

DEBTOR / CREDITOR

Final Examination

Professor Hurn

Fall 2009

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 or by e-mail to the Registrar. 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 essays.

Multiple Choice

(30 questions— up to 90 minutes suggested)

1. A crook persuaded a dealer to sell and deliver a valuable antique desk to the crook, paying with a forged check. Before the forgery was discovered, the crook sold and delivered the desk to a second dealer who had no notice of any wrongdoing. In an action by the original owner to recover the desk from the dealer
 - a. The original owner will win because one can get no title from a thief.
 - b. The original owner will win because no one can acquire rights through forgery.
 - c. The second dealer will win because the crook took possession.
 - d. The second dealer will win because the crook had voidable title.

2. Professor Stern absentmindedly left his 1815 edition of Blackstone's Commentaries on the Boston bus. Finder took it to Commonwealth Books and sold it to them for a considerable sum. Commonwealth Books sold it in the ordinary course to buyer. When Professor Stern was next in the shop, he bemoaned his loss to the manager, who recalled the earlier purchase and sale. On these facts, Professor Stern may
 - a. Recover the book from Buyer (only).
 - b. Sue Finder and/or the Shop for conversion (only).
 - c. Recover the book from Buyer or sue any combination of Finder, Shop, and Buyer for conversion.
 - d. Professor Stern has no remedy on these facts.

3. Debtor owned an antique store. One afternoon the Sheriff served a writ of execution covering all inventory at the store. This is effective under local law when recorded in the

Article 9 registry. It was recorded that day. The next day, before calling his lawyer, Debtor contracted to sell an immense Victorian desk out of inventory to Buyer, who made a down-payment. They agreed Debtor would deliver the desk the following Saturday. In a dispute over the desk between the Buyer and the Attaching Creditor.

- a. Buyer will win and the Creditor gets nothing.
- b. Buyer will win if s/he tenders the amount not yet paid on the contract to the Creditor.
- c. Buyer will lose because s/he didn't take delivery.
- d. Buyer will lose because the execution preceded the contract.

4. In a state with a traditional Dead Man's Statute, testimony about which of the following transactions would be barred?

- a. An otherwise un-witnessed oral contract between the party/witness and the deceased.
- b. An otherwise un-witnessed oral gift *causa mortis* by the deceased to the party/witness.
- c. Testimony would be barred about both of these transactions.
- d. Testimony would be barred about neither of these transactions.

5. Landlord was in financial trouble. His best asset was an office building leased 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.). Before any of the tenants were notified of the assignment, the old Landlord, in return for lump-sum payments, extended the leases of several tenants. When the Assignee (new landlord) discovers this it may:

- a. Disregard the extensions.
- b. Recover any provable loss in a warranty action against the old Landlord.
- c. Recover the amount of the lump sum payments from the tenants, leaving them to sue the old Landlord.
- d. Do either a. or b. but not both.

6. Assignments of contract rights NOT governed by UCC Article 9 fall under either the American Rule or the English Rule, depending on the state. Under the American Rule, when there are successive, irrevocable assignments of the same right, the owner is

- a. The first person to whom assignment is made.
- b. The first assignee to notify the obligor under the original contract.
- c. The last assignee to take without notice of any prior conflicting rights.
- d. The last assignee for value without notice of any prior conflicting rights.

7. Same subject. When assignments ARE governed by Article 9 and there are successive, irrevocable assignments of the same right, the owner is

