

SECURED TRANSACTIONS

Final Examination
Spring 2006

Mr. Czarnetzky

INSTRUCTIONS

1. Put your EXAM NUMBER at the top of this page. DO NOT put your name, ID number, or any other form of identification on your exam. Answer the questions only in the space allowed in the exam.
2. **Assume that judicial liens on personal property arise in ALL JURISDICTIONS mentioned in the exam once a judgment is enrolled in the local jurisdiction AND the local sheriff levies on the personal property. Moreover, the proper statewide filing office is the office of the Secretary of State.**
3. Make your answers complete, but succinct. You have limited space and time, so do not waste either. Please note that your submission of answers to this examination constitutes assent to the following pledge which you should read well and appreciate:

HONOR PLEDGE

BY THE ACT OF SUBMITTING MY EXAMINATION PAPER AND/OR BLUE BOOKS FOR EVALUATION, I DO PLEDGE ON MY HONOR THAT I HAVE NEITHER GIVEN NOR RECEIVED ANY IMPROPER ASSISTANCE AND THAT I WILL REPORT ANY IMPROPER ASSISTANCE GIVEN OR RECEIVED BY OTHERS OF WHICH I BECOME AWARE.

5. This is an **OPEN BOOK** exam. You may use any material that you bring with you to the examination. You **MAY NOT** collaborate with any individual or use any library resources OR ANY OTHER resource other than materials that you have brought to the examination. Any violation of these rules is a violation of the above Honor Pledge. I will respond to violations of the above Honor Pledge by failing the parties involved.
6. You have **3 hours** to complete this examination. Work efficiently. Good luck.

QUESTION I
(13 Points)

Casimir, a sole proprietor and mobile home dealer, sells mobile homes to customers in exchange for a small down payment and a "Contract for Sale" which provides that the customer will pay the remainder of the purchase price over 10 years, and that Casimir retains title to the mobile home until full payment is made. (Assume the Contracts for Sale are NOT instruments under the U.C.C.). The mobile homes are not attached to the ground at Casimir's sales lot, though customers of course do install them once Casimir delivers their mobile home to them. Casimir, out of an abundance of caution, properly recorded each "Contract for Sale" in the appropriate recording offices for both real estate and for personal property filings.

Casimir then approached Local Bank which lent Casimir money in exchange for Local Bank taking possession of all of the Contracts of Sale generated in Casimir's business.

Casimir has had extreme financial difficulties for the past two years, and therefore filed for relief under chapter 7 of the United States Bankruptcy Code. Both the Chapter 7 trustee in Casimir's bankruptcy and Local Bank claim that they have priority in the Contracts of Sale. You are the Bankruptcy Judge assigned to the case. What is each side's best argument(s)? Who will prevail and why?

QUESTION II
(15 Points)

Boleslaw, a sole proprietor, obtained a loan from Beacon Bank (“Beacon”) in order to purchase a stone smashing machine for his stone smashing business. Beacon loaned Boleslaw the money and took and properly perfected a security interest in the stone smasher by filing in the appropriate state office.

After another six months and several missed payments, Beacon sent Repo Ralph (“Ralph”) out to Boleslaw’s place of business to repossess the stone smasher. At that time, the total principal, interest and late fees that Boleslaw owed Beacon totaled \$300,000. Late at night, Ralph grabbed the stone smasher out of Boleslaw’s workshop in his backyard, which is a three-sided structure open on one side. Ralph took the stone smasher without any incident and turned it over to Beacon.

Beacon sent Boleslaw a notice two days later, on the 15th of the month, telling him that the car would be sold sometime after the first of the month. Boleslaw immediately went to Beacon with a suitcase full of cash and offered to “make good” on his debts by paying the past due payments, plus interest. Beacon refused his offer (the “First Offer”).

The next day, Boleslaw checked the “Stone Smasher Professional’s Magazine,” a trade publication, and saw similar used stone smashers selling for \$250,000. Upon seeing these prices, Boleslaw’s Uncle Stash offered to pay Beacon \$250,000 in cash the next day for the stone smasher (“the Second Offer”). Beacon’s Vice President for Debt Enforcement informed Boleslaw and Uncle Stash that Beacon follows a policy of selling stone smashers at the monthly stone smasher wholesale auction held 20 miles away in Bedford.

About 3 weeks later, Beacon sold the stone smasher for \$225,000 at the monthly wholesale stone smasher auction. Uncle Stash was not allowed to attend as the auction is open to stone smasher dealers only. Beacon has made a demand for the \$75,000 deficiency on Boleslaw.

- (A) Was Beacon within its rights to reject the First Offer and Second Offers? Explain.
- (B) If Boleslaw could have tendered the proper amount at the time of the Second Offer, would it have made good sense for him to have done so? Explain.
- (C) Please give all good-faith arguments on behalf of Boleslaw that might relieve him of liability for the \$75,000 deficiency. What recovery for the deficiency, if any, should Beacon receive?

QUESTION III
(18 Points)

Green, a law professor, purchased a large sailboat from Pulaski Marina, a boat dealer, for \$15,000 – \$2,000 down and \$13,000 financed by Green, who took a security interest in the boat. Pulaski Marina immediately assigned its interest in the boat and in the contract with Green to Myers, who promptly filed a financing statement in the proper state office. The financing statement listed Myers as the secured creditor, was signed by Green as the debtor, and contained all other necessary information.

