



California  
Bar  
Examination

Essay Questions  
and  
Selected Answers

February 2005

# California Bar Examination

Answer all three questions.  
Time allotted: three hours

Your answer should demonstrate your ability to analyze the facts in question, to tell the difference between material and immaterial facts, and to discern the points of law and fact upon which the case turns. Your answer should show that you know and understand the pertinent principles and theories of law, their qualifications and limitations, and their relationships to each other.

Your answer should evidence your ability to apply law to the given facts and to reason in a logical, lawyer-like manner from the premises you adopt to a sound conclusion. Do not merely show that you remember legal

principles. Instead, try to demonstrate your proficiency in using and applying them.

If your answer contains only a statement of your conclusions, you will receive little credit. State fully the reasons that support your conclusions, and discuss all points thoroughly.

Your answer should be complete, but you should not volunteer information or discuss legal doctrines which are not pertinent to the solution of the problem.

Unless a question expressly asks you to use California law, you should answer according to legal theories and principles of general application.

**ESSAY QUESTIONS AND SELECTED ANSWERS**  
**FEBRUARY 2005 CALIFORNIA BAR EXAMINATION**

This publication contains the six essay questions from the February 2005 California Bar Examination and two selected answers to each question.

The answers received good grades and were written by applicants who passed the examination. The answers were prepared by their authors, and were transcribed as submitted, except that minor corrections in spelling and punctuation were made for ease in reading. The answers are reproduced here with the consent of their authors and may not be reprinted.

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## Question 1

A State X statute prohibits the retail sale of any gasoline that does not include at least 10 percent ethanol, an alcohol produced from grain, which, when mixed with gasoline, produces a substance known as “gasohol.” The statute is based on the following legislative findings: (1) the use of gasohol will conserve domestic supplies of petroleum; (2) gasohol burns more cleanly than pure gasoline, thereby reducing atmospheric pollution; and (3) the use of gasohol will expand the market for grains from which ethanol is produced.

State X is the nation’s largest producer of grain used for making ethanol. There are no oil wells or refineries in the state.

Oilco is an international petroleum company doing business in State X as a major retailer of gasoline. Oilco does not dispute the legislative findings underlying the statute or the facts concerning State X’s grain production and lack of oil wells and refineries. Oilco, however, has produced reliable evidence showing that, since the statute was enacted, its sales and profits in State X have decreased substantially because of its limited capacity to produce gasohol.

Can Oilco successfully assert that the statute violates any of the following provisions of the United States Constitution: (1) the Commerce Clause, (2) the Equal Protection Clause, (3) the Due Process Clause, and (4) the Privileges and Immunities Clause? Discuss.

## Answer A to Question 1

1)

Oilco is asserting that the State X statute violates the 1) Commerce Clause, 2) the Equal Protection Clause, 3) the Due Process Clause, and 4) the Privileges and Immunities Clause of Article IV.

### Justiciability

#### Standing

In order to successfully bring an action, Oilco must demonstrate that they have standing. A party has standing where there is injury, the injury is caused by the defendant, and the court can provide relief. Here, Oilco will be injured by the legislation because they do business in State X and do not currently meet the State's gasoline regulations. Oilco could lose profits from loss of business. The loss of profits is directly caused by the statute's ban on non-ethanol based gasoline. The court can provide relief for Oilco by invalidating the statute. Thus, Oilco has standing.

#### Eleventh Amendment

The Eleventh Amendment prohibits a party from suing a state without the state's permission. It appears from the facts that Oilco is suing State X and thus would be barred by the Eleventh Amendment. If Oilco sues the appropriate official, the suit will not be barred by the Eleventh Amendment.

#### Ripeness

The courts will not hear a case unless there is some threat of immediate injury caused by the defendant. Here, the statute could result in a significant loss of profits for Oilco, so the State's argument for dismissal based on ripeness will fail.

#### Commerce Clause

The Commerce Clause grants the federal government power to regulate the channels and instrumentalities of commerce, and other activities that affect interstate commerce. If a valid federal law under the commerce clause conflicts with state law, the federal law invalidates the state law because of the Supremacy Clause. Even if the federal law and state law do not conflict, the federal law may preempt the state law by occupying the field. Where Congress is silent on a matter, a state has the power to regulate the local aspects of commerce as long as the regulation is not discriminatory and does not unduly burden interstate commerce.

Here, there are no facts suggesting that there is a federal law that either conflicts with the State X statute or preempts the field. Thus, State X's statute will be valid as long as it does not discriminate against out-of-state interests and does not unduly burden interstate commerce.

### Discrimination against out[-]of[-]state interests

The Dormant Commerce Clause prohibits a state from discriminating against out-of-state interests. Discrimination can appear on the face of a regulation, or it can be discriminatory in its impact on interstate commerce. Here, the statute prohibits the retail sale of any gasoline that does not include at least 10 percent ethanol, an alcohol produced from grain, which, when mixed with gasoline, produces a substance known as gasohol. State X will argue that [t]he statute on its face does not discriminate against any out[-]of[-]state interests, as any other state meeting these requirements would not be prohibited from selling gasoline inside State X.

However, Oilco's strongest argument will be that the Statute has a discriminatory impact. Here, Oilco will argue that State X is the nation's largest producer of grain used for making ethanol. Oilco will also point out that State X has no oil wells or refineries inside State X. Putting these two facts together, Oilco will argue that by passing the statute, State X is promoting its own interests by encouraging the consumption of ethanol while harming out-of-state oil refineries and wells. Since State X has no oil refineries or wells, they will not be harmed by the statute at all. This, Oilco will argue, is discrimination against out-of-state interests and[,] thus, is violative of the Dormant Commerce Clause. Oilco will also point to the legislative finding that State X's statute will "expand the market for grains from which ethanol is produced", strengthening its argument that this regulation is merely economic protectionism, and violative of the Dormant Commerce Clause.

State X will counter by arguing the important interest exception: a state may discriminate against out[-]of[-]state interests where there is an important state interest in the regulation and there are no non-discriminatory options. State X will point to the legislative findings regarding the conservation of petroleum, and the reduction in pollution. These, State X will argue, are important state interests. State X will also argue that achieving these goals cannot be achieved by non-discriminatory means. State X will argue that in order to conserve petroleum and reduce pollution, State X must ban the sale of non-ethanol based gasoline inside the state.

Oilco will argue that there are available non-discriminatory means of meeting the state interests. Oilco can argue that a phaseout of non-ethanol based gasoline is a less discriminatory means of achieving their goals, and would provide time for out-of-state sellers of non-ethanol based gasoline to meet State X's stringent requirements.

State X may attempt to argue the market participant exception which allows a state to discriminate against out-of-state interests where it is a market participant. However, the

facts do not indicate that the regulation only applies when State X is purchasing gasoline. The effect of the regulation is to prohibit sale of all non-ethanol based gasoline to residents, and the State. Thus, the state will not successfully argue the market participant exception.

Because the statute discriminates against out[-]of[-]state interests, the court should find that the statute violates the Dormant Commerce Clause.

#### Undue burden on interstate commerce

Even if the court finds that the statute does not discriminate against out[-]of[-]state interests, the statute will be invalidated if it unduly burdens interstate commerce. Here, Oilco will argue that it is a major retailer of gasoline inside State X. The effect of the statute is to prohibit all sales of non-ethanol based gasoline inside the state. Oilco will introduce their evidence showing the reduction in sales and profits, and will argue that if every state enacted similar statutes, the effect would greatly burden interstate commerce.

State X will argue that the statute does not significantly burden interstate commerce, as Oilco is still free to sell their gasoline in other states or comply with State X's regulations. However, since the impact of the statute will burden interstate commerce, a court would likely find that the statute is violative of the Dormant Commerce Clause.

#### Equal Protection Clause

In order to assert an equal protection claim, Oilco will need to show some state action. State action exists where the act is an exclusive public function or there is significant state involvement. Here, the State X legislature passed a law. Thus, Oilco will easily be able to show state action.

The Equal Protection Clause of the 14<sup>th</sup> Amendment provides that the state must provide all citizens and organizations in their jurisdiction the equal protection of the laws. Where the regulation does not affect a suspect or quasi-suspect class, and where the regulation does not affect a fundamental right, the regulation must pass the rational basis test – that is, the regulation must be rationally related to a legitimate government interest.

Here, Oilco is an international corporation. The statute does not involve a suspect class – race or alienage – and it does not affect a quasi-suspect class – gender or legitimacy. The statute also does not affect a fundamental right such as 1<sup>st</sup> Amendment protections or the right to privacy. Thus, the rational basis test will be used in scrutinizing the statute. Under the rational basis test, a regulation will generally be upheld as long as it is not arbitrary.

State X will argue that there is a legitimate government interest involved – the conservation of domestic supplies of petroleum, and the reduction in atmospheric pollution. State X will

also argue that the prohibition of non-ethanol based gasoline is rationally related to the government interest, since the prohibition will reduce the amount of petroleum used in producing gasoline, and will also reduce the pollution because ethanol is cleaner than pure gasoline. Thus, the statute will pass rational basis, and the court will find no equal protection violation.

## Due Process Clause

### Substantive Due Process Clause

In order to assert a substantive Due Process violation, Oilco will need to show state action. As explained above, Oilco will easily show state action because State X passed a statute.

The [S]ubstantive Due Process Clause prohibits states from infringing on a fundamental right. If the state infringes on a fundamental right, the action must pass strict scrutiny. Under strict scrutiny, the regulation must be necessary to achieve a compelling government interest. Where no fundamental right is involved, the regulation must pass rational basis – that is, the regulation must be rationally related to a legitimate government interest.

Here, the right to sell gasoline is not a fundamental right. Thus, the statute must pass the rational basis test. As explained above, State X will successfully argue that there is a legitimate interest in conserving petroleum and reducing pollution, and that the regulation passed is rationally related to achieve those goals. Thus, Oilco's claim under the Due Process Clause will also fail.

### Procedural Due Process

In order to assert a substantive Due Process violation, Oilco will need to show state action. As explained above, Oilco will easily show state action because State X passed a statute.

The procedural Due Process prohibits the taking of life, liberty or property without due process of law. Oilco may assert that the statute takes away their right to sell gasoline inside the state without an appropriate hearing. However, the Court will not find a procedural due process violation because the statute was validly passed by the state legislature.

