st Cir. 1982). Here, the bankruptcy court's order denying the proceeds held in escrow requires the inference that the bankruptcy court found the irrigation equipment to be a fixture.

1. To perfect a security interest in farm equipment, the secured party need only file a financing statement in the county where the debtor resides. Neb.Rev.Stat. § 9-401(a) (Reissue 1980), whereas to perfect a security interest in a "fixture," the filing must also be in the real estate records and indexed so that it will be found in a real estate search. Neb.Rev.Stat. § 9-313 (1972).

Appellant's financing statement was properly filed in Saline County, Mahloch's County of residence. If the bankruptcy court found the irrigation equipment to be personal property, the properly filed statement would be all that is necessary and appellant would have priority over the appellee and entitled to recover the \$17,250 in escrow.

Since the irrigation equipment was considered a fixture, § 9-313 requires a fixture filing describing the underlying real estate. Here the real estate was incorrectly shown. The bankruptcy court's denial of appellant's motion for the \$17,250 proceeds indicates that the bankruptcy court found the irrigation equipment to be a "fixture," requiring a proper description of the underlying real estate.

The "clearly erroneous" standard of review applies to findings of fact, but it does not apply to conclusions of law made by the bankruptcy court. *Solomon v. Northwestern State Bank*, 327 F.2d 720 (8th Cir. 1964). Determination of whether irrigation equipment is personal property or a fixture is a mixed question of fact and law. *Cook v. Beerman*, 201 Neb. 675, 271 N.W.2d 459 (1978). The clearly erroneous standard of review, however, remains applicable in cases of mixed questions of fact and law. *In re Bolton Hall Nursing Home*, 432 F.2d 528 (D.Mass. 1977); *In re Sierra Trading Corp.*, 482 F.2d 333 (10th Cir. 1973).

To conclude that a finding by the bankruptcy court was clearly erroneous, the Court must be left with the definite and firm conviction that a mistake was committed. *Southern Illinois Stone Co. v. Universal Engineering Corp.*, 592 F.2d 446 (8th Cir. 1979); *In re Tomash*, 24 B.R. 568 (D.Ia. 1982); *Prudential Credit Services v. Hill*, 14 B.R. 249 (D.Miss. 1981); *In re Moyer*, 13 B.R. 436 (D.Mo. 1981).

It should also be noted that the court can consider any issue presented by record, even though not discussed by the bankruptcy court, but the court must accept the bankruptcy court's findings of fact unless such a finding was clearly erroneous. *In the Matter of Cabezal Supermarket, Inc.*, 406 F.Supp. 345 (D.N.D. 1976). Therefore, though the issue of whether the irrigation equipment was a fixture was not discussed by the bankruptcy court, it does not preclude review of the matter by this Court.

Accordingly, the Court will consider the question of whether the irrigation equipment was a fixture or personal property and will consider it under the clearly erroneous standard.

2. Fixture Question

Analysis of the merits of the case begins with a discussion of a recent Nebraska Supreme Court decision in the *Bank of Valley v. U. S. Nat'l Bank of Omaha*, 215 Neb. 912, 341 N.W.2d 592 (1983). In *Bank of Valley*, the Nebraska Supreme Court set forth its long-standing three-tier test to determine whether property is a fixture:

In determining whether a thing has become a fixture, the following factors are considered: 1st. Actual annexation to the realty, or something appurtenant thereto. 2d. Appropriation to the use or purpose of that part of the realty with which it is connected. 3d. The intention of the party making the annexation to make the article permanent accession to the freehold. This intention being inferred from the nature of the articles affixed, the relation and situation of the party making the annexation, the structure and mode of annexation, and the purpose or use for which the annexation has been made. [Citation omitted.] 215 Neb. at 341 N.W.2d at 594-5.

The *Bank of Valley* court noted that the crucial consideration is the intention of the parties: "The third test, namely that of intention, appears by the clear weight of modern authority to be the controlling consideration." 215 Neb. at 915, 314 N.W.2d at 595. See also *T-V Transmission v. County Bd. of Equalization*, 215 Neb. 363, 366 N.W.2d 752 (1983).

