

NEW YORK STATE BAR EXAMINATION
FEBRUARY 1996 QUESTIONS AND ANSWERS

THIS EXAM HAS JUMBLED TEXT IN PARTS. I CLEANED UP SOME OF IT, BUT IN SOME PARTS, IT SEEMS ENTIRE PHRASES ARE MISSING, SO DON' T RELY ON THESE EXAM ANSWERS TOO MUCH.

Question-One

Ric, a purchasing agent for GEM, an auto manufacturer, telephoned Jan, the sales manager of PAR, a manufacturer of brake pistons, to discuss the availability of pistons. GEM had previously purchased pistons from PAR on many occasions. Ric said, "We could probably use up to 1000 Model Z pistons in the next six months, but we need to be sure you can fill our orders when we place them." Jan said, "No problem."

GEM then sent PAR a printed form entitled "GEM Supply Confirmation" which provided that GEM would be entitled to purchase up to 1000 Model Z pistons from PAR during the next six months. The form further provided that PAR's obligation to sell the pistons for six months was irrevocable and also provided that any dispute arising between GEM and PAR would be subject to arbitration as the exclusive remedy. The form contained several other provisions but did not recite any consideration and did not state a price or other terms of sale.

Jan signed the GEM form at the bottom but did not otherwise write on it. Jan returned the form to GEM together with a PAR printed form entitled "PAR Purchase Order." The PAR form stated "Confirm 1000 Model Z pistons available," but did not state a time period during which the pistons would be available. The form also stated "Orders must be accompanied by a \$10,000 down payment." GEM received the form but did not respond to it.

In all the previous transactions between GEM and PAR, the purchase price had always been negotiated, and no payment had ever been required on placement of an order. None of the parties' prior agreements had required that disputes be resolved exclusively by arbitration, or that any offer be held open for a specific period of time.

Two weeks later, GEM wrote to PAR stating, "Send 300 Model Z pistons." No payment accompanied the order. PAR's written reply stated, "We will not fill your order because you did not remit a \$10,000 down payment." GEM's written reply stated, "We had a deal that didn't call for a down payment. Send us the pistons." PAR did not ship the pistons.

Four months after the initial conversation and exchange of forms, PAR wrote to GEM stating, "We will no longer supply GEM with pistons on any terms." GEM immediately sent an order to PAR for 1000 Model Z pistons and accompanied it with a \$10,000 check. PAR refused to ship the pistons.

GEM served a demand for arbitration upon PAR. GEM then commenced a proceeding in Supreme Court against PAR seeking a preliminary injunction requiring PAR to hold 1000 Model Z pistons ready for delivery to GEM pending arbitration of the parties' dispute. On PAR's motion, the court (1) dismissed the injunction proceeding, holding that the parties' agreement required all aspects of the dispute be submitted to arbitration.

(a) Was the court's ruling (1) correct?

(b) What are the contractual rights and obligations, if any, of GEM and PAR arising out of the foregoing facts?

ANSWER TO QUESTION ONE

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(a) Issue 1: Is a preliminary injunction proper in a breach of contract action? No. Here the court was correct in dismissing the injunction proceeding.

A preliminary injunction is an equitable remedy. Equitable remedies are granted by the court when there are no adequate remedies at law. A preliminary injunction is made by a motion to the court on notice to the adversary. The movant must show that defendant threatens the value of the goods the defendant has an interest in and the movant must be seeking a permanent injunction. The movant must post an undertaking (security, bond) and file an affidavit to show probable success on the merits.

(To accelerate the return date on a preliminary injunction the movant can motion for a temporary restraining order.)

Here GEM's action is in breach of contract and should be seeking money damages, not an equitable remedy.

(b) Is an oral contract for a quantity valid? Yes -- (GEM will prevail over PAR)

Requirements/output contracts.

Ric is seeking assurances that PAR can meet its requirements of up to 1000 model 2 pistons over six months. This is a valid contract so long as GEM does not make disproportionate requirements. (However, Ric stated "We could probably use up to 1000 model 2 pistons." Probably is a vague term and when a material term, such as a quantity is vague or ambiguous there will not be a valid contract.)

There are certain contracts that are required to be in writing to satisfy the Statute of Frauds. Contracts for marriage, a year or longer, sale of land, executor to pay debts of an estate, goods for sale of \$500 or more, where one agrees to be a surety. Here, this contract would fall within a contract for \$500 or more. Though the telephone call created an oral contract, GEM sent a supply confirmation. An exception to the statute of frauds is where there is an oral contract between merchants subject to the statute of frauds and one of the parties sends a confirming letter, or contract, to the merchants involved, it will be enforceable against the merchants even though they didn't sign unless the merchant rejects the contract in 10 days. If no rejection it is a valid contract.

(Statute of Frauds requires -- certain contracts be in writing, state subject matter and signed by the party to be charged.)

Furthermore, GEM's supply confirmation is a firm offer. A firm offer is an irrevocable offer that is in writing, signed by a merchant, promising to keep the offer open for the stated time not to exceed 3 months. After 3 months it becomes a regular offer and is up to the offeror to revoke.

Here, GEM will prevail over PAR as PAR did not reject GEM's supply confirmation as PAR responded two weeks later (not in 10 days) concerning the failure of the \$10,000 down payment which is a material term and not specifically agreed to.

Is there a valid contract when a purchase order differs from the supply confirmation?

Under New York common law an acceptance must mirror the offer or it is not a contract. Under modern law the UCC uses the Battle of the Forms. If the acceptance contains non-material different terms from the offer then the non-material terms become part of the contract unless rejected within a reasonable time. If the acceptance contains material terms they do not become part of the contract unless specifically agreed to.

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(Non-material terms -- parties are both merchants, terms not rejected within a reasonable time, terms are not restricted to the terms of the offer and the new term is non-material.)

Here the arbitration clause is a material term in the GEM Supply Confirmation and will not be enforced against PAR as he did not specifically agree to it.

(New York courts enforce arbitration clauses if freely entered into in writing and the dispute falls within the arbitration clause. As a result a court will send the dispute to arbitration and not interfere unless there has been fraud or illegality, the arbitrator is biased or the arbitrator exceeded his powers.)

However Jan's signing the supply confirmation would imply he read the confirmation and has agreed to the arbitration clause, thereby binding PAR to arbitration.

The PAR Purchase order required a \$10,000 down payment. This is a UCC Battle of the Forms issue. The \$10,000 down payment is a material term and GEM is not bound to it as he did not specifically agree to it. GEM's failure to respond cannot make the term enforceable against him as failure to respond is only in regard to non-material terms. Here the down payment is a material term.

The letter two weeks later that GEM wrote PAR for 300 "Z" pistons is enforceable against PAR as the \$10,000 down payment, a material term, did not become part of the contract.

Here, the revocation by PAR is valid as a firm offer is only valid for the time stated and not to exceed 3 months. GEM's supply confirmation created a firm offer for 6 months. This is invalid and the offer will be irrevocable for only 3 months. After 3 months it is a regular offer which PAR may revoke.

Here GEM's service of demand for arbitration, which PAR must respond to within 20 days, is valid and the courts will enforce the clause as it was in writing and signed by Jan, an agent for PAR.

ANSWER TO QUESTION ONE

(a) Ruling (1) was correct.

The issue is whether the clause in the "GEM Supply Confirmation" memo requiring arbitration became a term of the agreement between GEM and PAR.

The rule is that under the Uniform Commercial Code as adopted by New York in an agreement between merchants, persons who regularly deal in merchandise of the kind, that additional terms contained in memoranda become part of the agreement if they are not objected to within a reasonable time (10 days). The terms will also become part of the agreement if consented to.

Here, the arbitration term contained in the GEM confirmation memo was consented to by Jan, an employee of PAR. Jan consented to the term by signing the confirmation memo and returning it to GEM, without objecting to the additional term requiring arbitration of disputes. Because this writing was signed by an agent of PAR (an agent will bind the principal, his employer, as long as he has apparent authority to do so and here Jan had the authority) it satisfies the requirements of both the UCC and Statute of Frauds in New York, which requires that a contract for a sale of goods for more than \$500 be in writing and signed by the party to be charged. The arbitration term becomes part of the agreement.