### Privileges and Immunities Clause of Article IV

The Privileges and Immunities Clause of Article IV prohibits states from discriminating against non-residents. The Clause does not protect against aliens or corporations. Here, Oilco is a corporation, and is not afforded protection under the Clause. Thus, any claim under the Privileges and Immunities Clause of Article IV will fail.

## Answer B to Question 1

1)

### Standing and ability to bring suit

The first issue is whether Oilco (“O”) can bring a suit against State X asserting that the statute violates the US Constitution. To bring a lawsuit, O must meet the following requirements: (1) standing, (2) ripeness, and (3) mootness. O has standing because it has suffered present injury that can be redressed by a favorable court decision. In addition, the lawsuit is ripe because O has suffered injury and thus the court would not be rendering an advisory opinion. And finally, the lawsuit is not moot because O is suffering from a live controversy.

### Protection of US citizens only?

While the facts do not clearly indicate whether O is a foreign corporation, assuming that it is a foreign corporation, State X may argue that because O is an international corporation, it cannot invoke the protections of the US Constitution since it is not a citizen of this country. But since O does business in State X, it should be allowed to challenge the constitutionality of the statute. The fact that O may not be a US corporation may preclude it from raising certain arguments, but it will not prevent it from bringing a lawsuit.

The following analysis in turn addresses each of the potential arguments.

### **1. The Commerce Clause**

The issue is whether O can assert that State X’s statute violates the Commerce Clause. The Commerce Clause provides Congress the power to regulate interstate commerce. The Dormant Commerce Clause or the negative implications of the Commerce Clause provides that even if Congress has not acted in a certain area, states may not be able to regulate those activities if they place an undue burden on interstate commerce. Under the Dormant Commerce Clause, O can make two separate arguments: (1) that the statute discriminates against out[-]of[-]stater, or (2) that even if the statute doesn’t discriminate against out[-]of[-]stater, it places an undue burden on interstate commerce and is[,] thus, unconstitutional.

#### Statute discriminates out[-]of[-]stater

The first argument O can make is that the statute discriminates out[-]of[-]stater. Where a state statute discriminates against out[-]of[-]stater, the Dormant Commerce Clause requires that the state statute must be necessary to an important state interest. Here, although the state statute does not discriminate out[-]of[-]stater on its face, O can argue that because state X is the nation’s largest producer of grain that is used in making ethanol

and because the use of gasohol will expand the market for grains, the statute in effect favors its in-state companies. Here, it's unlikely that a court will find that the statute discriminates against out-of-staters because it's neutral on its face - it regulates in-state companies the same way it regulates out-of-state companies.

If, however, the court does find that the statute discriminates out-of-staters, State X must meet the intermediate scrutiny test for regulations that discriminate out-of-staters. State X must show that the statute is necessary to meet an important interest. Here, it can argue that it has an important interest in conserving domestic supplies of petroleum and that gasohol burns more cleanly than pure gasoline. Thus, State X will likely prevail on the argument that it has an important interest in preventing pollution. Furthermore, the statute is substantially related to its interest because it requires all gasoline to be sold with 10% ethanol.

Moreover, as indicated above, because O may be a foreign corporation, State X may argue that because O is an international corporation, it cannot invoke the protections of the US Constitution since it is not a citizen of the country. But since O does business in State X, this argument should be rejected and it should be allowed to challenge the constitutionality of the statute.

#### Market participant

State X may also try to argue that it is a market participant, thus has not violated the Dormant Commerce Clause. One of the exceptions of where a state can discriminate against out-of-staters is if it is a market participant. Here, the facts indicate that State X is the largest producer of grain used for making ethanol, but it's not clear on whether the state itself is actually a participant or simply that the companies within the state are the makers of grain. If it's only the companies within State X and State X itself does not produce any grain, it will not prevail in making the argument that it is a market participant.

#### Statute doesn't discriminate out-of-staters - balancing test

Where a state statute doesn't discriminate out-of-staters, in order to meet the constitutional requirements of the Dormant Commerce Clause, it must not place an undue burden on interstate commerce. In determining whether a statute places an undue burden on interstate commerce, courts will look at the state's interest and the cost of compliance. As discussed above, state X can argue that it has an important interest in conserving domestic supplies of petroleum and that gasohol burns more cleanly than pure gasoline. Moreover, it will argue that since it doesn't discriminate out-of-staters, the cost to all companies to comply will be the same. O can argue that the cost of compliance is great because as indicated in the facts, its sales and profits has [sic] decreased substantially because of the limited capacity to produce gasohol. It's not clear from the facts whether other companies are also affected and to what extent they are affected. But assuming that other producers are able to produce gasohol without a great deal of problems - - that the

cost of compliance is not great - - then the statute will likely meet the requirements under the Dormant Commerce Clause.

## **2. The Equal Protection Clause**

The Equal Protection Clause of the 5<sup>th</sup> amendment applies to the states through the 14<sup>th</sup> amendment. It provides that all citizens must be offered the equal protection of the laws.

As stated above, because O may be a foreign corporation, State X may argue that because O is an international corporation, it cannot invoke the protections of the US Constitution since it is not a citizen of this country. But since O does business in State X, this argument should be rejected and it should be allowed to challenge the constitutionality of the statute.

### State action

The first is whether there is state action. In order to bring a challenge under the Equal Protection Clause, there must be state action. Here, State X has enacted a statute[;] this requirement has been met.

### Classification

The Equal Protection Clause protects against different treatments of classes of persons or corporations. The first issue, therefore, is whether the statute classifies people differently. Here, O can argue that because the statute favors grain producers in State X, the largest producers in grain, it is treating the state companies differently than out[.]of[.]staters. State X, on the other hand, will argue that the statute is neutral on its face, it does not classify different companies[,] and thus the Equal Protection Clause does not apply. Here, because the statute does not treat any company based on a particular classification, a court will likely find for state X.

At best, O can argue that the classification is companies that produce grain vs. companies that, like itself, cannot produce grain for the ethanol. Even if O succeeds on this argument, it will be a rational basis scrutiny because this classification doesn't involve any fundamental right or suspect or quasi-suspect classification. O may argue that because its sales and profits in State X have decreased dramatically, it is impinging on a fundamental right to make a living. O will fail in this argument, however.

Under the rational basis test, the statute will be upheld as long as there is any rational basis to promote a legitimate state interest. Here, as discussed, State X can argue that it has an [sic] legitimate interest in conserving domestic supplies of petroleum and that gasohol burns more cleanly than pure gasoline. Thus, State X will likely prevail on the argument that it has an [sic] legitimate interest in preventing pollution and the statute is rationally related to its interest because it requires all gasoline to be sold with 10% ethanol.

In sum, O will not be able to assert that State X has violated the Equal Protection Clause.

### **3. The Due Process Clause**

The Due Process Clause also applies to the states through the 14<sup>th</sup> amendment and it also requires state action. As discussed above, State X has enacted a statute[;] this requirement has been met.

State X can advance several arguments under the due process clause - - under the takings clause, the substantive due process clause[,] and the procedural due process clause.

#### Takings Clause

The Takings Clause provides that a state may not take the property of anyone without just compensation. In order to invoke the protection of the takings clause, O must show that the statute impacted its profits and in substance amounted to a takings [sic]. Here, O can show with reliable evidence that since the statute was enacted, its sales and profits in State X have decreased substantially because of its limited capacity to produce gasohol. This fact, along [sic], however, is not likely sufficient to show that there has been a taking. It appears that O is still making money. Simply because the profits have decreased, O hasn't satisfied the burden of showing that it amounts to a taking.

Where a state legislation doesn't amount to a taking, the state will not need to provide just compensation so long as it is substantially related to an important interest. As discussed above, State X will likely meet this burden. Here, it can argue that it has an important interest in conserving domestic supplies of petroleum and that gasohol burns more cleanly than pure gasoline. Thus, State X will likely prevail on the argument that it has an important interest in preventing pollution. Furthermore, the statute is substantially related to its interest because it requires all gasoline to be sold with 10% ethanol.

#### Substantive due process

The substantive due process clause, which also applies to states through the 14<sup>th</sup> amendment, provides that the government may not take away life, liberty or property without the due process of law. To meet this requirement, it depends on whether the right infringed upon is a fundamental right. If it is not, then the rational basis test applied and so long as the statute is rationally related to a legitimate interest, it will be upheld.

Under the rational basis test, the statute will be upheld as long as there is any rational basis to promote a legitimate state interest. Here, as discussed, State X can argue that it has an [sic] legitimate interest in conserving domestic supplies of petroleum and that gasohol burns more cleanly than pure gasoline. Thus, State X will likely prevail on the argument that it has an [sic] legitimate interest in preventing pollution and the statute is rationally related to its interest because it requires all gasoline to be sold with 10% ethanol.

Thus, O will not prevail under this argument.

#### **4. The Privilege and Immunities Clause**

The Privilege and Immunities Clause of Art IV offers protections to individuals against state's discrimination of out[-]of[-]stater. It provides that if a state action discriminates out[-]of[-]stater [sic] residents, the statute must be necessary to achieve an important interest. The P&I clause, unlike the Dormant Commerce Clause, however, does not offer protection to corporations. Because O is a corporation and not an individual, it will not be able to prevail under the P& I Clause.

## Question 2

PC manufactures computers. Mart operates electronics stores.

On August 1, after some preliminary discussions, PC sent a fax on PC letterhead to Mart stating:

We agree to fill any orders during the next six months for our Model X computer (maximum of 4,000 units) at \$1,500 each.

On August 10, Mart responded with a fax stating:

We're pleased to accept your proposal. Our stores will conduct an advertising campaign to introduce the Model X computer to our customers.

On September 10, Mart mailed an order to PC for 1,000 Model X computers. PC subsequently delivered them. Mart arranged with local newspapers for advertisements touting the Model X. The advertising was effective, and the 1,000 units were sold by the end of October.

On November 2, Mart mailed a letter to PC stating:

Business is excellent. Pursuant to our agreement, we order 2,000 more units.

On November 3, before receiving Mart's November 2 letter, PC sent the following fax to Mart:

We have named Wholesaler as our exclusive distributor. All orders must now be negotiated through Wholesaler.

After Mart received the fax from PC, it contacted Wholesaler to determine the status of its order. Wholesaler responded that it would supply Mart with all the Model X computers that Mart wanted, but at a price of \$1,700 each.

