

When UCC Fixture Filings Survive Foreclosure

Yes. . .you read that correctly. Under some circumstances a UCC Fixture Filing has priority over a deed of trust **even when that deed of trust was filed first**. Whoa. . .say what? Take a look at § 25-9-334 (the statute is found at the bottom of this article). This is a somewhat unique fact pattern, but not so unique as we have come across it several times over the years. Take a look at Section (d) of the Statute. I have highlighted it for you for ease of reference. The fact pattern that causes the issue is when the personal property that is the subject of the Fixture Filing is part of a purchase money transaction. The most obvious example is a hot water heater purchased on credit from Piedmont Natural Gas. When the property owner purchases (and installs) the hot water heater on credit from PNC and PNC endeavors to perfect their security interest within 20 days, then they are entitled to priority. . .**in the water heater**. Let me say that again to make it clear. PNC's security interest in the water heater trumps the 1st lien deed of trust against the property. . .**insofar as it relates to the water heater**.

So, let's fast forward to the point where these things become issues for us. . .1st Lienholder Forecloses on the deed of trust. The result is that the high bidder owns the real estate subject to the security interest against the water heater. PNC's Fixture Filing has **NOT** been extinguished and PNC can exercise its Article 9 rights against the water heater. (Presumably, by repossessing it).

I am not sure how many of you are aware of this law. I was not exposed to it until I became a title agent. It's a little tricky and, perhaps, somewhat difficult to conceptualize. It certainly goes against our general understanding of priorities. In those cases where it has been an issue, post-foreclosure, the "solution" was to call the creditor and have them either (i) terminate the UCC; or (ii) remove the fixture that is the basis of the Filing. At that point, we could insure without exception to the Fixture Filing.

As always, please feel free to contact us with any questions.

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§ 25-9-334. Priority of security interests in fixtures and crops.

(a) Security interest in fixtures under this Article. – A security interest under this Article may be created in goods that are fixtures or may continue in goods that become fixtures. A security interest does not exist under this Article in ordinary building materials incorporated into an improvement on land.

(b) Security interest in fixtures under real-property law. – This Article does not prevent creation of an encumbrance upon fixtures under real property law.

(c) General rule: subordination of security interest in fixtures. – In cases not governed by subsections (d) through (h) of this section, a security interest in fixtures is subordinate to a conflicting interest of an encumbrancer or owner of the related real property other than the debtor.

(d) **Fixtures purchase-money priority. – Except as otherwise provided in subsection (h) of this section, a perfected security interest in fixtures has priority over a conflicting interest of an**

encumbrancer or owner of the real property if the debtor has an interest of record in or is in possession of the real property and:

- (1) The security interest is a purchase-money security interest;
- (2) The interest of the encumbrancer or owner arises before the goods become fixtures; and
- (3) The security interest is perfected by a fixture filing before the goods become fixtures or within 20 days thereafter.

(e) Priority of security interest in fixtures over interests in real property. – A perfected security interest in fixtures has priority over a conflicting interest of an encumbrancer or owner of the real property if:

- (1) The debtor has an interest of record in the real property or is in possession of the real property and the security interest:
 - a. Is perfected by a fixture filing before the interest of the encumbrancer or owner is of record; and
 - b. Has priority over any conflicting interest of a predecessor in title of the encumbrancer or owner;
- (2) Before the goods become fixtures, the security interest is perfected by any method permitted by this Article and the fixtures are readily removable:
 - a. Factory or office machines;
 - b. Equipment that is not primarily used or leased for use in the operation of the real property; or
 - c. Replacements of domestic appliances that are consumer goods;
- (3) The conflicting interest is a lien on the real property obtained by legal or equitable proceedings after the security interest was perfected by any method permitted by this Article; or
- (4) The security interest is:
 - a. Created in a manufactured home in a manufactured-home transaction; and
 - b. Perfected pursuant to a statute described in G.S. 25-9-311(a)(2).

(f) Priority based on consent, disclaimer, or right to remove. – A security interest in fixtures, whether or not perfected, has priority over a conflicting interest of an encumbrancer or owner of the real property if:

- (1) The encumbrancer or owner has, in an authenticated record, consented to the security interest or disclaimed an interest in the goods as fixtures; or
- (2) The debtor has a right to remove the goods as against the encumbrancer or owner.

(g) Continuation of subdivision (f)(2) priority. – The priority of the security interest under subdivision (f)(2) of this section continues for a reasonable time if the debtor's right to remove the goods as against the encumbrancer or owner terminates.

(h) Priority of construction mortgage. – A mortgage is a construction mortgage to the extent that it secures an obligation incurred for the construction of an improvement on land, including the acquisition cost of the land, if a recorded record of the mortgage so indicates. Except as otherwise provided in subsections (e) and (f) of this section, a security interest in fixtures is subordinate to a construction mortgage if a record of the mortgage is recorded before the goods become fixtures and the goods become fixtures before the completion of the

construction. A mortgage has this priority to the same extent as a construction mortgage to the extent that it is given to refinance a construction mortgage.

(i) Priority of security interest in crops. – Except as provided in G.S. 42-15, a perfected security interest in crops growing on real property has priority over a conflicting interest of an encumbrancer or owner of the real property if the debtor has an interest of record in or is in possession of the real property. (1965, c. 700, s. 1; 1967, c. 562, s. 1; 1975, c. 862, s. 7; 2000-169, s. 1.)