- a. The first person to whom assignment is made.
 - b. The first assignee to notify the obligor under the original contract.
 - c. The first assignee to file in the Article 9 registry.
 - d. The first assignee for value without notice of prior conflicting rights to file in the Article 9 registry.
8. Farmer stored soybeans in a Warehouse, taking back a negotiable warehouse receipt. Farmer duly endorsed and delivered it, for value, to a Speculator. Speculator duly endorsed and delivered it, for value, to a Food Manufacturer. Before the Manufacturer took delivery of the beans, there was a flood at the warehouse. Most of the beans were destroyed, there was no flood insurance, and the warehouse is insolvent. Manufacturer's remedy for any loss not covered by the warehouse's bond is:
- a. Suit against Speculator on its warranty.
 - b. Suit against Farmer on its warranty.
 - c. Suit against both Speculator and Farmer on their warranties.
 - d. Manufacturer has no remedy against either Speculator or Farmer.
9. You represent the successful plaintiff in a state-court products liability suit against a California manufacturing company. The judgment is unpaid. You refer it for collection to California counsel. There is no reason to fear fraudulent concealment of assets. In that case, the most efficient and least expensive legal action is:
- a. Suit on the original cause of action, with quick summary judgment due to res judicata.
 - b. Suit on the judgment debt, with quick summary judgment.
 - c. Action under the Uniform Enforcement of Foreign Judgments Act.
 - d. A long-arm writ of execution sent from the original court to the appropriate sheriff in California.
10. Under the Uniform Fraudulent Transfer Act, in the absence of any Bankruptcy filings, which preferences are voidable?
- a. All preferences
 - b. All preferences during or causing insolvency.
 - c. Only Insider preferences.
 - d. Only Insider preferences during or causing insolvency.
11. A local contractor did grading and paving on credit, taking from each customer a downpayment and a simple installment sales contract for the balance. These contracts were subject to a properly created and perfected floating lien in favor of the local Bank. The customers are all businesses. Despite the ready flow of working capital which this provided, the contractor's affairs became disordered and it defaulted on (breached) a

number of contracts. These disputed claims triggered the default clause in the security agreement. In an action by the bank against the customers to collect on the contracts

- a. The bank will win if it had no notice of the contractor's defaults when it made the security agreement.
- b. The bank will win even if it did have notice of the contractor's defaults when it made the security agreement.
- c. The bank will lose only if it acquiesced in the contractor's breaches.
- d. The bank is subject to all defenses good against the contractor.

12. Same facts as previous question EXCEPT contractor took promissory notes from its customers. On these facts

- a. The bank will win if it had no notice of the contractor's defaults when it acquired an interest in the notes.
- b. The bank will win even if it did have notice of the contractor's defaults when it acquired an interest in the notes.
- c. The bank will lose only if it acquiesced in the contractor's breaches.
- d. The bank is subject to all defenses good against the contractor.

13. A Debtor took grain in which Bank had a security interest and, completely without authority or awareness by the Bank, put it into the warehouse of an honest warehouser in return for a negotiable warehouse receipt. Debtor then endorsed and sold the receipt to an innocent grain processor. Before the processor/holder called for the grain, it was sold by mistake to a buyer in ordinary course of business. Of these parties, who has the best claim to the grain?

- a. Debtor.
- b. Bank.
- c. Processor/Holder.
- d. Buyer in Ordinary Course.

14. Same facts. Who has the second best claim to the grain?

- a. Debtor.
- b. Bank.
- c. Processor/Holder.
- d. Buyer in Ordinary Course.

15. 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 one minor discrepancy. The time is about to run on the decision whether to pay or dishonor, and the Buyer has not yet returned its calls. If the Bank pays without Buyer's permission:

- a. It will be liable to Buyer for any loss due to the non-conformity.

- b. It will be subrogated to Buyer's rights to pursue Seller for the non-conformity.
- c. Both a. and b. are correct.
- d. Neither a. nor b. is correct.

16. Patentee sold and assigned his invention to Peter on January 1, 2004. Patentee sold and assigned the same invention to Quentin on February 1, 2004. Neither assignee was aware of any impropriety. If Peter recorded in the PTO on March 1 and Quentin recorded on March 2, the patent belongs to:

- a. Peter because he was the first assignee.
- b. Peter because his recording relates back to January 1.
- c. Quentin because he was a BFP.
- d. Quentin because his recording relates back to February 1.

17. Which of the following procedures does not require notice and opportunity to be heard by the defendant-debtor whose property is being pursued?

- a. Attachment.
- b. Replevin.
- c. Execution.
- d. Neither Replevin nor Execution requires notice and opportunity to be heard.

18. Creditor #1 had a valid security agreement and took an accurate financing statement in proper form to the filing office. Creditor #1 paid the correct fee and the officer took the financing statement. Receipts and stamped copies prove this. However, due to a series of emergencies and power failures that day, the officers never indexed Creditor #1's financing statement. Several months later Creditor #2 entered a valid security agreement on the same collateral and filed a proper financing statement which was in fact properly indexed. In a dispute between the two Creditors, which will have priority?

- a. Creditor #1 because its has satisfied the requirements for an effective filing.
- b. Creditor #1 because Creditor #2 was negligent in trusting the debtor.
- c. Creditor #2 because the attempted first filing was ineffective.
- d. Creditor #2 because Creditor#1 was negligent, having had sufficient time to confirm its filing and failing to do so.