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Because the arbitration term in the agreement is valid, all matters surrounding the agreement must be submitted to arbitration. The arbitrator has the authority to bind the parties and order relief as is fit. Because New York has a strong policy favoring arbitration, the courts will not interfere if the arbitration clause is valid. The dispute should be submitted to arbitration.

(b) GEM's rights under the agreement.

GEM has the right to receive 300 pistons from PAR. If this is not done, GEM has the right to recover the difference between the market value of the pistons at the time of PAR's breach and the fair market value of the pistons purchased from another source, including any incidental damages.

The issue is whether the correspondence between GEM and PAR constituted a valid requirements contract between the parties, and if so, whether the term requiring a \$10,000 down payment became a part of the contract.

The rule is that between merchants, defined previously, confirmatory memoranda will be binding on the parties as long as, under the UCC, the items are identified and authority is determined. The UCC also states that additional terms, which do not materially alter the agreement will become part of the contract if not objected to within 10 days. An exception to this is where the parties have prior dealings.

It should also be noted that in a contract between merchants under the UCC, consideration is not needed to hold an offer open for any period of time. Here the parties have dealt together on "many occasions" and no down payment was ever required prior to this agreement. Because of their prior dealings, the down payment term did not become part of the agreement. Unlike the arbitration term discussed in Part (1), the party to be charged did not sign the memoranda indicating the clause. Because no one from GEM signed off or affirmatively consented to the additional term for a down payment it did not become part of the contract.

GEM may only receive 300 pistons because their order for 1000 pistons came 4 months after making the contract. Under the UCC, an option contract is only required to be held open for 3 months. It may be held open longer, but there is no requirement that it be held open longer.

GEM is entitled to the difference between the fair market value of the 300 pistons at the time of contract and that of the pistons at the time of PAR's repudiation. Although the agreement between PAR and GEM did not state a price for the pistons, under the UCC, in a contract between merchants, if a price term is left out, a contract may still be formed, and the price term will be deemed to be the fair and reasonable price at the time of contracting. Because the price term was omitted in the GEM/PAR contract, it will be whatever was the fair market value at the time of the contract.

The Rights and Duties of PAR.

PAR has an obligation to ship 300 pistons to GEM, at their fair market value at the time of contracting.

The issue is whether PAR's refusal to ship the pistons invalidated the agreement and whether there was a valid contract between the parties.

The rule as stated above is that a valid contract is made if, between merchants, an agreement is reached and some confirmatory memo is present.

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Because both of these requirements are present, PAR is bound to the contract for at least 3 months. PAR must deliver the pistons at a fair market value, or be liable for only cover damages (difference between contract price and replacement price) plus incidental damages.

Question-Two

In 1994, Sleepyville, a village in upstate New York, had experienced numerous unsolved residential burglaries.

On a Sunday evening in June 1994, at about 11 P.M., Sam, a resident of a nearby community, in response to a telephone call from his daughter, drove his car to Sleepyville. Sam's daughter was visiting a friend on Maple Avenue in Sleepyville, and Sam was annoyed because his daughter had promised to call him much earlier. Sam was unfamiliar with the streets in Sleepyville, so he drove slowly along Maple Avenue with the window on the driver's side open, pausing and looking carefully at each house, trying to locate the address his daughter had given him.

Joe, Sleepyville's only uniformed police officer, while driving a patrol car on Maple Avenue behind Sam, saw Sam pause and look at each house on Maple Avenue, and he became suspicious. While Sam was paused in front of one house, Joe pulled his patrol car alongside Sam's car, rolled down his patrol car window, asked Sam to identify himself, and inquired what Sam was doing there. Sam, ill-tempered, ignored Joe, rolled up his car window, and kept on driving. His suspicions heightened, Joe turned on his car's overhead turret light and, using his loudspeaker, ordered Sam to pull over to the curb. Sam did so.

When Joe got out of his patrol car and walked to Sam's car, he saw a handgun lying on the rear seat of Sam's car. Joe immediately ordered Sam out of his car and, fearing for his own safety, he patted down Sam's outer clothing, searching for another weapon. Joe found no other weapon, but felt what he believed was an object used to hold illegal drugs. He reached inside Sam's jacket and removed a vial containing crack cocaine.

Joe immediately advised Sam that he was under arrest for criminal possession of the gun and crack cocaine, and ordered Sam to get into the patrol car. Sam then shoved Joe and ran down the street. Joe was not injured and, after a brief chase, Joe subdued Sam, forced him into his patrol car, and drove him to the police station. Sam was subsequently indicted for criminal possession of the handgun and the crack cocaine, and also for resisting arrest and assaulting Joe.

Before Sam's trial, Sam timely moved to suppress the handgun and the crack cocaine. The court granted both branches of the motion. Sam thereafter waived his right to a jury trial and proceeded to trial before the court on the charges of resisting arrest and assaulting Joe. Upon proof of the foregoing relevant facts, the court found Sam guilty on both charges.

- (a) Was Sam's motion to suppress the gun properly granted?
- (b) Was Sam's motion to suppress the crack cocaine properly granted?
- (c) Was Sam properly convicted of resisting arrest?
- (d) Was Sam properly convicted of assault?

ANSWER TO QUESTION TWO

(a) Sam's motion to suppress was properly granted. The issue here is whether the gun was the product of an illegal stop and, hence, must be suppressed as "fruits of the poisonous tree."

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Under New York and federal law, a police officer may make reasonable inquiries of a person, such as identification. Further, under both New York and federal law the police may detain a person if the officer has reasonable suspicion that criminal activity is afoot, i.e., a crime is about to happen or is currently happening. However, such reasonable suspicion cannot arise from a mere failure to answer the officer's inquiries.

It should be noted that the Fourth Amendment to the U.S. Constitution, made applicable to the states through the 14th Amendment, requires that in the absence of an exception, the police or law enforcement authorities need a search warrant before searching an area in which one has a reasonable expectation of privacy. This is because the 4th Amendment guarantees a right to be free from unreasonable search and seizure. However, one of the exceptions to this requirement (recognized by New York) is the "plain view" exception. Under this exception, if police are lawfully present on the premises, see an article which the police can clearly deduce to be illegal, the police may seize such object or article despite the absence of a search warrant.

However, to deter illegal police activity and to protect citizens' 4th Amendment rights, New York and federal courts have developed the "fruits of the poisonous tree doctrine." Under this doctrine or rule of law, any evidence seized as a result of illegal police activity will be suppressed, unless the taint of the initial search is cleansed.

Here, Officer Joe saw Sam driving "suspiciously." Hence Joe asked Sam to identify himself. This was permissible because the police have a right to inquiry. Sam ignored Joe -- this was permissible. Citizens are under no obligation to answer such inquiries. However, Sam's failure to answer caused Joe to have "his suspicions heightened" and, subsequently, Joe pulled Sam over. In so doing, Joe acted improperly. A police officer needs reasonable suspicion to believe criminal activity is afoot. As stated above, this suspicion cannot come from Sam's mere failure to answer Joe's inquiries. Hence, the stop was illegal.

When Joe walked up to Sam's car he saw the gun. However, the plain view exception does not apply because Joe was not lawfully present. Hence the seizure was illegal. Further, Joe was only present as a result of his illegal stop; hence the gun should be suppressed as a "fruit" of Joe's illegal stop of Sam. It should be noted an exception to the search warrant requirement would have to be present because Sam had a reasonable expectation of privacy within his car.

(b) Sam's motion to suppress the crack cocaine was properly granted. The issue here is two-fold. First, whether the crack cocaine (crack) was the result or fruit of an illegal stop and, second, whether Joe's pat-down search and subsequent seizure was lawful.

Since New York protects suspects against the seizure of such items (not believed to be weapons), the search and seizure was illegal under New York law. Consequently, under the "fruits of the poisonous tree doctrine" as well as the excessive stop and frisk search, the crack should be suppressed.

(c) Sam was properly convicted. The issue here is whether Sam could use force to evade an illegal arrest.

