



# Lien Times

**When a winery can't pay for the grapes they've contracted to buy, grape growers can resort to grower's liens, but is it a good idea?**

By Meghan Leerskov

**A**s the California wine industry muddles its way through the recent downturn, North Bay vineyard owners have good reason to ensure that they get fair payment for all their hard labor. That's not always easy. The precarious financial position of some local wineries has resulted in several grape growers having their contracts "renegotiated" suddenly, receiving only partial payment for grapes or even having grape deliveries denied by wineries. Such actions have left many growers stuck with a grape crop costly to cultivate and difficult to find new buyers for.

Back in the late '90s, selling wine was easy. The U.S. was in one of the longest periods of expansion on record, and even pragmatists were giddy at the prospect of endless growth in the new economy. New wineries were as plentiful as tech IPOs, and demand for grapes was skyrocketing. But an unusual

confluence of events—from the tech bubble bursting to the Sept. 11 attacks and the war in Iraq—roused the old bear business cycle from its cave.

Just as the rising tide of boom times had lifted all boats, the recession that followed decimated them just as indiscriminately. A worldwide grape glut, in addition to the economic pressures of the downturn, pushed many wineries to the edge. Over the past few years, several North Bay wineries have been forced into bankruptcy—including Sonoma Creek, De Loach and Liparita—and industry insiders expect more, even as the grape glut eases. The question is, what recourse do growers have when confronted with a winery's bankruptcy or nonpayment?

#### Lien on me

Grape growers for California's \$33 billion wine industry often fall back on what are called "statutory producer's liens" to guarantee payment for their grapes. Agriculture is an industry

where payment routinely comes after delivery, leaving farmers in a vulnerable position. Statutory liens, commonly called "grower's liens," were created by the Legislature in Article 9 of the California Food and Agriculture Code to protect the producers of any crop. The grower's lien is unique in the commercial world. While many liens require formal documentation or public filings to become effective, the grower's lien attaches automatically once the crop is delivered. "The basic benefit to the grower—and it is significant—is that the grower's lien is automatic," says attorney Richard Abbey of Abbey, Weitzenberg, Warren & Emery in Santa Rosa. "Once the grapes are delivered, the lien literally just pops into existence."

Grower's liens are also substantial because they supersede other liens against a winery. "The grower's lien is valuable because it automatically has priority over most other liens or security interests in the grapes or wine without requiring the grower to make a filing or take other action," says attorney Matt Lewis of San Francisco- and St. Helena-based Farella Braun + Martel. "The standard example is that most wineries, because they are so capital-intensive, have a relatively large amount of bank financing, which results in a blanket consensual lien on all assets of the winery including inventory—the grower's lien even becomes superior to that claim by the lender," says Abbey. "The flip side of the coin is that lenders consider that every grape that comes into the winery has a lien on it that could impact the bank, and this impacts how much money they are willing to lend." With this in mind, some financial institutions have required that a waiver of the lien be part of the contracts that are routinely drawn up between growers and wineries. "There was a movement awhile ago where wineries were trying to get growers to waive their lien rights. Most growers wouldn't do it, and I question if those waivers would hold up in court anyway because it is a strong statutory scheme," says Abbey.

Lien waivers can be potentially devastating to growers, leaving them at the mercy of the winery. "The handful of wineries that ask that liens be waived do that because their bank requires them to or they are looking for additional ways to make sure their assets aren't encumbered. Banks don't want a lot of liens on the inventory until the growers are paid, but it is by no means standard

*"There was a movement awhile ago where wineries were trying to get growers to waive their liens," says attorney Richard Abbey of Abbey, Weitzenberg, Warren & Emery. But waiving a lien, he cautions, can be devastating to growers.*



*"Liens are not a be-all-and-end-all solution to a troubled grower/winery relationship," says attorney Matt Lewis of San Francisco- and St. Helena-based Farella Braun + Martel.*

*When amicable negotiation fails, attorney John Mackie of Carle, Mackie, Power & Ross in Santa Rosa suggests that growers who are having trouble getting paid pursue a Uniform Commercial Code lien in addition to a grower's lien.*



*Attorney Matthew Eisenberg of Dickenson Peatman & Fogarty in Napa points out an odd loophole in grower's liens: once the winery sells the wine, the grower's lien disappears.*

practice," says Jeff Bitter, vice president of Allied Grape Growers, a cooperative of growers based in Fresno. "The growers don't want to do that voluntarily, but some wineries use it as a standard part of their contract, and some growers are desperate enough to sell grapes because it's harvest time and there are no other buyers or it is a soft market."

