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Institute Examination in Law

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[The following answers to the questions set by the board of examiners of the American Institute of Accountants at the examinations of May, 1930, have been prepared at the request of The Journal of Accountancy. These answers have not been reviewed by the board of examiners and are in no way official. They represent merely the personal opinions of the author.—*Editor*, The Journal of Accountancy.]

Examination in Commercial Law

May 16, 1930, 9 A.M. to 12:30 P.M.

Group I

Answer all questions in this group.

No. 1:

$5,000 No. 657

The First National Bank

Newark, N. J., Jan. 15, 1929.

E. R. Cater has deposited in this bank Five Thousand Dollars payable to the order of himself on the surrender of this certificate properly endorsed, with interest at 4½%.

J. H. Benedict, *Cashier.*

Is the foregoing a negotiable instrument? What is it called? What is its use?

Answer:

(a) The foregoing is a negotiable instrument, because it is a written unconditional promise by the bank to pay a sum certain in money, on demand, to the order of E. R. Cater.

(b) It is called a certificate of deposit.

(c) It serves as an acknowledgment by the bank of the receipt of a sum of money on deposit, which in this case the bank promises to pay to the order of the depositor, whereby the relation of debtor and creditor between the bank and the depositor is created.

No. 2:

Jones decides to purchase a tractor for use on his farm. The George Tractor Company manufactures and markets a tractor under the trade name of "Challenge Tractors." Jones purchases a "Challenge" tractor but after two weeks' use he finds that it is not of sufficient power for his work because his farm is largely soft muck land used for raising market vegetables. He seeks to return the tractor and the George Tractor Company seeks to recover an unpaid balance of the purchase price. Which of them would succeed?

Answer:

The George Tractor Company would succeed in recovering the unpaid purchase price. The sale could be rescinded only upon the theory of breach of an implied warranty of fitness. In the case of the sale of a specified article under its trade name, and in the absence of a reliance on the seller to furnish an article fit for a disclosed use, there is no implied warranty as to its fitness for any particular purpose for which the buyer intends to use it.

No. 3:
Jones, Johnson and Perry form a partnership. Jones contributes $5,000, Johnson $3,000 and Perry $1,000. The partnership agreement omits any provision indicating how the profits are to be divided. If the business results in profit how will such profit be shared by the partners?

Answer:
In the absence of any agreement for division the profits of the partnership should be shared equally. The difference in contribution of capital may be offset by differences in services performed, and courts decline to look into the question of which partner may have made the greatest contribution.

No. 4:
A man dies on August 15, 1929. His estate is still in process of settlement on December 31, 1929. How is the income of the decedent and of his estate for 1929 returned for federal income-tax purposes? What personal exemption would be allowed against the 1929 income of the decedent, his estate and his widow?

Answer:
The income of the decedent should have been returned by his executor or administrator on or before March 15, 1930. The income of his estate should likewise have been returned by his executor or administrator on or before March 15, 1930. The full personal exemption of $3,500 would be allowed against the 1929 income of the decedent. The full exemption of $1,500 would be allowed against the income of his estate. The full exemption of $1,500 or $3,500 would be allowed against the income of his widow, depending upon whether or not she was the head of a family at the close of the taxable year.

No. 5:
You become secretary of a large corporation and, among other duties, have charge of all transfers of the corporation's stock. To safeguard the corporation what formalities would you require with reference to each certificate presented for transfer?

Answer:
I would insist on having a trust company appointed registrar and another trust company appointed transfer agent, and would turn the matter over to them. No large corporation should have the transfer of its stock handled by its secretary.

GROUP II

Answer any five of the questions in this group, but no more than five.

No. 6:
What is the distinction between insolvency laws and bankruptcy laws?

Answer:
The only distinction which now exists between insolvency laws and bankruptcy laws is a matter of terminology; the term "bankruptcy act" referring to the federal statute, and the term "insolvency statutes" referring to statutes of the several states.

No. 7:
The M Company, a boatbuilder, selected certain mahogany lumber in the Y Company's yard and bought and paid for it. The Y Company agreed to load the lumber on a railroad freight car to be placed on the siding in its yard.

Before the Y Company had the opportunity to do so, the lumber was destroyed by a fire which was not due to any fault of the Y Company. On whom does the loss fall?

Answer:

The loss falls on the Y Company. The general rule is that a person having the title to the property bears the loss. Unless a contrary intention appears, where a contract for the sale of specific goods requires the seller to deliver such goods at a particular place, it is presumed under the uniform sales act that the parties do not intend that title should pass until such delivery is made. This is true even though the property has been paid for by the buyer. In the present case, the Y Company was required by contract to load the lumber on a freight car. This loading would be the delivery, and title did not pass until that was done. (In this answer I assume there is no particular significance in the word "bought" contained in the question. If the word "bought" implies a special contract by reason of which title passed the answer would be otherwise.)