Under New York law, a suspect, in almost all cases, may not use force to evade an arrest, even if such arrest is illegal. This is known as the "no sock" rule. Here Sam "shoved" Joe when Joe advised him he was under arrest and ordered him into the car. Even though this arrest may not have been legal (see a and b), Sam was not privileged to use this force and to run away. Since Sam shoved Joe and ran away, he was properly convicted of resisting arrest.

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(d) Sam was not properly convicted. The issue here is whether Sam's shoving amounted to an assault.

New York's crime of assault is more like common law battery. The New York Penal Law states that an assault occurs when one causes a harmful or offensive contact. However, there must be some form of physical injury. Mere petty shoves are not sufficient. Here, Sam shoved Joe, but Joe was not at all injured. Because Sam's action consisted of a mere shove and Joe did not sustain any physical injury, Sam may not be convicted.

It should be noted, as above, that Sam's conduct was not privileged because New York follows the "no punch" rule.

ANSWER TO QUESTION TWO

(a) The motion to suppress the gun was properly granted. Because it was seized without a warrant, the issue is whether its seizure comes within any of the warrantless seizure exceptions to the 4th Amendment (and New York equivalent).

The exception that the police would rely on here is the plain view exception. The policy may validly seize weapons, contraband or other evidence of illegality that they have probable cause to believe are such that are in plain view, if the police have a legal right to be where they are when they see it. Here, however, the police did not have probable cause to pull over Sam's car, and so did not have the legal right to be where they were when they saw the gun.

Probable cause means more than mere suspicion; it means facts such that a reasonable person would believe that a crime is or has been committed. Here, although Joe did have grounds to request information from Sam while Sam's car had paused, the standard is whether Joe was acting on "whim or caprice," and here he was not because Sam was driving slowly and looking at each house, consistent with "casing" the houses. Sam was under no duty to respond under New York law. Moreover, Sam's failure to respond under New York law is not sufficient to give Joe probable cause to stop Sam's car. None of the other facts about Sam's behavior -- merely driving slowly, looking at houses, and failing to answer Joe's questions -- rise to the level of probable cause to believe that Sam was committing a crime.

(Note that the other exception for pulling over a car -- administrative stops, for example roadblocks for alcohol, which require a set method for pulling over cars (e.g., every third car) is not applicable here. Nor can Sam be deemed to have consented by pulling over, in light of Joe's use of the turret lights and order to stop.)

Joe's seeing the gun was thus the result of his illegal stop of Sam's car, and under the fruit of the poisonous tree doctrine, must be excluded. (Under the fruit of the poisonous tree doctrine, evidence obtained as a result of a prior illegal search or seizure must be excluded, absent an exception such as inevitable discovery. No such exceptions apply here.)

(b) The motion to suppress the cocaine was properly granted, for two reasons. First, for the same reasons as discussed above, the pat-down was the result of Joe's illegal stop of the car, and should therefore be excluded under the fruit of the poisonous tree doctrine. Second, even if that doctrine did not apply, Joe's pat-down exceeded the permissible scope of the pat-down under New York law. An officer may pat down a suspect he believes may be armed once he has stopped them. Second, on a reasonable suspicion that criminal activity is under foot. Under New York law, however, he may only frisk for weapons, whereas under federal law (Terry), he may pat-down for weapons and contraband under the "plain feel" doctrine. Here, Joe had a reasonable suspicion that Sam might be armed, based on seeing the gun, and could seek to ensure his safety by performing a pat-down for weapons. When Joe, however, felt the vial and proceeded to search inside Sam's

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jacket and seize it, his actions were unlawful under New York law, because the seized object as a result of the pat-down was contraband, not a weapon. (Joe's actions might have been lawful if he had had reasonable suspicion that Sam had contraband on his person. The facts here, however, did not give Joe any grounds for such a suspicion, given that he had only seen a gun before and no other evidence or activity suggesting drugs.) The cocaine was therefore properly excluded under New York law on this ground alone.

(c) Sam was properly convicted of resisting arrest.

To be convicted of resisting arrest, the following elements must be present: (1) resisting a lawful arrest by (2) someone who the defendant knows is a police officer. The second element is met here. Sam knew that Joe was a police officer because he was driving a marked patrol car and was in uniform.

The issue is on the first element, specifically whether Joe's arrest of Sam was lawful. To be a lawful arrest, Joe must have a reasonable belief that a crime is being committed in his presence. Here, the presence of the gun and the cocaine gave Joe such grounds. The fact that such evidence may have been unlawfully obtained and seized, while it goes to whether the evidence is admissible at trial, does not affect the lawfulness of Sam's arrest for purposes of the resisting arrest charge. Because the arrest was lawful, and Sam resisted the arrest when he shoved Joe and ran away, the conviction was valid.

(d) Sam's conviction for assault is invalid. Under New York law, an assault involves an unlawful touch that causes injury to someone else. (It is thus closer to common law battery rather than common law assault, where no touching -- only an apprehension of an unlawful touch -- would be required for an assault, and only a touch -- not injury -- would be required for assault.)

The injury need not be great, but some injury is required. Here, the facts clearly indicate that Joe was not injured. One of the essential elements for the crime was not present.

(Sam does not have a self-defense defense. To be valid, again, the arrest would have to be outside of the privilege. Here, Joe had reasonable grounds for believing that Sam was committing a crime, and so had a privilege to use force to arrest Sam.)

Question-Three

Arthur, a salesman, and Hester, a management consultant, were married in 1980 and thereafter purchased and resided together in a one-family house in the Bronx. In 1981, using \$1,000 the couple had received as a wedding present, Hester opened her own management consulting business. Arthur took no part in Hester's business. Throughout their marriage, Arthur and Hester filed separate tax returns, maintained separate financial records, and contributed equally from their respective incomes to household expenses.

In 1982, Hester began a romantic relationship with Roger and in 1983, without Arthur's knowledge, Hester used funds earned in her consulting business to make a substantial down payment on Pearl Acre, a one-family house in Dutchess County. That same year, at Hester's invitation, Roger began living at Pearl Acre. Roger did not pay rent, but paid the utility bills and real estate taxes. He told neighbors and others that he owned Pearl Acre. Hester often stayed overnight at Pearl Acre with Roger. She made various improvements to the property over the years and paid off the purchase money mortgage on the property with funds earned in her consulting business.

Arthur learned of Hester's relationship with Roger in March 1994 and immediately commenced an action in Supreme Court, Bronx County, seeking a divorce on the ground of adultery and

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demanding equitable distribution of the couple's marital assets. Hester timely filed an answer. Arthur thereafter served a demand upon Hester for an affidavit of net worth and a demand for discovery and inspection of all financial records of Hester's consulting business. Hester moved for a protective order barring discovery of the financial records of her consulting business, arguing that such discovery was impermissible because Roger had never taken part in the business and the couple had always maintained separate financial records. The court (1) denied Hester's motion. Hester thereafter responded to Arthur's demands, but deliberately failed to disclose in her affidavit of net worth her ownership of Pearl Acre, now worth \$100,000.

In September 1994, Hester and Arthur entered into a written stipulation settling the divorce action. Although the stipulation of settlement included statements that each party had made full disclosure of all assets and had entered into the agreement in reliance upon the representations of the other, Hester had not disclosed her ownership of Pearl Acre. The stipulation identified and valued the couple's assets as: the couple's marital residence in Bronx County (\$100,000); Hester's consulting business (\$50,000); and \$50,000 cash. The stipulation further provided that the value of all of the assets would be divided equally, with Arthur receiving the marital residence and Hester receiving the cash and the consulting business. The stipulation of settlement survived the final judgment of divorce, which was entered on November 30, 1994.

In January 1995, Hester ended her relationship with Roger and demanded that he vacate Pearl Acre. Roger, who had paid substantial sums for utilities and real property taxes for Pearl Acre over the years, asked his attorney what ownership rights, if any, he had to Pearl Acre. His attorney advised him (i) that he could claim title to Pearl Acre by adverse possession. Before commencing an action to determine title, Roger's attorney filed a notice of pendency with the County Clerk of Dutchess County, and served a copy of the notice upon Hester. A week later, Roger duly filed and served his summons and complaint on Hester. Hester moved to cancel the notice of pendency on the ground that no action had been pending when it was filed. The court (2) denied the motion.