On November 15, Mart sent a fax to PC stating:

We insist on delivery of our November 2 order for 2,000 units of Model X at the contract price of \$1,500 each. We also hereby exercise our right to purchase the remaining 1,000 units of Model X at that contract price.

PC continues to insist that all orders must be negotiated through Wholesaler, which still refuses to sell the Model X computers for less than \$1,700 each.

1. If Mart buys the 2,000 Model X computers ordered on November 2 from Wholesaler for \$1,700 each, can it recover the \$200 per unit price differential from PC? Discuss.

2. Is Mart entitled to buy the 1,000 Model X computers ordered on November 15 for \$1,500 each? Discuss.

## Answer A to Question 2

2)

### Uniform Commercial Code

All contracts for the sale of goods, defined by 2-105 as those things identifiable at the time of contract, are governed by the UCC.

This is a contract for the sale of computers, goods movable and identifiable at the time of contract, and it is therefore governed by UCC rather than the Common Law.

### Merchants

Merchants, defined by 2-104 as those who deal in goods of that kind sold, are held to a higher standard of good faith.

PC manufactures computers, and Mart retails those computers, so both deal in the computers and are therefore merchants as that term is used in the UCC.

If a contract exists, it is a contract for goods under the UCC, and both parties are merchants.

### Offer

An outward manifestation of present contractual intent, communicated to the offeree in such a way as to make the offeree reasonably believe that the offeror is willing to enter into a contract.

The facts state that PC and Mart had been engaged [in] “preliminary discussions” prior to August 1. Because of these preliminary negotiations, PC’s fax was probably not a general advertisement sent out to possible retailers (advertisements are generally not offers). The August 1 fax on letterhead from PC to Mart, based on those discussions, was probably an offer. Although it did not state a specific quantity (up to 4000), it did indicate the identity of the parties, subject matter of the contract, and price, and the time of performance would be implied as a reasonable time. The limitation that no more than 4000 computers could be ordered makes the offer sufficiently definite to be enforced. Although the specific quantity of goods is required by 2-201, the statute of frauds, it is not necessary for formation, so this is apparently a valid offer.

Although PC would argue that there was no intent to be bound, in which case Mart would have made the offer on September 10, the court would probably disagree. Because PC delivered the goods without further communication, the court would probably conclude that it was not receiving offers, but had made an offer, to which it was bound.

PC's fax to Mart was probably a valid offer.

### **Merchant's Firm Offer Rule**

Under 2-205, a merchant who promises to hold an offer open with "words of firmness" will not be permitted to revoke the offer for the time stated, but in no case will the offer be irrevocable for longer than three months.

PC's fax was a firm offer from one merchant to another. PC specifically stated that they "agreed to fill any offers during the next six months." Although this offer would only remain irrevocable during the next three months (through November 1), it would remain in effect unless revoked until the end of the six months.

PC's fax was a merchants' [sic] firm offer, irrevocable prior to November 1, and though revocable at that time, in the absence of revocation it was valid under the six months expired.

### **Acceptance**

An outward manifestation of assent to the terms of the offer.

Mart's fax of August 10 was not an acceptance. Although it manifested some assent, it did not indicate a quantity of computers accepted, but only a general agreement to sell computers, and this alone was not sufficient to form a contract.

On September 10, Mart mailed an order for 1,000 computers to PC. This was sufficiently definite in quantity and indicated an intent to be bound. It was therefore a valid acceptance.

Similarly, Mart's November 2 letter was an appropriate acceptance. Though sent by letter rather than by fax, it was effective, since under the UCC an offer may be accepted by any reasonable means. The letter communicated assent to the proposed terms, and specified a quantity (200). This was therefore a valid acceptance of PC's offer. Under the Mailbox Rule, an acceptance is [sic] effective upon dispatch, though a revocation is only effective upon receipt. Mart's letter was sent before PC's revocation was receive[d], and it is therefore effective.

Although the November 15<sup>th</sup> fax similarly stated an intent to be bound on 1000 more computers, the offer had been properly revoked prior to that time, as discussed below, and Mart therefore could not accept it. This attempted acceptance would be invalid as an acceptance, and would instead be merely an offer, which PC summarily declined to accept.

Mart's November 2 letter was a valid acceptance.

## **Revocation**

A revocation is a statement that an offer may no longer be accepted. It is effective upon receipt by the offeree.

Mart received PC's fax on November 3, and it was therefore effective from that date forward. However, it would have no effect prior to that date, and therefore would not affect the validity of Mart's purported November 2 acceptance of the offer.

Because a revocation is not effective until received, PC's letter would not accept Mart's ability to accept the contract until November 3, and thus would not affect the outcome of this case, although it would prevent any further acceptance.

## **Consideration**

Bargained[-]for exchange of legal detriment

PC promised to sell and Mart promised to buy 2000 computers at \$1500 each. This was valid and sufficient consideration.

Because there was a valid offer, accepted and supported by consideration, PC and Mart have a contract.

## **Statute of Frauds - Defense to Enforcement**

The statute of Frauds (2-201) requires that all contracts for the sale of goods be in writing.

Although PC's original offer was on letterhead, they did not respond to the acceptance and no integrated contract was signed. The court would probably find, though, that Mart's letter of November 2, was a valid written confirmation, which would allow the contract to be enforced against both parties, although it might find that PC's refusal to agree that there was a contract was sufficient objection within ten days.

The court will probably find that the Statute of Frauds was satisfied by Mart's acceptance under the exception for a written confirmation, unless PC properly objected within ten days.

## **Material Breach**

A refusal to perform under the contract which goes to the heart of the promised performance.

PC refused to tender the 1000 computers ordered by Mart. This was material breach of the contract, since the purpose of the contract was the delivery of those computers. If PC and Mart had an enforceable contract, PC's refusal to tender them was an anticipatory

material breach, and Mart could immediately consider the contract breached (rather than waiting to see if PC would actually perform), and pursue remedies.

PC's refusal to deliver the computers to Mart was probably a material breach.

## **Remedies**

### **Cover**

Under the UCC, a buyer can purchase replacement goods on the market at the time of the breach and recover the difference between the contract price and the price of cover, plus incidental costs.

Mart has a duty to mitigate its damages, which probably means they should buy computers, even at a higher price, rather than completely lose the business. Although generally a party may wait until performance is due, where there is a complete repudiation of the contract by the other party prior to that time, there is probably a duty to mitigate damages. If Mart did purchase replacement computers, from Wholesaler or any other seller, they would [be] entitled to recover the difference between the price they were forced to pay and the price they had agreed on with PC as the cost of cover from PC. Any attempt to cover, however, must be exercised in good faith.

Mart will be able to recover the cost of Cover from PC.

#### **I. Whether Mart will be able to recover the extra \$200 purchase if it buys the computers from Wholesaler?**

Because PC and Mart apparently had a valid contract, and it was probably enforceable under the Statute of Frauds because of Mart's written confirmation, Mart can probably recover the cost of cover from PC, so long as it acts in good faith. For 2000 computers with an additional cost of \$200 each, Mart would probably recover \$400,000, plus costs incidental to cover.

If the cover found that the Statute of Frauds was not satisfied, Mart would not be able to enforce the contract, and would recover nothing.

#### **II. Whether Mart can enforce a contract based on the Nov. 15 fax for 1000 final computers?**

Because PC properly revoked its offer to Mart on November 3, Mart no longer had the power to accept that offer on November 15, and it has no enforceable rights against PC for the 1000 computers offered on that date.

## Answer B to Question 2

### Mart vs. PC

#### UCC Applies

The UCC applies to all contracts for the sale of goods. Here, the agreement between Mart and PC relates to the Model X computer, a good, so the UCC applies.

In addition, under the UCC, there are sometimes special rules governing agreements between merchants. Merchants are entities that regularly buy, sell and/or trade on the good at issue. Here, both PC and Mart are merchants under the UCC because PC manufactures and sells computers and Mart operates electronics stores that buy and sell computers.

#### Contract Formation

In order for the agreement between PC and Mart to be enforceable, there must be ① an offer, ② a valid acceptance[,], and ③ consideration.

#### Offer

An offer must demonstrate a present intent to be bound and must recite the necessary terms with appropriate specificity.

#### PC's August 1 Fax

PC'S August 1 Fax to Mart likely satisfies the requirements of an offer. In that fax, PC "agree[s] to fill any orders", thereby demonstrating the requisite present intent to be bound. The August 1 Fax also recites the subject matter (the Model X computer), the price (\$1,500 each) and the parties (PC and Mart). While the August 1 Fax does not recite a specific quantity of Model X computers to be purchased, it specifies any quantity ordered by Mart within the next six months up to a maximum of 4,000 units. This is an offer for a kind of requirements contract, wherein PC would be obligated to sell Mart however many Model X computers Mart requires up to a maximum of 4,000. Therefore, the August 1 Fax constitutes a valid offer.

#### Acceptance

An acceptance must be an acceptance of the terms in the offer before termination of the offer.

#### August 10 Fax from Mart

Here, the August 10 fax from Mart is a valid acceptance. While the August 1 Faxed offer from PC was still open, Mart responded that Mart “accept[ed] [PC’s] proposal”. Mart did not seek to change the terms of the offer or add any conditions or additional terms. Thus, the August 10 fax from Mart is a valid acceptance.

### Consideration

To be enforceable, a contract must include valid consideration. Consideration is a promise with value or detriment.

Here, PC provided consideration in that PC promised to sell up to 4,000 Model X computers to Mart over the next six months. However, the issue is whether Mart provided sufficient consideration. Mart promised to pay \$1,500 for any Model X computers it purchased, but Mart was not obligated to purchase any Model X computers. While Mart stated that it was going to conduct an advertising campaign, it is not clear whether that was a promise by Mart or simply a gratuitous statement of a present intent to place ads that is [sic] was not bound to place. If the statement about advertising were found to bind Mart, the contract would be effective as of Mart’s August 10 fax.

However, the better result is that there was not a binding contract until September 10, when Mart placed its first order for 1,000 Model Xs. As of September 10, Mart’s consideration was its promise to buy 1,000 Model X computers at \$1,500 each and PC’s consideration was its promise to sell those computers to Mart.

