

## **Secured Transactions**

### **Sample Exam**

#### **Professor Meadows**

#### **Question 1 (One Hour)**

Don Smith owns Smith's Shady Acres, a farm in Dauphin County, Pennsylvania. In February of 1994, Don granted a security interest in all his farming equipment, existing or after-acquired, to Perry County Bank to secure a \$125,000 loan. The Bank filed a financing statement with the Secretary of State on March 1, 1994. At that time, Don owned a John Deere Model 4430 tractor which he had been using for a number of years.

In September 1994, Don contacted Parker Tractors about the purchase of a new tractor. Don decided to trade his Model 4430 in for a John Deere Model 4450. The difference in price between the two models was \$28,000. Don could not afford the difference, so he contacted his father, Erwin, also a local farmer. On September 2, 1994, Don and Erwin agreed that Erwin would pay Parker Tractors directly for the balance of the tractor. The tractor would be delivered to Erwin initially, but when Don paid Erwin \$5,000 towards the purchase price, Erwin would release the tractor to Don. They further agreed that Erwin would be the owner of the tractor until Don had paid Erwin in full. On September 6, Don delivered his Model 4430 tractor to Parker and signed a sales agreement with Parker for the Model 4450. That same day, Don inspected the Model 4450 tractor that he was to receive and told Parker it was acceptable. On September 7, Erwin wrote a check to Parker Tractors to pay for the Model 4450 and took delivery of the tractor. On September 9, Don signed an agreement with Erwin, agreeing to pay the \$5,000 on September 20 and to pay the remaining \$23,000 in equal monthly installments over the next five years. The writing memorialized their agreement including the provision that Erwin would remain the owner of the tractor until the entire \$28,000 was repaid. Don made the required payment on September 20 and took possession of the tractor.

Everything went well until August 1995, when a severe drought damaged Don's crops. Because of the drought, Don was unable to make his September and October payments to either the Bank or his father. On October 15, 1995, the Bank declared Don in default and peacefully repossessed the tractor. On November 1, 1995, Erwin learned of the Bank's repossession and immediately notified the Bank, by fax, that he objected to the Bank's repossession and claimed ownership of the tractor. The next day, Erwin's attorney sent the Bank a letter claiming that not only was Erwin the owner of the tractor, but because of his agreement with Erwin, Don never had an interest in the Model 4450 tractor against which the Bank could claim a security interest.

**A.** The bank is uncertain as to what to do. It has retained you to give it an opinion as to the priority of the respective claims of the Bank and Erwin in the Model 4450 tractor. Write the opinion, fully explaining your reasoning.

**B.** At this time, Don owes the Bank over \$100,000, an amount greater than the value of the Model 4450. Therefore, the Bank also wishes to repossess the Model 4430 which is still in the possession of Parker Tractors. Can it? Explain your answer.

**Question 2 (30 minutes)**

7/1/95 - Meridian Bank takes a security interest in the existing and after-acquired consumer goods of Eleanor Walker and lends Walker \$5,000. Meridian properly files.

7/15/95 - Walker purchases a diamond ring from Cordelle Jewelers. Walker signs an agreement that provides that Cordelle Jewelers will retain title to the ring until Walker has paid the entire purchase price. Walker takes possession of the ring.

7/20/95 - Walker borrows \$10,000 from Tri-State Finance Company giving Tri-State a security interest in all of Walker's household and personal goods. Tri-State takes possession of the ring to have it appraised.

7/25/95 - Walker's landlord attaches a judicial lien to the ring.

8/1/95 - Tri-State properly files.

8/15/95 - Tri-State returns the ring to Walker.

9/1/95 - Walker stops paying everyone.

Each party is claiming an interest in the ring. What are the relative priorities of each party in the ring? Explain fully your answer.

