Smith & Roberson's

BUSINESS LAW

RICHARD A. MANN • BARRY S. ROBERTS

17TH EDITION

SMITH & ROBERSON'S

Business Law

SEVENTEENTH EDITION

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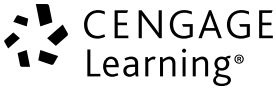

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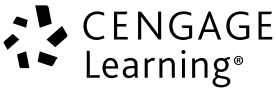

Smith & Roberson's Business Law, Seventeenth Edition
Richard A. Mann and Barry S. Roberts

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Senior Art Director: Michelle Kunkler

Cover/Internal Designer: cmillerdesign

Interior design credits: Ida Jarosova/iStock/ Getty Images Plus/Getty Images; Africa Studio/ShutterStock.com

Library of Congress Control Number: 2016945890

ISBN: 978-1-337-09475-7

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Printed in the United States of America
Print Number: 01 Print Year: 2016

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Preface

The format of the *Seventeenth Edition* follows the tradition established by prior editions, in that chapters contain narrative text, illustrations, cases consisting of selected court decisions, chapter summaries, and end-of-chapter questions and case problems.

Topical Coverage

This text is designed for use in business law and legal environment of business courses generally offered in universities, colleges, schools of business and commerce, community colleges, and junior colleges. By reason of the text's broad and deep coverage, instructors may readily adapt this text to specially designed courses in business law or the legal environment of business by assigning and emphasizing different combinations of chapters.

Furthermore, this text covers the following parts of the CPA Exam: (1) the business law area and the legal duties and responsibilities of accountants area of the Regulation Section and (2) the corporate governance area of the Business Environment and Concepts Section.

Emphasis has been placed upon the regulatory environment of business law: the first eight chapters introduce the legal environment of business, and *Part 9 (Chapters 39 through 46)* addresses government regulation of business.

Up-to-Date

The constitutional law chapter (*Chapter 4*) discusses recent U.S. Supreme Court decisions in cases challenging the constitutionality of (1) a Federal statute restricting how much money an individual donor may contribute in total to all candidates or committees during a political cycle, (2) Michigan's constitutional amendment banning affirmative action in admissions to the State's public universities, and (3) States' refusal to license a marriage between two people of the same sex and to recognize a marriage between two people of the same sex when their marriage was lawfully licensed and performed out of state. The Administrative Law chapter (*Chapter 5*) discusses the recent U.S. Supreme Court case making the Patient Protection and Affordable Care Act's tax credits available in those States that have a Federal Exchange. The new Restatement (Third) of Torts: Liability for Economic Harm is covered in *Chapters 7, 8, 11, 18, and 44*. The new Restatement (Third) of Restitution and Unjust Enrichment is covered in *Chapters 9, 11, 13, 14, 15, 17, 18, 19, and 50*. Coverage of limited liability companies has been updated and expanded in *Chapter 32*. Coverage of benefit corporations has been added in *Chapter 33*. Coverage of suretyship in *Chapter 37* has been updated and expanded. The Intellectual Property chapter (*Chapter 39*) includes the new Defend Trades Secrets Act of 2016 and the 2016 amendments to the Economic Espionage Act of 1996. The Consumer Protection chapter (*Chapter 41*) covers the FCC's net-neutrality rule. The Employment Law chapter (*Chapter 42*) covers the Genetic Information Nondiscrimination Act and the U.S. Supreme Court case holding that in disparate-treatment claims, an employer may not make an applicant's religious practice a factor in employment decisions. The chapter on Securities Regulation (*Chapter 43*) covers the U.S. Securities and Exchange Commission's new Regulation A and Regulation Crowdfunding exemptions. The Environmental Law chapter (*Chapter 45*) includes coverage of the EPA's regulation of greenhouse gases and the 2016 amendments to the Toxic Substances Control Act. The International Business Law chapter (*Chapter 46*) covers the United Nations Convention on the Law of the Sea (UNCLOS).

Readability of Narrative Text

To make the text as readable as possible, all unnecessary "legalese" has been omitted, and necessary legal terms have been printed in boldface and clearly defined, explained, and illustrated. Each chapter is carefully organized with sufficient levels of subordination to enhance the accessibility of the material. The text is enriched by numerous illustrative hypothetical and case examples, which help students relate the material to real-life experiences. The end-of-chapter cases are cross-referenced in the text, as are related topics covered in other chapters.

Chapter Objectives

Each chapter begins with a list of learning objectives for students.