The bankruptcy court did not analyze whether the parties to the lease agreement intended the irrigation equipment to be considered a fixture. Moreover, the bankruptcy court did not consider the "nature of the article affixed, the relation and situation of the parties making annexation," or any of the other factors reflecting intent listed by the *Bank of Valley* court. Indeed, the bankruptcy court did not even have the benefit of the *Bank of Valley* decision as it ruled on appellant's motion prior to the Nebraska Supreme Court's announcement of the *Bank of Valley* decision.

There is substantial evidence that the parties intended the irrigation equipment as "personal property" and not fixtures of the land. The lease agreement between the parties specifically provided:

Equipment is and shall at all times be and remain, personal property notwithstanding that the equipment or any part thereof may now or hereafter become, in any manner affixed or attached to real property or any improvements thereof. Plaintiff's Exhibit 1 stipulation, Exhibit A, Term 20. No. 82-0069 (Bankr. D.Neb. 1983).

Under the *Bank of Valley* decision, the lease provision setting forth the parties' intent is entitled to great weight:

The intention of the parties may be made manifest by an agreement between the parties Parties are at liberty to make any agreement or arrangement with regard to the property . . . that they see fit, and if the agreement is such a one as will make the property personal property, as between those parties, it is personal property, and may be so treated. . . .

The parties concerned may give to fixtures the legal character of realty or personalty at their option, and the law will respect and enforce their understandings. 215 Neb. at 915, 341 F.2d at 595.

Applying the *Bank of Valley* rule stated above, it is clear that the parties' characterization of the irrigation equipment as "personal property notwithstanding that the equipment . . . may . . . become . . . attached to real property" is given weighty consideration. If the Court is to "respect and enforce" the understanding of the parties to this action as *Bank of Valley* requires, it must find the irrigation equipment to be "personal property" as agreed upon in the lease agreement.

The facts in *Bank of Valley* strengthen appellant's argument that the irrigation equipment in the instant case was personal property and not a fixture. In *Bank of Valley* two lien creditors each sought priority to a house built on leased land. The lease contained a "removal clause" which allowed removal of all improvements made by the lessee if removed within sixty (60) days following the end of the lease. The *Bank of Valley* court held that since the lease provided for removal of any improvements the parties intended that the house remain personal property and not become a fixture of the land.

Similar to *Bank of Valley*, appellant and appellee's lease agreement contains a specific clause designating the property "personal property," regardless of whether or not the property becomes attached to the land. Appellee argues that *Bank of Valley* stated only that where there

was a removal clause, standing alone, in the absence of any contrary intent, could the conclusion be drawn that the property was personal property and not a fixture. Appellee further argues that the bankruptcy court's finding that the irrigation equipment was a fixture is evidence of contrary intent and, therefore, *Bank of Valley* is distinguishable.

Appellee's argument on these points is misplaced. First, there is no language in *Bank of Valley* that limits the holding only to cases involving lease removal clauses. Second, the mere fact the bankruptcy court found the equipment to be a fixture is of no consequence. The trial court in *Bank of Valley* found the property there to be a fixture and the Nebraska Supreme Court reversed this finding.

Other provisions of the lease agreement also evince the intent of the parties to make the irrigation equipment personal property. The lease expressly provided that the irrigation equipment remain the property of appellant (Plaintiff's Exhibit 1, *supra*), and that it be returned upon termination of the lease if the appellee did not exercise its purchase option (Plaintiff's Exhibit 1, Term 18, *supra*).

Appellee argues that the irrigation equipment was intended as a fixture because the bankruptcy court found the agreement to be a disguised conditional sale rather than a true lease. It is true that the bankruptcy court found the parties intended an installment sales contract rather than a lease, but this finding sheds no light on the question of whether the parties intended the irrigation equipment to be considered a "fixture"

of the land. Regardless of whether the parties intended the contract to be a financing arrangement or a lease, it is clear that the parties intended the property to be "personal property" and not a fixture (Plaintiff's Exhibit 1, *supra*).

Examination of the other two tests of the fixture question, actual annexation to the realty and appropriation for the use of the realty, further supports the conclusion that the irrigation equipment here was personal property and not a fixture.

There was no evidence before the bankruptcy court that the irrigation equipment was actually "affixed" to the realty. Appellant asserts and appellee does not deny that the irrigation equipment here did not include a pump, well head or well, appurtenants which would clearly "affix" to the realty. To the contrary, the irrigation equipment here is described as a movable sprinkler system consisting only of "pipe."