### Defense to Formation/the Statute of Frauds

The Statute of Frauds requires that any agreement for the sale of goods exceeding \$500 must be in writing to be enforceable. Here, the August 1 fax, the August 10 fax[,] and the September 10 order would likely constitute a sufficient writing to satisfy the Statute of Frauds.

There do not appear to be any other applicable defenses to formation (such as duress, illegality, fraud[,] etc.).

① Can Mart recover \$200 per unit from PC if Mart buys 2,000 Model X computers from Wholesaler?

The primary issue here is whether PC’s November 3 fax to Mart purporting to terminate its agreement with Mart excuses or discharges PC’s obligation to sell Mart up to 4,000 Model X computers before the six month period expires. The issue is also whether Mart’s November 2 order for 2,000 Model X’s, that was sent without knowledge of PC’s November 3 purported revocation [sic].

Thus, the ultimate issue is whether Mart’s November 2 letter ordering 2,000 more

units is effective when mailed (Nov. 2) or when received by PC. I believe the Mailbox Rule applies and provides that the acceptance/order of Nov. 2 was effective when mailed or sent. In other words, Mart's November 2 order is effective as of November 2 - the day before PC's purported revocation. Thus, PC is obligated to sell Mart the 2,000 Model Xs ordered on November 2.

Because PC is in breach of the contract by refusing to perform - i.e., to sell Mart the 2,000 Model X's ordered Nov. 2, PC is liable to Mart for damages.

### Mart's Remedies

As noted in the question, one of Mart's available remedies is to buy the 2,000 Model X computers from Wholesaler for \$1,700 each and then sue PC for damages. In that situation, Mart would be entitled to expectation damages. Expectation damages are those damages sufficient to put Mart in the position they would have been in if PC had not breached – namely, Mart would have purchased 2,000 Model X computers for \$1,500 each. Thus, PC is liable to Mart for \$200 per unit (\$1,700 - \$1,500) multiplied by 2,000 units. Mart could also recover any incidental damages it incurred in procuring the computers from Wholesaler. For example, if Wholesaler was further away and therefore shipping costs were more expensive than [sic] when Mart bought from PC, PC would be liable for the incremental increase in the shipping costs.

### 2. Is Mart entitled to buy the 1,000 Model X Computers Ordered on November 15 for 1,500 each?

By November 15, when Mart ordered the additional 1,000 computers, Mart knew that PC had revoked its offer to sell up to 4,000 units in that 6 month period or, in other words, had anticipatorily repudiated its obligation to sell Mart the full 4,000 units. Thus, Mart is not entitled to buy [sic] the 1,000 Model X's under a contract theory.

### Quasi-Contract/Unjust Enrichment

Rather, if Mart is found to be entitled to buy [sic] the 1,000 computers it will be because Mart told PC (as far back as August 10 & September 10) that, in reliance on their contract, Mart was going to spend money to place ads for the Model X. Thus, Mart relied to its detriment on PC's promise to sell 4,000 units, so Mart may be able to buy the final 1,000 units under a theory of quasi-contract based upon detrimental reliance.

Even if Model X [sic] is not entitled to actually buy the 1,000 computers from PC, Mart should be able to recover restitutionary damages from PC because PC has been unjustly enriched by Mart's advertising efforts.

### Question 3

Molly and Ruth were partners in the operation of a dry cleaning store. Recent government environmental regulations relating to dangers posed by dry cleaning fluids increased their exposure to liability and caused a decline in their business. Molly and Ruth decided to convert their partnership into Dryco, Inc. ("Dryco"), a corporation, to limit their potential personal liability.

Molly and Ruth each contributed \$20,000 in cash to Dryco. In return, each received a \$15,000 promissory note from Dryco and 5,000 shares of stock with a value of \$1 per share.

Prior to incorporation, Molly entered into a contract on behalf of Dryco with Equipment Company ("EC") for the unsecured credit purchase of an environmentally safe dryer for \$100,000. EC was aware that Dryco had not yet been formed. EC delivered the dryer one week after the incorporation, and Dryco used it thereafter and made monthly installment payments.

Dryco had been incorporated in compliance with all statutory requirements, and Molly and Ruth observed all corporate formalities during the period of Dryco's existence. One year after incorporation, however, Dryco became insolvent and dissolved. At the time of the dissolution, Dryco's assets were valued at \$50,000. Its debts totaled \$120,000, consisting of the two \$15,000 notes held by Molly and Ruth and a \$90,000 balance due EC for the dryer.

1. As among EC, Molly, and Ruth, how should Dryco's \$50,000 in assets be distributed? Discuss.
2. On what theory or theories, if any, can Molly and/or Ruth be held liable for the balance owed to EC? Discuss.

### **Answer A to Question 3**

#### 1. Distribution of Dryco's \$50,000 in Assets

##### Valid De Jure Corporation

A corporation is conclusively formed when the articles of incorporation are filed with the state. Here, the facts indicate that Dryco had been incorporated in compliance with all statutory compliances. Therefore, Dryco will be treated as a de jure corporation.

##### The Equipment Company Contract (EC)

Whether EC will have a claim to Dryco's assets on dissolution depends on whether EC's pre[-]incorporation contract with Molly as a promoter was adopted by Dryco.

A corporation is not liable for pre-incorporation contracts unless the corporation adopts the contract. Since Dryco did not exist at the time the contract was made, it can have liability unless: i) the corporation expressly adopts the contract (i[.]e[.]) through board resolutions or ii) the corporation accepts or retains benefits from the contract and therefore impliedly adopts the contract.

On these facts, Dryco accepted the dryer, used it, and made monthly payments on it. Even though EC was aware that Dryco had not yet been formed, Molly entered the contract on Dryco's behalf. Further the dryer was delivered after incorporation. EC will argue that Dryco's acceptance and use of the dryer constitutes implied adoption, and will likely prevail.

Therefore, EC has a valued unsecured claim against Dryco's assets.

##### Promissory Note

Promissory Notes are debt securities of a corporation. The holders of these notes have a creditor/debtor relationship with the corporation, and are on equal grounds with other unsecured creditors of the corporation.

##### Shareholders' Claims

Shareholders own an equity interest in a corporation. Shareholders are not entitled to distribution of a dissolved corporation's assets until all debts of the corporation have been satisfied.

##### Distribution

EC and Molly and Ruth stand on equal footing as unsecured creditors. As

shareholders, Molly and Ruth will receive no part of the \$50K, as explained above.

As between unsecured creditors, however, there is a possibility that Molly/Ruth's claim will be subordinated by a court to EC's claim, based on corporate veil piercing principals [sic] due to inadequate capitalization at the outset of the corporation.

### Piercing the Corporate Veil

A corporation is a separate legal entity designed to insulate its officers, directors, and shareholders from personal liability. However, the corporate form will be ignored in some circumstances, including when i) the corporation is acting as the alter ego of the shareholders or ii) when there was inadequate capitalization of the corporation at the outset.

Inadequate capitalization is determined by looking at if the corporation had adequate funds to meet its prospective liabilities. The time between incorporation and dissolution is also considered.

Here, Dryco was funded with \$40,000, and dissolved within one year. The short time in existence may be an indication that the corporation was not adequately funded. However, it is unclear from these facts what caused Dryco's dissolution. If Molly/Ruth were aware of increasing environmental costs and liability, \$40,000 may not have been sufficient. If this is so the corporate veil will be pierced. (Desire to shield from personal liability from environmental regulation is not enough to pierce the veil in and of itself.)

When shareholders use the corporation's assets as their own or otherwise ignore corporate formalities, the corporate form may be ignored to hold the SHs personally liable for the corp's debts. Here, there is no indication that Ruth/Mary used Dryco's assets as their own, and they did observe all corporate formalities. Therefore, the veil will not be pierced on this theory.

Since the veil can be pierced due to inadequate capitalization, however, Ruth/Mary's claim on the unsecured notes will be subordinated to EC's claim. EC will receive the entire \$50,000.

In the event the claims are not subordinated, EC, Mary and Ruth will equally divide the \$50,000.

## 2. Molly and/or Ruth's liability

A corporation is a separate legal entity that insulates its SHs from personal liability. As discussed above, Dryco was a de jure corporation. Unless circumstances exist to pierce the corporate veil, Ruth/Mary will not be liable to EC for the excess debt.

### Piercing the Veil

As explained above, the corporate veil may be pierced for inadequate capitalization at the outset. Also as explained above, if the veil is pierced, Ruth/Mary will be liable to EC for the \$40,000 of unpaid debt.

### Promoter Liability

When a promoter raises capital or enters contracts on behalf of a [sic] unformed corporation, the promoter is personally liable on those contracts. Absent novation, this liability remains even if the corporation has adopted the contract.

Here, Molly entered the contract with EC on behalf of Dryco. Therefore, absent novation, she is personally liable. There is no indication of a novation here, so Molly will be liable for the 40K even though Dryco adopted the K.

Ruth may be liable based on vicarious liability. Ruth and Molly were joint venturers, co-promoters, so EC may try to reach Ruth on this theory, or at minimum, Molly may seek contribution from Ruth. Since Ruth did not sign the contract[,] however, this theory will likely fail.

### Answer B to Question 3

3)

1. Distribution of \$50,000 of Dryco's assets

Dryco has [sic] \$120,000 in debt at the time the corporation became insolvent. This includes the \$30,000 in promis[s]ory notes to Molly and Ruth, and the \$90,000 still owed to EC, for the environmentally safe dryer. Dr [sic]

Pre-incorporation contract

The issue is whether the debt to Equipment is owed by the corporation. Corporations are only liable for pre-incorporation contracts that they adopt. Here before the corporation was formed, Molly entered into a contract for the the [sic] purchase of the dryer. The facts do not indicate that there was an express adoption of this contract. However the fact that after the corporation was formed, the dryer was delivered to Dryco, used by Dryco, and the monthly installment payments totaling \$10,000 were made by Dryco, is sufficient to establish that Dryco impliedly adopted this contract. Furthermore without the Dryer the business might not be able to comply with the governmental regulations imposed on the drycleaning industry. Therefore the dryer is an essential piece of equipment to Dryco and its adoption of the purchase contract entered into by Molly[.]

Inside/Outside Debt

Dryco only has \$50,000 in assets, and has \$120,000 in debt. Therefore it must be determined which creditors have prio[r]ity for satisfaction. In determining which creditors will be satisfied first the court will generally, in the interest of fairness, subvert inside debt, and allow outside debt to be satisfied first. The reason for this is that the insiders, Molly and Ruth, could have given the \$15,000 for stock interests, which would only receive distributions after creditors are satisfied.