19. Your client sold a major home entertainment system to Debtor, on credit, obtaining a signed security agreement covering the system. As was its practice in consumer sales, client did not file a financing statement. Debtor became unemployed and defaulted. When asked for a surrender of the collateral, Debtor reluctantly said he had sold it to a neighbor. You are asked to file a replevin suit against the neighbor to recover the collateral.

- a. You may do so because PMSI's of consumer goods are automatically perfected.

- b. You may do so ONLY if you can prove the sale was a fraudulent transfer.
- c. Both the perfected PMSI and the fraudulent transfer theories can succeed.
- d. Neither the PMSI nor the fraudulent transfer theories can reach this property.

20. You represented one spouse in a recently completed divorce. The court awarded your client the couple's new Lincoln Navigator. It is presently titled in the other spouse's name, clear of any liens. Which of the following will fully protect your client's rights against a possible wrongful sale of the automobile to an innocent party?

- a. Record the court order in the Article 9 registry and take possession of the car.
- b. Send the court order to the Motor Vehicle Registry and get a new Certificate of Title in Client's name.
- c. Take possession of the car.
- d. Both b. and c. are necessary.

21. Which of the following facts will defeat the claims of a person otherwise qualified as the holder in due course of a negotiable instrument under UCC Article 3?

- a. The original obligor was a minor.
- b. A necessary endorser was a minor.
- c. BOTH facts will defeat a holder in due course.
- d. NEITHER fact will defeat a holder in due course.

22. In the absence of a special statute or government regulation, a common carrier's liability for conversion of goods may:

- a. Be unconditionally limited by the parties in the contract of carriage.
- b. Be limited by the parties in the contract of carriage if, and only if, the shipper is given the option of purchasing higher liability limits at the time of contracting.
- c. Be limited by the parties in the contract of carriage only to the extent of excluding liability for consequential damages.
- d. Not be limited.

(22 - 24) A local business has gone bankrupt. During its operations it generated a substantial stream of chattel paper from its customers (of the type which included promissory notes). A local bank held a security interest in the chattel paper, perfected by filing in the Article 9 registry. The customers have been paying, but the business failed for other reasons. In a desperate move just prior to collapsing, the business wrongfully sold the same chattel paper to a factoring company endorsing the notes and transferring possession of the actual files. To further complicate matters, one of the general partners of the factoring company picked this time to turn crook and endorsed the notes over to a holder in due course, absconding with the proceeds just before the original business went bankrupt.

22. Of the following people, who has the best claim to ownership of the notes?

- a. The bank.
- b. The factoring company.
- c. The holder in due course.
- d. The Trustee in Bankruptcy.

23. Who has the second best claim?

- a. The bank.
- b. The factoring company.
- c. The holder in due course.
- d. The Trustee in Bankruptcy.

24. On just these facts alone, the party with rights to the chattel paper has the following rights:

- a. Immediate, full payment of the balances of the customers' notes.
- b. Immediate possession of the customers' chattels.
- c. BOTH a. and b.
- d. NEITHER a. nor b.

25. You represent a major unsecured creditor of Peter Smith who does business as Pepperoni Pete's Pizza House (a sole proprietorship). Smith is insolvent. Yesterday he assigned all the equity in his non-exempt assets to a local accountant in trust for the benefit of his creditors. You've gotten a call telling you this and inviting negotiations for a work-out. Your client is furious and wants to seize assets. No bankruptcy has been filed. In this situation:

- a. The transfer is Fraudulent. You can set it aside and pursue any unencumbered assets.
- b. You and the other creditors can garnish the trustee in a collections priority-race.
- c. You can ignore the transfer because this is a voidable preference preempted by the federal Bankruptcy Code.
- d. The assignment is effective and you have to deal with it.

26. Which of the following liens capture after-acquired property?

- a. Attachment Lien
- b. Federal Tax Lien
- c. Judgment Lien
- d. Both b. and c.

27. 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 trade it for some unmounted jewels of equal value because they "would be easier to lose or mislay, if you know what I mean." Friend

agreed and then later gave the artwork to an innocent museum. Debtor loses the lawsuit and no non-exempt property is found. Under the Uniform Fraudulent Transfer Act:

- 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 and the museum are both liable for \$15,000 and in the alternative the museum is liable for return of the artwork
- d. No one is liable to the judgment creditor because the first transfer was for fair value.

