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United States V. Kimbell Foods, Inc.: A Problem Or Solution In Resolving Lien Priority Disputes?

UNITED STATES V. KIMBELL FOODS, INC.: A PROBLEM OR SOLUTION IN RESOLVING LIEN PRIORITY DISPUTES?

The recent Supreme Court decisions in *United States v. Kimbell Foods, Inc.*[1] and *United States v. Crittenden*[2] represent the Court's first examination of the choateness doctrine in over a decade.[3] The Court's holding, that the relative priority of private liens and consensual liens arising pursuant to government lending programs is to be determined "under non-discriminatory state laws"[4] raises more questions than it answers, and sets the stage for further judicial and legislative reform in a particularly chaotic area of the law.[5] Clearly, the Court's opinion calls into question the continuing viability of the choateness doctrine, which the Court itself introduced fifty years ago.[6]

The choateness doctrine was formulated by the Supreme Court to resolve priority conflicts between competing federal and non-federal liens.[7] Under the choateness doctrine, a non-federal lien's priority is measured from the time the lien becomes definite in at least three respects. The identity of the lienor, the property to which the lien attaches, and the

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[1] 99 S. Ct. 1448 (1979), *aff'g sub nom.* Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d 491 (5th Cir. 1977).

[2] 99 S. Ct. 1448 (1979) (vacating and remanding 563 F.2d 678 (5th Cir. 1977)).

[3] *See, e.g.*, United States v. Equitable Life Assur. Soc'y, 384 U.S. 323, 327-28 (1966) (mortgage foreclosure proceeding involving recorded federal tax lien and an inchoate state mortgage lien); United States v. Vermont, 377 U.S. 351, 355 (1964) (antecedent state tax lien upon property of solvent taxpayer held choate for purposes of priority over subsequent federal tax lien); United States v. Pioneer Am. Ins. Co., 374 U.S. 84, 87-92 (1963) (claim for attorneys' fees remained inchoate until finally fixed in amount in mortgage foreclosure decree entered subsequent to filing of unpaid federal tax liens; thus, claim for attorneys' fees held subordinate to federal tax liens even though federal tax liens were filed after claim for attorneys' fees had become enforceable at state law).

[4] 99 S. Ct. at 1465.

[5] *See* text accompanying note 148 *infra.* As a result of the *Kimbell* decision, the Supreme Court vacated Chicago Title Ins. Co. v. Sherred Village Assocs., 568 F.2d 217 (1st Cir. 1978), for further consideration. Hercoform, Inc. v. Chicago Title Ins. Co., 99 S. Ct. 1987 (1979). *See* note 63 *infra.*

[6] The inception of the choateness doctrine can be traced to County of Spokane, Washington v. United States, 279 U.S. 80 (1929); see notes 20-21 *infra.*

[7] *See* text accompanying notes 19-22 *infra. See generally* Kennedy, *From Spokane County to Vermont: The Campaign of the Federal Government Against the Inchoate Lien,* 50 IOWA L. REV. 724 (1965) [hereinafter cited as Kennedy]; Kennedy, *The Relative Priority of the Federal Government: The Pernicious Career of the Inchoate and General Lien,* 63 YALE L.J. 905, 911-19 (1954) [hereinafter cited as *Relative Priority*]; MacLachlan, *Improving the Law of Federal Liens and Priorities,* 1 B.C. INDUS. AND COM. L. REV. 73 (1959) [hereinafter cited as MacLachlan]; Plumb, *Federal Liens and Priorities—Agenda for the Next Decade,* 77 YALE L.J. 228 (1968) [hereinafter cited as Plumb]; Plumb, *Federal Tax Collection and Lien Problems,* 13 TAX. L. REV. 459 (1958) [hereinafter cited as Federal Tax Collection]; Wolson, *Federal Tax Liens—A Study in Confusion and Confiscation,* 43 MARQ. L. REV. 180 (1959).

amount of the lien must be ascertained in order for a nonfederal lien to be "choate" and thus perfected against subsequently arising federal liens.[8]

The choateness doctrine, however, was not the first solution for resolving priority conflicts between competing claims. Congressional enactments granting priority to claims due the federal government originated in the late eighteenth century.[9] The federal tax lien dates from the conclusion of the Civil War.[10] The original federal tax lien was a secret lien which prevailed over even subsequent bona fide purchasers.[11] Since 1913, however, Congress has enacted legislation protecting certain purchasers, mortgagees, judgment lien creditors, and pledgees against federal tax liens which have not been filed for purposes of public notice.[12]

When a debtor is unlikely to have sufficient funds to satisfy all his creditors' claims, the device for ensuring governmental priority in an insolvency proceeding is the federal priority statute, Revised Statute section 3466.[13] Section 3466 grants first priority to the federal government but does not operate as a lien.[14] Whereas a lien is a charge, security, or encumbrance upon specific property,[15] section 3466 merely provides that the federal government's claims will be satisfied first whenever any person indebted to the United States is insolvent or involved in one of several liquidation

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[8] United States v. City of New Britain, 347 U.S. 81, 84 (1954); Illinois *ex rel.* Gordon v. Campbell, 329 U.S. 362, 375 (1946); see note 39 *infra.*

[9] *See, e.g.,* Act of Mar. 3, 1797, Ch. 20, § 5, I stat. 515; Act of July 31, 1789, Ch. 5 § 21, I stat. 42. *See also* Coogan, *The Effect of the Federal Tax Lien Act of 1966 Upon Security Interests Created Under the Uniform Commercial Code,* 81 HARV. L. REV. 1369 (1968) [hereinafter cited as Coogan]; *Relative Priority, supra* note 7, at 907-11.

[10] Act of March 3, 1865, Ch. 78, 13 Stat. 470.

[11] United States v. Snyder, 149 U.S. 210, 213-15 (1893). *See also* Plumb, *supra* note 7, at 228 n.2, 229; *Relative Priority, supra* note 7, at 920-21. The original federal tax lien was a "secret" lien because there was no requirement that notice of its existence be filed. Plumb, *supra* note 7, at 228 n.2.

[12] Act of March 4, 1913, Ch. 166, 37 Stat. 1016; Revenue Act of 1939, § 401, 53 Stat. 882. Because searching for federal tax liens is impractical for purchasers of securities and motor vehicles, Congress has provided priority for such purchasers over even existing federal tax liens. I.R.C. § 6323(b)(2). For other purchasers prior to the 1966 Federal Tax Lien Act, however, the federal tax lien remained effective against the taxpayer and all other creditors. Public notice was unnecessary. *See* Plumb, *supra* note 7, at 229. *See also Relative Priority, supra* note 7, at 920-22.

[13] 31 U.S.C. § 191 (1976). Section 3466 provides:

> Whenever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be satisfied; and the priority established shall extend as well to cases in which a debtor, not having sufficient property to pay all his debts, makes a voluntary assignment thereof, or in which the estate and effects of an absconding, concealed, or absent debtor are attached by process of law, as to cases in which an act of bankruptcy is committed.

[14] United States v. Oklahoma, 261 U.S. 253, 254 (1923); United States v. Hooe, 7 U.S. (3 Cranch) 73 (1805). *See Relative Priority, supra* note 7, at 9907-08.

[15] D. EPSTEIN & V. LANDERS, DEBTORS AND CREDITORS 1-2 (1978) [hereinafter cited as EPSTEIN & LANDERS].

procedures, including probate, attachment, or assignment for the benefit of creditors.[16]

Initially, federal priority pursuant to section 3466 was valid only against unsecured creditors.[17] Section 3466 did not interfere with pre-existing liens.[18] *County of Spokane, Washington v. United States*[19] heralded a significant departure from the established interpretation of section 3466 and introduced the choateness doctrine into federal common law.[20] The Supreme Court held that a federal tax claim is superior to an antedating local lien which is neither specific nor perfected in accordance with state law.[21] Hence, the federal priority statute, section 3466, was employed in an insolvency proceeding to defeat a local tax lien.[22]

The requirement that local liens be specific and perfected was subsequently expanded in *United States v. Waddill, Holland and Flinn, Inc.*[23] The issue in *Waddill* was whether in a state proceeding under a general assignment for the benefit of creditors, section 3466 gave priority over a landlord's lien and a municipal tax lien.[24] The landlord argued that federal

[16] *See* note 13 *supra. See also* McLachlan, *supra* note 7, at 76-77; *Relative Priority, supra* note 7, at 909-11.