Applying the Law

The Applying the Law feature provides a systematic legal analysis of a realistic situation that focuses on a specific concept presented in the chapter. It consists of (1) the facts of a hypothetical case, (2) an identification of the broad legal issue presented by those facts, (3) a statement of the applicable rule, (4) the application of the rule to the facts, and (5) a legal conclusion in the case. The Applying the Law feature appears in fourteen chapters. We wish to acknowledge and thank Professor Ann Olazábal, University of Miami, for her contribution in preparing this feature.

Practical Advice

Each chapter has a number of statements that illustrate how legal concepts covered in the chapter can be applied to common business situations.

Case Treatment

All the cases have been edited carefully to preserve the actual language of the court and to show the essential facts of the case, the issue or issues involved, the decision of the court, and the reason for its decision. We have retained the landmark cases from the prior edition. In addition, we have incorporated twenty-seven recent cases, including the following U.S. Supreme Court cases: *DIRECTV, Inc. v. Imburgia; Perez v. Mortgage Bankers Ass'n.; Omnicare, Inc. v. Laborers District Council Construction Industry Pension Fund; Husky International Electronics, Inc., v. Ritz; Harris v. Viegelahn; Young v. United Parcel Service, Inc.; Environmental Protection Agency v. EME Homer City Generation, L. P;* and *OBB Personenverkehr Ag v. Sachs*.

Illustrations

We have used more than 210 classroom-tested figures, diagrams, charts, tables, and chapter summaries. The figures and diagrams help students conceptualize the many abstract concepts in the law; the charts and tables not only summarize prior discussions but also help to illustrate relationships among legal rules. Moreover, each chapter has a summary in the form of an annotated outline of the entire chapter, including key terms.

End-of-Chapter Questions and Case Problems

Classroom-proven questions and case problems appear at the end of chapters to test the student's understanding of major concepts. Almost all of the chapters include one or more new questions and/or case problems. We have used the questions (based on hypothetical situations) and the case problems (taken from reported court decisions) in our own classrooms and consider them excellent stimulants to classroom discussion. Students, in turn, have found the questions and case problems helpful in enabling them to apply the basic rules of law to factual situations.

Taking Sides

Each chapter—except for *Chapters 1 and 2*—has an end-of-chapter feature that requires students to apply critical-thinking skills to a case-based fact situation. Students are asked to identify the relevant legal rules and develop arguments for both parties to the dispute. In addition, students are asked to explain how they think a court would resolve the dispute.

Appendices

The appendices include the Constitution of the United States (Appendix A), the Uniform Commercial Code (Appendix B), and a comprehensive Dictionary of Legal Terms (Appendix C).

Pedagogical Benefits

Classroom use and study of this book should provide students with the following benefits and skills:

1. Perception and appreciation of the scope, extent, and importance of the law.
2. Basic knowledge of the fundamental concepts, principles, and rules of law that apply to business transactions.
3. Knowledge of the function and operation of courts and government administrative agencies.
4. Ability to recognize the potential legal problems which may arise in a doubtful or complicated situation and the necessity of consulting a lawyer and obtaining competent professional legal advice.
5. Development of analytical skills and reasoning power.

Additional Course Tools

MINDTAP

New for Smith and Roberson's *Business Law*, 17th edition, MindTap is a personalized teaching experience with relevant assignments that guide students to analyze, apply, and improve thinking, allowing instructors to measure skills and outcomes with ease. Teaching becomes personalized through a pre-built Learning Path designed with key student objectives and the instructor syllabus in mind. Applicable

reading, multimedia, and activities within the learning path intuitively guide students up the levels of learning to (1) Prepare, (2) Engage, (3) Apply, and (4) Analyze business law content. These activities are organized in a logical progression to help elevate learning, promote critical-thinking skills and produce better outcomes.

This customizable online course gives instructors the ability to add their own content in the Learning Path as well as modify authoritative Cengage Learning content and learning tools using apps that integrate seamlessly with Learning Management Systems (LMS). Analytics and reports provide a snapshot of class progress, time in course, engagement, and completion rates.

INSTRUCTOR RESOURCES

Instructors can access these resources by going to login.cengage.com, logging in with a faculty account username and password, and searching by ISBN 9781337094757.

