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CHATTEL MORTGAGES UPON FIXTURES

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THE enormous growth throughout the United States of installment purchases has brought to the fore many interesting as well as controversial questions. As controversial as any is the question of the rights of a holder of a chattel mortgage upon fixtures, where real estate mortgagees or subsequent purchasers are involved. Concerning this subject one can by a search of the authorities find support for almost any theory urged. An utter lack of harmony exists among the courts and their opinions are based upon conflicting theories, grounds and reason.

The early authorities laid down the rule that whatever was annexed or affixed to the realty became a part of it. Exceptions soon arose to meet "modern exigencies of trade and commerce." (Hurxthal v. Hurxthal, 45 W. Va. 584, 32 S. E. 237.) The question is further complicated by the fact that courts have altered their views as to the circumstances and the tests to be applied in determining when chattels retain their character as such and when they become fixtures, so as to become a part and parcel of the realty.

For illustration, in Colorado the original test laid down by the courts to determine what is a "fixture" was the *permanence* of its *attachment*. This is illustrated in the case of Vaughn v. Grigsby, 8 C. A. 373, 46 P. 624, which involved a windmill erected upon realty. The decision was rendered in 1896, and the test suggested was, whether the mill was "*so attached to the land as* to be a part of it." The breaking away from this test is shown by the opinion in the case of Cary Hardware Co. v. McCarthy, 10 C. A. 200, 50 Pac. 744:

"Formerly the controlling question in deciding on which side of the line of division an article belonged was: Is there a physical attachment to the realty of a nature indicating permanence? If there was, it became a fixture. If not it was personal property and its disposition was governed by the law applicable to such property. * * * Now it is not absolutely necessary that in order to constitute a fixture, so as to take an article from without the line of personal property, it should be perma-

nently affixed to the freehold by physical attachment. This may or may not be the case. * * * The controlling questions now, in determining as to a large class of articles whether they partake of a real or personal character, are the intention of the party to make a permanent accession to the freehold, and the use to which the article is to be applied."

And in the later case of Dawson v. Scruggs-Vandervoort-Barney Co., 268 Pac. 584, 84 C. 152, a more liberal rule is stated, that:

"It is not now considered absolutely necessary that an article be actually attached to the free hold in order to make it a part of it."

The Colorado court again recognized the difficulties involved in fixture cases when as stated in the case of Rare Metals Co. v. Power Co., 73 Colo. 30, 213 P. 124, "No two cases are exactly alike and hence no general rule can be applied to every case."

Principally two situations arise which require determination as to the rights of a conditional vendor of chattels, such as a chattel mortgagee, where fixtures are involved. The word "fixture" is used here in its descriptive sense:

(1) *As against a prior and existing realty mortgage.*
(2) *As against a subsequent mortgagee or purchaser.*

In the first instance what usually occurs is that the owner of real estate purchases chattel property upon the installment plan to be affixed or attached to his property, while there is outstanding a trust deed or realty mortgage.

We are here discussing not such articles as doors or windows which integrate into the realty or improvement on the land, but such chattels as furnaces, gas ranges, refrigerators and the like, which between the original purchaser and lien holder by the instrument used, are made chattels, since chattel mortgages deal only with personalty, but as to the rights of a real estate mortgagee, or purchaser of the personal property or fixtures, as the facts may justify.

Let us now discuss the priority involved between the prior real estate mortgagee and the holder of a chattel mortgage which covers chattels annexed to the realty. That is to say, while the recorded real estate mortgage existed, the owner

of the fee title added chattels thereto and executed a chattel mortgage to evidence the balance of the purchase price. The general rule by a preponderance of authority is as follows:

"Where the removal of the fixtures will not materially injure the premises, a seller thereof retaining a lien thereon may assert his rights as against a prior mortgagee of realty."

This general rule was followed in Colorado in the case of Beatrice Creamery Co. v. Sylvester, 65 Colo. 569, 179 Pac. 154, in 1919. The facts in the Beatrice-Sylvester case were briefly as follows:

Sylvester owned a farm upon which the Wallace State Bank held a realty mortgage. Thereafter, Sylvester purchased from Beatrice Creamery Co. two silos and at the time of the purchase executed notes reserving title in the vendor until full payment. The notes also recited that the annexation of the silos to the land should not affect the rights of the vendor. The notes, which were, in effect, conditional sales contracts, were not of record nor acknowledged in accordance with the chattel mortgage statutes.

