

DEBTOR / CREDITOR

Final Examination

Professor Hurn

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Instructions: This examination is for three hours. It is fully “open book,” meaning you may refer to any written materials that you may have brought with you. However, you may not work with or consult any other person about your answers. Answer the multiple choice questions on the Scantron sheet provided and the short answers and essay in a Bluebook. Do not assume that familiar-looking questions are the same as those on old exams.

Unless otherwise indicated, assume all transactions occur in the USA in states with the uniform codes and statutes printed in your statutory supplement, with typical versions of other sorts of statutes. If something appears missing or mistaken, plainly state a corrective assumption and proceed with your answer

Remember to put your exam number on the answer forms and bluebooks.

Multiple Choice

(thirty questions, up to 90 minutes at 3 minute average)

1. Buford was old and sick. He got the flu, which led to pneumonia. His doctor told him it was pretty likely he would die. Buford called in his relatives and told them he had taken care of most things in his will. Then he called for his watch and chain. He took a key off the chain and handed it to Sadie, saying “this opens that gun case in the hall—everything in it is yours.” He then handed the watch and chain to Bobbie and said “this is going to be yours.” Sadie and Bobbie took the guns and watch home with them that day. To everyone’s surprise, Buford recovered and wants to go hunting. He wants his guns and watch back.

- a. He can recover neither.
- b. He can recover the guns (only).
- c. He can recover the watch (only).
- d. He can recover both.

(2-3) Ada had an old Volvo she drove in bad weather. It was entirely paid for and so old it no longer needed a certificate of title. She took it to Billy’s Used Car Sales and Repair Shop for a new head gasket. By the time the job was done, it was spring and Ada was in no hurry to pay. Billy notified her he was asserting a retaining lien. She ignored him. He then, without statutory authority, took the car to a wholesale auto auction and sold it for a fair price to a Volvo collector.

2. In an action against Billy for conversion, Ada will
- a. Win
 - b. Lose because she entrusted the car to a dealer.

- c. Lose because the Billy had a lien.
- d. Lose because Billy had the right of immediate possession.

3. In an action against the collector for replevin, Ada will

- a. Win
- b. Lose because she entrusted the car to a dealer.
- c. Lose because the Billy had a lien.
- d. Lose because Billy had the right of immediate possession.

4. At the retirement party of Isadora, a successful choreographer, a theatrical producer soberly announced to the crowd that because the choreographer had served so long and well for such comparatively little pay, the producer was assigning 5% of the net income of his forthcoming musical comedy to her. Two weeks later, to secure a loan, the same producer signed a security agreement with a bank giving it a lien on all present and after-acquired intangible rights. The bank filed a UCC-1 in the proper place. Thereafter the show began and is a success, but the producer went broke due to unrelated debts. He surrendered all his collateral to the bank, which put him on a salary to continue the show.

Isadora wants her 5%. In an action against the bank to declare her rights and collect amounts due so far she will

- a. Lose because you cannot assign a mere expectancy.
- b. Lose because the assignment to her was revocable.
- c. Win because her assignment was prior in time.
- d. Win because the bank cannot perfect a lien in property not yet owned by the debtor.

5. A fraud has been discovered at a local art dealership. The manager was a crook. The nature of the scheme was that for about three weeks the manager took some credit card orders over the phone for moderately expensive prints. However, he wrote down on the credit card slips much larger sums than the price of the print before endorsing and depositing them for collection. When the money came in from the credit card company he had a way of skimming off the excess, leaving the dealership even. Visa paid several thousand dollars extra this way (and the manager disappeared) before any customers noticed the problem. Under local tort law the employer is not liable for this kind of criminal act. In a commercial law suit against the dealership for the amount lost:

- a. Visa will lose because credit card drafts without signatures lack warranties.
- b. Visa will lose because credit card drafts without signatures aren't negotiable.
- c. Visa will win because it is subrogated to its customers' rights.
- d. Visa will win because of the dealership's transfer warranty.

6. George hired Ned to plow the snow off his driveway for \$50.00. He gave Ned a \$50 bill which he actually and reasonably believed was genuine. However, it was a high grade counterfeit, and when Ned tried to deposit it in his bank, it was discovered, seized, and delivered to the Secret Service. As between George and Ned

- a. George will bear the ultimate loss because he still owes Ned \$50.00.
- b. George will bear the ultimate loss because he warranted the authenticity of the bill.
- c. Ned will bear the ultimate loss because the bill purported to be bearer paper.
- d. Ned will bear the ultimate loss because he accepted the tender, legal or not.