- **Instructor's Manual** The Instructor's Manual, prepared by Richard A. Mann, Barry S. Roberts, and Beth D. Woods, contains opening ethics questions, suggested activities, and research projects; chapter outlines; teaching notes; answers to the Questions and Case Problems; briefs to cases; and suggested case questions for students.
- **PowerPoint® Slides** These slides clarify course content and guide student note-taking during lectures.
- **Test Bank** The Test Bank contains thousands of true/false, multiple-choice, and essay questions. The questions vary in level of difficulty and meet a full range of tagging requirements so that instructors can tailor their testing to meet their specific needs.
- **Cognero** Cengage Learning Testing Powered by Cognero is a flexible, online system that allows you to
  - author, edit, and manage test bank content from multiple Cengage Learning solutions
  - create multiple test versions in an instant
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- No special installs or downloads needed
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- Cross-compatible capability. Import and export content into other systems.

Acknowledgments

We are grateful to those who provided us with comments for previous editions of the book: Miriam R. Albert, Fordham University; Mark Altieri, Cleveland State University; Wm. Dennis Ames, Indiana University of Pennsylvania; Albert Anderson, Mount Aloysius College; Albert Andrews, Jr., University of Minnesota; Michael Balsamo, SUNY–Old Westbury; Denise A. Bartles, Missouri Western State College; Lois Yoder Beier, Kent State University; Monika Lovewell Bellows, SUNY–Canton; Robert Bing, William Paterson College; Joell Bjorke, Winona State University; William N. Bockanic, John Carroll University; Andrea Boggio, Bryant University; Donald Boren, Bowling Green State University; Joyce Boland-DeVito, Esq., St. John's University; Joe Boucher, University of Wisconsin–Madison; L. Brooks, Nichols College; Nicolaus Bruns, Jr., Lake Forest Graduate School of Management; Mark A. Buchanan, Boise State University; Deborah Lynn Bundy, Marquette University; Michael Burg, University of St. Thomas; Debra Burke, Western Carolina University; Thomas J. Canavan, Long Island University–C. W. Post Campus; Regina W. Cannon, University of Georgia; Donald Cantwell, University of Texas–Arlington; John P. Carnasiotis, University of Missouri; Albert L. Carter, Jr., University of the District of Columbia; Thomas D. Cavenagh, North Central College; Jennifer Chapman, Georgia Gwinnett College; Jeff Charles, Bowling Green State University; John Cirace, CUNY–Lehman College; Richard R. Clark, University of the District of Columbia; Arlen Coyle, University of Mississippi; Mitchell F. Crusto, Washington University–St. Louis; Richard Dalebout, Brigham Young University; Arthur S. Davis, Long Island University; John Davis, Ashland Community & Technical College; Kenneth R. Davis, Fordham School of Business; William Day, Cleveland State University; Alex DeVience, Jr., DePaul University; Craig Disbrow, Plymouth State College, New Hampshire; Robert H. Doud, Adelphi University; William G. Elliott, Saginaw Valley State University; Edward Eramus, State University of New York–Brockport; Kurt Erickson, South West Michigan College; Jay Ersling, University of St. Thomas, Minnesota; Robert Evans, Rockford College; Alfred E. Fabian, Ivy Tech Community College; J. Royce Fichtner, Drake University; Thomas Fitzpatrick, Assumption College; Joe W. Fowler, Oklahoma State University–Stillwater; Karla H. Fox, University of Connecticut; Stanley