[17] *Relative Priority, supra* note 7, at 929. Professor Kennedy argued that § 3466 probably was enacted solely for purposes of reaching unencumbered property of the insolvent debtor. He insisted that Congress did not intend that priority payments should be made from property already subject to a mortgage or other lien. Indeed, in several nineteenth century cases, the Supreme Court refused to grant federal priority over antecedent liens. *Id.* at 907-08. *See* Brent v. Bank of Wash., 35 U.S. (10 Pet.) 262 (1836); United States v. Hack, 33 U.S. (8 Pet.) 96 (1834); Conard v. Pacific Ins. Co., 31 U.S. (6 Pet.) 110 (1832); Conard v. Nicoll, 29 U.S. (4 Pet.) 74 (1830); Conard v. Atlantic Ins. Co., 25 U.S. (1 Pet.) 637 (1828); United States v. Hooe, 7 U.S. (3 Cranch) 73 (1805).

[18] *Relative Priority, supra* note 7, at 908 n.16, 908-09, *citing* Conard v. Atlantic Ins. Co., 25 U.S. (1 Pet.) 637, 651 (1828) [no previous Supreme Court decision has established a proposition that "a specific and perfected lien can be displaced by the mere priority of the United States"].

[19] 279 U.S. 80 (1929).

[20] *Relative Priority, supra* note 7, at 908-11. The Supreme Court in *Spokane County* held that pursuant to § 3466, taxes owed the federal government by an insolvent debtor enjoyed priority over county taxes assessed on personal property of the taxpayer prior to appointment of a receiver. 279 U.S. at 93-95. The Court stressed that the county tax assessment was not supported by a specific lien under state law, because the property subject to the lien had not been seized by the sheriff nor had "any . . . necessary procedure mentioned in the statute . . ." been initiated to secure the property. *Id.* at 94. An unperfected or unspecific lien is "inchoate." *See* United States v. Equitable Life Assurance Soc'y, 384 U.S. 323, 327-28 (1966).

[21] 279 U.S. at 93-95. *See* note 20 *supra.* In order for a lien to be specific and perfected, there usually must be a public filing, such as for consensual liens and many statutory liens, or there must be an actual seizure of the property, such as for judicial liens. *See* Epstein & Landers, *supra* note 16, at 2. *See generally* Illi, Inc. v. Margolis, 267 Md. 80, 296 A.2d 412 (1972); Cannon Mills, Inc. v. Spivey, 208 Tenn. 419, 346 S.W.2d 266 (1961).

[22] 279 U.S. at 93-95. *See* Kennedy, *supra* note 7, at 725; *Relative Priority, supra* note 7, at 809-19, 929, MacLachlan, *supra* note 7, at 77-78; 3 RUTGERS-CAMDEN L. REV. 592, 595-96 n.25 (1972).

[23] 323 U.S. 352 (1945).

[24] *Id.* at 356-57.

priority pursuant to section 3466 would be defeated by a specific and perfected lien upon the property prior to the insolvency or voluntary assignment.[25] The Supreme Court, however, held that state law notwithstanding, federal law determines whether a lien arising as a result of a particular state statute is sufficiently choate to rise above federal claims.[26] Consequently, the courts were no longer bound by the individual states' perfection requirements.[27]

Shortly thereafter in *United States v. Security Trust and Savings Bank,*[28] the Supreme Court extended the choateness doctrine to grant federal tax liens superiority over antedating inchoate liens.[29] The Court held that a federal tax lien was superior to a local attachment lien where the tax lien was recorded after the attachment lien but before the attaching creditor obtained a judgment.[30] The *Security Trust* decision was clearly contrary to thirty lower court decisions which denied the supremacy of federal tax liens over antedating rival claims without any discussion of choateness.[31]

Confusion with regard to the correct application of the choateness doctrine was further exacerbated by the Supreme Court's decision in *United States v. City of New Britain.*[32] The Court in *New Britain* held that antedating state tax liens did not rise above a federal tax lien, because the state tax liens had not ripened into a judgment at the time the federal lien attached, and thus the state tax liens were inchoate.[33] The significance of the *New Britain* decision stems from the fact that the Court erroneously equated the well-established common law principle of "first in time is first in right" with the relatively recent choateness doctrine.[34]

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[25] *Id.* at 355.

[26] *Id.* at 356-57.

[27] *Id.*

[28] 340 U.S. 47 (1950).

[29] *Id.* Under California law, a subsequent judgment lien merged with the attachment lien and related back to the time when the attachment was recorded. *Id.* at 48-50. The federal tax lien arose after the attachment lien, and according to California law, was subject to the prior lien. *Id.* The Supreme Court, however, emphasized that the federal tax lien arose before the California creditor obtained a judgment. *Id.* at 50. Hence, the Court held that the attachment lien was contingent and thus inchoate. *Id.* The government reasoned, and the Supreme Court agreed, that since the priority of the California creditor's lien would be defeated if § 3466 were applicable, the federal tax lien should be accorded the same priority by analogy. *Id.* at 50-51. *Security Trust* marked the first time that the Supreme Court applied the choateness doctrine to a situation where the debtor was not insolvent. *See* Texas Oil & Gas Corp. v. United States, 466 F.2d 1040, 1045 (5th Cir. 1972).

[30] 340 U.S. at 48-51.

[31] *Relative Priority, supra* note 7, at 924 n.115.

[32] 347 U.S. 81 (1954).

[33] *Id.* at 82-88. *See* United States v. Ringwood Iron Mines, Inc., 251 F.2d 145, 146 (3rd Cir.), *cert. denied,* 356 U.S. 974 (1958).

[34] *See* 347 U.S. at 85-86. The choateness doctrine and "first in time" however, are two distinct principles. Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d at 499; Texas Oil & Gas Corp. v. United States, 466 F.2d at 1045; Plumb, *supra* note 7, at 230.

Under the "first in time" rule, the first lien which attaches to the property interest has priority over subsequently attaching liens, unless the first lien is otherwise defective.[35] Although the Supreme Court in *New Britain* insisted that it was applying "first in time," grafting the choateness doctrine onto "first in time" effectively nullified the "first in time" rule.[36] Except for certain possessory liens and certain local tax liens which attached to the property in specific amounts and were summarily enforceable without judicial proceedings, no common law, equitable, or statutory lien could satisfy the choateness test until the lienor's claim had been reduced to a judgment.[37]

A second source of confusion originating in the *New Britain* opinion was the precise peramaters of the choateness doctrine. The Court expanded a doctrine which originated in insolvency proceedings to apply to federal tax liens.[38] The Supreme Court failed to indicate whether choateness would be extended further to protect additional federal interests.

In the late 1950's, the lower federal courts began applying the choateness doctrine to give priority to federal liens in situations which did not involve a federal tax lien or debtor insolvency.[39] In the first of these decisions, *United States v. Ringwood Iron Mines, Inc.*, the Third Circuit upheld the priority of an antedating federal mortgage lien over a lien for unpaid real estate taxes.[40] The court stated that the only difference between *Ringwood Iron Mines* and *New Britain* was that the former involved the execution of a mortgage and the latter involved a tax lien.[41] According to the Third Circuit, the *New Britain* decision provided that the choateness doctrine should be applied to protect federal liens, regardless of whether the debtor was insolvent or the federal lien was a claim for taxes.[42]

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[35] The "first in time" rule was summarized by Chief Justice Marshall in *Rankin v. Scott:*

> [t]he principle is believed to be universal, that a prior lien gives a prior claim, which is entitled to prior satisfaction, out of the subject it binds, unless the lien be intrinsically defective, or be displaced by some act of the party holding it, which shall postpone him in a court of law or equity to a subsequent claimant.

7 U.S. (12 Wheat.) 104, 105 (1827). Thus, under the "first in time" rule, the first lien which attaches to the property interest has priority over subsequently attaching liens, unless it is otherwise defective. Prior to United States v. Security Trust and Sav. Bank, 340 U.S. 47 (1950), the lower courts had denied supremacy to federal tax liens over antedating liens based upon the "first in time" principle without reference to choateness. *Relative Priority, supra* note 7, at 924-25. In *Security Trust and Savings Bank,* the Supreme Court held for a nonfederal lien to be "first in time," the lien must be choate. *See* text accompanying notes 28-30 *supra.* The Supreme Court employed the same analysis in United States v. City of New Britain, 347 U.S. at 84-85.

[36] Plumb, *supra* note 7, at 230.

[37] *Id. See* Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d at 499. *See generally* United States v. Vermont, 377 U.S. 351, 358-59 (1964); note 51 *infra.*

[38] *See* text accompanying notes 20-22, 29-31 *supra.*

[39] *See* text accompanying notes 40-46 *infra.*

[40] 251 F.2d 145, 146-47 (3rd Cir. 1958).

[41] *Id. See* 347 U.S. at 82-85; *Relative Priority, supra* note 7, at 927-29.

[42] 251 F.2d at 146-47.