The silos were 24 feet in diameter and 40 feet in height, placed upon cement foundations. The weight of the silos held them in place and they were fastened to the foundation by cables and easily detachable. The value of the farm was not affected by the addition of the silos and *the silos were removable without material injury to the land.*

Under these facts the court sustained the lien of the vendor of the silos, even though its contract was a secret lien, stressing the factor involved in the case, *"That the silos were removable without injury to the land."* The reasoning of the court to arrive at its decision was:

"One already holding a mortgage of the realty has no equitable claim to chattels subsequently annexed to it. He has parted with nothing on the faith of such chattels. Therefore the title of a conditional vendor of such chattels or a mortgagee of them, before or at the time they were attached to the realty, is just as good against the mortgagee of the realty as it is against the mortgagor." (Jones on Chattel Mortgages, 5th Ed., Sec. 133a.)

Stating the decision in the Beatrice-Sylvester case, just

discussed in another way, it would appear to be authority for a converse situation, namely, *that if the removal of the chattels would materially injure the premises the rights of the real estate mortgagee would be superior to that of the conditional vendor.*

The rule, under such circumstances and supported by the weight of authority, seems to be as follows:

> "Where the property sold has become so intimately connected with or embodied in that which is subject to the mortgage that to reclaim it would more or less disintegrate the property held by the mortgagee, the reservation of title is ineffectual as to preserve the rights of the seller as against the rights of the prior mortgagee of the realty." (13 A. L. R., note, page 473.)

In the case of Barbour v. Ewing, 16 Ala. App. 280, 77 So. 430 (1917), the Alabama courts held that a steam heating system, consisting of a boiler, the necessary piping, and radiators placed in a building, lost their character as personalty and became realty so that a lien to the conditional vendor was ineffective.

A similar ruling was announced by the District of Columbia in 1933, in the case of Buss Mach. Works v. Watsontown, 2 Fed. Supp. 758, where it was held that a conditional vendor of a sprinkling system installed in a building could not reclaim them as against a prior mortgage.

The California courts have placed their decisions upon another ground, as held in the case of Dauch v. Ginsburg (1931), 214 Cal. 540, 6 Pac. (2nd) 952, where it was stated that plumbing fixtures and heating equipment installed under a conditional sales contract in a hotel building, being attached to the rough plumbing by means of slip joints, threaded unions and flanges, was indispensable for use in the operation of the hotel and that the rights of the prior mortgagee of the realty were superior to those of the conditional vendor of the fixtures. The court stated *the plumbing and heating fixtures were permanent in character and absolutely essential to the purpose for which they were constructed.*

In the case of Holland Furnace Co. v. Suzik (1935), 180 At. 38, 118 Pa. Super. 405, the Pennsylvania court had before it a case involving a furnace conditionally sold. The court in this instance took into account the effect of removal of the

furnace upon the heating plant in the dwelling. It refused to recognize the lien of the conditional vendor of the furnace even though its removal would not materially injure the building. It laid down the following rule:

"The question is not whether a removal causes material injury to the building, but to the operating plant, which includes all machinery and equipment * * * in these modern days a dwelling house essentially consists of not only foundations, walls, roofs, etc., but lighting, heating, plumbing, and sewage disposal systems also are regarded as integral parts thereof. It is very generally known that very few houses are now constructed without provisions for installing of a furnace in the cellar. A heating plant is regarded as indispensable in this climate, and is usually considered a component part of a building. Although this furnace might be removed without serious injury to either the furnace or the house, its removal would have completely destroyed the heating system."

Many courts have refused to follow the decisions of the California or the Pennsylvania courts, namely, that if the chattels were essential to the building or its operation they became part of the real estate, and have adhered to the rule that "material injury to the freehold" is the proper test to apply. (Domestic Elec. Co. v. Mezzaluna (1932), 109 N. J. L. 574, 162 At. 722.)

This is illustrated by a Wyoming opinion where upon exactly the same facts involved as in the Pennsylvania case above cited, Holland Furnace Co. v. Suzik, the courts held contrary to the foregoing case and sustained the rights of the conditional vendor of a furnace applying the test that no damage would be done to the building. The case is that of Holland Furnace Co. v. Bird, 21 Pac. (2nd) 825 (Wyo.). The facts and reasoning of the court will appear from the following excerpt from the case:

"In the case at bar, the testimony on the part of both the plaintiff and defendant is to the effect that the furnace can be removed from the dwelling house without injury to the latter, the only things necessary to be done to accomplish the severance being to unscrew pipe unions as to the gas fuel feed, remove the smoke pipe from the heater by simply slipping it off the casting and disconnect the furnace from the hot and cold air pipes by slipping them apart, at the same time breaking the asbestos paper covering at the location of the joints. In all of the Holland Furnace Company cases cited above, where there were contracts with provisions similar to the contract at bar, and where the installation

processes were similar to that pursued in this case, it was held that the furnaces were removable as against a prior mortgagee or one occupying a similar situation. For example, in Industrial Bank of Richmond v. Holland Furnace Company, supra, the contract contained the clause, 'The furnace and piping in basement shall remain personal property at all times and the title thereto shall remain in us until final payment therefor, with the right in us to remove same in default of payment.' There appeared as facts in that case, that the 'furnace was set up in the basement of the residence but was not attached to the floor, being held in place by its own weight. At each connection with a hot or cold air pipe was a collar, two screws, and a wrapping of asbestos.'

"The plaintiff had no knowledge of the sales contract, and it was not recorded. On January 12, 1929, the residence was sold under the deed of trust, the plaintiff becoming the purchaser. The deed from the trustees recited a consideration of $300.00. Subsequently defendant asked permission of plaintiff to remove the furnace, which was refused. The court, in the course of the opinion, disposing of the legal questions involved, said:

"As the furnace was connected with the piping in such a manner that it could be detached without damage to the building, the intention of the parties when it was installed becomes the controlling factor in whether it became a fixture. Bronson on Fixtures, par. 21 (d); Ewell on Fixtures (2nd Ed.) 30, 31; Freeman v. Truax, 103 W. Va. 132, 136, 136 S. E. 697; Kanawha Nat. Bank v. (Blue Ridge) Coal Corporation, 107 W. Va. 397, 148 S. E. 383, and authorities cited on page 401. That intention as stated in the sales contract was that the furnace 'shall remain personal property' until paid for, with the right of removal in case of default in payment. The weight of modern authority upholds such a contract as against a prior secured creditor; particularly when he advanced nothing on faith of the annexation and the chattel annexed may be detached without impairing the creditor's original security. Bronson, supra, par. 29 (a); 26 C. J., p. 684, par. 49; 11 R. C. L. p. 1066, par. 9. The furnace was not paid for, so personal property it remained with the legal title in the defendant."

In a case decided in 1933, Hammel v. Mortgage Guarantee Co., 18 Pac. (2nd) 993, the California court held that gas radiators installed in an apartment house, attached to the pipes by threaded unions, could not be removed by a conditional vendee in face of a prior realty mortgage.

In the case of refrigeration the New Jersey courts, in McLeod v. Satterthwait, 109 N. J. Eq. 414, 157 At. 670, have distinguished between a complete installation in an apartment building, where a complete refrigeration system, including units, pipes and boxes was installed, and a case where merely units and cabinets were installed, connected with pipes

already in place. In the first case the court held the complete installation to be a part of the real estate and in the second situation the refrigeration was held to remain personal property.

The rule in Massachusetts is that in respect to prior mortgages of realty, an agreement between the mortgagor and the vendor of a chattel that the title to it shall remain in the seller, after it is affixed to the real estate, is invalid, the reason being that all fixtures are covered by the mortgage and the mortgage contract cannot be changed by an agreement to which the mortgagee is not a party. (Meagher v. Hayes, 152 Mass. 228 (25 N. E. 105).

Ordinarily, electric ranges, roll-about beds and similar chattels have been held to retain their status as personal property (Dunn v. Assets Realization Co. (1932), 141 Ore. 298, 16 P. (2nd) 370.

The fact that chattels are worn out and are replaced does not affect the rule followed in various jurisdictions; nor does the fact that the mortgagee of realty has a clause covering after acquired property of the mortgagor affect the rule in the respective jurisdictions. (Hill v. Sewald, 53 Pa. 271, 91 Am. Dec. 209.)

The foregoing discussion relates to the controversies between mortgagees who have recorded liens upon real estate and claimants who claim a lien upon chattels subsequently annexed or attached to realty. Now let us discuss the rights of the parties where a recorded chattel mortgage is prior in time to the real estate mortgage or the real property is purchased by one without actual notice of the prior chattel mortgage of record.

If a subsequent mortgagee or purchaser of the realty has *actual notice* of the unpaid lien for fixtures, it follows that his rights are subject to the rights of the conditional vendor. This rule seems generally accepted. But whether the constructive notice of the recording or filing statutes amounts to such notice as to prevail, where a subsequent mortgagee or purchaser is involved, is again a proposition on which courts have not agreed. One line of authorities holds that *constructive notice* is as potent notice as *actual notice.* Other authorities declare that the vendor of chattels having consented that the property

sold be affixed or attached to realty, cannot thereafter question the same. The chattel having become realty, the record of a lien upon the chattels as personal property became inoperative and of no effect as to these third persons.