Fuchs, Fordham University; Samuel B. Garber, DePaul University; Nathan T. Garrett, Esq., North Carolina Central University; Michael J. Garrison, North Dakota State University; Daniel Gillespie, DePaul University; Dr. Roy Girasa, Pace University; Marvin Gordon, Loyola Chicago University; Sue Gragiano, Bowling Green State University; James Granito, Youngstown State University; John Gray, Faulkner University; Sally Terry Green, Texas Southern University; Dale A. Grossman, Cornell University; Donald Haley, Cleveland State University; Marc Hall, Auburn University Montgomery; Brian Hanlon, North Central College; Dr. Ivan Harber, Indian River State College; James V. Harrison, St. Peter's State College; Lori K. Harris-Ransom, Caldwell College; Edward J. Hartman, St. Ambrose University; Frances J. Hill, University of Wisconsin–Whitewater; Telford F. Hollman, University of Northern Iowa–Cedar Falls; Georgia L. Holmes, Mankato State University; James Holzinger, Muhlenberg College; Norman Hope, Tabor College; Sarah H. Hudwig, Mary Baldwin College; Velma Jesser, Lane Community College; Theresa Johnson, Cleveland State University; Marilee Jones-Confield, California State University–Long Beach; Al Joyner, Eastern Illinois University; Mary C. Keifer, Ohio University; Randall Kilbourne, Northwestern State University; Barbara Kirkpatrick, Virginia Intermont College; Edward M. Kissling, Ocean County College, New Jersey; Robert Klepa, UCLA Extension; Louise Knight, Bucknell University; William J. Koval, Jr., Notre Dame College; Duane R. Lambert, California State University–Hayward; Joseph F. Lenius, Northeastern Illinois University; Andrew Liput, Felician College; Avi Liveson, Hunter College; Romain Lorentz, University of St. Thomas; Sarah H. Ludwig, Mary Baldwin College; Richard Luke, Ricks College; Tanya M. Marcum, Bradley University; Pat Maroney, Florida State University; Sharon Martin, Empire State College–Brooklyn Unit; Bruce Marx, SUNY–Old Westbury; Michael A. Mass, American University; Cheryl Massingale, University of Tennessee–Knoxville; Greg K. McCann, Stetson University; Bruce McClain, Cleveland State University; Ann L. McClure, Fort Hays State University; James McGee, College of Westchester; Charles R. McGuire, Illinois State University; Herbert McLaughlin, Bryant College; James Molloy, University of Wisconsin–Whitewater; Sebrena R. Moten, Troy University; Donald Nelson, University of Denver; Carol L. Nielsen, Bemidji State University; Christopher J. Nyhus, University of Mary; L. K. O'Drudy, Jr., University of Virginia; Ann Morales Olazabal, University of Miami; David Oliveiri, University of Rochester; Richard Paxton, San Diego Community College; Gail P. Petravick, Bradley University; Jim Pingel, Everest University–Brandon; Jonathan Politi, Columbus College of Art & Design; James L. Porter, University of New Mexico; Lisa Rackley, Rich Mountain Community College; Elinor Rahm, Central Missouri State University; Samuel H. Ramsay, Jr., Bryant College; Decateur Reed, Boise State University; Richard E. Regan, St. John Fisher College; Roger Reinsch, Emporia State University; L. Reppert, Marymount University; Caroline Rider, Marist College; Roland W. Riggs, Marietta College; George Roe, University of Illinois–Chicago; Stanford Rosenberg, La Roche College; Alan Ross, University of California–Berkeley; Mark Rossi, Briar Cliff University; Tim Rueth, Marquette University; Stuart Schafer, University of Mississippi; Eric D Schwartz, LaRoche College; Donald H. Shoop, North Dakota State University; Carol Wahle Smith, Central Florida Community College; Peter Smithfield, Argyle Academy; Michael J. Sovansky, Saginaw Valley State University; Janis Stamm, Edinboro University of Pennsylvania; Beverly E. Stanis, Oakton Community College; James Staruck, DePaul University; Al Stauber, Florida State University; David Steele, University of Wisconsin–Eau Claire; Lowell E. Stockstill, Wittenberg University; Peter Strohm, Georgian Court College; Al Talarczyk, Edgewood College; James D. Taylor, Claremont McKenna College; Kevin M. Teeven, Bradley University; Robert J. Tepper, University of New Mexico; Dale B. Thompson, University of St. Thomas; Leonard Tripodi, St. Joseph's College; Alix Valenti, University of Houston–Clear Lake; Karen Vitori, Schoolcraft College; Nancy A. Wainwright, Eastern Washington University; Charles H. Walker, University of Mississippi; Michael G. Walsh, Villanova University; Daniel Warner, Western Washington University; Peter M. Wasemiller, Fresno Pacific College; David Webster, University of South Florida–Tampa; Scott A. White, University of Wisconsin; E. Marshall Wick, Gallaudet University; John G. Williams, Northwestern State University; Amy Wilson, Zane State College; Wells J. Wright, University of Minnesota; Rizvana Zameeruddin, University of Wisconsin–Parkside; and James B. Zimarowski, University of Notre Dame.

We express our thanks and deep appreciation to Debra Corvey for administrative assistance. For their support we extend our thanks to Karlene Fogelin Knebel and Joanne Erwick Roberts. And we are grateful to Vicky True-Baker, Amanda White, and Rebecca von Gillern of South-Western for their invaluable assistance and cooperation in connection with the preparation of this text.

This text is dedicated to our children Lilli-Marie Knebel Mann, Justin Erwick Roberts, and Matthew Charles Roberts.

Richard A. Mann
Barry S. Roberts

Table of Cases

Cases in italic are the principal cases included at the ends of the chapters. Reference numbers are to pages.