The cogency of the Third Circuit's analysis is questionable and underscores the confusion created by the *New Britain* opinion.[43] The Third Circuit could have based its decision upon the "first in time" rule without relying upon the choateness doctrine because the federal mortgage lien in *Ringwood Iron Mines* was recorded prior to the real estate tax lien.[44] Similarly, several early circuit court applications of the choateness doctrine to nontax federal liens beyond the purview of section 3466 involved situations where the federal lien was prior in time to the interest of the competing lienor and could have been resolved in accordance with "first in time," without reference to choateness.[45] Later decisions, however, began to apply the choateness doctrine to grant priority to federal liens where "first in time" would not have afforded them such priority.[46]

From its inception, the choateness doctrine has been criticized severely for the inequities resulting from the doctrine's application.[47] The first legis-

[43] Reliance on *New Britain* and the choateness doctrine appears unnecessary and misplaced. The federal mortgage lien in *Ringwood Iron Mines* was perfected prior to the real estate tax lien and thus was "first in time." 251 F.2d at 146-47. The federal tax lien in *New Britain,* however, arose after the local liens and could overcome the prior liens only if the local liens were adjudged inchoate. 347 U.S. at 85.

Furthermore, *New Britain* was a federal tax lien case. *Id.* at 82. *Security Trust and Savings Bank* established that the priority of the federal tax lien was based upon the government's need "to insure prompt and certain collection of taxes due to the United States. . . ." United States v. Security Trust and Sav. Bank, 340 U.S. 47, 51 (1950). *See* text accompanying notes 28-30 *supra.* Thus, the aplication of the choateness doctrine in *New Britain* was an extension of the *Security Trust and Savings Bank* rationale that federal tax revenues are so vital to the workings of government that federal tax liens require the additional protection afforded by the choateness doctrine. 347 U.S. at 51. The rationale for protecting federal tax revenues in *Security Trust and Savings Bank* and *New Britain* is inapplicable to *Ringwood Iron Mines,* a federal mortgage lien case. 251 F.2d at 146. Neither *Security Trust and Savings Bank* nor *New Britain* suggested that the special protection afforded federal tax liens should be extended to all federal tax liens in situations not already covered by Revised Statute § 3466. *See generally* 340 U.S. at 48-51; 347 U.S. at 82-88.

[44] 251 F.2d at 146-47; *see* note 34 *supra.*

[45] *See* United States v. County of Iowa, 295 F.2d 257, 259 (7th Cir. 1961) (state tax liens denied priority over antedating federal mortgage, contrary state law notwithstanding); United States v. Roessling, 280 F 2d 933, 936 (5th Cir. 1960) (federal loan secured by mortgage granted priority over subsequent state tax lien); Southwest Engine Co. v. United States, 275 F.2d 106, 107 (10th Cir. 1960) (Small Business Administration chattel mortgage granted priority over subsequent mechanic's lien, contrary state law notwithstanding).

[46] United States v. Oswald & Hess Co., 345 F.2d 886, 887-88 (3rd Cir. 1965) (inchoate local lien held subordinate to subsequently arising federal claim on judgment in mortgage foreclosure action); *In re* Lehigh Valley Mills, Inc., 341 F.2d 398, 399-401 (3rd Cir. 1965) (federal lien under SBA security agreement held superior to antedating inchoate state tax liens); J.S. Purcell Lumber Corp. v. Henson, 405 F. Supp. 1130, 1132-33 (E.D. Va. 1975) (FHA lien held superior to antedating inchoate mechanic's lien); Bellegarde Custom Kitchens v. Select-A-Home, Inc., 385 F. Supp. 318, 319-20 (D. Me. 1974) (mortgage liens of FHA granted priority over subsequently filed mechanic's lien, even though material and labor furnished prior to recordation of FHA mortgage).

[47] *See Report of the Special Committee on Federal Liens,* 84 ABA REP. 645, 645 (1959) [hereinafter cited as *Report*]. Commentators emphasize that the choateness doctrine subordinated statutory and contractual security interests to federal tax liens without providing

lative attack against choateness, the 1966 Federal Tax Lien Act (the Act),[48] was in response to application of the choateness doctrine to section 6321 of the Internal Revenue Code.[49] Section 6321 states that an individual's liability for taxes owed to the federal government creates a lien in favor of the United States.[50] Prior to the Act, only choate liens enjoyed priority over subsequently arising federal tax liens or any federal tax lien arising pursuant to the debtor's insolvency.[51] The Supreme Court repeatedly awarded priority to federal tax liens over antedating mechanic's liens,[52] real estate

affected creditors with an opportunity to protect their interests. Furthermore, advancements made by creditors, particularly mechanics and materialmen, enhanced the value of the taxpayer's property to the benefit of the Internal Revenue Service, which appropriated the property to satisfy tax liens. MacLachlan, *supra* note 7, at 73-78; Note, *Choateness and 1966 Federal Tax Lien Act,* 52 MINN. L. REV. 198, 200-01 (1967) [hereinafter cited as *Choateness and the Act*].

[48] I.R.C. § 6323.

[49] 26 U.S.C. § 6321 (1976). Section 6321 provides:

> [i]f any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, additional amount, addition to tax, or assessable penalty, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

[50] *Id. See generally* Young, *Priority of the Federal Tax Lien,* 34 U. CHI. L. REV. 723, 724 (1967).

[51] *See* United States v. Security Trust and Sav. Bank, 340 U.S. at 51; United States v. Waddill, Holland & Flinn, Inc., 323 U.S. 353, 356-57 (1945); County of Spokane, Washington v. United States, 279 U.S. at 93-95; Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d at 499. The Supreme Court defined choateness very narrowly. The exact amount of the lien, for example, usually is not determined until the debtor has exhausted judicial procedures in challenging the lien itself. *Id.* at 499 n.11, *citing* United States v. Gilbert Assocs., Inc., 345 U.S. 361, 365-66 (1953) (only possession or reduction to judgment by lienor can satisfy choateness rule). *See also* United States v. Equitable Life Assurance Soc'y, 384 U.S. 323 (1966); United States v. Pioneer Am. Ins. Co., 374 U.S. 84 (1963); 12 GA. L. REV. 692, 694 (1978). *But cf.* United States v. Vermont, 377 U.S. 351, 358-59 (1964) (state tax lien which had not been reduced to judgment held choate for purposes of prevailing over federal lien). The precedential value of *Vermont* is probably limited, however, because the statutory lien in *Vermont* had the force of a judgment. *Id.; see Choatness and the Act, supra* note 47, at 200-01.

Finally, the impact of the choateness doctrine was alleviated, at least in part, by judicial formulation of the "no property" rule whereby the federal tax lien could be defeated or limited to the extent that the taxpayer had no property under state law. *See* Aquilino v. United States, 363 U.S. 509, 512 (1960). In *Aquilino,* the petitioners argued that state law created a trust of the proceeds received by a general contractor for the benefit of unpaid contractors. *Id.* at 510-13. The petitioners reasoned that while the subcontractors remained unpaid, the contractor possessed no property interest upon which the federal lien could attach. *Id.* at 512-16. The Supreme Court held that the courts must look to state law in determining whether the contractor had a property interest to which the lien could attach. *Id.* at 512-13. The case was then remanded in order that the state court could determine whether the contractor in fact had "property." *Id.* at 515. *See also* United States v. Durham Lumber Co., 363 U.S. 522 (1960); *Choateness and the Act, supra* note 47, at 203 n.24.

[52] *See, e.g.,* United States v. White Bear Brewing Co., 350 U.S. 1010 (1956) (per curiam). In *White Bear Brewing,* the mechanic had finished his work, filed his lien, and commenced foreclosure proceedings before the federal tax lien arose and notice was filed. *Id.* at 1010-11.

tax liens,[53] mortgagee's liens for fees of a foreclosing attorney,[54] surety's liens,[55] landlord's liens and security interests,[56] and liens of attaching creditors.[57]

Cognizant of the broad scope of section 6321 and the courts' application of the choateness doctrine, Congress determined that certain lienors likely to be unaware of an existant tax lien and the holders of specific property interests merited statutory insulation against application of choateness.[58]

The mechanic, however, had not reduced his lien to a judgment. *Id.* The Supreme Court held that the mechanic's lien was not specific and that the federal tax lien was entitled to priority. *Id.* Justice Douglas observed in his dissent:

> [t]he Court holds that a federal tax lien has priority over a statutory mechanic's lien, even though the mechanic's lien was specific, prior in time, perfected in the sense that everything possible under state law had been done to make it choate, and was being enforced before the federal tax lien arose.

Id. at 1010. Indeed, other mechanic's liens fared equally badly in the Supreme Court during the 1950's. *See, e.g.*, United States v. Hulley, 358 U.S. 66 (1958) (*per curiam*); United States v. Vorreiter, 355 U.S. 15 (1957) (*per curiam*); United States v. Colotta, 350 U.S. 808 (1955). *See also Report, supra* note 47, at 651.

