Question 3 – February 2014 – Selected Answer 1

1. First Bank has the superior interest in the 9 notebook computers still in Electronics' inventory. First Bank and Bell both have security interests in the 9 notebook computers. The issues here are who prevails in priority as between two competing perfected security interest holders and when a party is entitled to superpriority status in inventory. First Bank obtained a security interest in Electronics current and after-acquired inventory. Inventory are goods that are sold, consumed or otherwise used up by a business. A security interest in inventory can be perfected through the filing of a financing statement which First Bank filed on July 3, 2013. The 9 computers would be considered after-acquired inventory and First Bank would have a perfected security interest in that property. The time of perfection in the after- acquired property would relate back to the date of the financing statement filing. On the other hand, Bell obtained a perfected security interest in the computers on February 8, 2014 when it sold the books to Electronics' on credits, filed a financing statement and delivered the computers to Electronics. The general rule as to priority between two perfected security interest in the same collateral is that the first to file or perfect prevails. However, there is another wrinkle here because of the nature of the security interest that Bell has in the 9 computers.

2. A purchase money security interest ("PMSI") arises when a party sells goods to another on credit and takes a security interest in those goods as collateral for the debt. A PMSI-holder is entitled to superpriority against even prior perfected security interests in the same collateral. Because Bell sold the computers to Electronics' on credit and took a security interest in that inventory PMSI status is available to it in that inventory. However, to be entitled to PMSI superpriority over a previously perfected security interest in inventory, a party seeking PMSI status must first give notice to other parties with a security interest in that collateral before delivering the goods. Here, Bell is not entitled to superpriority because it failed to give notice to First Bank, a perfected security interest holder in the after acquired inventory of Electronics', before delivering the goods. Consequently, despite still have a PMSI in the inventory, Bell would not have superpriority over First Bank's interest because of its failure to give proper notice. The general rule as to priority between two competing perfected security interests would apply, and First Bank prevails because it was the first-in-time to become perfected in the collateral.

3. Patrick has the superior interest in the notebook computer because he is a buyer in the ordinary course of business. At issue are the rights of a buyer in the ordinary course of business. A buyer in the ordinary course of business is one who: 1) buys goods from a person in the business of selling those goods; 2) in good faith; and 3) without notice of any violations of a security agreement. A buyer of goods in the ordinary course takes free of any security interest in those goods. Here, Patrick has purchased the notebook computer from Electronics, which is a retail store in the business of selling computers and computer-related equipment. The facts do not indicate that he took in bad faith or was aware that the sale of those goods would violate the terms of any security agreement concerning those goods. Therefore, Patrick is entitled to status as a buyer in the ordinary course, and has a superior interest in the notebook computer. First Bank would have priority in the $1,000 check Patrick used to pay for the computer. A party with a perfected security interest in collateral is entitled to automatic perfection for 20 days in the proceeds of the sold collateral. First Bank and Bell had security interests in the computer that Patrick purchased. As explained above, First Bank maintained priority in the inventory because of Bell's failure to give notice of its PMSI in the goods. Thus, when any of those goods were sold, First Bank has automatic perfection in the proceeds of the sale for 20 days and has a superior interest given its priority in the collateral.

Question 3 – February 2014 – Selected Answer 2

1. First Bank has priority of the nine computers left in the inventory. The issue is whether First Bank's security interest takes priority over Bell's purchase money security interest (PMSI). The collateral in question is the computers that were acquired from Bell Computers. Since Electronics, Inc. is in the business of selling computers, the 10 purchased computers are considered inventory to their store. First Bank loaned $50,000 to Electronics and received a promissory note along with a security agreement covering current and after acquired inventory. This is a proper description of the collateral as it describes inventory in general and it also works to allow First Bank an interest in after acquired inventory since it is named in the security agreement

(although inventory presumes after acquired status, thus they didn't need to put it in the security agreement, but doing so creates an even easier argument for First Bank). First Bank properly perfected this interest by filing a financing statement with the Secretary of State on July 3, 2013. We can assume that this financing statement is properly formatted as the facts do not indicate otherwise.

Bell obtained its security interest in the computers by taking a security interest in the 10 computers. A PMSI is when a creditor takes a security interest in the collateral as a way to secure the debt. Typically, a creditor that takes a PMSI in goods will prevail over other secured creditors if they perfect within 20 days of giving the debtor the collateral. Here, Bell perfected its interest on February 8, 2014 which is within the 20 day timeframe of when Electronics received the computers, thus creating the super-priority of the PMSI over any other secured creditors (regardless of the timing of their filing or perfection). However, where inventory is concerned, in order for a PMSI to take priority over other perfected interests, Bell must notify the other perfected parties of their intent to take a PMSI in the inventory prior to delivering the collateral to the debtor. Here, that was not done as we are not told that Bell notified First Bank of their intent to take a PMSI in the computers. Thus, First Bank has priority over the computers since they were the first to file or perfect in a battle between two secured creditors.