7. Bank makes annual loans to Farmer, secured by a properly perfected article 9 lien on his soybean crop. Their arrangement has always been to put the beans in a warehouse and take a negotiable receipt in their joint names. This year, however, Farmer takes advantage of a new manager and makes no mention of the bank, taking a receipt in his sole name. He then endorses and delivers it to Continental Grain, a processor unfamiliar with him or his bank. Farmer departs for Paraguay with the proceeds. The same day Continental Grain presents its receipt Bank demands the beans. Warehouse files interpleader against Bank and Processor to determine ownership of the beans.

- a. Bank will win because you can never get title from a thief.
- b. Bank will win because its rights are prior in time.
- c. Processor will win because of Bank's risky behavior.
- d. Processor will win because title to the document gives title to the goods.

8. A burglar stole a valuable book from the original owner and sold it to a dealer who had no notice of the wrongdoing. The dealer sold it to a regular customer. In an action by the original owner to recover the book from the customer

- a. The original owner will win because the dealer's title was void.
- b. The original owner will win because merchants warrant the title of goods they sell.
- c. The customer will win because the burglar entrusted the book to the dealer and the customer bought in the ordinary course of business.
- d. The customer will win because s/he is a bona fide purchaser for value.

9. The passage of title in a sale of goods automatically controls

- a. Who has the insurable interest in the goods.
- b. When it first becomes possible for the buyer to get specific performance of the contract.
- c. What jurisdiction may levy a sales tax.
- d. All of the above.

10. Buyer secured an irrevocable letter of credit from its bank, naming seller the beneficiary and specifying various documents to be presented as conditions of payment. Seller has tendered all the documents and they have no discrepancies. However, Buyer has now instructed the bank to refuse to pay on the letter of credit. The time is about to run on the decision whether to pay or dishonor. The bank should:

- a. Pay only if the customer changes its mind and gives permission in time.
- b. Pay only if the seller agrees to indemnify it.
- c. Pay.
- d. Refuse to pay.

11. Landlord has leased business premises to several tenants, in writing, for various terms of years. Landlord sold the building and assigned and delegated all the leases to Assignee, as of June 30. Assignee also signed a written assumption of the duties (utilities, upkeep, clearing walks and parking area, etc.) All the tenants are notified in advance. Through various suspicious mix-ups several tenants pay the July rent to the old Landlord, who keeps the money. Tenants blame landlord, landlord blames tenants. Assignee's remedy is

- a. Against the tenants for the unpaid rent.
- b. Against the old Landlord under assignment law.
- c. Both a. and b. are correct remedies.
- d. Neither a. nor b. is correct.

12. When assignments there are successive, irrevocable assignments not subject to Article 9 in an English Rule jurisdiction, the owner is

- a. The first assignee.
- b. The first assignee to notify the obligor under the original contract.
- c. The first assignee for value without notice of prior conflicting rights.
- d. The first assignee with reasonably foreseeable detrimental reliance.

13. Client, an art dealer, shipped a stone sculpture worth at least \$2,500 to Customer by Confederate Express, a common carrier. Out of ignorance, Client's clerk did not take the clearly expressed option to insure the package for an extra \$2 per hundred valuation. This is a real option, often take by client in the past. With that section of the agreement left blank, the only provision for loss limited ConFed's liability on the package to \$50. ConFed's delivery crew dropped the sculpture off the truck, destroying it. There is no dispute about the facts. In an action for the value of the sculpture

- a. Client's recovery will be limited to \$50.
- b. Client's recovery will be for the full value because it can prove actual negligence.
- c. Client's recovery will be for the full value based on the presumption of conversion.
- d. Client's recovery will be for the full value because destruction is actual conversion.

14. The law governing the survival and descent of a right of publicity generally is:

- a. The law of the state of first public use.
- b. The law of the state of the first licensing.
- c. The law of the state of the celebrity's domicile at the time of first use.
- d. The law of the state of the celebrity's domicile at the time of death.

15. Debtor is being sued for a large sum. Debtor had some valuable artwork worth about \$15,000 dollars. Debtor went to a friend who had always admired the art, explained his situation and indicated he would like to sell it and leave the country. Friend paid him \$15,000 and then later gave the artwork to an innocent museum, taking an appropriate tax deduction. Debtor loses the lawsuit and no non-exempt property is found. If the transaction with Friend is discovered:

- a. Friend is liable to the judgment creditor for \$15,000.
 - b. Friend is liable to the judgment creditor for the whole amount of the plaintiff's judgment.
 - c. Friend is liable to the judgment creditor for \$15,000 and the museum is liable for \$15,000 or return of the artwork.
 - d. No one is liable to the judgment creditor because the first transfer was for fair value.
16. Debtor is being sued for a large sum. Debtor had some valuable artwork worth about \$15,000. Debtor went to a friend who had always admired the art, concealed his situation and said he would sell the art for \$2,000, which he claimed was his original cost. Friend agreed. Debtor loses the lawsuit and no non-exempt property is found. If the transaction with Friend is discovered:
- a. Friend is liable to the judgment creditor for \$15,000.
 - b. Friend is liable to the judgment creditor for \$13,000.
 - c. Friend is liable to turn over the artwork to the judgment creditor.
 - d. Friend is liable to turn over the artwork to the judgment creditor only if arrangements are made to return his \$2,000.
17. A writ of replevin can NOT reach:
- a. goods
 - b. instruments
 - c. accounts
 - d. either b. or c.
18. Which of the following liens capture property which the creditor has not yet identified?
- a. Attachment Lien
 - b. Federal Tax Lien
 - c. Judgment Lien
 - d. Both b. and c.
19. When a client has the option of suing in Trover or in Replevin, s/he should generally prefer Replevin if:
- a. The market value of the misappropriated property is expected to be less at the end of the trial than at the time of the misappropriation.
 - b. The market value of the misappropriated property is less than the subjective value placed on it by the client.
 - c. Replevin is preferable in BOTH situations.
 - d. Replevin is preferable in NEITHER situation.
20. A heating company did commercial furnace work on credit, taking from each customer a downpayment upon signing its contracts, and a promissory note for the balance. It then sold

these notes at regular intervals to a bank through its factoring department. Despite the ready flow of working capital which this provided, the contractor's affairs became disordered and it defaulted on a number of contracts after having sold the notes. In an action by the bank against the customers to collect on the notes

- a. The bank will win if it had no notice of the debtor's defaults when it bought the notes.
- b. The bank will win even if it did have notice of the debtor's defaults when it bought the notes.
- c. The bank will lose if the debtor's behavior was fraudulent.
- d. The bank will lose if the debtor (the primary obligor) is unable to perform or pay damages.

21. Same facts as above, except that after the heating company's troubles became widely publicized in the community, the bank discounted the notes to a larger regional bank. In an action by the regional bank against the customers to collect the notes

- a. The regional bank will win if it had no notice of the contractor's defaults when it bought the notes.
- b. The regional bank will win even if it did have notice of the contractor's defaults when it bought the notes.
- c. The regional bank will lose if the contractor's behavior was fraudulent.
- d. The regional bank will lose if the contractor (the primary obligor) is unable to perform or pay damages.

22. Which of the following warranties CAN NOT be disclaimed even by express language?

- a. A merchant's warranty against infringement.
- b. An assignor's warranty s/he knows of no defenses impairing the enforceability of contract rights assigned.
- c. An endorser's warranty of the authenticity of prior endorsements on a check.
- d. All of the stated warranties can be effectively disclaimed.

23. Debtor was a small, incorporated business. It began to experience difficulties when the IRS disallowed some tax deductions and credits during an audit. The IRS assessed a substantial tax liability and demanded payment. To raise money to pay this and deal with other financial problems, Debtor, for the first time, negotiated a large, lump-sum bank loan, secured by a properly created and perfected Article 9 security interest in its present and after-acquired equipment, inventory, and receivables. Unfortunately the loan proceeds were applied to purposes other than the tax claim. The IRS then properly recorded its notice of tax lien. In a subsequent dispute between the IRS and Bank over the collateral

- a. The IRS will win because its lien arose on assessment.
- b. The IRS will win because among comparable liens those of the sovereign have priority.
- c. The Bank will win if, and only if, it perfected within 45 days of the IRS assessment.
- d. The Bank will win because it was first to perfect.

24. Debtor was a drug dealer and flying instructor. With now-traceable drug proceeds Debtor made a down-payment on a small airplane used it to transport his illegal inventory. He borrowed the rest of the purchase from a bank, giving it a properly perfected security interest in the plane. The bank can prove it had no knowledge of the drug dealing. The government has now seized the plane and filed forfeiture proceedings. If the bank intervenes to assert its interest it

- a. Will lose because the government's rights arose when the plane was bought.
- b. Will lose because among comparable liens those of the sovereign have priority.
- c. Will win if, and only if, it perfected within the 20-day PMSI look-back period.
- d. Will win because it is an innocent owner without notice of the government's claim.

25. A Receiver's title is generally:

- a. Good against the whole world from the moment of his/her appointment.
- b. Good against the whole world from the moment s/he posts bond.
- c. Good against everyone except bona fide purchasers for value without notice from the moment of his/her appointment.
- d. Good only when recorded in the Registry of Deeds and the Article 9 Registry.

(26-28) Assume an insolvent debtor lives in a house on which there is a first mortgage, and a mechanics lien for roofing work. The property taxes are past due. The local homestead exemption is \$100,000.

26. Who has the most senior claim to the real estate?

- a. The mortgagee to the extent of the mortgage.
- b. The mechanic to the extent of his/her lawful claim.
- c. The taxing authority to the extent of the property taxes.
- d. The debtor to the extent of his/her homestead.