[53] United States v. New Britain, 347 U.S. 81 (1954); *see* text accompanying notes 32-38 *supra.*

[54] United States v. Pioneer Am. Ins. Co., 374 U.S. 84 (1963).

[55] United States v. R. F. Ball Constr. Co., 355 U.S. 587 (1958). Before *Ball* the choateness doctrine had been applied only to statutory liens or liens created by garnishment or attachment. In *Ball,* however, the Supreme Court held that a chose in action arising from the performance of a construction contract and assigned for value to a bonding company was subject to a federal tax lien which arose before the assignment. *Id.* at 588-89. The Court held that the surety's interest was "inchoate," because the amount of the assignment had not been determined at the time the tax lien arose. *Id.* at 588-90, 594. For a discussion of *Ball,* see United States v. Pioneer Am. Ins. Co., 374 U.S. 84, 89-91 (1963). *See also* Texas Oil & Gas Corp. v. United States, 466 F.2d 1040, 1045 (5th Cir. 1972); *Report, supra* note 35, at 646-47; Salter, *Priority Accorded the Sovereign in Bankruptcy: The American and British Views,* 63 COM. L.J. 354, 355-56 (1958).

[56] United States v. Waddill, Holland & Flinn, Inc., 323 U.S. 353 (1945). *See* text accompanying notes 23-27 *supra. See generally* United States v. Menier Hardware No. 1, Inc., 219 F. Supp. 448 (W.D. Tex. 1963); Terry v. Title & Trust Co., 207 Ore. 356, 295 P.2d 161 (1956). *See also* Plumb, *supra* note 7, at 680-81, 681 n.499; Creedon, *The Federal Tax Lien Act of 1966,* 20 ABA TAX SEC. BULL. 101, 101 (1966) [hereinafter cited as Creedon].

[57] United States v. Acri, 348 U.S. 211 (1955). *See* Creedon, *supra* note 56, at 101.

[58] *Hearings on H.R. 11256 and H.R. 11290 Before the House Committee on Ways and Means,* 89th Cong., 2d Sess. 45- 46-47 (1966) [hereinafter cited as *Hearings*]. *See Choateness and the Act, supra* note 47, at 205-06. Interests afforded protection pursuant to the 1966 Act include purchases of securities by bona fide purchasers; retail sales of personalty in the ordinary course of business; automobile sales to consumers; casualty sales of personalty worth less than $250; repairmen's possessory liens; real property taxes and assessments; certain mechanic's liens; certain attorney's liens; insurance policy loans made by an insurance carrier; certain passbook loans; and real property construction or improvement loans. 26 U.S.C. 6323(b) (1976). Section 6323(a) also provides that a federal tax lien is invalid against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor until notice of the tax lien has been filed. 26 U.S.C. § 6323(a) (1976). *See* Plumb, *supra* note 7, at 232-33.

The protection afforded certain interests under § 6323(b) becomes illusory, however, if the taxpayer becomes insolvent because insolvency proceedings are controlled by Revised

Thus, section 6323 was passed in 1966 to grant priority to certain interests which would not otherwise be considered "choate" by the courts.[59] These protected interests are generally characterized as "superpriorities."[60] In situations delineated in the Act which involve superpriority interests, the choateness doctrine is inapplicable.[61] Although the 1966 Act restricted the reach of the choateness doctrine as applied to federal tax liens, the intended scope of this limitation remained unclear.[62] In recent years, contro-

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Statute § 3466. *See* note 13 *supra,* and note 62 *infra.* Section 3466 grants priority to the federal government in insolvency proceedings, regardless of the protection provided in § 6323(b). *See* text accompanying notes 13-22 *supra;* Plumb, *supra* note 7, at 234, 237-39; Dennon, *The Secured Creditor and the Federal Tax Lien Act,* 86 BANKING L.J. 677, 681-84 (1969)[hereinafter cited as Dennon]. For a discussion of the relationship between §§ 6323 and 3466, see Nesbitt v. United States, 445 F. Supp. 824, 828-31 (N.D. Cal. 1978). The *Nesbitt* court acknowledged that the policies of fairness and equity reflected in § 6323 appear inconsistent with the sweeping authority of § 3466 over claims of creditors otherwise protected by § 6323. *Id.* The court concluded, however, that § 6323 does not create an implied exception to § 3466. *Id. See generally* Plumb, *The Federal Priority in Insolvency: Proposals for Reform,* 70 MICH. L. REV. 3 (1971).

[59] *See* 26 U.S.C. §§ 6321, 6323 (1976); *Hearings, supra* note 46, at 45, 47, 64. Indeed, § 6323(b) provides that certain interests which arise *after* the tax lien has attached and notice of its existence has been filed nonetheless enjoy priority over the federal lien. 26 U.S.C. § 6323(b); *see* note 58 *supra.* Since the 1966 Act contains provisions governing the tax lien's priority with regard only to specifically delineated nonfederal property interests, several courts have reasoned that Supreme Court decisions applying the choateness doctrine to priority disputes between federal tax liens and nonfederal property claims remain good law in the areas not covered by § 6323. *See* Chicago Title Ins. Co. v. Sherred Village Assocs., 568 F.2d 217, 221 n.5 (1st Cir. 1978).

[60] "Superpriorities" are interests that rise above already existing and filed tax liens. Plumb, *supra* note 7, at 229.

[61] *See Hearings, supra* note 58, at 45-47. The legislative history of the Act confirms that the choateness doctrine was not abolished but only restricted in its application. *Id.;* H.R. REP. No. 1884, 89th Cong., 2d Sess. 35 (1966); Plumb, *supra* note 7, at 232-33, 245, 678-82. *See also* Texas Oil & Gas Corp. v. United States, 466 F.2d 1040, 1053 (5th Cir. 1972); Creedon, *supra* note 56, at 134-35. Congress, for example, declined to accept an American Bar Association (ABA) recommendation that superpriority status be afforded to innkeepers' liens; liens on breeding animals; liens providing for the care, safekeeping and transportation of personal property; and liens upon animals, vehicles or vessels for the damages they caused, regardless of whether the lien arose by operation state law or by contract. *See Report, supra* note 47, at 691, 719-20. Similarly, Congress rejected ABA recommendations to protect landlords' statutory or contractual liens against federal tax liens arising after the lease contract was finalized. Creedon, *supra* note 56, at 135, (citing ABA FINAL REPORT OF THE COMMITTEE ON FEDERAL LIENS, 24-25 (1959)). Thus, in the situations listed above the choateness doctrine remains applicable, subject only to the notice filing provisions of § 6323(a) and (f). 26 U.S.C. § 6323(a), (f) (1976).

[62] *Hearings, supra* note 58, at 45-47; H.R. REP. No. 1884, 89th Cong., 2d Sess. 35 (1966). Section 6323 does not refer to the choateness doctrine. The legislative history of the Act, however, confirms that one of the Act's purposes was to circumscribe the doctrine's application. *Id.*

The priority of federal tax claims enacted in § 6323 is subject to two important exceptions. The first is the federal insolvency statute, § 3466, which controls insolvency proceedings. *See* notes 13 & 58 *supra.* The second is the Revised Bankruptcy Act. Unsecured federal tax claims rank sixth in the order of priorities for payment out of the bankrupt estate. 11

versies over varying interpretations of the choateness doctrine and whether choateness should be applied at all, have been waged almost exclusively outside the tax field.[63] Lacking any statutory guidelines or Supreme Court instruction, the circuit courts fashioned their own rules for applying or rejecting choateness.[64] The first point of contention between the circuits stemmed from a fundamental uncertainty as to which body of law the courts were to apply. In resolving lien priority disputes, some courts applied the choateness doctrine of federal common law,[65] other courts attempted to apply federal law as guided by the Model Uniform Commercial Code,[66] and still other relied upon state procedures.[67]

Even before the Supreme Court's decision in *Kimbell Foods,* it was clear that whether a state lien was sufficiently perfected to defeat a subsequently arising or subsequently filed tax lien, was a question of federal law.[68] Similarly, the character and collection of federal debts and taxes are

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U.S.C. § 507 (1976). However, § 545(b) of the Bankruptcy Act limits the trustee's power to avoid tax liens. 11 U.S.C. § 545(b); S. REP. No. 598, 95th Cong., 2d Sess. 5, *repinted in* [1978] U.S. CODE CONG. & AD. NEWS 4717, 5799-5801, 5871-72. For a comparison of federal lien priorities in general and priorities in bankruptcy, see Plumb, *supra* note 7, at 233-85. *See also* Kennedy, *supra* note 7, at 745-50. *But see* SBA v. McClellan, 364 U.S. 446 (1960). The *McClellan* Court held that where the Small Business Administration (SBA) had joined a private bank in making a loan and the borrower filed bankruptcy, the SBA's interest in the unpaid balance of the loan was entitled to the priority provided for "debts due to the United States" under Revised Statute § 3466 and § 64 of the Bankruptcy Act of 1898. *Id.* at 450-52. The Court reasoned that since the SBA acquired a beneficial interest in the loan prior to the petition in bankruptcy, it was immaterial that a formal assignment of the note to the SBA did not occur until after the borrower declared bankruptcy. *Id.*