2. Patrick has priority in the computer that he bought. The issue is who has priority between a buyer in the ordinary course of business (BIOCOB) and perfected secured creditors. A BIOCOB takes free and clear of any secured creditors interests if he meets the following test: the creditor is not perfected by possession, the purchase was made in the ordinary course of business, bought in good faith, no notice of a security interest violation, the seller created the security interest, and the collateral is not farm products. Here, the computers are not in the possession of either of the secured creditors. Patrick bought the items in the ordinary course of business since Electronics is in the business of selling computers. There are no facts establishing that Patrick bought the items in bad faith. He had no notice of any type of security interest violation. Electronics did create the security interests from both First Bank and Bell and we are certainly not dealing with farm products. Thus, Patrick, as a BIOCOB will take the computer free and clear of any security interest.

3. First Bank will have priority in the check. The issue is who has priority in the proceeds of the sale of inventory. Here, Electronics sold an item of inventory to Patrick and received a check for payment. Since First Bank has priority in the inventory, they will also receive priority in the proceeds (proceeds is defined as whatever is acquired in the sale or disposition of the collateral). The fact that Electronics has not cashed the check does not matter as checks are instruments of payment that can be considered as proceeds. If Electronics does cash the check, as long as the money is identifiable First Bank will continue to have priority. Proceeds can be perfected in the same manner as other items of collateral and will have the super-priority if perfected within 20 days of the collateral becoming proceeds. Here, since the item is currently an instrument, First Bank needs to perfect within 20 days of February 28, 2014.

Question 3 – February 2014 – Selected Answer 3

1. First Bank has the superior interest in the nine notebook computers still in Electronics' inventory. The issue is who has the superior interest in inventory, when there is a perfected creditor who filed first in after-acquired inventory and a perfected creditor with a PMSI in inventory who filed before the debtor took possession of the collateral but did not give notice to other creditors. Under the U.C.C., when two perfected creditors have an interest in the same collateral, the first to perfect or file a financing statement has the superior interest. However, a creditor who has a Purchase Money Security Interest (PMSI) in the collateral has a superior interest to a non-PMSI creditor. To have a PMSI, the creditor must loan the debtor money, and the debtor must give a security interest to the creditor in the exact collateral that was purchased from that loan money. For a creditor with a PMSI in inventory, the creditor must file the financing statement before the debtor takes possession of the collateral, or within 20 days of the debtor taking possession. The creditor must also file notice to any creditor's with a competing interest in the collateral, describing the collateral. Inventory is collateral that is used for sale by a business.

Here, First Bank acquired a security interest in Electronics' current and after-acquired inventory. The collateral is inventory because they are computers, which Electronics sells. First Bank filed a financing statement on July 3, 2013, and Electronics borrowed the $50,000 on July 2, 2013. First Bank is a perfected, secured creditor. Bell

Computers acquired a PMSI when it signed a security agreement with Electronics for the ten computers that Bell gave to Electronics on credit. Bell filed a financing statement on Feb. 8, 2014, the day before Electronics took possession of the computers. However, Bell did not give notice with First Bank that it had a PMSI in the ten computers. While Bell filed on time to get a superior interest in the inventory its, failure to give notice causes Bell to not have a superior interest in the ten computers. Bell is a perfected, secured creditor with a PMSI in the computers, but it does not have a superior interest to First Bank. Therefore, First Bank has the superior interest in the nine notebook computers still in Electronics' inventory.

2. Patrick has the superior interest in the notebook computer sold to him because he is a buyer in the ordinary course of business. The issue is who has the superior interest in sold inventory, when a creditor is perfected and secured in inventory, but a buyer purchases the inventory within the ordinary course of business.

Under the U.C.C., a buyer in the ordinary course of business has a superior interest over a perfected and secured creditor. To be a buyer in the ordinary course of business, the buyer must give value, have no notice of a security agreement, the creditor must not have possession of the collateral, the item must be an item that the seller sells in its ordinary course of business, and the buyer must purchase it in the ordinary course of business. Here, Equipment is in the business of selling computers and computer-related equipment. Therefore, selling computers is in its ordinary course of business. Patrick also bought the computer in a transaction that is in the ordinary course of business as a consumer. First Bank did not have possession of the computer. The facts do not indicate that Patrick had knowledge of the security agreement with either First Bank or Bell. Patrick also gave a check for $1,000 to Equipment for the computer. So, Patrick meets all the elements of being a buyer in the ordinary course of business, and he has a superior interest in the computer sold to Patrick. Therefore, Patrick has the superior interest in the notebook computer sold to Patrick because Patrick is a buyer in the ordinary course of business.

3. First Bank has the superior interest in the $1,000 check, because it has temporary perfection over the proceeds of the inventory. The issue is who has the superior interest in proceeds from the sale of inventory when it is within 20 days of the payment. A perfected, secured creditor has temporary perfection from the proceeds of the sale of any collateral it has a perfected security interest in for 20 days. It must file a financing statement over the proceeds within the 20 days, or it loses its perfection. Here, as stated above, First Bank has the superior interest in the notebook computers that Electronics has in its inventory. Because one of them was sold, First Bank has temporary perfection in the proceeds for a period of 20 days. First Bank must file a financing statement within the 20 days, or it will lose its perfection. Then Patrick would have the superior interest in the check. Because Feb. 18, 2014 was not more than 20 days ago, First Bank would still have temporary perfection at this time. Therefore, First Bank has the superior interest in the $1,000 check because it has temporary perfection over the proceeds of the sold computer.