Thereafter, Arthur discovered that Hester had purchased Pearl Acre in 1983 and that Roger had been living at Pearl Acre since that time. Arthur immediately moved, on papers including affidavits setting forth the foregoing pertinent facts, to set aside the settlement stipulation dividing the couple's assets, asserting that he would not have agreed to permit Hester to receive the consulting business and the couple's cash had he known about Pearl Acre. Hester opposed Arthur's motion but admitted that she had failed to disclose her ownership of Pearl Acre. The court (3) denied the motion without a hearing, holding that the stipulation was final and could not be disturbed.

(a) Were the numbered rulings (1), (2) and (3) correct?

(b) Was the attorney's advice (i) correct?

ANSWER TO QUESTION THREE

(a) 1. Hester's motion to bar discovery

The Court correctly denied Hester's motion to bar discovery of her consulting business records. The issue is whether Arthur is entitled to records of his wife's consulting business, commenced after marriage, in a divorce action when the wife denies the consulting business is a marital asset.

Discovery under the New York CPLR is broad. A party may obtain discovery of documents or things that may lead to admissible evidence at trial and that are relevant. Here, Hester is claiming

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the consulting business assets are not relevant because she takes the position that the business is a separate and not a marital (property of both husband and wife) asset.

Hester's assertion is incorrect under the law of Domestic Relations in New York. Under New York's equitable distribution law, pursuant to which assets are allocated upon divorce, marital assets are divided equitably. Marital assets are assets which are attributed to the couple, as opposed to separate assets which are treated as solely belonging to the individual. Separate assets do not get divided in divorce.

Separate assets include assets owned prior to marriage and gifts solely to one spouse.

Marital assets include all income earned during the marriage, gifts to the couple, property obtained and investments made during the marriage (and incremental increases of these assets).

Here, the consulting business is a marital asset. The issue is whether a business started post-marriage, using as its initial capital a gift to the couple, is a marital asset, notwithstanding separate financial records and Arthur's non-involvement in the business.

As stated previously, because the business was started after they married, the business squarely falls within the definition of marital assets. That the couple keeps separate financial records and contributes equally is irrelevant to whether the business is a marital asset. Moreover, Hester started the business with a \$1,000 gift that she and Arthur received as a wedding present. This \$1,000 is a marital asset and its investment value in the business is also a marital asset within the New York DRL.

Accordingly, because the financial records of Hester's business were clearly relevant to the divorce litigation, the court properly denied her motion for a protective order.

A protective order should only be granted in limited circumstances not present here.

2. Motion to cancel the notice of pendency.

The court correctly denied Hester's motion to cancel the notice of pendency. The issue is whether a notice of pendency is appropriately filed prior to service of process.

Under the New York CPRL a notice of pendency is a provisional remedy that is available when the subject matter (land) of the litigation is directly at issue. For example, in a foreclosure or partition action, a notice of pendency is appropriate as to the real estate.

The effect of the notice is to put others on notice of the filer's claim to the real estate and gives the filing party a priority interest in the land.

There is no requirement of a court order or the posting of a bond for a notice of pendency. Moreover, the notice may be filed before service of process, as long as process is served within 20 days. If process is not duly served in that time, the notice expires.

The notice must also be filed in the county where the land is situated.

Here, Roger was entitled to file the notice of pendency prior to serving process as long as he filed process within the requisite period. Here, Roger filed process a week from filing the notice. Because this falls within the 20 day period, Roger's filing was valid. That "no action had been pending," as Hester asserted, is therefore of no consequence and the court correctly denied her motion to cancel the notice.

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3. The court incorrectly denied Arthur's motion to set aside the settlement of the divorce action. The issue is whether a stipulation settling a divorce may be set aside where a party to the agreement had made material misrepresentations that acted as a fraud on the other party.

Although in most respects the divorce agreement was valid -- it was in writing and signed by both and did not contain provisions contrary to public policy -- the agreement should be disregarded in the face of manifest fraud.

Arthur signed the agreement under the mistaken impression that Hester had disclosed all her assets. As the contract provided, each party claimed to fully disclose their assets and had relied on those representations. Where a party, like Hester, materially and intentionally misleads the other contracting party as to a marital fact with the intention of inducing reliance on the misrepresentation and the party does justifiably rely and is economically harmed, Hester has defrauded Arthur.

A marital agreement, like any other contract, can be set aside on the ground of fraud. Fraud deprives the party's capacity to assent to the terms of the contract.

Thus, the court should have set aside the settlement stipulation. Especially in the domestic relations area where the court has the power to equitably distribute property and set maintenance in its discretion, the court should have exercised its discretion to void the stipulation in such exceptional circumstances.

(b) Roger's attorney's advice re adverse possession.

Roger's attorney was mistaken in his advice that Roger could obtain title to Pearl Acre by virtue of adverse possession. The issue is whether Roger can adversely possess property Hester permitted him to inhabit, even though he pretended to own it in some ways.

Adverse possession vests title to property in an individual who satisfies the following elements.

Under New York Real Property Law, adverse possession requires that the individual: (1) actually inhabit the property, living there as a true owner and using it as a true owner would; and (2) that the actual possession be exclusive. The possessor cannot recognize any other interest in the property; and (3) that the possession be hostile and under a claim of right. That is, possession is hostile to the owner. This means that the owner has not given permission for the possessor to use the property and he or she is acting as if he or she has a right to own the property; and (4) the possession must be open and notorious. That is, obvious to the observer. This puts the owner on notice that someone is claiming a right to the property; and (5) possession must be continuous for the statutory period. In New York, the statutory period is 10 years. Continuousness can include seasonal use.

Notwithstanding the fact that Roger tells neighbors and others that he owned Pearl Acre, and therefore seems to assert a claim of right to it in an open and notorious manner, Roger is living there with Hester's permission. Therefore, his possession is not hostile to Hester's interest in the land. That he paid taxes and bills does not change the result. Moreover, Hester paid the mortgage and improved the property, so she was asserting her ownership of the property.

The other elements are, however, largely met. But for her permission, the attorney's advice would be correct. Roger is a mere licensee.

Roger occupied under a claim of right because he exerted ownership incidents by paying taxes and bills and telling others he owned the land.

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Roger's occupation was obvious to all and to Hester. Thus it was open and notorious.

His occupation was actual -- he actually lived there. But it was not exclusive. By allowing Hester to pay the mortgage and improve the property, he recognized Hester's superior ownership interest.

Finally, his possession was continuous for 12 years from 1983 to 1995, thus it met the statutory period.

Thus, Roger's attorney was incorrect in concluding he could acquire title to Pearl Acre by adverse possession, because Roger possessed with permission (not hostile) and non-exclusively.

ANSWER TO QUESTION THREE

(a) 1. The court's order was correct. The issue is whether a spouse's business is marital or separate property under New York's Domestic Relations Law ("DRL") of Equitable Distribution of Assets and what discovery is permitted.

The DRL provides that all marital property shall be subject to equitable distribution. Equitable distribution is the allocation of assets to the parties to the marriage and is based on statutory factors including the finances of the parties, the duration of the marriage, special needs (such as custody of children), and issues of waste, contribution and tax consequences. Marital fault is not a consideration in the property distribution though it may be in the court decree of maintenance.

The court must determine which property constitutes separate property not subject to equitable distribution and which is marital. Title does not determine this issue for property acquired during the marriage. Here the business was begun with funds that were jointly held and it must be considered marital property, though the contributions of each partner to the development of the asset will be a consideration in distribution.

The second issue is whether discovery is appropriate. New York CPLR limits discovery in marital actions and requires a court order to ensure that parties do not overstep the bounds. There is, however, some discovery regarding the parties' financial assets, to ensure a fair negotiation of an arrangement and ultimate decree of divorce. Hester is not entitled to a protective order (an order of the court barring the discovery demanded in Arthur's notice) and the court appropriately denied the motion because the business developed during the marriage with assets that were marital property and because title or separate financial records is not determinative.