[63] *See, e.g.,* Willow Creek Co. v. Porter County Plumbing & Heating, Inc., 572 F.2d 588, 590-91 (7th Cir. 1978) (choateness doctrine applied to deny mechanic's lien priority over subsequently arising and recorded federal mortgage lien); Chicago Title Ins. Co. v. Sherred Village Ass'n, 568 F.2d 217, 218-19, 222 (1st Cir. 1978) (mechanic's lien, not required to be recorded under state law, held inchoate and denied priority over subsequently arising and recorded federal agency mortgage); United States v. Crittenden, 563 F.2d 678, 688-89, 691-92 (5th Cir. 1977) (unrecorded mechanic's lien granted priority over subsequently arising FHA perfected security interest; Uniform Commercial Code, not choateness test, determines federal lien priorities); United States v. California-Oregon Plywood, Inc., 527 F.2d 687, 688-89 (9th Cir. 1975) (federal deeds of trust denied priority over subsequently accruing local property taxes; congressional intent in abolishing choateness doctrine controls); T.H. Rogers Lumber Co. v. Apel, 468 F.2d 14, 20 (10th Cir. 1972) (FHA mortgage entitled to priority over inchoate materialmen's lien, notwithstanding state law that materialmen's liens relate back to date on which material was first furnished).

[64] Chicago Title Ins. Co. v. Sherred Village Ass'n, 568 F.2d 217, 221 (1st Cir. 1978).

[65] *See* text accompanying notes 7-8, *supra.*

[66] *See* United States v. Crittenden, 563 F.2d 678, 679 (5th Cir. 1977); *see also* United States v. Kimbell Foods, Inc., 99 S. Ct. 1448, 1456-57, 1465 (1979): notes 96, 100 *infra.*

[67] *See* Ault v. Harris, 317 F. Supp. 373, 376 (D. Ala. 1968) *aff'd per curiam* Ault v. United States, 432 F.2d 441 (9th Cir. 1970). Although acknowledging that federal law determines lien priorities, the *Autl* court concluded that the Alaska law of lien priorities should be adopted as the applicable federal rule and rejected "first in time." *See also* United States v. California-Oregon Plywood, Inc., 527 F.2d 687, 689 (9th Cir. 1975).

[68] 99 S. Ct. at 1457; United States v. Pioneer Am. Ins. Co., 374 U.S. 84, 88-89 (1963);

governed by federal law.[69] Before *Kimbell Foods,* however, the relationship between state and federal law in lien priority disputes remained uncertain.[70] Indeed, the relationship is still uncertain.

The First,[71] Second,[72] Fourth,[73] Seventh,[74] and Tenth Circuits[75] have affirmed the choateness doctrine's continuing viability in nontax, noninsolvency proceedings. These circuits held that the 1966 Act abrogates the choateness doctrine only insofar as federal tax liens are concerned and only with regard to certain, carefully delineated nonfederal interests.[76] These courts concluded that areas not specifically addressed in the Act are governed by the choateness doctrine. Moreover, they reasoned that Congress was cognizant of lower federal court decisions applying choateness in order to grant priority to nontax federal liens and therefore would have specifically abolished choateness altogether had it intended to do so.[77] The

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Clearfield Trust Co. v. United States, 318 U.S. 363, 367 (1943). The *Clearfield Trust* Court observed:

> [w]hen the United States disburses its funds or pays its debts, it is exercising a constitutional function or power. . . . The authority [to do so] had its origin in the Constitution and the statutes of the United States and was in no way dependent on the laws [of any State]. The duties imposed upon the United States and the rights acquired by it . . . find their roots in the same federal sources. In absence of an applicable Act of Congress it is for the federal courts to fashion the governing rule of law according to their own standards. (Citations and footnotes omitted).

Id. at 366-67, *quoted* 99 S. Ct. at 1457.

[69] Glass City Bank v. United States, 326 U.S. 265, 267-68 (1945); Clearfield Trust Co. v. United States, 318 U.S. 363, 366-67 (1943).

[70] *See* Chicago Title Ins. Co. v. Sherred Village Ass'n, 568 F.2d 217, 221 (1st Cir. 1978). *See also* note 63 *supra.*

[71] Chicago Title Ins. Co. v. Sherred Village Ass'n, 568 F.2d 216 (1st Cir. 1978).

[72] United States v. General Douglas MacArthur Senior Village, Inc., 470 F.2d 675 (2d Cir. 1972), *cert. denied,* 412 U.S. 922 (1973) (antedating federal mortgage lien held superior to inchoate local real property tax liens).

[73] H.B. Agsten & Sons, Inc. v. Huntington Trust and Sav. Bank, 388 F.2d 156 (4th Cir. 1967), *cert. denied,* 412 U.S. 922 (1973) (circuity of lien priorities case; inchoate mechanic's liens subordinated to SBA mortgage deed of trust). *See* J.S. Purcell Lumber Corp. v. Henson, 405 F. Supp. 1130 (E.D. Va. 1975) (subsequently arising and perfected mechanic's lien held inchoate and subject to FHA recorded deed of trust, contrary state law notwithstanding).

[74] Willow Creek Lumber Co. v. Porter County Plumbing & Heating, Inc., 572 F.2d 588 (7th Cir. 1978) (lien held by HUD as a result of assignment of a mortgage entitled to priority over inchoate mechanics' liens).

[75] T.H. Rogers Lumber Co. v. Apel, 468 F.2d 14 (10th Cir. 1972) (antedating FHA mortgage lien entitled to priority notwithstanding state law that mechanics' and materialmen's liens relate back to date on which materials or labor were first furnished).

[76] *See* notes 71-75 *supra.* The Third Circuit has not addressed the question of the continuing viability of the choateness doctrine in nontax situations since the passage of the 1966 Act. In two decisions prior to the Act, however, the Third Circuit applied the choateness doctrine to grant priority to SBA mortgage liens. Thus, choateness remained the controlling principle for resolving nontax lien priority disputes in the Third Circuit prior to the Supreme Court's *Kimbell Foods* decision. *See* United States v. Oswald & Hess Co., 345 F.2d 886 (3d Cir. 1965); *In re* Lehigh Valley Mines, Inc., 341 F.2d 398 (3d Cir. 1965).

[77] Willow Creek Lumber Co. v. Porter County Plumbing & Heating, Inc., 572 F.2d 588, 590 (7th Cir. 1978); Chicago Title Ins. Co. v. Sherred Village Assoc., 568 F.2d 217, 220 n.4

Circuits which continued to apply the doctrine surmised that Congress is in a better position than the courts to determine the impact of federal lien priorities.[78] If priorities between competing liens were to be altered, the legislature, not the courts, should initiate the change.[79]

The Fifth[80] and Ninth Circuits,[81] however, concluded that in light of congressional disapproval of the choateness doctrine in the tax field, there was no justification for prolonging the doctrine's existence in areas less crucial to preservation of the government. These Circuits reasoned that if Congress had determined to restrict severely the choateness doctrine with regard to the federal government's role as the "involuntary creditor of the taxpayer,"[82] then application of the choateness doctrine to situations where the federal government voluntarily extends credit is inequitable and unnecessary.[83] Specifically, these courts have refused to apply the choateness doctrine to ensure priority for government agencies that operate as commercial lendors or loan guarantors in general commerce.[84]

In sum, the choateness doctrine was formulated by the Supreme Court to protect federal claims in insolvency proceedings and subsequently expanded by the Court to shelter federal tax liens.[85] The Court's erroneous conclusion that choateness and "first in time" are synonymous, was accepted by several of the circuit courts, which extended the choateness doctrine to grant priority to federal mortgages and loans.[86] In 1966, Congress severely circumscribed the doctrine in order to insulate otherwise "inchoate" interests.[87] A number of courts, however, continued to apply

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(1st Cir. 1978); T.H. Rogers Lumber Co. v. Apel, 468 F.2d 14, 18 (10th Cir. 1972).

[78] Chicago Title Ins. Co. v. Sherred Village Assoc., 568 F.2d 217, 221 (1st Cir. 1978), *citing* United States v. General Douglas MacArthur Senior Village, Inc., 470 F.2d 675, 679 (2d Cir. 1972); T.H. Rogers Lumber Co. v. Apel, 468 F.2d 14, 17-20 (10th Cir. 1972); H.B. Agsten & Sons, Inc. v. Huntington Trust & Sav. Bank, 388 F.2d 156, 160 (4th Cir. 1967).