### **Question 3 (30 minutes)**

Geiger Memorial Hospitals, Inc. is a corporation, which owns hospitals in Pennsylvania and New Jersey. Its headquarters are in Philadelphia, Pennsylvania. Geiger contracted with Burch Medical Supply of New York for the purchase of 40 hospital beds for use in Geiger's Philadelphia hospital. Burch agreed to finance the purchase. On June 1, 1995, Geiger signed a security agreement giving Burch a security interest in the beds. Burch agreed to ship the beds directly to Philadelphia no later than June 30, 1995. Burch identified the beds to the sales contract on June 10, 1995. At that time, the beds were in Burch's New York warehouse. On June 11, 1995, Burch filed a financing statement in New York. On June 27, Burch shipped the beds to Geiger. The beds arrived at Geiger's Philadelphia hospital on July 1. On August 1, 1995, Burch filed in the proper offices in Pennsylvania.

Late in August, Geiger began to experience severe financial problems and decided to downsize its Philadelphia operation. Therefore, on September 12, 1995, Geiger moved the 40 beds purchased from Burch to its hospital in Newark, New Jersey.

Geiger's attempt to restructure its operations was not successful. Geiger filed for bankruptcy on October 12, 1995. Burch has asserted its security interest in the beds against the trustee. Will Burch be successful? Explain your answer.

### **Question 4 (1 hour)**

Erase-A-Board is a retail distributor of state-of-the-art bulletin and blackboards with factories and distribution centers in 20 states and its main headquarters in Seattle, Washington. In Pennsylvania, it has a factory in Philadelphia and a regional distribution center in York. It has given a security interest in all its inventory in Pennsylvania to Commonwealth Financial Services. Commonwealth has filed a proper financing statement with the Pennsylvania Secretary of State.

On December 1, 1994, Erase-A-Board enters into a contract with South-Central Pennsylvania Art School (located in Harrisburg) for the acquisition of 20 portable blackboards of different types, for a total price of \$40,000. The agreement states that South-Central will lease the 20 boards from Erase-A-Board for a period of three years. South-Central will pay \$4,000 at the beginning of the lease and \$1,250 per month for the three years. The lease may not be terminated by either party during the course of the lease. If South-Central pays all lease payments when due, it may purchase the boards at the end of the lease for an additional payment of \$1,000. (Boards such as these have a useful life span of 15-20 years.) The papers are properly signed on December 1, 1994, and the boards delivered to South-Central on December 2, 1994. On December 2, South-Central pays the initial \$4,000.

On January 15, 1995, South-Central gives a perfected security interest in all its existing and after-acquired equipment to Mellon Bank. At that time, Mellon Bank lends \$50,000 to South-Central.

In February of 1995, Cliff's Manufacturing receives a judgment against Erase-A-Board and attaches a judicial lien in the amount of \$30,000 against all of Erase-A-Board's assets. In order to forestall collection on the lien, Erase-A-Board agrees to turn over the lease agreement it has with South-Central to Cliff's and permits Cliff's to collect the monthly payments directly from South-Central. Cliff's takes the lease, but retains the right to collect against other assets of Erase-A-Board if South-Central stops making timely payments. Cliff's notifies South-Central to make all future payments to it.

**A.** On March 25, 1995, Commonwealth learns that Erase-A-Board has turned over the lease to Cliff's. Commonwealth notifies South-Central that it claims the priority interest in its lease to Erase-A-Board, that Erase-A-Board's transfer of the lease to Cliff's constitutes a default in its agreement with Commonwealth and hereafter, all payments should be made to Commonwealth. South-Central has consulted you for advice as to whom it should make its next monthly payment, Cliff's or Commonwealth. (You may assume that the transfer of the lease from Erase-A-Board to Cliff's does constitute a default in the agreement between Erase-A-Board and Commonwealth, which gives Commonwealth the right to collect on the lease if it has priority.) Advise South-Central as to whom it should make its next payment. Justify your advice with a complete explanation and proper citations to Code sections.

**B.** All goes well for South-Central until August 9, 1996. Until this time it has made every payment required under the lease. Unfortunately, a downturn in applications to Art School has resulted in significant cash flow problems for South-Central. South-Central stops paying on the lease with Erase-A-Board and its debt with Mellon. South-Central does not really want the blackboards and wishes to return them to the party with priority in them. It asks for your advice as to whom South-Central should return the blackboards. Advise South-Central as to which party has priority in the blackboards. Justify your advice with a complete explanation and proper citations to Code sections.

**END OF EXAM**