The majority rule, supported by logic and reason, would appear to be that *a purchaser or subsequent mortgagee of realty is bound only to search the record title of the realty and the record of any chattel lien would not be notice either constructive or actual under such circumstances.* (1 Jones Chattel Mortgages, Sec. 134—6th Ed.)

A citation of the opinions in some of the pertinent cases will illustrate the views of the various courts and their lack of harmony.

In the case of Abramson v. N. W. Penn. Co. (1928), 156 Md. 186, 143 At. 795, the court considered the matter of *gas radiators* in a dwelling and stated as follows:

(1) Does a conditional sales contract duly recorded under Article 21, par. 55, Code, afford to the purchaser of real property constructive notice that the title to articles described in such sales contract, which at the time it was made were chattels, but which at the time said real estate was purchased were so incorporated therewith as to become an integral part thereof, is reserved to the conditional vendor (a) when the character of the chattels is such that the conditional vendor must have known that they would in ordinary course be so used and converted; (b) where they were not of that character?

(2) Were the radiators involved in this proceeding, in fact, at the time appellant took title to the property in which they were located, so annexed to the realty as to become a permanent and integral part thereof?

(3) If the purchaser of the realty at the time of his purchase had constructive notice of the conditional sales agreement, will he be permitted to assert title to the chattels against the conditional sales vendor, whether the chattels were at that time integrated with the real estate or whether they were not?

The proposition first stated is novel in this court, and, while the question has not infrequently arisen in other jurisdictions, the decisions in respect to it are too conflicting to establish any rule which can be said to be generally accepted. Many courts of high standing have taken the view that the recordation of a chattel mortgage or a conditional sales contract, under a statute making such recordation constructive notice to third persons, is sufficient to charge a bona fide purchaser for value of real estate to which chattels are annexed with notice of any lien or title reserved in such mortgage or conditional sales contract to or against such chattels. Sword v. Low, 122 Ill. 487, 13 N. E. 826; Eaves v. Estes, 10

Kan. 314, 15 Am. Rep. 345; Keeler v. Keeler, 31 N. J. Eq. 181; Ford v. Cobb, 20 N. Y. 344; Kribbs v. Alford, 120 N. Y. 519, 24 N. E. 81; Monarch Laundry v. Westbrook, 109 Va. 382, 63 S. E. 1070. Other courts have taken the opposite view. Elliott v. Hudson, 18 Cal. App. 642, 124 P. 103, 108; Tibbets v. Horne, 65 N. H. 242, 23 A. 145, 15 L. R. A. 56, 23 Am. St. Rep. 31; Brennan v. Whitaker, 15 Ohio St. 446; Phillips v. Newsome (Tex. Civ. App.), 179 S. W. 1123.

But such cases as Sword v. Low, supra, Eaves v. Estes, supra, limit the application of the rule that recordation of the chattel mortgage or conditional sales contract is constructive notice to a purchaser or subsequent mortgagee of realty to which the chattels described in the chattel mortgage or sales contract are annexed to cases *where the chattels are of such a character that they may be removed without damage to the freehold, and where their* essential utility does not require that they *should be so annexed to the freehold as to become a part thereof.* So that they are consistent with the theory that, where the nature of the chattels is such that, if used for the purpose for which they were made, they would naturally and necessarily be annexed to and become a part of some freehold, such recordation would not be constructive notice to the purchaser of such real estate. That limitation is very precisely illustrated by the case of Keeler v. Keeler, supra, where a chattel mortgage duly recorded was held to afford constructive notice to a subsequent mortgagee of the mortgagee's lien against such chattels, as spinning frames, etc., but no notice at all to such mortgagee of a lien reserved against a steam boiler, which had been so annexed to the realty as to become incorporated therewith. The weakness of that position seems to be that it rests upon no surer foundation than casual and subjective opinion as to the character of a given article, and affords little security either to the vendor of the chattel or the purchaser of the realty, nor has it any logical basis in reason or technical law.