[79] *See* note 78 *supra.*

[80] United States v. Crittenden, 563 F.2d 678, 685 (5th Cir. 1977); Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d 491, 501 (5th Cir. 1977); Connecticut Mut. Life Ins. Co. v. Carter, 446 F.2d 136, 139 (5th Cir.), *cert. denied,* 404 U.S. 857 (1971).

[81] United States v. California-Oregon Plywood, Inc., 527 F.2d 687, 689 (9th Cir. 1975); Ault v. United States, 432 F.2d 441, 441 (9th Cir. 170).

[82] Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d 491, 500 (5th Cir. 1977).

[83] Chicago Title Ins. Co. v. Sherred Village Assoc., 568 F.2d 217, 221 (1st Cir. 1978); *see* Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d 491, 500-03 (5th Cir. 1977); Ault v. Harris, 317 F. Supp. 373, 374-76 (D. Ala. 1968), *aff'd sub nom.,* Ault v. United States, 432 F.2d 441 (9th Cir. 1970).

[84] Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d 491, 500 (5th Cir. 1977); United States v. California-Oregon Plywood, Inc., 527 F.2d 687, 688-89 (9th Cir. 1975). *See also* Plumb, *The Relative Priority of Federal and Business Claims: Yesterday, Today and Tomorrow,* 27 BUS. LAW 1195 (1972) [hereinafter cited as *Federal and Business Claims*]; Comment, *The Relative Priority of SBA Liens: An Unreasonable Extension of Federal Preference,* 64 MICH. L. REV. 1107 (1966) [hereinafter cited as *SBA Liens*].

[85] *See* text accompanying notes 7, 19-22, 28-29 *supra.*

[86] *See* text accompanying notes 34-36, 40, 45-46 *supra.*

[87] *See* text accompanying notes 58-59 *supra.*

choateness outside the tax field.[88] Against this backdrop, the Supreme Court agreed to review two Fifth Circuit decisions, *Kimbell Foods v. Republic National Bank* and *United States v. Crittenden.*[89]

The Supreme Court in *United States v. Kimbell Foods, Inc.* reiterated the well-established principle that the priority of liens stemming from federal lending programs must be determined pursuant to federal law.[90] The Court reasoned, however, that a national rule of priorities to protect federal loan programs is unnecessary, absent a congressional mandate to the contrary.[91] Thus, incorporating "nondiscriminatory state laws" to resolve lien priority disputes between the federal government and private lienors will not interfere with federal loan programs.[92] The Court specifically emphasized that the agencies' own operating practices acknowledge that the federal government's security interests are controlled by the commercial laws of the states.[93] Finally, the Supreme Court determined that deference to customary commercial practices will not conflict with the objectives of federal lending programs, since the government as lender is in essentially the same position as private lenders and does not require the special protection afforded by the choateness doctrine.[94] Thus, the Court concluded that the "prudent course" was to adopt the readymade body of state commercial law as the federal rule of lien priorities until Congress strikes a different accommodation.[95]

In the two decisions which provided a vehicle for the Supreme Court's rejection of the choateness doctrine in nontax, noninsolvency proceedings, the Fifth Circuit refused to apply choateness.[96] Rather, the Fifth Circuit fashioned a federal common law rule based upon the Uniform Commercial Code (U.C.C.).[97] In *Kimbell,* the court was required to determine which creditor of a merchantile chain was entitled to priority for repayment from the proceeds of a sale of assets.[98] Under Texas law, Kimbell retained a

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[88] *See* text accompanying notes 71-75 *supra.*

[89] 99 S. Ct. at 1448.

[90] 99 S. Ct. at 1457. *See* Clearfield Trust Co. v. United States, 318 U.S. 363, 366-67 (1943); *see also* note 57 *supra.*

[91] 99 S. Ct. at 1458-64.

[92] *Id.* at 1465.

[93] *Id.* at 1460.

[94] *Id.* at 1462-63.

[95] *Id.* at 1465.

[96] Kimbell Foods, Inc. v. Republic Nat'l Bank, 557 F.2d 491, 503 (5th Cir. 1977). Although the Fifth Circuit did not apply Texas law, the court determined that the outcome of the case would be the same under both Texas law and the UCC. *Id.* at 497; 99 S. Ct. at 1455. In *United States v. Crittenden,* the Fifth Circuit also determined the respective lien priorities based on the UCC, but declined to consider whether the result would be the same under Georgia law. 563 F.2d 678, 688-89 (5th Cir. 1977); 99 S. Ct. at 1465. Thus, the Supreme Court, in deciding that state law was to be applied to resolve lien priority disputes, affirmed the Fifth Circuit's *Kimbell* holding, based on Texas law, and vacated the *Crittenden* decision for resolution under Georgia law. 99 S. Ct. at 1465.

[97] *See* note 96 *supra.*

[98] 99 S. Ct. at 1453-54; 557 F.2d at 493.

perfected security interest superior to the bank's subsequently arising lien.[99] As the bank's assignee and guarantor of a private loan to the debtor, the Small Business Administration (SBA) held an inferior state lien.[100]

The SBA argued that the federal common law principle of "first in time, first in right," coupled with the choateness doctrine, entitles federal claims to priority over all inchoate nonfederal interests.[101] Under those two common law rules, the SBA lien would have enjoyed priority, because Kimbell's perfected security interest had not been reduced to a judgment at the time the SBA recorded its assignment from the bank.[102]

Similarly, *United States v. Crittenden* involved the competing priorities between a possessory mechanic's lien and a Farmers Home Administration (FHA) security interest.[103] The FHA argued that its security interest in the tractor was superior to Crittenden's mechanic's lien, because the mechanic's lien was inchoate at the time the FHA security interest attached.[104] In resolving the question of lien priorities, the Fifth Circuit rejected state law as well as "first in time" and the choateness doctrine.[105] Rather, the court fashioned a "federal common law rule" based on the Model Uniform Commercial Code.[106] The court determined that under this

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[99] 99 S. Ct. at 1453-54; 557 F.2d at 498. *See* TEX. BUS. & COM. CODE ANN. § 9.312 (1968).

[100] 99 S. Ct. at 1453-54; 557 F.2d at 498. In 1968, O.K. Super Markets borrowed $27,000 from Kimbell Foods, Inc. The supermarket's equipment and merchandise were listed as collateral in the two security agreements executed between the parties. The two security agreements also contained standard clauses providing that the collateral would secure any future advances from Kimbell to O.K. Super Markets. The security agreements were duly filed in accordance with Texas law. In February 1969, the O.K. Super Markets obtained a loan from the Republic National Bank. The bank perfected its security interest by filing a financial statement which listed the same property specified in Kimbell's 1968 agreement. The bank's loan was guaranteed up to 90% by the SBA. In 1971, Kimbell commenced state proceedings against O.K. Super Markets to recover its inventory debt. Shortly before Kimbell filed suit, O.K. Super Markets defaulted on its bank loan. The bank assigned its security interest to the SBA late in 1970, and the assignment was recorded in January of 1971. In February of 1971, O.K. Super Markets with the approval of its creditors, sold its equipment and inventory and placed the proceeds in escrow pending resolution of conflicting claims to the funds. Kimbell subsequently obtained a judgment against O.K. Super Markets which it attempted to enforce. 99 S. Ct. at 1453-54. The District Court applied the choateness doctrine in order to grant the SBA priority over the inchoate Kimbell lien. 401 F. Supp. 316, 321-22 (N.D. Tex. 1975). The Fifth Circuit, however, refused to apply the "peculiar patina" of the choateness doctrine. 557 F.2d at 498, 499.

[101] 99 S. Ct. at 1454, 1454 n.7; 557 F.2d at 498.

[102] 99 S. Ct. at 1454; 557 F.2d at 449 n.11.

[103] 99 S. Ct. at 1455-56.

[104] *Id.*; 563 F.2d at 683-84. The District Court granted summary judgment in favor of Crittenden on alternative grounds. According to the district court, the agency had not properly perfected its security interest because the collateral was inadequately described in the financing statement. Moreover, even if the description were sufficient, both federal and state law accorded priority to the mechanic's lien. United States v. Crittenden, Civ. Action No. 75-37-COL (MD Ga. Sept. 25, 1975); 99 S. Ct. at 1456.

[105] 563 F.2d at 684-88, 685-86 n.13.

[106] *Id.* at 689.

rule, Crittenden's lien for the final repair bill of the tractor was entitled to priority over the FHA security interest.[107]

Thus, the Supreme Court was confronted with two Fifth Circuit approaches to the dilemma of federal lien priorities. Both approaches rejected application of the choateness doctrine;[108] both acknowledged that federal law was controlling and declined to base their decisions on state law;[109] both looked to the U.C.C. as the standard for federal common law;[110] and both reasoned that federal loan agencies operating in the private sector should be required to conform to the same commercial practices as private lenders.[111] The primary distinction between them was that *Kimbell* acknowledged the continued viability of "first in time"[112] whereas *Crittenden* rejected it.[113]

Unfortunately, the Supreme Court in *Kimbell Foods* never clearly indicated whether "first in time" remains a valid principle in federal common

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[107] *Id.* at 691-92.