2. The court appropriately denied Hester's motion to cancel the notice of pendency. The issue is whether a lis pendens may be filed prior to service of the complaint and summons.

A lis pendens is a provisional remedy that places a cloud on title. By filing such an impediment on title, all potential interior of property by a claimant who does not hold actual title for a sufficient number of years to acquire title by operation of law).

A lis pendens can be filed prior to issuing the summons, as long as the summons and complaint are filed within 30 days. The notice is filed in the County where the property is located with a copy of the complaint.

Here, Roger appropriately filed because Pearl Acre is in Dutchess County and he served the summons and complaint within the 30 day period because he served Hester a week later. (Note: the facts do not indicate whether Roger filed a copy of the complaint with the notice. If not, Roger did not satisfy the filing requirement.)

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3. The court erred in refusing a hearing.

The issue is whether a couple's agreement may be set aside based on misrepresentation which formed the basis of the agreement.

A written separation agreement which is made without duress, not unconscionable, incorporated and survives a divorce decree, is a valid contract between the parties and is treated as a contract under the domestic relations law. Breaches of agreement and problems with formation, however, are also interpreted under contract principles. (Note: the court will ordinarily not set aside an agreement without a showing of extreme hardship, but this will not apply if the contract itself is void.)

Here, when Hester and Arthur contracted to separate their assets, they did not do so with full information because Hester committed fraud. Fraud is a knowing misrepresentation of a material fact which is intended to induce reliance and does induce reasonable detrimental reliance, causing damages. Where a confidential relationship exists, as here, the parties must affirmatively disclose information that is material to the contract. Because Hester intentionally concealed the information about Pearl Acre, she violated this requirement and fraudulently induced Arthur to enter the agreement. Therefore, the court erred in denying Hester's motion without a hearing based on a "finality" assessment of the contract.

The motion required the court to address the validity of the contract to determine whether it was enforceable on its terms. The court refused to do so and thus erroneously treated a voidable contract as a duly negotiated and enforceable one.

(i) Roger in the statutory period of 10 years (CPLR) in satisfaction of the requirement of (1) adverse and hostile possession that is (2) open and notorious, (3) for a continuous and uninterrupted period as required under the Real Property Law ("RPL"), and (4) in actual and exclusive possession. Adverse and hostile means under claim of right to ownership even though the adverse possessor may know that he has no such right. (Note: a "constructive" adverse possessor gives a person inquiry notice that someone claims ownership. Here Roger informed neighbors that he owned Pearl Acre and paid the utility bills and real estate taxes, which are normal ways to claim ownership. Thus, Roger has satisfied the open and notorious requirement, because even Hester should be informed of his claim when she visits the area. Neighbors would normally consider Roger the owner and a stranger who viewed the arrangement with an eye to purchase would inquire if he were the owner.

Roger also has lived on Pearl Acre continuously and uninterrupted by abandoning it so he satisfies that requirement. Continuity is such as normal ownership of the land would result in -- a home is normally occupied year round by one who associates with neighbors. Thus Roger satisfies the continuity requirement because he has occupied the land continuously throughout the statutory ten year period from 1983.

Exclusive possession means that the adverse possessor has held the property and that the true owner has not been on the property as owner. Actual possession means that the adverse possessor actually occupies the entire tract of property.

Roger does not satisfy the requirement of actual and exclusive possession. Hester has been in possession of Pearl Acre as owner at the same time as Roger. She has acted as owner by making improvements and by paying off the purchase money mortgage on the property. Thus, while Roger has satisfied many of the requirements for adverse possession, he has failed to remain in actual and exclusive possession due to Hester's co-occupancy and claim of ownership right.

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The fact that Hester has retained these rights also suggests that Roger's occupancy has not been genuinely adverse. To be adverse, a possessor must hold without permission of the actual owner. Hester has, in fact, given Roger permission up until 1995 when she made her first demand that he vacate upon the end of their relationship. Thus, although Roger has occupied the house and claimed to others that he is the owner, his possession is not adverse.

Question-Four

On February 15, 1995, Amy, a State X domiciliary, was injured in a car accident which occurred on a public highway in State X near the New York State line. Amy was a passenger in a car driven by her friend, Bill, which collided with a car owned and driven by Carl. Bill was domiciled in Westchester County, New York, and Carl was domiciled in State X.

The accident occurred while Bill was driving Amy to her home in State X and Carl was driving to Suffolk County, New York, where he owned a vacation home. Bill and Carl were both negligent. Following the accident, Amy was taken by ambulance to a nearby hospital in New York, where she remained for six weeks under treatment for her injuries.

On June 1, 1995, Amy, seeking to recover \$500,000 for her injuries resulting from the accident, filed with the Clerk of the Supreme Court, Westchester County, a summons and complaint naming Bill and Carl as defendants. The summons and complaint were personally served on Bill in New York and on Carl in State X.

Bill duly served an answer, consisting of a general denial and an affirmative defense based on the State X statute. Carl also duly served an answer, consisting of a general denial and an affirmative defense that the court lacked personal jurisdiction over him.

Carl then timely filed a notice of removal in federal district court for the Southern District of New York to remove the action to that court. Amy duly moved in that court to remand the action to Supreme Court, Westchester County. The federal district court (1) granted Amy's motion.

Amy then moved to dismiss the affirmative defense asserted in Bill's answer. The court (2) denied Amy's motion. Amy also moved to dismiss Carl's affirmative defense, asserting that New York has personal jurisdiction over Carl based on the facts that (a) Amy's injuries were treated in New York, and (b) Carl owned real property in New York. Carl cross-moved to dismiss the complaint against him. The court (3) denied Amy's motion and granted Carl's cross-motion.

Upon trial of the action, Amy's lawyer issued a subpoena to compel Witt, who resided in State X near the location where the accident occurred and who witnessed the accident, to attend the trial and give testimony. The subpoena was personally served on Witt at his residence in State X, and at the same time he was tendered the authorized traveling expenses and one day's witness fee. When Witt refused to travel the 95 miles between his residence and the Westchester County Court House, Amy moved to compel compliance. The court (4) granted the motion.

Were rulings (1), (2), (3) and (4) correct?

ANSWER TO QUESTION FOUR

(2) The court's ruling was correct. The issue is whether New York will apply State X's guest statute in Amy's suit against Bill.

Ue applied is a law regulating conduct or a loss distribution rule. If it is the former resulting in the latter the New York choice of law rules with respect to torts, the first inquiry is whether the law sought to be of the situs being applied to tort actions. If the law is a loss distribution rule, New

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York employs the governmental interests analysis approach. This approach requires the court to look at the competing interests of the states if the plaintiff and defendant have different domiciles and one is a domiciliary of the situs, the law of the situs should be applied if it helps the domiciliary. If not, the law State X (which New York does not have) is a loss distribution rule. Thus, the governmental interests analysis will be applied. In this case, the victim, as well as one of the defendants, are domiciliaries of State X. Moreover, the accident occurred, the defendant attempting to use the guest statute. State X has a guest statute, while New York does not. The policies behind State X's guest statute is to prevent ungrateful passengers from recovering against its drivers and to protect its insurance companies from collusion because it wants its citizens to be able to recover for their injuries, regardless of their status. Here, Amy, the victim, is not a domiciliary of New York, so New York's policy would not be served by refusing to apply the guest statute. Moreover, the accident happened in State X and Amy is a State X domiciliary. To apply the guest statute would not promote State X's policy of protecting its drivers from ungrateful guests or to protect its insurance companies from collusion, since B's insurance company, presumably a New York one, would be required to pay. Under the *Neumeier* rules, Amy and Bill are not domiciliaries of the same state and Amy is a domiciliary of State X. If the law of State X, the situs, would help Amy, it should be applied, but it doesn't. However, unless New York shows an overwhelming interest, the law of State X should still be applied. Since New York does not have an overwhelming interest, the law of State X should be applied. The court's decision was correct.

(3) The court's decision was correct. The issue is whether the New York court has personal jurisdiction over Carl under the long-arm statute.