On the other hand, Elliott v. Hudson, supra, Tibbets v. Horne, supra, Brennan v. Whitaker, supra, and Phillips v. Newsome, supra, take the position that, if the chattel has with the knowledge of the vendor been sold to be annexed to real estate and has been so annexed, the purchaser of such real estate is not affected by the recordation of a chattel mortgage or conditional sales contract, reserving to the conditional vendor, or the mortgagee of the chattel, any title or lien to or against it, on the ground, that if in fact the property has become a part of the freehold, it has ceased to be a chattel, and that the record of the chattel mortgage or conditional sales agreement ceased to afford constructive notice of the creation of the lien or the reservation of title at the time when the article ceased to be a chattel and became real property. And that seems to us the sounder conclusion, and one more consistent with the legislative policy of this state * * * The radiators were so far as the record shows, ten separate heating appliances, having no more connection with the freehold than an ordinary gas heater, portable kitchen range or heating stove, which are certainly by the weight of authority, held not to be fixtures. Ewell on Fixtures, p. 300. Such

cases as Keeler v. Keeler, 31 N. J. Eq. 181, are not in point, for while the pipes to which the court referred in that case were readily removable without damage to the freehold, they constituted a necessary part of a heating plant which itself was a part of a freehold * * *.

Inasmuch as the chattels retained their character as personal property, and since it was admitted that they were described in the conditional sales contract under which the appellee retained title to them and that such contract was duly recorded, such recordation was sufficient to charge appellant with notice of the fact that the vendor retained title to them.

A case of interest is that of Lasch v. Columbus Heating and Ventilating Co. (1932), 163 S. E. 486, 174 Ga. 618, which involved a furnace and its fixtures sold under a conditional sales contract duly recorded and the rights of a subsequent purchaser of the real estate without actual notice. The furnace was installed in such a manner that it could be removed without material injury to it or the realty.

The holding of the Court sustained the rights of the conditional vendor upon the ground that recording of his instrument *was notice even though constructive,* of his unpaid balance. The court's ruling is as follows:

"Our statute provides for the record of retention-title contracts, and makes such record notice to the world * * * These statutes furnish easy and available means by which an intending purchaser of real estate can acquire notice of the existence of all retention-title contracts between the owner and other parties; with this information prospective purchasers can determine whether chattels attached to real estate are held by the owner thereof under retention-title contracts. The duty imposed upon prospective purchasers of realty to make such investigation and inquiry does not impose upon them any very onerous burden; certainly not such a burden as would justify the destruction of the rights of sellers of articles under retention-title contracts duly recorded. There are cases holding to the contrary of what we rule, but we are of the opinion that our ruling states the true law upon this subject."

In the case of North Shore Co. v. Broman (1933), 247 N. W. 505 (Minn.), the court sustained a recorded conditional sales contract upon boilers, and heating and plumbing equipment installed in a building as against a subsequent mortgage of the realty, applying the sole test and placing its ruling upon the ground that "the removal could be made without substantial injury to the realty."

In some cases the courts have held that the chattels, although affixed to the realty, may retain their intrinsic character

as personalty. An illustration of this is the case of Gardner v. Buckly and Scott (1932), 280 Mass. 106, 181 N. E. 802, which involved an oil burner used for heating a dwelling, set upon and inside a boiler upon four lets, removable by unscrewing and an oil storage tank resting on a cement floor. Under such circumstances the court found the chattels still retained their character as such and upheld the claimants to them.

Now as to the probable rule in Colorado, first as the rights of the parties where a prior realty mortgage is involved and a subsequent chattel mortgagee of fixtures. The proponents representing the holder of the chattel mortgage would no doubt place great stress and urge the case of Beatrice Creamery Co. v. Sylvester, 65 Colo. 569, as definitely adjudicating their rights as superior to the real estate mortgage. It is true that such a general rule was announced, but upon facts which clearly disclosed that the silo was easily removable. Should this same rule apply to such fixtures as a furnace, which might be removable without material injury to the freehold? In my opinion the better rule to follow would be the California rule, which I have previously discussed, namely, that even though the furnace is removable without material injury to the freehold, in this modern day it is an *essential* part of a house and a house without a furnace or other heating equipment greatly impairs its use as such.

What rule should govern in Colorado where the facts disclose a valid recorded or filed chattel mortgage upon, for lilustration, a furnace, and a subsequent realty mortgage or purchaser? The weight of authority seems to be the better reasoned rule, namely, that the subsequent mortgagee or purchaser is bound only by the *recorded instruments relating to realty* and is not bound to search the *chattel mortgage records* to see if chattels affixed to the realty have liens outstanding.

As to these controversial questions, until the Supreme Court of our state announces a definite rule to follow, either party may find ample support for his position and urge the same, well fortified with decisions of high courts of many states.