Final Secured Transactions Review Problems

1. On May 1, Warren started a business as a sole proprietor and leased a $5,000 computer system from Leasco. The written lease, which was the only document generated in the transaction, provided for monthly payments for five years, with the right to purchase the system at the end of the term for $1.00.

On June 1, Warren borrowed $10,000 from Bank, with the understanding that $3,000 of the loan proceeds were to be used to purchase telephone equipment and $7,000 were to be used for working capital. Warren signed a promissory note to Bank payable on December 1. To secure the note, Warren executed a security agreement giving Bank a security interest in all of his office equipment now owned or thereafter acquired. Bank promptly perfected its security interest by filing a financing statement on June 3.

On June 2, Warren purchased and installed the telephone equipment.

On November 30, Warren purchased business video equipment for $2,000 on credit from A-1 Video Co. ("A- 1") and signed a promissory note payable to A-1 in twelve monthly installments. Warren executed a security agreement giving A-1 a security interest in the video equipment to secure the installment payments and took possession of the equipment on November 30.

Warren was unable to pay the Bank note when it became due on December 1. On December 5, Warren persuaded Bank to extend the note's payment for thirty days. To induce the Bank to do so, Warren gave Bank a stock certificate he owned for 100 shares of Dotcom Computer as additional collateral. Bank took immediate possession of the certificate.

On December 12, Warren filed a petition in bankruptcy for liquidation under Chapter 7 of the Bankruptcy Code.

On December 13, having learned of Warren's bankruptcy filing, A-1 quickly filed a financing statement with the intent of perfecting its security interest in the video equipment.

Which party among Leasco, Bank, A-1, and the Bankruptcy Trustee has the superior interest in the

a. Computer system? Explain fully.

b. Telephone equipment? Explain fully.

c. Video equipment? Explain fully.

d. 100 shares of Dotcom stock? Explain fully.

2. On April 1, Debtor authenticates a security agreement granting to A security interest in all of Debtor's existing and after-acquired inventory. That same day A files a financing statement covering the inventory. On May 1, Debtor authenticates a Security Agreement granting B a security interest in all of Debtor's existing and future accounts. That same day B files a financing statement covering the accounts. On June 1, Debtor sells inventory to a customer on 30-day unsecured credit basis.

Which secured party, A or B, has a first priority security interest in the amount owed the Debtor by the purchaser of inventory?

3. XYZ Co. ("XYZ") is an Illinois corporation that does business only in Illinois. XYZ owns the following personal property: (i) a negotiable promissory note by John Maker payable to the order of XYZ in the principal amount of $50,000.00; (ii) the goodwill attributable to XYZ's business; (iii) the right to payment of monthly rentals under an oral lease of a backhoe by XYZ, as lessor, to John Maker, as lessee; (iv) a securities account with Merrill Lynch; and (v) a written lease by XYZ, as lessor, to John Maker, as lessee, of a tractor for a rental of $2000.00 per month. As security for a loan from Bank, XYZ offers to grant a security interest in all of its personal property.

For each type of personal property ((i) through (v) above), (a) identify the term used in the UCC for such property and (b) the steps necessary to perfect Bank's security interest in that type of property. Your responses need not address the elements necessary for attachment to occur.

4. Bob's Builders, Inc., ("BBI") is an Illinois corporation engaged in a small home construction business. In December 2001, BBI borrowed $500 from Travis and promised to repay it in six months. BBI gave Travis BBI's portable cement mixer to hold until the loan was repaid. Travis has possession of the cement mixer.

On January 5, 2002, BBI borrowed $5,000 from Bank to finance a new job BBI had undertaken. BBI signed a promissory note and security agreement giving Bank a security interest in "all of BBI's equipment now owned or hereafter acquired." At the time, BBI owned the cement mixer and sundry construction tools. On the same day, Bank properly perfected its security interest by filing a financing statement with the Illinois Secretary of State.

On March 5, 2002, BBI reorganized and changed its name to House Levelers, Inc. ("HLI"), an Illinois corporation. At the same time, it filled out the necessary paper work and changed the name on its checking account at Bank from BBI to HLI.

On April 5, 2002, HLI purchased some new drilling equipment on credit from Drillco. HLI gave Drillco a promissory note and a security agreement covering the drilling equipment. Drillco properly perfected its security agreement on April 6, 2002 by filing a financing statement with the Illinois Secretary of State.

On July 10, 2002, HLI purchased a used grinding machine on credit from Grindco. HLI gave Grindco a promissory note and a security agreement covering the grinding machine. However, Grindco failed to file a financing statement.

It is now July 15, 2002, and HLI cannot pay its bills.

As among Travis, Bank, Drillco, and Grindco, which creditor's security interest, if any, has priority in the following items:

(a) The portable cement mixer? Explain fully.