In order to adjudicate claims against a party, the court must have personal jurisdiction over the party. Traditional bases for personal jurisdiction include physical presence at the time of service, domicile and doing business. Under New York's long-arm statute, the court will have jurisdiction over a defendant if the claim against him arose from: (1) transaction of business in New York; (2) contracting to provide goods and/or services in New York; (3) commission of a tortious act in New York; (4) commission of a tortious act outside New York causing injuries in New York; or (5) the ownership, use or possession of real property in New York.

In this case, none of the traditional bases for personal jurisdiction exist because Carl was served in State X, was a domiciliary of State X and was not doing business in State X. Amy must therefore rely on the long-arm statute. The first three bases are clearly inapplicable. The fourth basis is also inapplicable because although Amy was treated for her injuries in New York, her injuries did not arise last basis is also inapplicable because while Carl may own real property in New York, Amy's negligence claim does not out of Carl's ownership of such property. Therefore, the court lacks personal jurisdiction over Carl.

An eyewitness to the accident.

Under the CPLR the court can require the attendance of a material witness by subpoena so long as the witness resides within 100 miles of the courthouse and is reimbursed for traveling expenses and paid a witness fee. Carl resides within 100 miles of the courthouse, and was paid traveling expenses and his witness fee. Therefore, the court could compel his compliance.

ANSWER TO QUESTION FOUR

(2) The state court properly denied Amy's motion to dismiss, under New York's conflict of laws principles, a New York court should apply its own law (which does not have a guest statute) or the law of State X (which does have a guest statute).

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Notably, Bill's affirmative defense should only be dismissed if the law will apply to this dispute between Bill and Amy and so he should be able to proceed on this defense.

Though New York at one time took a vested rights approach to these sorts of conflicts, as the "Governmental Interests" analysis has developed, New York courts will look first to whether the laws in question are "rules of the road" which govern conduct. If the law is conduct governing, then the law of the location will be applied.

Here, however, we have a law concerned with loss distribution. That is, the dispute is over whether and when a driver can be held liable for injuries to passenger in that car. As a loss distribution issue, the New York court will apply a *Neiermeyer* analysis to assess which State's law is most appropriate under the circumstance. That analysis calls for the law of the state where both parties are domiciled to be applied no matter where the injury took place. Here, however, both parties are not domiciled in the same state. Specifically, Bill is a New York domiciliary while Amy is a domiciliary of State X.

The next step, then, in this conflict of law analysis is to assess whether the law of the other forum is designed to favor the plaintiff's cause of action. In this instance, the guest statute of State X is actually harmful to the plaintiff, Amy, as it will make it more difficult for her to recover in her tort claim. (She will have to prove gross negligence rather than simple regular negligence.)

Because of the nature of the laws in conflict and the fact that the accident occurred in State X and Amy is from State X, the final result of New York's conflict analysis is to have the law of State X defense based on State X's guest statute and thus it was proper for the state court to deny the motion by Amy to dismiss Bill's affirmative defense.

(3) The court properly granted Carl's motion to dismiss the complaint against New York's long-arm statute or otherwise.

Under the CPLR, there are a number of grounds upon which a plaintiff can base personal jurisdiction against a defendant. Specifically, if the defendant's motorist jurisdiction statute. Though Amy may be able to make reasonable claims under a number of grounds, they all seem to ultimately fail her.

Though Carl was driving to his vacation home in New York, the accident was still in State X and Carl had process served on him in State X. Thus Amy cannot claim Carl's presence provides jurisdiction, and further his vacation home does not count for domicile. (The facts state that Carl is a State X domiciliary.) Further, the fact that the accident was not in New York precludes jurisdiction based on the motorist statute. And the "doing business" ground only applies to those engaged in systematic and continuous commercial contact with New York. And, as for consent, though one might be able to argue that Carl's attempt to remove the action was tantamount to a consent to jurisdiction, it is not the case that such a filing will be deemed to be a form of consent.

So, we are left with jurisdiction only possible via New York's long-arm statute (CPLR 302). That statute provides for jurisdiction if a tort was the consequence of (1) transaction of business in New York, (2) a contract for the sale of goods or services in New York, (3) a tort committed in New York, or (4) a tort committed elsewhere with harm arising in New York.

Again because the accident took place in State X, the only real hope for Amy under the long-arm statute comes from (4) a tort committed elsewhere with harm arising in New York as the harm occurred in New York because she was taken to, and treated for 6 weeks in, a New York hospital. However, it is questionable whether treatment in New York can qualify as harm in New York when all of the accident occurred in State X. (Thent.)

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In any event, even if a court could find that some harm occurred in New York, this basis for long-arm jurisdiction requires some additional linkage in New York. Specifically, the plaintiff must show that the defendant was providing goods in New York based on this out of state tort. Such additional linkage appears wholly missing here, as Carl's ownership of a vacation home in New York does not suffice.

Consequently, long-arm jurisdiction also could and done, Carl's dismissal was proper.

(4) The court's granting of the motion to compel compliance with the subpoena was wrong. The issue concerns a state court's power to order a witness that resides in a foreign state to appear before it.

Under the CPLR a court generally has the power to compel witnesses to appear before it in accordance with a duly authorized subpoena as long as that person receives the appropriate traveling and witness expenses and fees. However, for a New York court that power only extends to New York locations as the court lacks the power to order someone from another state to appear no matter that the other resident lives nearby.

Whether the distance is 95 miles from the courthouse or across the country, the court's powers are limited and so the motion here should not have been granted.

Question-Five

Hal, a resident of Albany County, New York, duly executed a will, the dispositive provisions of which read as follows:

"1. I give \$200,000 to my wife, Win.

2. I give all the residue of my estate to my brother, Bob, and to my friend, Foy, in equal shares."

Hal died in August 1995 without having revoked. Hal was survived by Win and an infant son, Sam, born in December 1994. He was also survived by Bob and Foy.

Hal's net estate consisted of assets worth \$900,000 after payment of debts, estate tax to Win, the named beneficiary of one of the policies, and paid \$100,000 for the benefit of Sam, the named beneficiary of the other policy.

Win has duly filed an election to take against the will. Bob, who is a widower, has duly filed a renunciation of the residuary legacy provided for him in Hal's will. Bob's only child is his twenty-two year old daughter, Dee. Sam, by his duly appointed guardian ad litem, has asserted that he is entitled to receive \$450,000 as his share of Hal's estate.

(a) To what extent, if any, is Hal's estate entitled to claim a marital deduction on its Federal estate tax return?

(b) How should Hal's net estate be distributed?

ANSWER TO QUESTION FIVE

(a) Hal's estate is entitled to claim a marital deduction of \$300,000 on its Federal estate tax return. The issue is what portion of Hal's estate is eligible for the marital deduction.

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The general rule is that a marital deduction consists of (1) outright dispositions of property to the spouse and (2) property that qualifies for the QTIP (Qualified Terminable Interest Property) deduction. QTIP does not apply under these facts, so we turn to determine what outright dispositions are given to Win, Hal's wife.

The elective share statute provides that a spouse is entitled to \$50,000 or one-third of the deceased spouse's estate, whichever is greater. The facts state that Hal's net estate is worth \$900,000 and there is no information on any testamentary substitutes that would normally be added in. The two life insurance policies are nonprobate assets that pass outside the will, so they are not included as testamentary substitutes. Therefore, Hal's net estate is \$900,000 and Win's elective share, she is not. If the outright dispositions provide some but not all of the elective share amount, then she is entitled to take a limited elective. Under the will, Win is provided for \$200,000. Since this does not equal the \$300,000 elective share, she can take a limited elective share of \$100,000. Where the will does not fully provide for the spouse's elective share all of the other beneficiaries are required to contribute pro rata. Therefore, to prevent the spouse from being disinherited, Win will also receive the \$200,000 proceeds from the first life insurance policy.

Rights of Son, Sam.

The issue is whether Sam will take as a pretermitted child. Sam is entitled to the \$100,000 life insurance policy only. Sam will not receive anything under the will and does not have to contribute to Win's elective share.

Since Sam was born after Hal's will was executed, he is a pretermitted child. A pretermitted child will only take where (1) he is not provided for by will, (2) he is not provided for by any lifetime gifts (insurance policies) and (3) he is born or adopted after the will.