[108] 577 F.2d at 498-502; 563 F.2d at 584-88.

[109] 557 F.2d at 497-503; 563 F.2d at 681; *see* note 96 *supra.*

[110] 557 F.2d at 503-04; 563 F.2d at 681-83.

[111] 557 F.2d at 500; 563 F.2d at 686. *See Federal and Business Claims, supra* note 84, at 1217; *SBA Liens, supra* note 84, at 1128-29; Comment, *The Priority of Federal Lien Claims: Selected Problems and Theoretical Considerations,* 24 CASE W.L. REV. 521, 534-35 (1973).

[112] 557 F.2d at 498, 503.

[113] 563 F.2d at 683-88. The *Crittenden* court declined to apply "first in time" which would have given priority to the government's perfected security interest over the unrecorded mechanic's lien. *Id.* at 685-86 n.13, 685-88. The Fifth Circuit based its decision upon the reasoning of its previous rejection of "first in time" in *Connecticut Mutual Life Insurance Co. v. Carter* and the 1966 Act. *Id. See* Connecticut Mutual Life Ins. Co. v. Carter, 446 F.2d 136 (5th Cir. 1971).

In *Connecticut Mutal* the court held that where an FHA mortgage expressly stated that it was subject to a mortgage held by the insurance company, the FHA's lien was inferior to the insurance company's lien for attorney's fees provided for in the first mortgage. 446 F.2d at 139. The Fifth Circuit did not distinguish between choateness and "first in time." Rather, the court rejected the choateness doctrine and assumed that "first in time" was inapplicable. *Id. See* 563 F.2d at 685-86 n.13. The court determined that the FHA security interest was subject to the same state rules governing security interests that applied to other lenders. 446 F.2d at 139; 563 F.2d at 685-86 n.13.

Both *Connecticut Mutual* and *Crittenden* stressed that the 1966 Act's creation of superpriority status for certain interests which Congress determined were in need of protection against federal tax liens, evidenced congressional disapproval of choateness and "first in time." 446 F.2d at 139; 563 F.2d at 684-86. *See* note 60 *supra.* Specifically, the Fifth Circuit in *Crittenden* noted that the 1966 Act provides that even if notice of a tax lien has been filed, the tax lien is invalid with respect to a mechanic's lien arising under local law if the mechanic has been continuously in possession of the property from the time the lien arose. Both the *Crittenden* and *Connecticut Mutual* opinions reasoned that it would be anomalous to allow the government operating as a lending agency to prevail in a situation where the government operating as a tax lienor under the Act would have had an inferior interest, subject to the local lien. 563 F.2d at 686; 446 F.2d at 139-40. According to the *Crittenden* court, Congress' narrowing of choateness and "first in time" in the tax field "eliminated the jurisprudential underpinnings" for applying either common law rule to situations beyond the tax field. 563 F.2d at 687.

law. Rather, the Court side-stepped the issue. The Fifth Circuit's holding in *Kimbell Foods* was affirmed, not because of the Fifth Circuit's application of "first in time," but because the Court of Appeals found that Texas law gave preference to Kimbell's lien.[114] Similarly, the Fifth Circuit's holding in *Crittenden* was vacated and remanded, not because the Court of Appeals declined to apply "first in time," but because the Fifth Circuit failed to determine whether the FHA's financing statement was sufficient under Georgia law and whether Georgia law treats repairman's liens as superior to previously perfected consensual liens.[115] The Supreme Court did not explain, however, whether state law is to be applied in tandem with "first in time" or whether state law applied as the national rule is to supersede "first in time."

Instead, the Supreme Court glossed over potential conflicts between the federal common law of "first in time" and the new federal rule of state law in lien priority disputes which involve federal loan agencies. The Court, having determined that federal law controls, stressed that controversies affecting the operation of federal programs do not necessarily require the application of uniform federal rules.[116] When there is little need for a uniform body of federal law, state law may be incorporated as the federal rule.[117]

In analyzing whether a uniform federal rule was necessary in resolving lien priority disputes, the *Kimbell* Court was required to consider the extent to which application of a federal rule would upset commercial relationships predicated on state law.[118] The government contended that the effective administration of federal lending programs necessitated a uniform federal law of lien priorities. Furthermore, abrogation of "first in time" and choateness would conflict with the protectionist fiscal policies

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[114] *See* 99 S. Ct. at 1465.

[115] *Id.* The applicable Georgia law in *Crittenden* was far from clear, in part because Georgia had adopted a commercial code which contains slight aberrations of the UCC. 563 F.2d at 688 n.17. Furthermore, the Fifth Circuit feared that state law might discriminate against federal interests. *Id.* at 689 n.18.

[116] 99 S. Ct. at 1458, (citing United States v. Little Lake Misere Land Co., 412 U.S. 580, 594-95 (1973); Clearfield Trust Co. v. United States, 318 U.S. 363, 367 (1943)). In United States v. Standard Oil Co., 332 U.S. 301 (1947), the Supreme Court determined that "in many situations where Congress has not acted, the rights, interests and legal relations of the United States are determined by application of state law." 332 U.S. at 308. *United States v. Little Lake Misere Land Co.* makes it clear, however, that "hostile state rules do not provide appropriate standards for federal law." 412 U.S. at 595-96.

[117] 99 S. Ct. at 1458. Surprisingly, the Supreme Court in its *Kimbell* opinion never refers to the approach to choateness adopted by the Ninth Circuit. In both *United States v. California-Oregon Plywood, Inc.* and *Ault v. United States*, the Ninth Circuit declined to apply the choateness doctrine and elected instead to apply state law as the applicable federal rule, the very standard embraced by the *Kimbell* Court, 527 F.2d 687, 689 (9th Cir. 1975); 432 F.2d 441 (9th Cir. 1970), *aff'g sub nom.* Ault v. Harris, 317 F. Supp. 373, 374-76 (D. Ala. 1968).

[118] 99 S. Ct. at 1459.

underlying those programs.[119] The *Kimbell* Court, however, was unpersuaded.[120]

The Court determined that the application of state law would not hinder administration of the SBA and FHA loan programs.[121] The Court emphasized that SBA employees are instructed to follow state law.[122] Moreover, the SBA Financial Assistance Manual confirms that the SBA assumes its security interests are governed by each states' respective commercial law.[123] FHA regulations, observed the Court, also expressly incorporate state law.[124] Thus, the *Kimbell* Court concluded that the agencies' own operating practices belied their assertions that a uniform federal rule for resolving priorities was imperative.[125] The Court also emphasized that loan applications receive individual scrutiny. The Court reasoned that the agencies could readily tailor loan transactions to conform to state priority rules, just as the agencies evaluate other factual and legal considerations before dispensing federal funds.[126]

The government further contended that the application of local law would hinder the agencies' ability to recover disbursed funds and therefore would undermine the programs' objectives.[127] The government argued that money received in the collection of taxes was not materially different from money received in the repayment of federal loans. Therefore, the 1966 Federal Tax Lien Act, which allows for the continuing application of choateness and "first in time" to interests not expressly provided for under the Act, should apply by analogy to the collection of federal loans.[128] Since Congress did not abolish either choateness or "first in time," the government inferred that Congress implicitly approved the doctrines' application to federal loans.[129]

The *Kimbell* Court determined otherwise. The Court stressed that the government acting as a tax collector operates in an essentially involuntary

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[119] *Id.*

[120] *Id.*

[121] *Id.* The Court cited with approval its rejection of a similar argument advanced by the government in United States v. Yazell, 382 U.S. 341, 357 (1966). In *Yazell,* the Court dismissed arguments that a need for uniformity superceded application of state coveture rules to an SBA loan contract. 382 U.S. at 353-57. The Court reasoned that SBA operations were specifically adapted to state law and that the federal interest in uniformity was minimal. *Id.* at 353-54.

[122] 99 S. Ct. at 1459. *See* 13 C.F.R. § 101(d)(3) (1978); *SBA Financial Assistance Manual,* SOP 50-10, ch. 6 § 29-2(4)(b) (1978).

[123] *See* note 122 *supra.*

[124] 99 S. Ct. at 1460 n.27. *See, e.g.,* 43 Fed. Reg. 5504, 7978, 23986, 55882-55895, 56643-56647, 59078 (1978); 44 Fed. Reg. 170, 4431-4458, 6354, 10979-10980 (1979).

[125] 99 S. Ct. at 1460.

[126] *Id.*

[127] *Id.* As noted above, the 1966 Act did not completely abolish the choateness doctrine in the tax field. It severally circumscribed the doctrine, however, and called into question the continuing viability of choateness in noninsolvency situations. *See* notes 61, 62 *supra.*

[128] 99 S. Ct. at 1461.