Here Molly and Ruth elected to make \$15,000 of their \$20,000 contribution as a loan. They were trying to insulate themselves further from any potential losses, by only putting at risk the \$5,000 for their stock. The court will not allow inside shareholders to try to put their equity investment on an equal level with outside creditors who have no equity interest in the corporation.

Therefore EC should be given priority as an outside creditor and should receive the \$50,000 that Dryco has. Molly and Ruth's interest will be subverted to EC's interest and their loan will not be satisfied.

2. Molly and Ruth Personal Liability

After the \$50,00 in assets are given to EC, EC is still left with \$40,000 that has not been satisfied. EC will thus try to hold Molly and Ruth, as sole shareholders in Dryco[,] personally liable for the remaining debts.

### Incorporator liability

Prior to incorporation Molly entered into a contract with EC for the dryer. As a general rule, an incorporator is not relieved of liability of the pre-incorporation contract, until there has been a novation, that is[,] an agreement by all parties to relieve the incorporator of personal liability. Here Molly would have to show that both Dryco and EC to relieved[sic] Molly of personal liability. As discussed above, Dryco impliedly adopted the contract, and thus becomes primarily liable for the contract. However there is no indication that EC relieved Molly of her personal liability, and can be held secondarily liable, because there was no novation.

However, Molly can argue that the contract was entered into “on behalf of Dryco[.]” The corporation by estoppel doctrine holds that a party who knew the contract[sic] was being entered into on behalf of a corporation is estopped from later claiming that the other party is personally liable. Molly can argue that because EC knew that Dryco had not been incorporated yet, but knew that Molly was entering “on behalf of Dryco” they should be estopped from claiming that Molly is personally liable.

Molly will likely be successful in this claim, and EC will be estopped from claiming that Molly was personally liable, because EC knew that Dryco was not yet incorporated, but still signed a contract “on behalf of Dryco”. It would therefore not be equitable for EC to be able to hold Molly personally liable under this theory[.]

### Shareholder liability

As a general rule shareholders are not personally liable for the debts of the corporation. The shareholders only put at risk what they invest in the corporation. As discussed above Molly and Ruth each invested \$20,000, which will all be treated as equity in Dryco. Therefore under the general rule Molly and Ruth will not be liable for the \$40,000 remainder owed to EC.

However where it is necessary to prevent a fundamental unfairness courts may elect to pierce the corporate veil, and hold the shareholders personally liable. Courts generally elect to pierce the corporate veil where the corporation has attempted to defraud the corporation[']s creditors. Courts are much less likely to pierce the corporate veil for tort creditors than for contract creditors. Here EC was a contract creditor, so EC will have to have a very strong claim to succeed.

Courts will pierce the corporate veil where the shareholders of the corporation fail to follow corporate formalities, or where there [sic] corporation was inadequately capitalized

at the time of formation.

Here the facts state that Molly and Ruth observed all corporate formalities. There are no facts to indicate that there was any commingling of personal and corporate funds, or that Molly or Ruth treated any of the corporate assets as their own.

EC will try to argue that Dryco was inadequately capitalized at the time of formation, that is[,] that Dryco would be unable to pay debts at the time they came due. Because the EC is a contract creditor they have to make a strong showing. Here Molly and Ruth put in a total of \$40,000 cash. Because the inside claim will be subverted to EC claim the full \$40,000 should be considered[.] EC will fail on this claim because the facts indicate that Dryco was able to make the monthly installment payments.

The court will likely find that there was no fundamental unfairness in this transaction, especially because EC was a contract creditor. EC could have protected itself by entering into a separate agreement with Ruth and Molly to agree to personally assume the debt. Because EC did not do this they cannot later claim Molly and Ruth[s] personal assets. Therefore Molly and Ruth will not be personally liable on this claim.

#### Director liability

As the sole shareholder[s] of Dryco, Molly and Ruth are probably the directors, and as such owe Dryco fiduciary duties of Loyalty and Due Care. Directors can be held personally liable for injuries caused from breaching this duty. However there are no facts suggesting a violation of these duties, such as self[-]dealing or uninformed decision making and [they] should not be held liable for breaching their fiduciary duties.

## Question 4

Ann represents Officer Patty in an employment discrimination case against City Police Department ("Department") in which Patty alleges that Department refused to promote her and other female police officers to positions that supervise male police officers. Bob represents Department.

At Patty's request, Ann privately interviewed a male police captain, Carl, who had heard the Chief of Police (Chief) make disparaging comments about women in Department. Carl told Ann that Chief has repeatedly said that he disapproves of women becoming police officers, routinely assigns them clerical work, and would personally see to it that no female officer would ever supervise any male officer. Carl met with Ann voluntarily during his non-work hours at home. Ann did not seek Bob's consent to meet with Carl or invite Bob to be present at Carl's interview.

When Bob saw Carl's name as a trial witness on the pretrial statement, he asked Chief to prepare a memo to him summarizing Carl's personnel history and any information that could be used to discredit him. Chief produced a lengthy memo containing details of Carl's youthful indiscretions. In the memo, however, were several damaging statements by Chief reflecting his negative views about female police officers.

In the course of discovery, Bob's paralegal inadvertently delivered a copy of Chief's memo to Ann. Immediately upon opening the envelope in which the memo was delivered, Ann realized that it had been sent by mistake. At the same time, Bob's paralegal discovered and advised Bob what had happened. Bob promptly demanded the memo's return, but Ann refused, intending to use it at trial.

1. Did Ann commit any ethical violation by interviewing Carl? Discuss.
2. What are Ann's ethical obligations with respect to Chief's memo? Discuss.
3. At trial, how should the court rule on objections by Bob to the admission of Chief's memo on the grounds of attorney-client privilege and hearsay? Discuss.

## Answer A to Question 4

As Patty's attorney, Ann has a duty of confidentiality, loyalty, fiduciary responsibility and competence to her. This means that she must work hard on her case and follow up any possible leads that Patty may give her and follow up on any reasonable requests made by Patty. As an attorney, however, Ann has a duty of candor, fairness and dignity to the court, her adversary and the public. Because Ann knew that the Police Dept. (PD) was being represented by Bob (B), she was aware that any contact with a police officer could possibly be a violation of these duties. She could have a potential conflict because at minimum, the appearance would be that she was doing something unethical or wrong, even if she wasn't. She could have an actual violation of these duties if she were, in fact, having ex parte communications with a represented adversarial party.

Ann could argue that B represents the PD in general, but not Carl personally, & therefore she was w/i her right to contact him. The PD will argue that because Carl is a police captain, he is in a position of authority that someone would naturally look to for advice & information. Further, a police captain is in a position to make decisions that could bind the PD organization & his decisions could affect the PD. Because there is no one single individual to look to as being the defendant, you must look to those individuals who appear to represent the organization, can bind the organization by their decisions, has [sic] a leadership position & would be someone that one would look to for answers. Carl meets these qualities and therefore Ann violated her ethical duty to not have ex parte communication w/ a represented party. She should have gotten Bob's permission to speak w/Carl[.]

The PD could also argue that Carl is the equivalent of an agent & Ann will also need to obtain Bob's permission to talk w/any agent or employee of a business that may have information about the case & who's [sic] answers & information could be of detriment to the organization or bind the organization to a particular thought or conduct. Again, because Ann did not get Bob's permission to talk to a person who she knew was represented by counsel, she violated the ethical rules.

Although Patty asked Ann to talk with Carl, Ann cannot blindly follow the requests of her client if the requests would be illegal or aid or further an illegal act or if they would violate an ethical rule. A duty of competence is not outweighed by her duty of fairness & dignity to the court and her adversary.

### 2. Ann's ethical obligations with respect to the Chief's memo

As previously discussed, Ann has an [sic] duty of fairness, candor and dignity to the court, her adversary & the public. This means that she is not to use or benefit from or seek out any evidence which she knows is illegally or fraudulently obtained or to which she knows is clearly a mistake and privileged information. If an attorney knows or has reason to believe that any evidence or property that comes into her possession has been obtained

thru illegal means or fraud, she has a duty to turn it over to the authorities or the court. She cannot destroy the evidence nor can she instruct her client to destroy it. She also has an obligation not to use the information.

Here, after reading the memo[,] Ann clearly saw that the material was confidential attorney[-]client information. She could also tell that it was a document that was made in the course of litigation and therefore work product. She therefore had a duty to turn the memo over to either Bob or the Court immediately.

Ann also has a duty of competence to Patty, however. If she had information that could aid Patty in her case, she had a duty to follow up on it. The balance against the privileged information and her duty to Patty, however, is a difficult position for Ann. The memo gives her information about Carl which will give her an idea as to how much she can rely on his credibility and will give her damaging proof and admissions to the Chief's discrimination against females that all but proves her case. Despite the importance of the memo to her case, however, Ann is not entitled to benefit from another party's mistake and the confidential work product. She violated her duty of Fairness & Candor by reading and keeping the memo, as well as her duty of dignity to the court.

### 3. Bob's Objections to the Admission of the Memo

An attorney has [a] duty of Confidentiality to his client. This means that any information that he obtains during the course of his representation must be kept confidential, no matter how or when the information was obtained. It exists whether the client specifically asked him to keep it confidential or not and whether or not the release of information would harm or embarrass his client. The attorney[-]client privilege protects an attorney from divulging any confidential information about his client to anyone else, including the court, unless the client consents, the information is with regard to an imminent danger of serious bodily injury or death (although CA does not specifically provide for this) [,] the court orders the information be disclosed, the attorney is defending himself in a malpractice or bar complaint charge or bringing an action against his client for payment of services or seeking an ethical opinion.

Here, Bob has a duty of confidentiality to the Chief under the same analysis as he would be to Carl as previously discussed. The Chief can be considered his client because of his role in the PD, as discussed previously about Carl. Bob has a duty to keep the memo confidential because he asked Chief to write it, it's information central to the case and obtained while he represented the PD.

The document can clearly be categorized as confidential information bet/ a client and attorney. As such, the court cannot order that it be disclosed and used without the consent of the PD, as only the client can consent to it be[ing] used. Ann cannot force Bob to disclose the attorney[-]client priv[i]lege.