Here, Sam was born after the will, but since Hal provided for him through the life insurance policy, he is eligible to receive as a pretermitted child. As a pretermitted child with no other siblings, Sam would have received his intestate share which would have been taken off the top before the will was distributed. But since he was provided for through the life insurance policy, he will not take by will. Therefore, the guardian ad litem's assertion that he is entitled to \$450,000 is incorrect. Sam gets the \$100,000 life insurance proceeds.

Rights of Bob, Dee and Foy.

The issue is whether the anti-lapse statute applies to Dee.

The residuary estate, \$600,000 after Win's election, should be equally divided between Dee and Foy. Where a residuary legatee is an issue, brother, or sister of the deceased, the anti-lapse statute applies and his issue will take.

Bob renounced (disclaimed) his gift under the will which requires a signed writing that is acknowledged, accompanied by an affidavit stating that no consideration was received for the disclaimer, and it is irrevocable and filed with the Surrogate within 9 months of the testamentary letters. The facts state Bob "duly" renounced his gift under the residuary. New York law treats him as though he predeceased the testator. The anti-lapse statute applies and Dee receives his share.

Therefore, Bob takes nothing, and Dee and Foy each take \$300,000 (1/2 each of the \$600,000) after having each given Win \$50,000 totaling her \$100,000.

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ANSWER TO QUESTION FIVE

(a) Hal's estate is entitled to claim a marital deduction for \$500,000 on its federal estate tax return.

The issue is what assets are includable in the gross estate and what asset are subject to the marital deduction. Assets can be excluded from a spouse's taxable estate if they pass to the spouse ataxes to the spouse's death.

In general, the gross estate includes all probate transfers, several testamentary substitutes as well as life insurance policies where incidents of ownership have retained (unless insurance policies are assigned more than 3 years before death). The gross estate also includes all property over which the decedent held a general power of appointment (whether inter vivos or testamentary). In this case, Win has elected to exercise her elective share. Accordingly, she is entitled to one-third of the net augmented estate or \$50,000, whichever is greater, plus 6 percent interest beginning 7 months after issuance of letters.

The life insurance policies will not be included in determining tha augmented estate because they do not constitute testamentary substitutes, even if paid to the surviving spouse. Accordiuse she was given outright disposition of \$200,000 she can receive \$100,000 moge in reliance on the elective share right. The additional \$100,000 will be contributed pro rata by the other beneficiarht pursuant to the elective share is subject to the marital deduction because it will be includable in Win's gross estate to the extent not consumed or disposed of. In addition, the life insurance proceeds of \$200,000 paid to Win qualify for the marital deduction for the same reason. Accordingly, the total marital deduction is \$500,000.

(b) Hal's estate should be distributed as follows:

(1) Wife, Win, gets \$100,000 elective share, \$200,000 outright disposition and \$200,000 from life insurance policy.

(2) Dee takes Bob's residuary share = \$250,000.

(3) Foy maintains her residuary share = \$250,000.

Bob: fecause we are told Bob has duly filed a renunciation, the issue is who takes when a will beneficiary renounces. (To be vafidavit attesting to no consideration received for the renunciation, irrevocable and filed with the Surrogate within 9 months of decedent's death.) When a will beneficiar.

In this case, Bob was testator's brother and has left issue, Dee. Generally when a gift of the residuary estate is made to more than one person and gift to one fails, the other residuary beneficiaries share the whole thinn unless the anti-lapse statute applies. The anti-lapse statute trumps the residuary rule.

Therefore, Dee will take Bob'titled to rights under the pretermitted child statute.

The rule is that when a testator executes a will and thereafter has or adopts a child, if the re there are other children, the after-born child would share their gift unless it was only limited provision, in which case child would be entitled to intestate share.]

In this case, Sam was an after-born child because he was born after the will was executed. He was neither mentioned nor provided for in the will. However, he was provided for by life-time settlement. The life insurance policy qualifies as a life-time settlement. Accordingly, Sam is not

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entitled to claim an amount of Hal's estate that would equal his intestate share. He is only entitled to the proceeds of the life insurance policy. Thus, he gets \$100,000.

The residuary estate: Will be equally divided between Foy and Dee, each taking \$250,000.

Win: takes \$200,000 outright and \$200,000 by life insurance policy and \$100,000 by elective share.

Sam: takes under the insurance policy = \$100,000.

Question-Six

Ann, an expert in the data processing business, is president and a director of Comco, Inc (COM), which sells computer equipment and software. Ann owns 10 percent of COM's outstanding common stock. Ann is also chairman of the board of Info, Inc (IFI), a publicly held corporation, which provides data processing services to banks. Ann owns 15 percent of IFI's outstanding common stock.

Last year Ann concluded, based on her study of IFI's confidential marketing information, that the market price of IFI stock was likely to rise substantially, and she bought 10,000 shares. Eight months later, as predicted by the IFI marketing information, IFI's market expanded substantially, and, after IFI's public announcement to that effect, the market price of IFI's stock doubled. Ann thereupon sold the 10,000 shares of IFI stock at a profit of \$100,000.

Six months ago, IFI purchased ten high capacity computers and software from COM to process financial information for IFI's bank customers. Ann had persuaded IFI's management to do business with COM, but took no part in the negotiations which resulted in the sale. The terms of the sale were approved by the board of directors of each company at regular board meetings. Ann attended both meetings, but did not say anything about the computer sale and abstained from voting. The other directors of IFI were unaware of Ann's connections with COM.

After the COM computers were installed, IFI's bank customers complained about the service they were receiving. IFI determined after an investigation that the COM computers were incapable of handling the data processing needs of IFI's customers. IFI also learned that the COM computers had been obsolete when IFI purchased them and could never adequately meet the banks' requirements. As a result, a number of bank customers have stopped doing business with IFI. Ann, by virtue of her expertise in the data processing business, had known that the computers were obsolete when IFI purchased them.

Recently, Ann told IFI's board of directors that one of IFI's competitors had offered to buy all of her IFI shares at a premium price. The IFI board of directors, fearful that the competitor as a shareholder might not act in IFI's best interests, approved IFI's purchase of Ann's stock at \$21 per share. Ann did not attend the board meeting at which the purchase price was approved. The market price of the stock on the day of the purchase was \$19.50 per share.

Ann's shares were purchased by IFI out of surplus. At the same meeting the IFI board, without explanation, approved the sale of the same shares for \$18 per share to two directors who already owned substantial blocks of IFI stock. The par value of the stock is \$20 per share. Other shareholders were not notified of the sale. IFI's certificate of incorporation contains no provisions relating to the sale or reacquisition of shares. Several shareholders, who subsequently learned of the sale, have complained, claiming they would have purchased some of the shares if respect to (i) Ann's purchase and sale of IFI stock, (ii) the computer purchase from COM, or (iii) IFI's purchase of Ann's shares at a premium. He also asked (iv) whether the resale to two IFI directors

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of the shares purchased from Ann was for any reason improper. What advice would you give Joe with respect to his enumerated inquiries?

ANSWER TO QUESTION SIX

- (i) Legal action can be taken with respect to Ann's purchase and sale of IFI stock.
- (ii) The corporation can take action against Ann for false misrepresentation in tort.
- (iii) No legal action can be taken for IFI purchasing Ann's shares at a premium.
- (iv) The resale of the stock to the IFI directors was improper as the stock was sold for less than par value.
- (i) A director stands in a fiduciary relationship with the corporation and its shareholders and as such has an obligation to act in good faith and not act for personal gain or benefit or misappropriate a corporate opportunity to its own advantage.

When a director buys stock and then sells within 6 months at a profit the director is required to disgorge its profits mainly due to a built-in protection against insider trading. Here, Ann sold 8 months later. Here, however, the facts indicate that Ann's motivation to buy the stock was based on a study of confidential information not available to the general public regarding stock in a publicly held corporation. Ann has used her fiduciary position for personal gain by improperly acting upon confidential information of the corporation. She is therefore guilty of insider trading.