#### Lien limitations

While the advantages of an automatic and high-priority lien are obvious, less evident are its limitations. "The lien attaches from the time of delivery to the producer but then comes a big caveat: the wine or grapes must remain in the possession of the producer for the lien to remain in effect," says Matthew Eisenberg, an attorney specializing in vineyard law with Dickenson Pearman & Fogarty in Napa. If the winery sells the wine, then the grower's lien disappears as magically as it materialized, leaving the grower with little recourse. "Liens don't follow the wine," emphasizes Santa Rosa attorney John Mackie of Carle, Mackie, Power & Ross. "It only stays in effect while that wine is owned by the winery. And that brings up a disagreement about whether the proceeds of any sale of the wine are covered by the lien, and the answer is probably no." The trick with a grower's lien is that just because it is automatic

doesn't mean that growers can sit back and wait for the check in the mail. Growers need to use the court system to enforce their rights. Jeff Bitter with Allied Grape Growers has experience with the proactive measures necessary to make grower's liens

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work. Allied is responsible for marketing, contracting sales and collecting payment for its many members, who turn over the titles of their grapes to the organization. "There are instances where growers don't get paid, and you have to take wineries to court. It happens, but not as often as you'd think," he says. "We have been involved in a couple of situations during the last couple years, whereas in the 10 years before that we didn't have any."

A grower faced with enforcing a lien has several options, according to Bitter. A grower can simply draft a letter to the winery informing it of the grower's intent to implement the lien and demanding that the product not be used or moved until payment is received. However, Bitter feels that it is more effective and binding to involve the courts as soon as possible. "It depends how bold the winery is, but there may be some success in just writing a letter to enforce your lien—but what if your product is moved? You're going to wish you had a preliminary restraining order and injunction from the judge to protect you. Then if they move the wine, the short story is you can get the sheriff on them, and they're in a big heap of

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trouble," he says. "Involving the court is essentially perfecting the lien."

Allied was forced to invoke its lien recently involving the sale of some premium Russian River Valley grapes to a high-end winery that only submitted partial payment for the crop. "In this instance, it was a fair amount of money that was outstanding, so we went to court to get it," says Bitter. "Of course, this all costs money. So any time you hire attorneys to write up those papers, it better be a big sum you're going after to make it worth it. There have been other cases where the amount just wasn't worth it. In those cases, we handle it through more diplomatic means with the winery, and we don't go to court."

Mediation conducted by the Department of Agriculture is one of those more diplomatic means, but it's not a perfect solution. "The disadvantage of grower's liens is that they aren't always easy to enforce. Mediation through the Department of Agriculture isn't always an ideal road to take, either," says Matt Lewis of Farella Braun + Martell. "It isn't fast, and it doesn't have a lot of teeth to it. Ultimately, the grower has to go to court to foreclose on the lien if they are serious about collecting their money." Growers can also seek to have a fine levied against the winery should they resell the grapes without payment. "It is a misdemeanor with a fine of \$500 or more and up to one year in county jail, but I've never heard of it happening," says Eisenberg of Dickenson Peatman & Fogarty. Growers can also file a complaint with the California

Department of Agriculture which can ultimately result in a winery's processor's license being revoked. "There are a few cases where growers have gotten angry enough that they have initiated that," says Mackie. "I say 'angry enough' because, if a winery gets to a point where it loses its processor's license, then it probably doesn't have the capacity to pay the grower back, and the grower has effectively destroyed any hope of getting paid."