The memo can also be considered work product because it was made at Bob's request in anticipation of litigation. Such work product is protected by attorney[-]client privilege and cannot be disclosed w/o one of the previously discussed conditions being met. Chief is clearly not going to consent, Ann cannot order the disclosure, there is no threat to anyone's safety or life, there is no suit against or on behalf of Bob and he's not seeking a legal opinion. The court should exclude the memo on grounds of attorney[-]client privilege.

### Hearsay

Hearsay is any out of court statement that is being offered for the truth of the matter asserted. Hearsay is not admissible unless there is an exception.

The memo is hearsay because it is a statement by Chief made out of court and Ann wants to use it to prove that Chief and PD discriminate against women. It also has info about prior bad acts of Carl, which are not admissible to show that he did something wrong on this occasion.

If Chief testifies, this information is w/o his knowledge and he could potentially testify about same. Ann could argue that the memo is a stmt of a party opponent and therefore admissible. Ann could argue that the memo is an admission of fault by Chief & therefore also admissible. If a party makes an earlier out of court admission, it can be an exception to the hearsay rule and admissible.

Ann could also argue that the memo is a statement against interest made by Chief when he knew he was being sued. If a person makes [a] statement against his pecuniary interest, it is deemed reliable and admissible hearsay. The negative comments about women could clearly be construed as against his interests.

Chief could also argue that the memo contains prior bad acts about Carl[,] which is inadmissible character evidence. A party cannot offer evidence of prior bad acts to show that the person is guilty of the current act. Further, the issue of character cannot be admitted unless the suit itself deals with a person's character or it goes to their credibility. Then, the only thing they can discuss is the w's opinion about their reputation for truthfulness in the public. There is no evidence of that here at this time. Further, prior bad acts are only admissible in a criminal case to show motive, intent, mistake of fact, identity and common scheme or plan. It does not apply to civil cases.

Because the memo is protected confidential attorney[-]client privilege, it should be excluded. Even though Ann can show that there are several applicable exceptions to the hearsay rule, the ultimate test is whether the probative value of the memo outweighs the prejudicial affect to the PD. Here, the prejudice is high and the memo should be excluded.



## Answer B to Question 4

4)

Question 4

1. Ethical violations by Ann (A) for interviewing Carl (C)

Ann's interview of Carl raised several ethical concerns:

### Duty Regarding Communications with Parties or Employees of Parties Represented by Counsel

In the instant circumstance, C is an employee of an organization, the Department, which is represented by attorney Bob (B). The issue is whether it is permissible under the rules of professional conduct for A to interview C without notice t[o] B or representation by counsel.

To begin with, a lawyer may not have communications with a party who is represented by counsel when the counsel is not present or aware of the communications. In situations where, as where [sic], as here, a lawyer seeks to have communications with an employee of an entity represented by counsel, the lawyer must obtain consent from the organization's counsel if: 1) the employee works regularly or at the behest of counsel, 2) the employee has authority to bind the organization, or 3) the employee's actions may be imputed to the organization.

Here, since C is a police captain, he likely has sufficient seniority to bind the Department or for his actions to his actions [sic] to be attributed to the Department. Therefore, it was improper for A to interview him without the consent of Bob (B), who is counsel for the Department. A's actions were improper under the rules of professional conduct, regardless of the fact that C met with A voluntarily and after work hours.

Moreover, where a party is not represented by counsel and it appears that person should be, it is the duty of the lawyer to so advise that party. Thus, A should have advised C that he ought to have the benefit of counsel in his communications with her.

### Duty of Fairness to Third Persons

Furthermore, A likely violated her duty of fairness to third persons by interviewing C without notice to B or without the benefit of representation by counsel. In this situation, C acted at his peril and may well face negative consequences at work for his actions. In light of this risk, A should have advised C that he ought to have the benefit of counsel in his communications with her. By failing to advise B in this manner, A's conduct violated her ethical obligations.

## 2. A's Ethical Obligations Regarding the Chief's Memo

To begin with, the memo contains sensitive material that is protected both by the attorney-client privilege and work product privileges.

### Attorney-Client Privilege

The attorney-client privilege applies to confidences between a client and counsel in the course of representation. The attorney-client privilege is an evidentiary privilege. Under the evidentiary privilege, one may not be compelled to testify about a matter falling under the privilege. Here, the memo was made by Chief in response to B's request for the summary of certain information that could be used to discredit C. As such, the communication is one between Chief and his lawyer B and falls within the attorney-client privilege.

### Work Product Privilege

The work product privilege applies to all material made in anticipation [of] or preparation for litigation. Here, the memo was prepared at B's direction to aid at trial: specifically to discredit a potential witness. As such, the memo falls under the work product privilege.

### Duty to Return Material Mistakenly Delivered

A lawyer is under an ethical duty to return material mistakenly delivered to her. Here, the memo was inadvertently delivered by B's paralegal, and B promptly demanded its return, leaving no doubt in A's mind that it was accidentally delivered to her. Moreover, the material clearly contains sensitive material that falls under the attorney-client and work product privileges. The sensitive nature of this material also should have alerted A to the unintentional delivery of this material to her. Since this material plainly was not intended for delivery to her, A is under an ethical obligation to return it.

### Duty of Zealous Representation and Diligence

A lawyer has a duty to zealously and diligently represent her client. Absent the applicability a specific rule requiring an attorney to return material mistakenly delivered to her, A would be under a duty to use such material in connection with her obligation to zealously and diligently represent her client. However, in this circumstance, the rule requiring an attorney to return mistakenly delivered material trumps the duty of zealous representation and diligence.

### 3. Objections to Admissibility of Memo

#### a. Objection based on attorney-client privilege

As discussed above, the memo initially falls within the scope of the attorney-client privilege.

#### Waiver?

The issue is whether the accidental disclosure of the memo to A constitutes a waiver. In general, a privilege is waived if it is disclosed to a third-party. Here, if the disclosure were intentional, there is no doubt that a waiver would apply. However, in the instant circumstance, the disclosure by the paralegal was accidental and B promptly sought the return of the material. Moreover, A is under an ethical duty to return the material in all of the circumstances. In light of the accidental nature of the disclosure and the applicable ethical duty for A to have returned the material, a court would likely rule that a waiver has not occurred and allow the protection of the attorney-client privilege to remain intact.

#### b. Hearsay

Hearsay is an out-of-court statement offered to prove the truth of the matter asserted. Here, the memo can be said to constitute double hearsay: the memo is itself an out-of-court statement and it contains references to some things that the Chief said out of court: to wit, that he disapproves of women becoming police officers, routinely assigns them clerical work, and would personally see to it that no female officer would ever supervise a male officer. As double hearsay, an exception to the hearsay rule must apply for each level of hearsay.

#### Admission

The Chief's statements may be admissible, despite the hearsay objection, because it [sic] can be viewed as an admission. The very essence of the plaintiff's claim is that women are discriminated against. All of Chief's statements that he disapproves of women becoming police officers, routinely assigns them clerical work, and would personally see to it that no female officer would ever supervise a male officer amount to admissions of discrimination. As an admission, the memo can clear both levels of hearsay. Therefore, the court could overrule a hearsay objection on this basis.

#### Offered Not for the Truth But for The State of Mind

A can argue that the Chief's statements are being offered not for the truth of the matters Chief allegedly said, but rather to show his state of mind. This argument can be

an additional basis for allowing the chief's statements, but it does not solve the hearsay problem inherent in offering the memo, which is another out[-]of[-]court statement, being offered for the truth that Chief said such things.

#### No Business Record Exception

A business record exception can apply where a party makes a records [sic] in the regular course of business and is under a duty to record. Here, the business record exception would not apply b/c Chief had no duty to make the memo and it was made for litigation, not in the course of business.

#### No Official Record Exception

Similarly, the official record exception would not apply b/c Chief made the memo for litigation, and it was not made by an agency.

#### Conclusion

In conclusion, the memo may be admitted and not barred by hearsay b/c it is an admission.

## Question 5

Alice and Bill were cousins, and they bought a house. Their deed of title provided that they were "joint tenants with rights of survivorship." Ten years ago, when Alice moved to a distant state, she and Bill agreed that he would occupy the house. In the intervening years, Bill paid nothing to Alice for doing so, but paid all house-related bills, including costs of repairs and taxes.

Two years ago, without Alice's knowledge or permission, Bill borrowed \$10,000 from Lender and gave Lender a mortgage on the house as security for the loan.

There is a small apartment in the basement of the house. Last year, Bill rented the apartment for \$500 per month to Tenant for one year under a valid written lease. Tenant paid Bill rent over the next seven months. During that time, Tenant repeatedly complained to Bill about the malfunctioning of the toilet and drain, but Bill did nothing. Tenant finally withheld \$500 to cover the cost of plumbers he hired; the plumbers were not able to make the repair. Tenant then moved out.

Bill ceased making payments to Lender. Last month, Alice died and her estate is represented by Executor.

1. What interests do Bill, Executor, and Lender have in the house? Discuss.
2. What claims do Executor and Bill have against each other? Discuss.
3. Is Tenant obligated to pay any or all of the rent for the remaining term of his lease, including the \$500 he withheld? Discuss.

## Answer A to Question 5

### What interests do parties have in the house?

The court must decide between competing claims by Bill (B), Executor (Exec)[,] and Lender (L).

### Joint Tenancy

Alice and B originally took title as joint tenants with the right of survivorship. Joint tenancy required the existence of four unities – time, title, interest, and possession. Assuming these unities were present, the distinguishing feature of a joint tenancy, the right of survivorship, will apply.

Under the right of survivorship, on the death of one joint tenant, his/her interest automatically passes to the surviving tenant(s). Thus, if a joint tenancy existed between Alice and B, B would automatically get Alice's interest at her death.

The issue here, though, is whether any actions by the parties changed the joint tenancy before Alice's death.

### Severance/L's mortgage

A unilateral act of mortgaging the property may sever a joint tenancy, depending on the type of jurisdiction.

### Lien Theory

A lien theory jurisdiction holds that a unilateral mortgage does not automatically sever a joint tenancy. Therefore, if this is a lien theory jurisdiction, normal survivorship rules would apply, and at Alice's death the following would occur:

Alice's interest would pass to B through the right of survivorship. B would thus be left with a fee simple absolute, subject to L's mortgage. Exec gets nothing.

