Journal of Accountancy

Volume 70 | Issue 5 Article 15

11-1940

Institute Examination in Law

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INSTITUTE EXAMINATION IN LAW

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[Note.—The following answers to questions set by the board of examiners of the American Institute of Accountants at the examination of May, 1940, have been prepared at the request of The Journal of Accountancy. The 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.

To conserve space, the problems and questions are being omitted from this department, in view of the fact that the complete examination was published in the June issue. The editors would be glad to receive communications from readers who may feel that they are unduly inconvenienced by this procedure.—Editor.]

EXAMINATION IN COMMERCIAL LAW

May 17, 1940, 9 A.M. to 12:30 P.M.

GROUP I

No. 1 (10 points)

Solution:

X has no right to collect compensation from Z. There was no express contract between X and Z whereby Z agreed to pay any amount to X, and no contract can be implied whereby Z should be required to pay any amount to X since the advice given by X was purely gratuitous. If Z had gone to X for advice in circumstances where it might be presumed that Z would expect to pay for such advice (as in the case of a lawyer, doctor, or other consultant), and if X had given advice in response to the request of Z, X would have a basis for a claim for the reasonable value of his services, but even in such a case there would be no basis for demanding ten per cent of the amount of the life-insurance policy. The recovery would be in such amount as would be reasonable compensation for the services of X in advising Z.

No. 2 (10 points)

Solution:

(a) A de facto corporation exists if there is a statute under which a de jure corporation could have been formed, if an attempt has been made in good faith to comply with such statute, if there has been a failure to comply with some provision thereof with respect to the organization of the corporation, and if there has been a use ostensibly by the corporation of one or more of the powers it would have possessed if properly organized.

(b) A de facto corporation would exist in the case presented. Defects in the organization of a corporation, as distinguished from its creation, usually do not prevent its being a de facto corporation. There have been decisions that a de facto corporation exists even though no stock has been issued. The defect is in the issue of the stock which is usually done subsequent to incorporation. It might be necessary to correct the stock that was illegally issued, but that would not prevent the corporation from existing.

No. 3 (10 points)

Solution:

The question presupposes that X reasonably and necessarily incurred the expenses. Such reasonable and necessary expenses incurred by an accommodation endorser in consequence of the maker's default, including counsel fees and disbursements, can be recovered from the maker, and X, therefore, would have a valid claim against Y. If the accommodation endorser had no substantial defense to the action in which he was made a defendant, he should have paid the note without incurring the litigation, and in such a case he could not recover counsel fees and disbursements from the maker because such

expenses would not be reasonable ones necessarily incurred.

No. 4 (10 points)

Solution:

(a) The statute of frauds is not a principle of equity or common law, but it is found in one or more statutes enacted by the state legislature. These statutes closely follow old English statutes, and there has been a considerable body of decisions built up interpreting them.

(b) X cannot rely upon the statute of frauds in support of his claim. False misrepresentation of a material fact is not a type of fraud covered by these statutes.

No. 5 (10 points)

Solution:

(a) Two special types of partnership are:

1. A limited partnership, which permits special partners to escape liability in excess of the amount of capital contributed. There must be one or more general partners with full liability.
2. A joint stock company, in which any member may transfer his share, the transferee becoming a partner.

(b) There can be no change in the personnel of an ordinary partnership. A new firm is formed when an incoming partner joins an established firm. The old firm does not continue.

(c) At common law an incoming partner is not liable for debts contracted prior to the time of his becoming a partner, in view of the fact that he does not join the old firm but joins with members of the old firm in forming a new partnership. Under the uniform-partnership act a person admitted as a partner into an existing partnership is liable for all of the obligations of the partnership arising before his admission as though he had been a partner when such obligations were incurred, but this liability is to be satisfied only out of partnership property.

No. 6 (10 points)

Solution:

(a) It was enacted by the Senate and House of Representatives in Congress assembled and was approved by the President February 10, 1939.

(b) The income-tax provisions are applicable to taxable years beginning after December 31, 1938. There are no war-profits taxes in the Code. Excess-profits taxes are applicable to income-tax taxable years ending after June 30, 1939.

(c) Four other important taxes covered by the Code are the estate tax, gift tax, capital-stock tax, and employment taxes. In addition to these there are numerous excise taxes.

No. 7 (10 points)

Solution:

In spite of the fact that the bankrupt has vacated the premises, it is possible that his trustee in bankruptcy may wish to retain the lease as a valuable asset of the estate. In such a case, of course, the estate must pay the rent. If the estate does not wish to retain the lease, the landlord may recover possession by appropriate proceedings in the bankruptcy court, and in such case may have a claim allowed for damages up to the amount of the rent for a year after the surrender of the premises to the landlord by the trustee. Such a claim must be proved in the usual way.

No. 8 (10 points)

Solution:

(a) This contract may be terminated at will by either party upon reasonable notice to the other. It merely constitutes an indefinite general hiring, in the absence of a consideration other than the rendering of the services.

(b) In these circumstances B has a right to employment and compensation as long as B is able and willing to work and there is work to be done. B's relinquishment of his business is consideration for this additional right.

No. 9 (10 points)

Solution:

The accountant should accept the offer of a check already certified which would be given to him in three quarters of an hour. The negotiable-instruments act provides that where the holder of a check procures it to be certified, the drawer is discharged from liability thereon. If, therefore, the accountant accepts an uncertified check and has it certified himself on the way to the railroad station the result will be that the amount will be deducted from the corporation's account by the bank but the corporation will be released from its liability on the check. If the bank

should fail before the check is cashed, the accountant would lose the money. On the other hand, the drawer is not discharged when the check is certified by his procurement, so that if the corporation has the check certified and gives the accountant the certified check the accountant will not only have a claim against the bank but will have a claim against the corporation until the check is paid.

No. 10 (10 points)

Solution:

The contention is not sound. When an ultra vires contract has been fully performed on both sides neither party can maintain an action to set aside the transaction or to recover what has been parted with. The courts will not interfere in such a case to deprive either the corporation or the other party of property acquired under the contract.

No. 11 (10 points)

Solution:

In the absence of a statute precluding recovery by the mortgagee against the purchaser who contracted with the mortgagor to assume the mortgage debt, the mortgagee can enforce the agreement and compel the purchaser to pay the debt. In most jurisdictions the basis of this liability is the rule that where a contract is made for the benefit of a third person such person may maintain an action directly thereon. In a few jurisdictions, however, the liability of the purchaser is sustained on the theory that since, as between the parties to the sale, the purchaser, by his contract of assumption, becomes the principal debtor and the mortgagor the surety, the mortgagee is entitled to the benefit of this contract although he is unaware of its existence when made, under the doctrine that a creditor is entitled, by equitable subrogation, to all securities held by a surety of the principal debtor.

No. 12 (10 points)

Solution:

It may be argued that since the bank has no contractual relation with the payee named in a depositor's check unless it accepts or certifies the check, it, therefore, is not liable to a payee for paying a check to a swindler who has forged the payee's name. There are decisions, however, which hold that the payee may recover in tort from the bank in such a case on the theory of conversion of the check.