No case found specifically considers the question of whether irrigation "pipe" as opposed to irrigation pumps or well heads is a fixture. But, in *Cook v. Beerman*, 201 Neb. 675, 271 N.W.2d 459 (1978), the Nebraska Supreme Court considered realty which had affixed to it an irrigation well, complete with pump and motor, that was fed with fuel from an underground natural gas line. Unassembled "pipe" and the remaining parts of the sprinkler system were stacked on the property. After restating the rules regarding fixtures shown above, the *Cook* court held:

[I]t seems clear the pump and motor were fixtures. The motor was bolted to a concrete pad which measured approximately eight to ten feet in length and four feet in width. Natural gas to power the motor was supplied from an underground line. The pump was inside the well casing and secured by bolts. 201 Neb. at 681, 271 N.W.2d at 462-3.

As for the irrigation pipe, the *Cook* court went further and stated:

[T]here is authority that the irrigation pipe and sprinkler system were also fixtures even though they were not physically attached to the real estate. *Id.*

The *Cook* court statement above would appear to support appellee's position that irrigation pipe, along with the pumps and well heads, constitute fixtures. The Nebraska Supreme Court, however, in a per curiam opinion on motion for rehearing, retracted this statement holding, "The . . . statement [that irrigation pipe and sprinkler systems are fixtures] is stricken from the opinion because it constitutes mere dicta and appears to decide a matter not at issue." *Cook v. Beerman*, 202 Neb. 447, 276 N.W.2d 84 (1979).

Striking the statement as dicta, the Nebraska Supreme Court in *Cook* rejects the position that irrigation sprinkler "pipe" is necessarily a fixture. Notwithstanding the factual difference that the irrigation pipe and sprinkler system in *Cook* was stacked behind the house as opposed to being in operation as in the case at bar, the *Cook* opinion still retains importance. The real significance of *Cook* is that the Nebraska Supreme Court, by striking the statement, indicates that when considering the

issue of fixtures, separate consideration may be given to irrigation pumps and motors on one hand, and the pipe and sprinkler system on the other.

Appellee argues that the trustee's undisputed testimony was that the irrigation equipment remained on the property from its original acquisition until the time the property was sold and that the irrigation equipment was sold with the underlying realty. The evidence indicates, however, that there was no "affixation" of the irrigation equipment to the land. As stated previously, there was no evidence before the bankruptcy court that the irrigation equipment was attached to the realty. Moreover, the appellee does not dispute the fact that the irrigation equipment was nothing more than "pipe" of a movable sprinkler system.

The fact that the irrigation equipment and realty remained on the property and were sold simultaneously is also of no great moment. Mere coexistence of the irrigation equipment with a particular section of realty does not satisfy the "actual annexation" test. The test requires, as the words convey, actual annexation to the land, not merely an improvement. Appellee argues that the irrigation equipment was "affixed" to the land since the lease agreement provided that the irrigation equipment was not to be removed. The lease, however, provided that the irrigation equipment

2. Appellant did not raise objection to appellee's assertion that there was "actual annexation" because the underlying realty and irrigation equipment were sold together. However, the sale was made under agreement, the Court assumes, agreed upon so as not to prejudice the position of either party. In the interest of fair play, it seems the appellee should not be entitled to strengthen its position from its stipulated agreement by showing both realty and irrigation pipe were sold together.

was "not to be removed from the location specified above as the address for delivery," the address being "Mahloch Farms" of Dewitt County. Plaintiff's Exhibit 1, Term 4, *supra*. In other words, the lease prohibited removal of the sprinkler equipment from "Mahloch Farms," not from the quarter section of land on which the irrigation equipment sat prior to its sale. Therefore, appellee's argument that the irrigation equipment was "affixed" to the land due to the lease provision prohibiting removal is not persuasive.. Removal of the irrigation equipment in question to other parts of Mahloch Farms would not have resulted in breach of the lease agreement.

In conclusion and applying the clearly erroneous standard to the instant case, the Court is left with the definite and firm conviction that a mistake was committed. *Southern Illinois Stone Co. v. Universal Engineering Corp.*, 592 F.2d 446 (8th Cir. 1979). Accordingly, a separate order will be entered this date reversing the decision of the bankruptcy court and remanding the matter to that court for further proceedings consistent with this opinion.

BY THE COURT:

Albert G. A. Kelly

JUDGE, UNITED STATES DISTRICT COURT