No. 8:

Assume that in question No. 7 the Y Company had loaded the lumber on the freight car and had consigned the car to the M Company, but before the car was started on its journey fire had destroyed the car and its contents. Would there be any responsibility different from that developing from the conditions given in question 7 and, if so, why?

Answer:

On the principle stated in the preceding question, title passed from the Y Company to the M Company when the Y Company had loaded the lumber on the freight car. Therefore, as between the Y Company and the M Company, the M Company must bear the loss. But since the lumber had been consigned to the M Company, it was in the possession of the carrier, which, if it was a common carrier, would be liable for the loss of the lumber by the fire unless the fire was caused by an act of God or the public enemy. The fact that a railroad company does not own or control the siding on which it has placed its cars for the reception of freight but has furnished them to a shipper on a private switch, does not affect the carrier's responsibility if the essential elements of a delivery otherwise are present.

No. 9:

Allen, by fraud, induces Bates to issue a negotiable promissory note to him. Allen then sells the note to Cameron, who is a holder in due course. Cameron, in turn, negotiates the note to Davis who, while not a party to the fraud, has full knowledge of it. Can Davis recover from Bates? State the rule involved and the reason for it.

Answer:

Davis can recover from Bates. A holder of a note who derives his title thereto through a holder in due course thereof and who is not himself a party to any fraud or illegality affecting the note has all the rights of the holder in due course in respect of all parties prior to the latter. The protection of the holder in due course against diminution of the market for the note is the reason for the rule.

No. 10:

The board of tax appeals, in a case known as "Matter of McNeil," decided that commissions paid to brokers by owners for consummating leases of space in buildings are deductible in the year when paid, instead of in annual instalments spread over the terms of the leases as previously ruled by the commissioner of internal revenue. The commissioner announced his non-acquiescence in this

decision. What is the significance of this action and how would you advise a client to handle similar commissions in his income-tax return for 1929?

Answer:

The commissioner's non-acquiescence in the board's decision implies that he will not follow it in other cases involving that point, and that he will probably test the question in the courts. Pending such a final determination I should advise my client to follow the board's decision and deduct the commissions in his return for 1929.

No. 11:

X, Y and Z entered into a partnership which, by the provisions of the partnership agreement, was to continue for a term of three years. Z, however, during the first year disagreed many times with X and Y as to business policies, such disagreements resulting in strained personal relations between the partners. At the close of the first year X and Y decided to drop Z from the partnership and so informed him. Could X and Y compel Z to withdraw?

Answer:

X and Y can not compel Z to withdraw from the firm, the partners having agreed to continue the partnership for three years.

No. 12:

A owns 100 shares of stock of the X Steel Corporation. At a meeting of the board of directors held in January, 1929, a dividend was declared, payable April 1, 1929, to stockholders of record March 1, 1929. A died on March 15, 1929, leaving a will under which everything that he owned at the time of his death was left in trust, the income thereof only to be paid to his wife during her life. When the dividend was paid to the executors on April 1, 1929, was it proper to treat it as part of the trust estate or as income payable to the wife?

Answer:

It was proper to treat this dividend as a part of the trust estate. A being a stockholder of record March 1, 1929, was entitled to receive on April 1, 1929, a dividend on his 100 shares of stock of the X Steel Corporation. This made the X Steel Corporation the debtor of A on March 1, 1929, to the amount of the dividend, although it was not payable until later. This debt constituted a part of A's estate.

No. 13:

The commissioner of internal revenue has ruled adversely to your contentions on certain items of an income-tax return of your client and has assessed an additional tax. To what tribunals may the case be taken for review of the commissioner's action?

Answer:

The case may be taken to the board of tax appeals for a redetermination of the deficiency asserted by the commissioner. The decision of the board may be reviewed by a circuit court of appeals or the court of appeals of the District of Columbia, in accordance with section 1002 of the revenue act of 1926. The decision of either of these courts may be reviewed by the supreme court of the United States upon certiorari. If the additional tax has been paid, then the taxpayer may after filing a claim for refund sue in a district court of the United States or in the court of claims for its recovery. Such suit can be instituted six months after the claim is filed or immediately after its rejection by the commissioner. A decision of a district court may be reviewed by the circuit court of appeals and in turn by the supreme court of the United States on certiorari. A decision of the court of claims may be reviewed by the supreme court of the United States upon certiorari.