(ii) Because Ann is both a shareholder and director of Comco Inc and a shareholder and director of Info Inc, any persuasion she may use on management or the board should be made with full disclosure since as a shareholder she stands to personally benefit from COM's contract with IFI. She has a fiduciary obligation to make full disclosure to the board of directors and should not rely on the protections of the business judgment rule which insulates directors from liability in their ordinary business dealings and gives a favorable presumption to the director that her actions were in good faith and those of a reasonably prudent person. Here, Ann is an "interested director" and stands to personally gain from this transaction. The business judgment rule will not insulate her in such a situation and she can be held personally liable. Not only did she use her position to persuade management without disclosure, she made no disclosure to the board (notwithstanding their favorable vote in her absence) and she knew that the computers were worthless when they were purchased. She breached her fiduciary duty by failing to disclose and can be held liable for false misrepresentation where she failed to disclose, the corporation relied, and they have been damaged. Any shareholder can bring a derivative action against her on behalf of the corporation for damages in tort.

(iii) IFI may buy back the shares of any stockholder and hold them for treasury shares or resale and may pay a premium price so long as the price is not unreasonably disproportionate to the market price. Here the difference between the market price and the premium paid was \$1.50 per share, not unreasonably disproportionate. The Board properly voted on the issue and had an articulated business reason for paying the premium price. The stock purchase would fall under the business judgment rule giving rise to a presumption of good faith and reasonableness in the business decisions of the directors.

(iv) The resale of the treasury shares was improper only in that they were sold for less than par value. The shareholders have no pre-emptive rights in the shares since these shares are non-treasury shares and pre-emptive rights do not attach to treasury shares. However, the shares may not be sold for less than par value unless the certificate of incorporation is amended to change the par value which would require a majority vote of the board and the shareholders. A derivative

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action can be brought by any shareholder on behalf of the corporation seeking rescission of the sale.

Action can be taken against Ann holding her personally liable for her actions. Her removal for cause should be put to a vote and action should be taken against the board for sale of the shares for less than par value. 20 percent of the shareholders may bring an action for judicial dissolution against the two directors who purchased the shares for less than par on the theory they are looting the corporation if in fact they represent a majority of the shares.

ANSWER TO QUESTION SIX

(i) Ann's purchase and sale of IFI was in breach of her fiduciary duties to the shareholders from whom she bought the stock and to IFI. The issue is whether Ann violated her duty of loyalty by trading on inside information.

Under New York BCL, a director of a corporation, and a majority shareholder, owe a duty of loyalty to the corporation and to other shareholders. Under his duty of loyalty, a director must act in good faith and with the honesty and fair dealing that the law imposes on fiduciaries. Similarly, although a shareholder is not generally liable to other shareholders for his or her actions, a majority shareholder or a shareholder with influence on the board or access to confidential information has been held to have fiduciary duties to other shareholders not to act on inside information to his or her advantage. Inside information is any information which is not available to the public at large and which a reasonable investor would consider relevant in making his investment decisions. Where an insider trades on the basis of inside information, he breaches his fiduciary duties to the corporation and to other shareholders in the transactions. The insiders profits are disgorged by the imposition of a constructive trust or the affected shareholders or the corporation can sue to recover the profits.

In this case, Ann was a director of IFI and was also a majority shareholder with 15 percent of the stock. Ann had access to inside information which told him that the price of IFI stock would rise in the future. Ann traded on this information and made a \$100,000 profit. Ann can, therefore, be sued by (i) either the shareholders who sold Ann their 10,000 shares without knowing of the inside information, or (ii) the corporation for breach of fiduciary duties, and Ann's profits of \$100,000 can be disgorged.

(ii) Ann will be liable for IFI's damages resulting from the computer transaction with COM. The issues are (a) whether Ann breached her duty of loyalty to the corporation by entering into an interested transaction and (b) whether Ann breached her duty of care to IFI by failing to point out that the computers were obsolete.

(a) Breach of duty of loyalty

A director owes the corporation a duty of loyalty which means that the director, in his dealings with the corporation must act in good faith and with the honesty and fairness that the law imposes on fiduciaries. Under New York BCL, an interested transaction of a director with the corporation is a breach of this duty unless the director shows that (1) the terms of the transaction were fair and reasonable, or (2) after full disclosure the transaction was approved by a majority of the shareholders or a majority of the board with the interested director abstaining from voting.

In this case Ann, who was a director of IFI, persuaded IFI to enter into a transaction with COM when Ann was a director, an officer and a 10 percent shareholder of COM. This constituted an interested transaction. Ann did not disclose his interest to the board so it is irrelevant that the majority of the directors approved the transaction. Ann can only avoid liability if Ann shows that

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the terms of the transaction were fair and reasonable. The facts don't indicate whether the terms were fair.

(b) Duty of care

Under New York BCL, a director has the duty of care to the corporation which means that the director must act with the good faith, prudence, skill and care that a reasonable person would exercise under similar circumstances. When a director fails to act in a reasonable way he breaches his duty of care. However, to recover damages for the breach it must be shown that the corporation's injury was caused by the director's nonfeasance.

In this case Ann, a director of IFI, had expertise in data processing and had known that the computers were obsolete when IFI purchased them. However, Ann did not mention this fact during the Board's deliberations on the transaction. Thus, Ann breached her duty of care to the corporation by failing to act on information that a reasonably prudent person would have acted on. Moreover, the injury to IFI (i.e., loss of customers due to obsolete computers' incapacity to handle customer needs) was directly caused by Ann's failure to inform the board that the computers were obsolete. Consequently, the corporation can recover its damages from Ann.

(iii) The corporation's purchase of Ann's shares at a premium is valid. The issues are (i) whether Ann, as a shareholder with substantial stock, is entitled to a premium on the sale of her stock, and (ii) whether IFI's repurchase of Ann's stock for above market price is valid.

(i) Ann's entitlement to a premium

Generally, a controlling shareholder is entitled to a premium on the sale of her stock. It is only when bad faith is shown (i.e., when the controlling shareholder sells her stock to looters for a premium with knowledge that they will loot corporate assets) that a shareholder will be held liable for a sale of her stock for a premium.

In this case, Ann sold her 15 percent stock in IFI for a premium of \$1.50 per share. There is no evidence of bad faith on Ann's part because Ann's informing IFI board of her offer from IFI's competitor did not constitute bad faith. Consequently, Ann is entitled to her premium.

(ii) Board's repurchase of Ann's shares

Under the BCL, a corporation is allowed to repurchase its shares and to discriminate in the repurchase by not offering the same terms to others (unless it's a closely held corporation and unless its certificate provides otherwise). A corporation cannot discriminate on redemption rights which are set forth in the certificate. However, the corporation must show that the repurchase served some legitimate corporate purpose.

In this case, IFI paid a premium for Ann's shares because they feared that Ann might sell her 15 percent shares to IFI's competitors who may harm the business. Preventing harm to the corporation was a legitimate corporate purpose and the repurchase from Ann with a premium price was proper.

Note that if this had been a redemption, then IFI would have to offer the same terms to all shareholders with the same class of stock.

(iv) The resale to the two IFI directors was proper. The issues are (i) whether IFI can sell treasury stock for below par value and (ii) whether existing shareholders have preemptive rights with respect to the sale of treasury shares.

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(i) Below par value

Under New York BCL, a corporation is liable for selling its issued stock for below par value. However, treasury stock (that the corporation has repurchased) may be sold for any amount, even below par.

In this case, IFI sold stock repurchased from Ann to two directors for \$18 when its par value was \$20. Since this stock constituted treasury stock, IFI's directors are not liable for selling watered stock and the sale was proper.

(ii) Preemptive rights

Under New York BCL, existing shareholders of a corporation have the right to maintain their percentage of stock ownership by exercising their preemptive rights to purchase their existing percentage of any new stock issued for cash. These rights exist even if the certificate is silent as to preemptive rights. However, preemptive rights are not triggered when a corporation sells treasury stock (or stock not for cash, or stock within 2 years of its incorporation).

In this case, IFI sold treasury stock to the two directors. Thus, the preemptive rights of the existing shareholders were not triggered and IFI's sale to the directors without informing other shareholders was proper.