[129] *Id.*

capacity, whereas the government serving as a money lender is able to invoke protective measures against defaulting debtors.[130] Moreover, SBA and FHA lending programs are a form of social welfare legislation designed to assist individuals who are unable to obtain funds from private lenders. The Court surmised that had the Congress intended the private commercial sector to bear the risks of default entailed by these public welfare programs, it would have created a priority scheme superseding state law. Both Congress and the agencies, however, have expressly acknowledged the priority of certain private liens over federal security interests.[131] To the *Kimbell* Court, this acknowledgement indicated that the extraordinary safeguards of the choateness doctrine were unnecessary to protect federal lending programs.[132]

The Court pointed to the 1966 Act as additional evidence that placing the federal government on the same footing with other commercial lenders would not undermine the government's interests.[133] To ignore Congress' express disapproval of unrestricted federal priority in such a vital area as revenue collection would be inconsistent with the Court's responsibility to effectuate congressional policy.[134]

Finally, the Supreme Court stressed that the business community relies on state commercial law in order to make reasonable evaluations of the risks involved in financial transactions. Thus, the "prudent course" selected by the Court was to adopt "nondiscriminatory state laws" as the standard for determining the priority of private and consensual liens arising pursuant to federal lending programs.[135]

Underlying the Supreme Court's adoption of state commercial law is the assumption that commercial rules of law are, and will continue to be, fairly uniform throughout the nation.[136] Indeed, the Court noted that all of the states except Louisiana have adopted the U.C.C. with minor variations, and "[t]he differences between the [U.C.C.] rules, . . . are insignificant in comparison with the similarities."[137] The importance of the

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[130] *Id.* at 1362.

[131] *Id. See* notes 60, 61 *supra.* A significant indicium of congressional intent not mentioned in the *Kimbell* opinion is § 646 of the Small Business Act. 15 U.S.C. § 631-47 (1976). In § 646, Congress subordinated certain SBA liens to local property tax liens, thus ensuring the priority of the local lien. *See* United States v. California-Oregon Plywood, Inc., 527 F.2d 687, 689-90 (9th Cir. 1975).

[132] 99 S. Ct. at 1462, 1463.

[133] *Id.* at 1464. In enacting the 1966 Act, Congress sought to "improv[e] the status of private secured creditors" and prevent interference with commercial financing by "moderniz[ing] . . . the relationship of Federal tax liens to the interests of other creditors." *Id.* at 1463-64, *quoting* S. REP. No. 1708, 89th Cong., 2d Sess., 1-2 (1966), *reprinted in* [1966] U.S. CODE CONG. & ADMIN. NEWS 3722.

[134] 99 S. Ct. at 1464, (citing Reconstruction Finance Corp. v. Beaver County, 328 U.S. 204, 209-10 (1946)).

[135] 99 S. Ct. at 1464-65.

[136] *See* 99 S. Ct. at 1460 n.28, 1462 n.37.

[137] *Id.* at 1460 n.28. The Court's emphasis on uniformity in the Uniform Commercial Code is also somewhat misleading. Interpretations of the UCC vary from state to state. More

Court's reliance upon a generally uniform pattern of state commercial law stems from the fact that the Court elected to apply "non-discriminatory" state law. State commercial law based upon the U.C.C. clearly satisfied the *Kimbell* Court's criterion of being non-discriminatory.[138] Indeed, the priority rules established in Article 9 of the UCC are premised upon the general principle that "[c]onflicting security interests rank according to priority in time of filing or perfection," with several carefully delineated exceptions.[139]

Article 9, however, does not cover all varieties of secured transactions and defers to additional state law with regard to certain types of property of numerous local liens.[140] One area of law particularly beset with "local eccentricities" is the priority of material and mechanic's liens.[141] Depending upon the state, a subcontractor's lien for wages and materials may arise when he begins work, when the general contractor commences work, or when the subcontractor enters into the contract. Indeed, the lienor may be entitled to superpriority over a mortgage lienor regardless of whether the mortgage was recorded or the subcontractor's contract was executed.[142]

The Supreme Court's opinion in *Kimbell Foods* sheds no light on whether any or all of these state law provisions for protecting the mechanic or materialmen are "discriminatory." Perhaps if a state statute favors a particular class of lienors over *all* antedating or subsequent liens, the Court would consider the statute fair.[143] Perhaps too, local statutes which establish an order of priority between conflicting liens are discriminatory insofar as they favor certain interests over others.[144] The Court's failure to provide

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significantly, however, the UCC itself varies from one jurisdiction to another and variances between state commercial codes appears to be increasing. *See* Minahan, *The Eroding Uniformity of the Uniform Commercial Code,* 65 KY. L.J. 799, 810-11 (1977). Article 9 was amended significantly in 1972, and only about one third of the states have adopted the 1972 amendments. *Id.* at 810. Minahan explains that there are basically three ways in which state legislatures have defeated efforts to achieve uniformity in the UCC. First, the official text has been amended too freely. Second, many significant amendments recommended by the UCC's Permanent Editorial Board hav not been enacted. Additional state legislation, which varies or supercedes UCC provisions has also been promulgated. *Id.* at 807. *Cf.* Coogan, *Article 9—An Agenda for the Next Decade,* 87 YALE L.J. 1012, 1053-54 (1978) (Article 9 is largely uniform throughout the states).

[138] *See* 99 S. Ct. at 1460 n.28.

[139] U.C.C. § 9-312(5)(a) (1972 version).

[140] *See id.* § 9-104 (1972 version).

[141] Chicago Title Ins. Co. v. Sherred Village Assocs., 568 F.2d 217, 222 n.7 (1st Cir. 1978), *citing* Plumb, *supra* note 7, at 677.

[142] *See* note 141 *supra.*

[143] In Virginia, for example, perfected mechanics' and materialmen's liens are superior to any subsequently perfected liens on the property. VA. CODE § 43-3 (1950). In order for a general contractor to perfect his lien, he must file notice of his lien at any time after the work is completed and within ninety days after the project is finished. VA. CODE § 43-4 (1979 Supp.). If the lien is filed within the period required by the statute, the lien is secured from the time the material or labor was furnished, subject to being defeated by prior or intervening supply liens. *See In re* West Norfolk Lumber Co., 112 F. 759, 766 (E.D. Va. 1902).

[144] *See* GA. CODE § 67-2002 (1979 Supp.). The Georgia Code provides that mechanics' and

a lucid definition of the "variety of considerations always relevant to the nature of the specific governmental interests and to the effects upon them of applying state law"[145] leaves the question of lien priorities open to increased judicial scrutiny.

For all of their inequities, the choateness doctrine and "first in time rule" as applied to federal loan agency liens did provide a means of insuring the priority of federal interests where arguably "discriminatory" state law provided otherwise.[146] Moreover, recent history, particularly in bankruptcy law, strongly suggests that regardless of the *Kimbell* Court's mandate that state law should determine lien priorities, the federal courts are unlikely to abandon federal interests to the judgments of state legislatures when state law in any way hinders federal agency programs.[147]

Finally, the underlying problem with the *Kimbell* Court's decision may well be that what is needed, is a legislative rather than judicial solution. The Court's deference to "non-discriminatory state law" merely sets the stage for subsequent litigation as to the merits and shortcomings of various local statutes. Only the Congress can provide a series of specific guidelines, based upon carefully formulated policy considerations, for determining priorities between competing liens. The perfect model for resolving this controversy is the 1966 Federal Tax Lien Act, which clearly sets forth an equitable list of guidelines for determining priorities.[148] The Supreme Court in its efforts to remedy the uncertainties created by the choateness doctrine, has created a potential quagmire which only legislative action can eradicate.

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materialmen's liens are inferior to liens for taxes, laborers' liens, landlords' liens when a distress warrant for rent has been levied, certain purchase money claims, and certain other general liens when "actual" notice has been communicated before the work was done or materials furnished. A literal reading of § 67-2002 would deny priority to a lien for federal loan money which had been duly recorded but where no actual notice had been communicated to the mechanics or materialmen.

[145] 99 S. Ct. at 1458, (quoting United States v. Standard Oil Co., 332 U.S. 301, 310 (1947)).

[146] *See* Chicago Title Ins. Co. v. Sherred Village Assoc., 568 F.2d 217, 221-22 (1st Cir. 1978).

[147] *See* Countryman, *The Use of State Law in Bankruptcy Cases (Part I)*, 47 N.Y.U.L. REV. 407, 635-36, 642 (1972). Countryman argues persuasively that courts have repeatedly "molded" state law to effectuate what they believe is the federal policy underlying bankrutpcy law.

[148] *See* text accompanying notes 58-61 *supra*.