A month later, Green returned the boat to Pulaski Marina with the understanding that Pulaski Marina would sell the sailboat and that the proceeds of the sale would be used to satisfy Myers's security interest. One month later, Pulaski Marina sold the boat to Hector without authorization from anyone, for \$8,000, of which \$4,000 was financed by Pulaski Marina which properly retained and perfected a security interest in the boat. Pulaski Marina was listed as the seller of the boat on the sales contract with Hector. Pulaski Marina then assigned all of its rights to Big Bank.

Needless to say, Pulaski Marina did not satisfy Green's debt to Myers. When Green learned about the sale to Hector, she stopped making payments on her loan. This led Myers to declare the loan in default, and to repossess the boat from Hector (in a fine bit of detective work). Then, as fate would have it, Pulaski Marina filed a petition for relief under chapter 7 of the Bankruptcy Code.

Who will end up with the boat and why?

QUESTION IV
(4 Points)

Special rules govern priority disputes when one of the secured creditors in a case has a purchase money security interest ("PMSI") in the collateral at issue. Please describe and assess the PMSI priority rules, being certain that you explain the purpose of these rules and whether you believe they are effective.

QUESTION V
(8 Points)

Myers wanted to start a photography business. He borrowed \$20,000 from Rychlak to purchase the necessary equipment and supplies, and he signed a security agreement granting Rychlak a security interest in all the "equipment, supplies, and photography materials of the photography business, including any property hereinafter acquired." Rychlak filed a properly completed and signed financing statement in the Office of the Secretary of State which contained the same collateral description. Myers operated the business for one year, and sold all of the assets for \$5,000 in cash to Cochran, a law professor, who had no knowledge of Rychlak's security interest. Cochran immediately traded the assets to Casimir in exchange for 50 cases of rare Polish vodka. Five months later, Rychlak learned of Myers's sale of assets to Cochran, but Myers claimed to only have \$1,000 of the original money left, which Myers keeps in his sock drawer in his bedroom. Assume that Myers has no other creditors. What are Rychlak's rights, if any, in the \$1,000 and the 50 cases of rare vodka?

QUESTION VI
(7 Points)

On September 15th, Czarnetzky & Son, Inc. ("Czarnetzky & Son") borrowed money from Equipment Finance Corp. ("Equipment") and granted Equipment a security interest in all equipment then owned and thereafter acquired. A proper security agreement was executed by the parties, and a proper financing statement filed in the appropriate office. On October 15th, after the retirement of Bill Czarnetzky, Sr., Czarnetzky & Son changed its name to Czarnetzky Equipment, Inc ("Czarnetzky Equipment"). On that same date, Czarnetzky Equipment borrowed money from Small Bank and granted Small Bank a security interest in all equipment then owned and thereafter acquired. On December 15th, and then three months later on March 15, Czarnetzky Equipment purchased some equipment. Who has priority in the equipment purchased on December 15th and March 15th, and why?

QUESTION VII
(11 Points)

On July 1st, Montbanc, Inc. signed a security agreement with Big Bank, granting Big Bank a security interest in all “furniture, fixtures, and equipment of Montbanc, Inc.” Montbanc, Inc. is in the business of selling fancy fountain pens from its retail location in Anytown, MS. On July 5th, Big Bank filed a financing statement in the proper office listing “Mountebank, Inc.” as the debtor. The filed financing statement also listed Big Bank’s address as “123 State Street, Anytown, MS,” even though Big Bank’s correct address is 321 State Street, Anytown, MS. The description of the collateral in the financing statement was “furniture, fixtures, equipment, and inventory of Mountbank, Inc.” On July 20th, Montbanc, Inc. filed a petition for relief under chapter 7 of the bankruptcy code. Assume the President of Montbanc, Inc. is willing to testify that the description of collateral in the financing statement is the one that represents the bargain between the parties. You represent the bankruptcy trustee. Make all appropriate arguments that your client is entitled to the fancy fountain pens remaining in Montbanc, Inc.’s store on July 20th. Who will prevail?

Question VIII
(10 Points)

You represent Local Bank which wishes to loan money to Quadrilateral Books ("Quadrilateral") in exchange for a security interest in the inventory and equipment of the book store. Your client tells you that the "big cheese" at Quadrilateral Books is Bill Whitman. In fact, Whitman is the only "cheese" at Quadrilateral – he is the only employee and the owner. Quadrilateral is located in Pulaski, Minnesota.

After you draw up the security agreement, you are ready to instruct your legal assistant regarding what and where he should search regarding Quadrilateral's inventory and equipment. At this point, you know nothing else about Quadrilateral or Bill Whitman other than these facts. What do you tell your assistant? If he needs to find out further information for you, please delineate what information is necessary and why.

QUESTION IX
(10 Points)

Classify in the space provided the following collateral in the hands of a debtor under article 9 of the UCC:

- A. A violin in the hands of a singing group called Kid Schlock Rock?

- B. A violin in the hands of the five-year old daughter of one of the members of Kid Schlock Rock?

- C. Cash in a strong box of a building contractor?

- D. An agreement in writing stored in the same strong box to pay the building contractor in 60 days after the contractor completes work on a project?

- E. An Persian-style rug in the building contractor's home that the building contractor accepted for work he completed on a project?

PRACTICAL REMINDER:

"Never trust humanity without collateral security." -- Ambrose Bierce

*****FINIS*****