

320 Part 2: Elements of Traditional Business Law

- Security obtained by a creditor through the operation of law is called a *lien*. The procedures for using liens are determined by state law. The most common liens are the mechanic's lien (applicable to real property), the possessory lien (applicable to personal property), and court-decreed liens. In each case, the lender may obtain the lien without the borrower's consent by following statutory procedures.
- The bankruptcy code governs bankruptcy procedure. There are several approaches to bankruptcy, including Chapter 7 (providing for liquidation and fair distribution of the debtor's assets for creditors), Chapter 11 (allowing businesses to reorganize rather than being liquidated), and Chapter 13 (personal bankruptcy for individuals that reorganizes debts, but does not discharge them).
- The trustee (or debtor in possession) is the person in charge of the bankruptcy. It is the trustee's objective, under bankruptcy court supervision, to maximize the amount of the debtor's assets available for distribution to the creditors.
- Bankruptcy law states that certain creditors take priority over other creditors in receiving shares of the debtor's assets. Secured creditors take priority over unsecured creditors.

TERMS TO KNOW

You should be able to define the following terms:

negotiable instrument	debtor	floating lien
negotiation	principal	default
bearer	consumer reports	nonexempt property
bearer instrument	credit rating	homestead law
order paper	credit report	mortgage
bearer paper	open account	mortgagor
holder in due course	unsecured creditor	mortgagee
drawer	secured creditor	deficiency judgment
drawee	collateral	non-recourse debt
payee	guaranty	lien
check	suretyship	garnishment
cashier's check	surety	mechanic's lien
note	guarantor	possessory lien
maker	exoneration	attachment lien
promissory note	subrogated	judgment lien
draft	secured transaction	writ
bill of exchange	perfection of security interest	bankruptcy
sight draft	attachment	voluntary bankruptcy
confirmation	perfection	involuntary bankruptcy
certificate of deposit	tangible property	discharge
creditor	purchase money security interest	debtor in possession

DISCUSSION QUESTION

What are the basic differences between Chapters 7, 11, and 13 bankruptcy?

CASE QUESTIONS

1. Chung was at a racetrack operated by the New York State Racing Association. He bought a gambling voucher for use in SAMS, which are machines that take payments for gambling. The money credited to a voucher in a machine can be bet at once or can be used over time to make bets on SAMS. Chung forgot

- his voucher in a SAMS machine; it had several thousands of dollars of credit on it. Someone found it and traded it in for cash. The betting system does not link a person to a voucher, so the thief was unknown. Chung sued, contending that the racetrack should be liable for failing to check the identity and ownership of vouchers prior to their use. Is the racetrack liable or is Chung out of luck? [*Chung v. New York State Racing Assn.*, 42 UCC Rep.Serv.2d 867, Dist. Ct., N.Y.C., NY (2000)]
2. LaCombe practiced optometry as a sole proprietorship, LaCombe Eye Center. Slyfield worked for him at the front desk, but was not involved in bookkeeping. Over a four-year period, Slyfield embezzled checks made out to LaCombe by his patients, forged his signature, wrote her account number on it, and put the checks in her account at Bank One. LaCombe did not have an account at that bank. This scam worked for more than 500 checks totaling \$70,000 until discovered. LaCombe sued Bank One for negligence for accepting the forged checks for deposit and negotiation. The district court held for LaCombe. The bank appealed. Was it liable? [*LaCombe v. Bank One Corp.*, 953 So.2d 161, Ct. App., La. (2007)]
 3. McDowell owned and operated Big River Harley Davidson in Wapello, Iowa. As required by law, McDowell took out a motor vehicle dealer's surety bond for \$35,000 with United Fire and Casualty Insurance. The bond protects retail customers who get stuck when a motor vehicle dealer, perhaps because of fraud, does not deliver a vehicle that has been paid for. The surety bond was in force when Big River went out of business and McDowell left the state. While in business, Big River sold a Harley to Elworth Harley Davidson in Norfolk, Nebraska. Elworth paid \$12,000 for the Harley that was never delivered. Elworth sued United Fire as surety for the \$12,000. Can Elworth recover? [*United Fire and Casualty v. Acker*, 541 N.W.2d 517, Sup. Ct., Iowa (1995)]
 4. Bussewitz borrowed money from Citibank and signed a promissory note. Pitassi also signed the promissory note as co-maker of the note. When Bussewitz failed to make payments and defaulted on the note, Citibank, under the terms of the note, declared the entire unpaid balance due and sued both makers. Pitassi defended that he should not be liable because he signed the note only as a favor to Bussewitz and, furthermore, the note did not state when the first installment payment was due; that term had been left blank. Is Pitassi liable? [*Citibank v. Pitassi*, 432 N.Y.S.2d 389, Sup. Ct., App. Div., NY (1980)]
 5. Moody and three others bought a business and executed promissory notes for \$8.17 million. Moody owned 20 percent of the business; the other three owned the other 80 percent of the business. Moody was unable to make several payments on schedule. The other owners covered the payments he was supposed to make so the notes would not go into default. Moody was sued by the others for his contribution. He asserted that he was the same as a surety. Because they made the payments that were due for the business, he was no longer obligated on those payments. Is that correct? [*Krumme v. Moody*, 910 P.2d 993, Sup. Ct., Ok. (1996)]
 6. Mollinedo's home was damaged by fire. Her insurance company, Sentry, recommended ServiceMaster as a repair company. An adjuster for Sentry visited the home with the home contractor from ServiceMaster and approved \$30,000 worth of work, which ServiceMaster did with Mollinedo's approval. Sentry gave the \$30,000 to Mollinedo's mortgage company. Mollinedo filed for bankruptcy. ServiceMaster, which got nothing, sued Sentry for breach of contract and unjust enrichment. Did ServiceMaster, which never filed a lien, have a claim? [*Service-Master of St. Cloud v. GAB Business Services*, 544 N.W.2d 302, Sup. Ct., Minn. (1996)]
 7. The Boggess were declared bankrupt under Chapter 13. Shortly after their discharge, Somerville Bank and Trust contended that the Boggess did not pay off the interest on a loan secured by a mortgage on their principal residence. The bank had not raised the issue until after the bankruptcy court had issued its discharge order covering the indebtedness. The bank attempted to collect the debt as though there had been no discharge. Is the bank entitled to collect the interest? [*Boggs v. Somerville Bank and Trust*, 51 F.3d 271, 6th Cir. (1995)]
 8. Globe Building went into Chapter 7 bankruptcy, so a trustee was appointed to control the bankrupt estate. As a number of Globe employees had not been paid when the company went under, the state of Wisconsin, where Globe was located, filed a lien for wages against all property owned by Globe. Could the lien