### Title theory

However, in a jurisdiction which follows the title theory, a unilateral mortgage by a joint tenant is held to sever the joint tenancy. The result is that joint tenants become tenants in common, with the mortgagee the equitable owner of the undivided portion legally belonging to the mortgagor.

In a title theory jurisdiction, the following would occur:

Immediately upon B's mortgaging the property, the joint tenancy was destroyed. Alice and B were then tenants in common, each with an undivided  $\frac{1}{2}$  interest. B's interest was subject to L's mortgage[.]

At Alice's death, her undivided  $\frac{1}{2}$  interest passes through her estate. It will thus be held in trust by Exec to be distributed per the provisions in Alice's will. B will continue to hold his undivided  $\frac{1}{2}$  interest. L will have an equitable ownership interest in B's undivided share by virtue of its mortgage.

## 2. Claims of Exec and B against each other

Exec, as the executor of Alice's estate, may be legally able to assert any claim against B that Alice had during her life. B could counter with any claims he had against Alice.

### Exec's claims - Rent

A tenant has a duty to account to co-tenants for any rents or profits received from use of the land. Exec will claim interest in  $\frac{1}{2}$  of the rents B received from Tenant.

B rented out the basement apartment to Tenant for \$500/month. B received rent for seven months, a total of \$3,500. Since Alice had a right to  $\frac{1}{2}$  of the rents, Exec will lay claim to \$1,750.

### B's claims against Exec

B will counter for claims for Alice's share of house-related bills, repairs, and taxes.

### House-related bills

The house[-]related bills may or may not be subject to partial reimbursement from Alice's estate. Mortgages or loan payments are generally apportioned between the tenants according to their interest. Since Alice and B had equal interests, B may claim compensation for Alice's half of any such payments made by him.

Some bills, however, are the sole responsibility of the tenant in possession, since they are based on his use or enjoyment of the property. Therefore incidental expenses or use charges such as utility bills will not be subject to reimbursement.

### Repairs

Tenants in possession may receive contribution from non-possessory tenants for regular repairs (distinguished from improvements). Thus B may receive reimbursement from Alice's estate for  $\frac{1}{2}$  of the regular repairs B had done to keep the property in good condition.

## Taxes

Tenants out of possession are also liable for their respective share of taxes levied upon the property. B may therefore claim reimbursement for ½ of the taxes he has paid.

### 3. Tenant's obligation to pay remaining rent?

B and Tenant (T) entered into a one-year lease. After seven months, T refused to pay rent and has moved out. T will try to get out of his duty to pay rent for the remaining term.

## Warranty of habitability

Generally at common law, a tenant's duty to pay rent was considered independent of the landlord's duty to provide the premises. Tenants took the premises as they were; "caveat emptor" was the rule of the day.

Because the harshness of application to tenants, courts have modernly considered residential leases (commercial leases are not protected). Thus, if a landlord provides premises that are not inhabitable, tenant's duty to pay rent may be excused.

"Uninhabitability" has been fairly strictly construed by courts. Property is typically considered "uninhabitable" only if it fails to provide the barest essentials - four walls, a roof, and running water/plumbing.

Here, T will claim that the malfunctioning toilet and drain render the premises uninhabitable. A court will probably find for T, because the lack of working plumbing would result in a possible health hazard. T may thus be excused from paying rent until the problem is repaired.

Many courts allow the tenant, in cases where the landlord has failed to repair, to contract himself to have the repairs done and deduct that amount from the rent due.

Here, T did notify B of the need for repairs, and B never responded. T was therefore eligible to engage in "self-help" by contracting for the needed repairs himself. He did so, and withheld the amount from the rent owed to B. He was within his rights to do so.

## Constructive eviction

At issue is whether T can avoid the five months remaining on his lease with B.

If the problem with the toilet and drain render the premises completely uninhabitable,

forming a nuisance to T, then upon proper notice to B[,] T can quit the premises. He will be relieved of his obligation to make future rent payments by virtue of the doctrine of constructive eviction.

Here T notified L of the nuisance conditions. T's own plumbers were unable to repair. Because the condition was a nuisance - a health hazard - T could quit the premises. Since he did so, he can claim constructive eviction.

Therefore T is not liable for any rents remaining on his contract with B.

## Answer B to Question 5

5)

1. \_\_\_\_\_ Interests of Bill, Executor and Lender

### Joint Tenancy

Alice and Bill took title as “joint tenants with rights of survivorship.” The creation of a joint tenancy requires the presence of the four unities. Joint tenants must take by the same title instrument, at the same time, with identical interests and rights to possession. A and B took title at the same time and by the same deed and apparently had identical interests and rights to possession and thus a valid joint tenancy was created. Joint tenants have rights of survivorship that entitle surviving tenants to automatic ownership of the interests of deceased joint tenants. Thus a joint tenant’s interests are not devisable or descendible. As a consequence, as long as B did not sever the joint tenancy by mortgaging his interest, B became sole owner of the house upon A’s death.

### Title Theory v. Lien Theory of Mortgages

A joint tenancy is severed, i.e., survivorship rights cease and the tenancy becomes that of tenants in common, when, without the permission of the other joint tenant(s) one joint tenant transfers his or her ownership interest in the property. There are two conflicting theories regarding the consequences of one joint tenant mortgaging his or her interest in a joint tenancy without permission. The title theory of mortgages deems the tenancy terminated once the property is unilaterally mortgaged because it treats title as passing from the mortgagor to the mortgagee[,] thus severing the unity of title. The lien theory of mortgages holds that the joint tenancy remains intact despite the mortgage, concluding that the mortgagee only holds a lien on the property so the unity of title is not disrupted. Thus, the effect of B’s mortgage to Lender on his joint tenancy with A will depend on which theory the jurisdiction applies. If it applies the title theory, then the tenancy was severed and A’s interest became devisable and descendible and is thus now part of her estate. If the lien theory is applied, then the tenancy was not severed and B automatically took title to the house upon A’s death.

### Equitable Conversion

Lender certainly has an interest in the one-half share of the house that was B’s at the time he mortgaged the house. Lender’s rights to the other half depends on whether B took title to the entire property upon A’s death as discussed above. B only had the power to encumber what he owned – an undivided one-half interest – and thus at the time of the mortgage L only had a security interest in B’s half of the house. Whether L will have a security interest in the entire property, assuming the lien theory of mortgages applies, depends on the application of the doctrine of equitable conversion. Under this doctrine

equity deems done that which ought to be done. Thus, if B represented to L that he owned the house alone and thus L thought his security interest was in the entire property, then the doctrine of equitable conversion could apply to L's mortgage and give L an interest in the entire house.

## No Adverse Possession

If the title theory of mortgages applies and thus B does not take A's share of the house, he may argue that his uninterrupted possession of the house for the past ten years gives him title by adverse possession. Adverse possession operates to give title to one who occupies property under certain circumstances for a statutorily prescribed period (i.e., the statute of limitations on trespass). To make out a valid claim of adverse possession to possess a house, one must show that his possession was continuous for the prescribed period, that his possession was open and notorious (such that the rightful owner would have notice of the trespass), that possession of the property claimed was actual (no constructive possession) and that the occupation of the property was hostile (i.e., not with permission of the owner). B's possession of the house likely satisfied the first three requirements as he openly lived in the house; however, his claim will fail because occupation by a joint tenant is not hostile absent an ouster of the other tenants. A and B agreed that B would occupy the house after she moved away and thus there was no ouster and no hostility.

## 2. Claims of Executor and Bill

### Executor's Claims – Rents

The general rule is that joint tenants are not entitled to rents from other joint tenants even if one tenant has sole possession of the property unless there has been an ouster (i.e., exclusion of one tenant of another who has a right to possession). Thus, Executor will not be entitled to any rent claimed for B's occupation of the house because B had not ousted A from the house. However, joint tenants are entitled to their pro rata share of any rents collected from non tenants. Thus, Executor has a claim to half of the rents received by Bill from Tenant, i.e., \$1750.

### Bill's Claims – Repairs and Taxes

Joint tenants are responsible for their pro rata share of taxes and repair costs absent an agreement to the contrary. Joint tenants are not responsible for expenses related to another's use of the property. Here B paid for taxes and repairs with no contribution from A for the ten years that he was in sole possession of the house and thus under the general rule A's estate could be held liable to B for her half of these expenditures. Executor would argue that B was obligated to give A notice of any necessary repairs prior to making expenditures that she would be responsible for. Executor would also argue that A and B had an implied agreement that B would make

these payments in return for having exclusive use of the house. That B had never requested payment from A during the ten year period indicates that this was indeed the case. Finally, A's estate would not be liable for "house-related bills" that were incident to B's use of the property as joint tenant's obligations extend only to repairs and taxes.

### 3. Tenant's Obligations

#### Covenant of Quiet Enjoyment – Constructive Eviction

Every lease includes an implied covenant of quiet enjoyment. This covenant [sic] obligates a landlord to do and refrain from doing whatever is reasonably necessary to enable a tenant's quiet enjoyment of the leased premises. This obligation [sic] includes landlord's duty to make repairs to the premises if a condition is interfering with the tenant's quiet enjoyment. A continued refusal to comply with this obligation can give rise to a claim of constructive eviction. A constructive eviction will be found when 1) a condition causes a substantial impairment of the tenant's quiet enjoyment, 2) the tenant gave adequate notice to the landlord of the condition and the landlord failed to take appropriate remedial measures[,] and 3) as a result the tenant gave up the lease and moved out. A malfunctioning toilet and drain could certainly cause a substantial impairment of one's enjoyment of an apartment. This is especially true here where the premises consisted of a small basement apartment that likely had only one bathroom and not much ventilation. Tenant gave landlord notice of the problem and even attempted to have the problem fixed himself. Finally, tenant promptly moved out. Thus, tenant has a valid claim for constructive eviction and is thus not liable for the remaining term of the lease. Tenant could also recover damages from B for breach of contract.