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#### **Navigating bankruptcy**

Grower's liens continue to provide protection for vineyards in the face of a winery's bankruptcy. "In a bankruptcy, the grower becomes a secured creditor, and the winery can't get rid of the wine without paying the

grower or providing adequate protection for the grower," says Abbey. "This is in contrast to a situation without the procedural protections of a bankruptcy where a winery just simply can't pay a grower, sells the wine and the lien vanishes. Grower's liens are actually quite powerful in a bankruptcy situation." New case law and changes in the Uniform Commercial Code (UCC) in California law have opened up the question of whether grower's liens are subject to the UCC's public filing requirement. The UCC was extended to apply to agricultural



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The family soon received a bill from the government for the approximate value of the vineyards. In order to pay this, the children needed to sell a portion of their property, but they soon discovered that the county wouldn't allow agriculture-zoned property to be parceled out in sections less than 200 acres.

The family was forced to sell their entire property and business. They are now employees for the large conglomerate winery that bought their family vineyard.

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liens, and if the courts interpret a grower's lien to be an agricultural lien, growers would need to make the proper filings to ensure their lien is upheld. While more complex than a grower's lien, a UCC lien holder has potentially greater rights. In many cases, the grower's rights are preserved in both grapes that have been sold or transferred and in the proceeds of that sale or transfer. A UCC lien holder also has the right to repossess and resell the grapes without resorting to the courts.

"We recommend to grower clients that they try to get a UCC lien in addition to the grower's lien," says Mackie. "That requires a filing with the Secretary of State, but it has advantages such as a faster enforcement mechanism and the lien staying with the proceeds of sale. It allows the grower to take possession of the wine made from the grapes prior to going into court. That is a more expeditious way of fixing the problem." Attorney Matt Lewis agrees. "With the recent changes to the law, it is even easier for growers to protect themselves by using the UCC to supplement the existing grower's lien," Lewis says.

### Growing healthy relationships

Liens give growers some much needed equality and leverage in their relationships with vintners, but attorney Bruce Miroglio with Gaw Van Male Smith Myers & Miroglio in Napa believes that enforcing a lien can be penny-wise and dollar-foolish. "It is important to talk about the effect of these liens," he says. "Trying to resolve matters in an amicable fashion has such an impact on the relationship, and resorting to liens can be really devastating."

Miroglio recalls a recent case with a grower in the Central Valley and a North Coast vintner. "A dispute had erupted because of ambiguities in a poorly-written grape agreement," he says. "It had to do with typical yields in the Central Valley and yields that are expected on the North Coast—I am talking about pruning and limiting fruit such that you maintain high varietal characteristics and quality." The grower pushed the contract terms to the limit, producing more fruit but of a lesser quality. The miscommunication created a rift, and the vintner delayed payment while they were negotiating. The grower tried to enforce the lien, which led to the vintner filing for bankruptcy protection, and that ended up voiding the entire agreement the two had had to work together for the next six years. "Because



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***"Trying to resolve matters in an amicable fashion has such impact on the relationship, and resorting to liens can be really devastating," says Bruce Miroglio of Napa's Gaw Van Male Smith Myers and Miroglio.***

the grower pushed the envelope and pushed the lien, nobody was well served," he says. Miroglio stresses the importance of an expertly crafted grape contract and constant communication between the winery and the grower. "I have represented vintners that have had the ability to enforce certain provisions of a contract that weren't met or realized that they aren't living up to their end of the deal and recognized the importance of working together. So, they go down and say, 'You all know we could enforce our end, and you know you can enforce your end, but let's work together harmoniously,'" he says. The lien creates an incentive for growers and wineries to work together. "It's a sabbat to rattle, but when the lien is enforced, the relationship is gone." Despite a slight increase in the numbers of growers and wineries finding themselves embroiled in payment disputes, agriculture remains a business dominated by relationships, especially in the North Bay's close-knit wine country. "A lien, no matter how strong, is not a be-all-and-end-all solution to a troubled grower/winery relationship," says attorney Matt Lewis. "You may have legal rights that you don't pursue, depending on how you see your relationship with a winery going for the next couple years. Many growers weather a tough time with a winery because they see a strong relationship ahead."

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