(b) The drilling equipment? Explain fully.

(c) The grinding equipment? Explain fully.

5. Manufacturer, under a credit sale arrangement, delivers computers to ABC Company. ABC Company intends to lease the computers to various customers. Manufacturer then discovers a filed financing statement in favor of Bank granted by ABC Company covering all present and future inventory of ABC Company. Manufacturer sends written notice of the transaction to Bank three days after Manufacturer's delivery of the computers to ABC Company. Manufacturer also files its own financing statement on that date.

Which creditor, Manufacturer or Bank, has priority and why?

6. As of February, Illinois Bank has a perfected security interest in a piece of equipment in Illinois owned by ABC Co. ("ABC"), an LLC organized under the Illinois Limited Liability Company law. On March 1st, ABC moved the equipment to Iowa. On April 1st, an Iowa judgment creditor of ABC caused the equipment to be seized. Illinois Bank did not file a financing statement in Iowa until June 1st.

Does Illinois Bank prime the judgment creditor?

7. Jane wanted to purchase a computer for home use and for her young children to use for school work and entertainment. On January 15, Jane went to Dealer, a retail store specializing in computers, and told a salesperson of her family's needs. She was shown a computer that she was told would suffice. She agreed to buy the computer and told Dealer that she would have to borrow the money to pay for it. Dealer agreed to finance the sale and gave Jane $3,000 in credit to buy the computer. Jane took delivery and signed a security agreement that described the computer and granted Dealer a security interest in it. Dealer did not file a financing statement.

Immediately after purchasing the computer from Dealer, Jane changed her mind about how she would use it. Jane had just begun work as an independent consultant, so she took the computer to her office and began using it for business purposes. She did not inform Dealer of this change of use.

On May 1, Jane borrowed $25,000 from Bank as operating capital for her business. She executed a security agreement granting Bank a security interest in her office machinery, including the computer. Also on May 1, Bank filed a valid financing statement in all proper public offices.

Jane defaulted on the loans to both Dealer and Bank. On December 1, Dealer peacefully repossessed the computer. Both Dealer and Bank claim a security interest in the computer.

As between Dealer and Bank, whose security interest takes priority?

8. Al lives in and sells stereo equipment from his store in Chicago. Al borrows $100,000 from Betty for renovation and expansion of the store. As collateral for the loan, Al agrees to give Betty a "blanket lien" on all stereo equipment in his store. The "blanket lien" is evidenced by a two page Security Agreement which includes the following, provision: "Al grants to Betty a security interest on all stereo components and related merchandise now or hereafter acquired, and all proceeds thereof, as security for a $100,000 loan made by Betty to Al." For some unknown reason, Al signed his name at the bottom of page 1 of the Security Agreement, but neglected to sign his name on page 2 of the Security Agreement. Al also signed a Financing Statement in favor of Betty. The Financing Statement described the collateral as: "all stereo components and related merchandise now or hereafter acquired and all accounts, and all proceeds therefrom." The Financing Statement was then filed by Betty on August 15, 2001 with the Illinois Secretary of State's office.

Four months later, Al arranges a purchase of stereo merchandise from Stereo Factory ("Factory"). Prior to Al's purchase, Factory sends a written notice to Betty dated December 30, 2001 informing her that Factory plans to sell Al $75,000 worth of stereo merchandise on credit, and that Al will grant a security interest in the merchandise to Factory as collateral for the credit sale. After Betty's receipt of the notice, Factory files with the Illinois Secretary of State's office on January 10, 2002 a Financing Statement covering inventory and the proceeds therefrom. Al also signs on January 10, 2002 a Security Agreement in favor of Factory, affecting all inventory and proceeds, as security for payment of the $75,000 purchase price and an unrelated loan by Factory to Al.

On January 15, 2002 Factory delivered the stereo merchandise to Al. Al immediately sent one-half of the delivered merchandise to a customer. On January 25, 2002 Al received a check for $50,000 from the customer and deposited the check in the bank account which Al maintained for his store.

Betty's loan to Al is now in default. Betty comes to your office with a copy of Factory's written notice to her, and explains the foregoing scenario. Betty also tells you that the only stereo merchandise remaining in Al's store is the remainder of the merchandise delivered to Al by Factory. In addition, numerous customers owe Al for repairs made by him on stereos. **Advise Betty, giving full reasons for your answers, on the following:**

A. Is Betty's Security Agreement enforceable against Al?

B. Does Betty have a valid and enforceable security interest in accounts?

C. As between Betty and Factory, which party has the priority security interest affecting Al's remaining inventory of stereo merchandise?

D. As between Betty and Factory, which party has the priority security interest affecting the $50,000 customer payment in Al's bank account?