28. You are a trustee in bankruptcy. The debtor had licensed a trademark to Licensee, whose entire business was built around the mark. The license is exclusive for the particular product line. There are other potential licensee's who are willing and able to pay a higher royalty. You want to reject the original license and make a more lucrative deal. You

- a. May reject the license agreement.
- b. May reject the license if and only if the Court finds that the resulting gain to the estate outweighs the harm to the original licensee.
- c. Must permit the original licensee to use the mark on a non-exclusive basis so long as it pays the agreed royalty.
- d. Must permit the original licensee to use the mark on an exclusive basis so long as it pays the agreed royalty.

29. Same facts as above, but the license is of a patented invention. As trustee you

- a. May reject the license agreement.
- b. May reject the license if and only if the Court finds that the resulting gain to the estate outweighs the harm to the original licensee.
- c. Must permit the original licensee to use the invention on a non-exclusive basis so long as it pays the agreed royalty.
- d. Must permit the original licensee to use the invention on an exclusive basis so long as it pays the agreed royalty.

30. In the sale of goods of a value of \$500 or more, unless otherwise agreed between the parties, title passes:

- a. At the moment of contract formation.
- b. At the time of signing a written memorandum or confirmation sufficient under the statute of frauds.
- c. At the time of identification of the goods to the contract.
- d. At the time the seller completes his/her agreed duties with respect to delivery.

Short Answers
(up to 15 minutes recommended)

1. You represent a judgment creditor. The debtor owns some certificated stocks which you have reason to believe are kept in her home, her office, or in her bank safety deposit box. Assuming the debtor is basically honest, what is the simplest way to secure the certificates?
2. Briefly explain the nature of a Bank's right of setoff and how it can affect the success of a garnishment.
3. The holder of a first mortgage has properly notified your client of a foreclosure sale. Your client holds a second mortgage on the property. There are no unpaid real estate taxes or other liens. Your client is convinced that the property is worth considerably more than the outstanding balance due on the first mortgage. Assuming this is true, briefly state what your client should do and why.

Essay
(up to 75 minutes suggested)

Tracy is sole proprietress of a stained-glass business. It is not separately incorporated, so her business debts are also personal. She had a substantial line of credit with her Bank, secured by a legally sufficient Article 9 security agreement covering all her present and after-acquired personal property. The loan was a demand loan. There was a financing statement in proper form filed in the proper office before any of the following transactions happened.

Tracy started from scratch. She had a nice computer which was originally acquired for personal use, on long term credit, from a local computer dealer who took an automatically perfected security interest. The terms were easy, so she didn't pay off the dealer when her business started making money. As her business grew out of the "hobby" stage, she established a relationship with a Supplier who extended her credit for materials and for tools and fabricating machinery, covered by a purchase money security interest and a financing statement filed in the usual way. Tracy took a five-year lease on a kiosk at the local Mall. She hired her sister-in-law Wilma as a sales representative, mostly on commission. Wilma was very good. Actually too good, because she brought in orders at such an accelerating rate that the business was put in a cash bind. Buyers made only small deposits when they ordered, and Tracy had to front for all the materials, labor, and part of Wilma's commission until final payment on delivery. Tracy increasingly drew on her Bank line of credit.

The crash came when the biggest customer, a new age church, went bankrupt due to embezzlement, rejected the contract on a nearly completed order, and had no money for

the unsecured creditors. (Tracy finished the church windows. They were probably worth quite a lot, but she sold them fast and cheap to a dealer in architectural artifacts.)

Wilma tried to help by deferring her commissions for a while. They struggled on but increasingly delayed payment of bills and came to realize the situation was probably hopeless. To do right by Wilma, Tracy assigned Wilma Tracy's paid-up whole life insurance policy. Its cash-surrender value was about half what Tracy owed Wilma. The insurance company was notified in proper form. Tracy also boxed up her computer and sent it to Antonia, a favorite niece unrelated to Wilma. Antonia lived in another state and was attending design school.

Tracy sweet-talked and stonewalled her creditors for 91 more days and then declared bankruptcy. There is some money in the bank account, all of it proceeds of inventory.

Assume that only the assets and entities named above are involved. Assume also that Tracy will not use her exemptions on any of these assets. What are the rights of the parties in relation to each asset, and what will be left for the trustee (unsecured creditors), if anything?

End of Examination