27. Who has the next most senior claim?

- a. The mortgagee to the extent of the mortgage.
- b. The mechanic to the extent of his/her lawful claim.
- c. The taxing authority to the extent of the property taxes.
- d. The debtor to the extent of his/her homestead.

28. Who has the third most senior claim?

- a. The mortgagee to the extent of the mortgage.
- b. The mechanic to the extent of his/her lawful claim.
- c. The taxing authority to the extent of the property taxes.
- d. The debtor to the extent of his/her homestead.

29. Which of the following clauses of the U.S. Constitution puts no constraints on a federal Bankruptcy Court?

- a. The Taking Clause.
- b. The Fifth Amendment Due Process Clause.
- c. The Contracts Clause.
- d. Article III (the Judicial Branch)

30. Which of the following procedures does NOT require notice and hearing for the alleged debtor who is their target?

- a. Attachment.
- b. Garnishment./Trustee Process
- c. Replevin.
- d. Lis Pendens

Short Answers (up to 30 minutes)

1. You represent a judgment creditor and have discovered that the debtor owns a nearly new, valuable automobile with no liens on it. The debtor is completely untrustworthy, but you know where the car is. Briefly state the legal steps you would take to safely turn this asset into money for your client.

2. Your client, Norma, a previously healthy 30 year old computer programmer, was severely injured by a negligent driver. Norma retained you, agreeing in writing to pay a contingent fee of one-third of the gross recovery by settlement or judgment. You did not take an assignment, because your state is among the minority forbidding assignment, attachment, or other transfer of personal injury claims prior to judgment. Most of Norma's large medical bill was paid by insurance provided through her ERISA-qualified employee benefits package. Shortly after you filed the personal injury suit, the benefits manager's office sent you a copy of a subrogation agreement signed by your client at the time of employment giving them first-dollar claim on any compensation for medical expenses, up to the amount they paid.

Briefly state whether you should be concerned, and why or why not.

3. Please state, without elaboration, the lowest level method of perfecting an otherwise enforceable voluntary lien on each of the following items sufficient to defeat a trustee in bankruptcy. If recording is required please indicate the proper type of registry.

- a. Computers sold by the creditor for retail sale by the debtor.
- b. A new automobile sold by the creditor for debtor's personal use.
- c. A new automobile sold by the creditor for debtor's business use.
- d. A quantity of Chattel Paper.
- e. Un-certificated stock.
- f. A patent.
- g. A common law trade name.
- h. A cause of action for personal injuries.

Essay I (up to 60 minutes)

Frank was a jewelry designer who sold his own work through a wholly-owned corporation. At a time when the corporation was doing well and space was cheap he negotiated a very favorable lease that has several years to go. The corporation had a bank loan secured by a lien on all the statutory categories of collateral presently owned or after-acquired (recorded in the Article 9 registry).

Inventory was physically small, but valuable: gold, silver, and platinum wire and bars from a precious metals supplier, some small diamonds and semi-precious stones from another company. The metals were on credit, with a properly recorded PMSI held by the supplier. The stones were supposedly “on loan,” but Frank had authority to mount and sell them, paying the wholesaler’s pre-set price, or to return them. Of course both metals and stones were worked up together into finished pieces of inventory. Shortly before the events leading to the company’s bankruptcy Frank also purchased some valuable appraisal and assaying equipment, on credit, with a properly perfected security interest in the seller.

Frank was a good designer (and had formally assigned copyrights on a few of his best wedding bands to the corporation). He let people buy on a layaway plan—so much a month while he kept possession. He sometimes did specially commissioned work. These practices got him into trouble. He took what was for him a very large commission for some custom pieces for a one-time friend named Nick and asked for only a small deposit. Nick was rumored to have suffered business reverses about the time Frank was finishing the work. Although he still seems to have plenty of money Nick refused to pay, claiming dissatisfaction with the final product. The designs included family crests in filigree, so the pieces cannot be sold to others and will probably have to be salvaged for metal and stones.

While he was working on this commission Frank was bringing in little else. He made personal loans to the corporation to keep up with rent and the pay for his one assistant/clerk. A law student friend told him to at least have the corporation mortgage back the copyrights to him as security for these loans, which Frank did, but he waited another two months to file with the copyright office.

Business slowed for all the luxury trades and Frank ran out of savings. Nick never paid on the custom job. There was quite a bit of other finished work accumulating unsold in the cases. Some of the lay-away people stopped paying. Five weeks after he recorded the copyright mortgages Frank’s corporation filed for bankruptcy. It owed his assistant nearly a month’s wages. The only bills he was current on were utilities and all his tax obligations.

Identify all potential claimants and assets explaining what claims are enforceable against what assets (or are unsecured) with what relative priorities and why.

End of Examination