

STATE OF NORTH DAKOTA

ATTORNEY GENERAL'S OPINION 95-F-03

Date issued: February 13, 1995

Requested by: Gary R. Ness, Director, Aeronautics
Commission

- QUESTIONS PRESENTED -

I.

Whether a properly filed security agreement upon crops under North Dakota Century Code (N.D.C.C.) ch. 35-05 acts as notice to and a crop lien in favor of the filer relating to payments under federal crop insurance, hail loss insurance coverage or other disaster assistance payments relating to growing crops.

II.

Whether federal crop/hail insurance carriers have a duty to determine if such liens exist prior to making payment to loss payees under the respective policy.

III.

Whether the crop lien filing system acts as a priority system for payment purposes to lienholders.

- ATTORNEY GENERAL'S OPINIONS -

I.

It is my opinion that a properly filed security agreement upon crops under N.D.C.C. ch. 35-05 acts as notice of and a crop lien in favor of the filer relating to payments under federal crop insurance, hail loss insurance coverage and other disaster assistance payments relating to growing crops if the security agreement covers crop proceeds.

II.

It is my further opinion that federal crop/hail insurance carriers do not have a duty to determine if such liens exist prior to making payment to loss payees under the respective policy.

III.

It is my further opinion that the crop lien filing system does not determine to whom the insurance carrier is bound to make the insurance payment but does help determine the priorities for rights in the insurance proceeds received by the insured.

- ANALYSES -

I.

N.D.C.C. ch. 35-05 governs crop mortgages. N.D.C.C. § 35-05-01 prohibits security interests in growing and unharvested crops, but does not apply to:

any security interest or lien in favor of the United States, [the state of North Dakota], any county, or any department or agency of any of them, . . . nor to any financial institution as defined by section 6-01-02 or 21-04-01, nor to any other agricultural lending agency, nor to any security interest created by contract to secure money advanced or loaned for the purpose of paying government crop insurance premiums or to secure the purchase price or the rental or improvement of the land upon which the crops covered by the contract are to be grown.

A security agreement covering crops is not valid to create a security interest in crops if it also purports to claim a security interest in any other personal property. However, "crop proceeds and products, supplementary price payments and payments made in lieu of crop proceeds, including crop insurance payments" are not considered other personal property for this purpose. N.D.C.C. § 35-05-04.

N.D.C.C. § 41-09-27 defines proceeds to include insurance payable by reason of loss or damage to the collateral "except to the extent that it is payable to a person other than a party to the security agreement." Consequently, it is my opinion that a properly filed financing statement covering crops and their proceeds would act as notice of a crop lien in favor of the filer relating to payments under federal crop insurance, hail loss insurance coverage and other disaster assistance payments relating to growing crops.

It should be noted, however, that N.D.C.C. ch. 35-30 authorizes any person who processes any crop or agricultural product to obtain a lien upon the crop processed which has priority over all other liens and encumbrances on that crop. N.D.C.C. §§ 35-30-01, 35-30-03. Likewise, N.D.C.C. ch. 35-31 authorizes any person who furnishes supplies used in the production of crops to obtain a lien upon the crops. N.D.C.C. § 35-31-01. The agricultural supplier's lien has priority over all other liens or encumbrances on the crops except for any agricultural processor's lien. N.D.C.C. § 35-31-03. The court in In Re Glinz determined that agricultural supplier lienholders did not need to separately file under N.D.C.C. § 41-09-27 to protect their interest in crop proceeds. In re Glinz, 46 Bankr. 266, 277 (D.N.D. 1984).

II.

N.D.C.C. ch. 41-09 governs the rights of secured parties to collateral and, if specified in the security agreement, the products and proceeds of the collateral. Nothing in N.D.C.C. ch. 41-09 places a duty on insurance carriers to investigate or determine whether a third party holds a security interest in the insured property prior to paying a claim for damage to the property. As the court stated in Judah AMC & Jeep, Inc. v. Old Republic Insurance Co.:

The question becomes whether an insurer, before paying a routine loss, must conduct a search of public records in order to avoid becoming liable to some secured but otherwise undisclosed creditor. Such a startling and expensive requirement is certainly not required by the uniform commercial code. The act provides that insurance proceeds are subject to priority between lienholders. But these provisions would merely accord plaintiff a prior right to the insurance proceeds against a third party who might assert a claim or lien against [the property insured].

293 N.W.2d 212, 214 (Iowa 1980) (citations omitted). In accord is a recent Pennsylvania case in which the court stated:

"An insurer that has no actual knowledge of the existence of a security interest in the insured property may pay the loss directly to the debtor and is not required to examine the filing index to see if there is any security interest."

Chrysler Credit Corp. v. Smith, 643 A.2d 1098, 1101 (Pa. Super. Ct. 1994), quoting 68A Am.Jur.2d Secured Transactions § 92 (1993). Although the North Dakota Supreme Court has not addressed the issue, I believe that it would follow the rationale of the above cases. Therefore, it is my opinion that the federal crop hail insurance carriers do not have a duty to determine whether security interests or liens have been filed against the crops prior to paying the loss payees.

III.

N.D.C.C. § 41-09-33 determines priorities among conflicting security interests in the same collateral. No section of the Uniform Commercial Code covers payments made by an insurer to a loss payee under an insurance policy.

N.D.C.C. § 41-09-28 provides protection for both the buyers of crops and those having a lien or security interest in crops. Subsection 9 provides that if a secured party or lienholder intends to impose liability for a security interest or lien against a crop buyer, the secured party or lienholder must file a form with the Secretary of State or a county register of deeds to have the secured party's or lienholder's name appear on the list distributed by the Secretary of State pursuant to N.D.C.C. § 41-09-46(4). Subsection 11 of N.D.C.C. § 41-09-28 then requires a crop buyer to issue a check or draft in payment of the crop jointly to the farmer and the secured parties and lienholders who have an interest or lien in the crops and whose names appear on the list referenced in subsection 9 in order to take free of the security interest or lien on the crop. N.D.C.C. § 41-09-28(13). This section of the code only covers buyers, however. An insurance carrier is not purchasing the crop and therefore does not fall within the scope of N.D.C.C. § 41-09-28.

The priority of the various holders of security interests and liens to the proceeds of crops would be determined by the applicable sections of the statutes. As pointed out in section I above, N.D.C.C. §§ 35-30-03 and 35-31-03 both affect the priorities of holders of security interests or liens on crops. N.D.C.C. § 41-09-33(2), (5), and (6) also affect these priorities. Subsection 5 sets forth the rule that unless governed by other rules, the time of filing or the time the security interest first becomes perfected (whichever is earlier) determines the priority of conflicting security interests.

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For the foregoing reasons, it is my opinion that the crop lien filing system does not determine to whom the insurance carrier is bound to make the insurance payment, but that it does help determine the priorities of rights in the insurance proceeds received by the insured.

- EFFECT -

This opinion is issued pursuant to N.D.C.C. § 54-12-01. It governs the actions of public officials until such time as the questions presented are decided by the courts.

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