#### Implied Warranty of Habitability – Standard and Remedies

Also implied in every residential lease is the implied warranty of habitability. This warranty requires landlords to provide property that is fit for basic human habitation. The standard can be based on housing code but generally extends to basic amenities such as running water, electricity, heat in cold climates, etc. A malfunctioning toilet that is apparently beyond repair would very likely be found to be a breach of the implied warranty of habitability. Among a tenant's remedies for breach are 1) move out, 2) withhold rent (may be required to keep in escrow), 3) repair and deduct the cost from the rent[,] and 4) remain and sue for damages. Tenant availed himself of the third option by seeking to have the toilet and drain repaired, however the repair was beyond the abilities of the plumbers. As long as tenant's efforts were in good faith he should be entitled to repayment for the \$500 he spent to repair the conditions despite the fact that conditions were not capable of being repaired. The continuing breach also gave tenant the right to vacate and terminated his obligations under the lease.

## Question 6

In 2003, Sam executed a valid testamentary trust, naming Tom as trustee. The terms of the trust state:

- (a) All net income is to be paid to Bill, Sam's nephew, for life;
- (b) Tom may invade principal for Bill in such amounts as Tom, in his sole and absolute discretion, determines;
- (c) The trust terminates on Bill's death and any remaining principal is to be distributed to Alma Mater University;
- (d) The interests of the beneficiaries are inalienable and not subject to the claims of creditors.

In 2004, Sam died.

In 2005, Lender obtained a judgment against Bill for an unpaid credit card bill that includes charges for tuition, groceries, and stereo equipment. Lender now requests a court order directing Tom to pay all future installments of trust income to it rather than Bill until the judgment is satisfied.

Bill is delinquent in making child support payments to Kate, his former spouse, for their child. Kate now requests a court order directing Tom to pay all future installments of trust income to her rather than Bill until the arrearages are eliminated.

Bill wants Tom to invade the trust principal so Bill can promote a newly-formed rock band, but Tom has refused. Bill now requests a court order directing Tom to invade the trust principal.

Because of Tom's refusal to invade the trust principal, and because Alma Mater is concerned over Bill's debt difficulties, Bill and Alma Mater wish to terminate the trust in order to divide the trust principal, but Tom has refused. Both Bill and Alma Mater now request a court order terminating the trust.

How should the court rule on the requests made by Lender, Kate, Bill, and Alma Mater? Discuss.

## Answer A to Question 6

A trustee is a fiduciary relationship with respect to property where a settlor transfers property to a trustee who holds the property for the benefit of named beneficiaries, for a valid trust purpose. On the facts, Sam executed a valid express testamentary trust naming Tom as the trustee and Sam and Alma Mater University as beneficiaries. Sam has a life interest in the trust and Alma Mater has a remainder interest.

### ① Request by Lender

The express trust created creates a spendthrift clause under (d). As a general rule, a beneficiary's interest is both voluntarily and involuntarily alienable as a property right. Involuntary alienation allows a creditor to attach to the beneficiary's rights to future payments by obtaining a judgment.

A spendthrift clause is designed to protect the beneficiary from their spendthrift ways by prohibiting both voluntary and involuntary alienation of the beneficiary's right to future payments. Thus the spendthrift clause created in (d) prohibits Lender from attaching to Bill's future payments of income. The provision explicitly state's [sic] that the beneficiaries' interest is inalienable and not subject to creditor's claims.

However, the courts recognize exceptions to the protection provided by spendthrift provisions including where a creditor has provided necessities to the beneficiary. Necessaries include items such as food, clothing, shelter and medical care.

On the facts, Lender provided Bill with tuition[,] groceries[,] and stereo equipment. A court would likely find that only the groceries were necessities and would order that Lender be entitled to payment for the groceries from the income of the trust. Thus a court would likely grant Lender's requested order for payment of Bill's grocery debt.

With respect to the stereo and tuition, Lender could seek recovery based on surplus. The concept of surplus is recognized in some jurisdictions and allows a creditor to attach to future payments to the beneficiary despite a spendthrift clause where the income to be paid exceeds the beneficiaries['] station in life, thus resulting in a surplus. On the facts it is unclear what income is produced in relation to Bill's station in life. In making the determination as to whether surplus exists the court will only consider Bill's reasonable expenses. If Lender can establish surplus, a court would likely grant his requested order and direct Tom as trustee to pay future installments of surplus to Lender to satisfy Bill's debt.

### ② Request by Kate: Preferred Creditor

In addition to the two exceptions noted in relation to Lender, the courts have also recognized an exception for preferred creditors.

A court will disregard a spendthrift clause and allow a preferred creditor to attach to the beneficiary's future income payments from the trust. Preferred creditors include government debt and outstanding child and spousal support and alimony payments.

On the facts, the beneficiary Bill has failed to make child support payments to his former spouse Kate for the support of his child. Thus Kate is a preferred creditor and is entitled to attach to Bill's right to future income from the trust to satisfy the delinquent child support.

Therefore, a court would likely grant Kate's request and order Tom to pay trust income to Kate in satisfaction of Bill's outstanding child support obligation until the arrearages are eliminated.

### ③ Request by Bill - Discretionary Trust Provision

Under the terms of the will, Tom has sole and absolute discretion to determine whether or not to invade the trust principle [sic] for Bill's benefit. Tom as trustee has all express powers as set out in the trust and all implied powers required to exercise the express powers. As a fiduciary, Tom has an obligation to exercise his discretion in good faith. On the facts, there is no indication that Tom's refusal to invade the trust principal to allow Bill to promote the rock band was made in bad faith.

Therefore, based on the facts, the court would not interfere with Tom's discretion as explicitly set out in the trust and would deny Bill's request. The court would not therefore order Tom to invade the trust principal.

### ④ Request by Alma Mater & Bill - Termination

A court will not order a termination of a trust even with the consent of all beneficiaries where such termination would be in violation of the trust purposes and would be contrary to the testator's intent.

The trust established by Sam evidences a clear intent to provide for Bill during his lifetime. This is a valid trust purpose which continues until Bill's death. On the facts, Bill is still alive and thus the trust purpose is ongoing. As well, the termination of the trust would destroy Sam's intent to provide for Bill throughout Bill's life.

In addition, the trust has not become passive as Tom, the trustee, still has active duties in maintaining and managing the trust. Nor have circumstances changed such that the doctrine of changed circumstances would apply to modify the trust terms.

Therefore, the court would uphold Tom's refusal to terminate the trust and would deny Bill and Alma Mater's request since termination would destroy the settlor/testator (Sam's) intent.

### **Answer B to Question 6**

Trust actions are governed by the trust document.

#### Valid Trust

A valid inter vivos trust was created since Sam (S), the settlor, had an immediate intent to create a trust for a legal purpose, and delivered a presently existing res, title property interest, to Tom (T), the trustee, for the purposes of management for the benefit of the beneficiaries Bill (B) and Alma Mater (AM).

#### Type of Trust

##### Income

B has a life interest in the income of the trust, subject to its provisions.

##### Mandatory Distributions (Provision A)

The trust sets out mandatory distributions of income to B by T. T must then distribute the income to B.

##### Spendthrift Provision (Provision D)

All distributions, both income and principal, are subject to a spendthrift provision. This prevents creditors from attaching and beneficiaries from voluntary [sic] assigning their rights. This is held as valid restraint. B & AM may not alienate nor may creditors attach. There are, however, exceptions to the creditor[']s rule discussed below.

##### Principal

##### Discretionary to Bell (Provision B)

T is given discretionary power to distribute principal to B. T is thus not required to distribute any principal and may distribute as he feels is necessary) [sic][.]

##### AM (Provision C)

AM has a right to all of the principal remaining at B's death subject to the spendthrift limitation.

### T's Fiduciary Duty

Trustees are subject to fiduciary duties. T is thus bound to follow the provision set out by the trust. As such, his actions below with the individuals are governed by the document provisions discussed above.

### Parties['] Requests

#### Lender

As explained, as a spendthrift trust, creditors may not normally attach and T cannot be required to pay off the court order. Exceptions for creditors are made for the following creditors: government creditors, tort judgments, spousal or child support, alimony, necessities and surplus above station.

Here, Lender seeks reimbursement for groceries, a necessity. Since courts want beneficiaries to be able to obtain necessities based on credit, this exception exists and reimbursement may be made. Lender may also argue tuition is a necessity but this is likely to fail[.]

The right to collect for the stereo equipment and education may come under the surplus exception. Creditors may attach to the income a beneficiary receives beyond that which is necessary to maintain their station in life.

It is unclear here what amount B receives and what amount his past lifestyle dictates is necessary for maintenance[.] Lender may have an argument and thus gain attachment. T will then be required to make payments to Lender[.]

#### Kate

Again, the income to B is subject to the spendthrift provisions. Kate, however, has a claim under the exception for child support payments, since this is a creditor that courts have felt should not, in equity and public policy, be excluded. Kate may attach and require T to make payments to her. Her order ought to be granted.

#### Bill

Bill's order will fail. The trustee[']s fiduciary duties to the trust are governed by the document and T is granted discretion in his allocation of principal to B. T's decision not to support B's rock band plans, especially in light of B's other monetary problems, is reasonable. T appears to be using his discretion to fulfill his duty of care, acting as a reasonably prudent person managing other people's money, under the circumstances.

Further, in using his discretionary powers, T must also adhere to his duty of loyalty to all beneficiaries. While AM only has a right to the leftover, he may also consider that all parties', including B's, best interests may be served investing the principal. B's order should be denied.

### Alma Mater

B&AM have both requested that the trust be terminated. A trust may be terminated where all the beneficiaries, including unborn beneficiaries represented by legal counsel, petition the court for determination. The court must also find that all of the purposes of the trust have been fulfilled.

While all the beneficiaries (present & future) are currently petitioning, B&AM, the court is likely to find that the trust's purposes have not been fulfilled. S created a trust that granted B a lifetime right in the income of the trust subject to a spendthrift clause[.]

It appears from the terms that S was attempting to insure for the provision of income to B, despite his issues with spending wisely. To prematurely cancel the trust would leave B without the protections that S intended. Cancellation would be directly at odds with this purpose.

Though it may fulfil the purpose of AM's gaining some of the principal, their express right in the trust is only to the remaining principal and not the most principal they can receive. Further, this purpose of S is best protected by T's discretionary power over the principal. B&AM's order to terminate should thus be denied.

Additionally, AM's concerns over the debts fail since B's right to the principal, AM[']s interest, is subject to T's discretion. Even if the creditors could attach under an exception, attached creditors to a discretionary interest only have a right to collect when T chooses to pay out. Only in that scenario is T required to pay the creditor. AM's interest is thus further protected and S's purposes are better furthered through the continuation of the trust and the order ought to be denied.