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PART 1

The Legal Environment of Business

CHAPTER 1

Introduction to Law

CHAPTER OUTCOMES

After reading and studying this chapter, you should be able to:

- Identify and describe the basic functions of law.
- Distinguish between (1) law and justice and (2) law and morals.
- Distinguish between (1) substantive and procedural law, (2) public and private law, and (3) civil and criminal law.
- Identify and describe the sources of law.
- Explain the principle of *stare decisis*.

Law concerns the relations of individuals with one another as such relations affect the social and economic order. It is both the product of civilization and the means by which civilization is maintained. As such, law reflects the social, economic, political, religious, and moral philosophy of society. The laws of the United States influence the lives of every U.S. citizen. At the same time, the laws of each State influence the lives of its citizens and the lives of many noncitizens as well. The rights and duties of all individuals, as well as the safety and security of all people and their property, depend upon the law.

The law is pervasive. It interacts with and influences the political, economic, and social systems of every civilized society. It permits, forbids, or regulates practically every human activity and affects all persons either directly or indirectly. Law is, in part, prohibitory: certain acts must not be committed. For example, one must not steal; one must not murder. Law is also partly mandatory: certain acts must be done or be done in a prescribed way. Taxes must be paid; corporations must make and file certain reports with State or Federal authorities; traffic must keep to the right. Finally, law is permissive: individuals may choose to perform or not to perform certain acts. Thus, one may or may not enter into a contract; one may or may not dispose of one's estate by will.

Because the areas of law are so highly interrelated, an individual who intends to study the several branches of law known collectively as business law should first consider the nature, classification, and sources of law as a whole. This enables the student not only to understand any given branch of law better but also to understand its relation to other areas of law.

1-1 Nature of Law

The law has evolved slowly, and it will continue to change. It is not a pure science based upon unchanging and universal truths. Rather, it results from a continuous effort to balance, through a workable set of rules, the individual and group rights of a society.

1-1a DEFINITION OF LAW

A fundamental but difficult question regarding law is this: what is it? Numerous philosophers and jurists (legal scholars) have attempted to define it. American jurists and Supreme Court Justices Oliver Wendell Holmes and Benjamin Cardozo defined law as predictions of the way that a court will decide specific legal questions. William Blackstone, an English jurist, on the other hand, defined law as "a rule of civil conduct prescribed by the supreme power in a state, commanding what is right, and prohibiting what is wrong." Similarly, Austin, a nineteenth-century English jurist, defined law as a general command that a state or sovereign makes to those who are subject to its authority by laying down a course of action enforced by judicial or administrative tribunals.

Because of its great complexity, many legal scholars have attempted to explain the law by outlining its essential characteristics. Roscoe Pound, a distinguished American jurist

and former dean of the Harvard Law School, described law as having multiple meanings:

> First, we may mean the legal order, that is, the regime of ordering human activities and relations through systematic application of the force of politically organized society, or through social pressure in such a society backed by such force. We use the term "law" in this sense when we speak of "respect for law" or for the "end of law."
>
> Second, we may mean the aggregate of laws or legal precepts; the body of authoritative grounds of judicial and administrative action established in such a society. We may mean the body of received and established materials on which judicial and administrative determinations proceed. We use the term in this sense when we speak of "systems of law" or of "justice according to law."
>
> Third, we may mean what Mr. Justice Cardozo has happily styled "the judicial process." We may mean the process of determining controversies, whether as it actually takes place, or as the public, the jurists, and the practitioners in the courts hold it ought to take place.

1-1b FUNCTIONS OF LAW

At a general level, the primary function of law is to maintain stability in the social, political, and economic system while simultaneously permitting change. The law accomplishes this basic function by performing a number of specific functions, among them dispute resolution, protection of property, and preservation of the state.

Disputes, which inevitably arise in a society as complex and interdependent as ours, may involve criminal matters, such as theft, or noncriminal matters, such as an automobile accident. Because disputes threaten the stability of society, the law has established an elaborate and evolving set of rules to resolve them. In addition, the legal system has instituted societal remedies, usually administered by the courts, in place of private remedies such as revenge.

The recognition of private ownership of property is fundamental to our economic system, based as it is upon the exchange of goods and services among privately held units of consumption. Therefore, a second crucial function of law is to protect the owner's use of property and to facilitate voluntary agreements (called contracts) regarding exchanges of property and services. Accordingly, a significant portion of law, as well as this text, involves property and its disposition, including the law of property, contracts, sales, commercial paper, and business associations.

A third essential function of the law is preservation of the state. In our system, law ensures that changes in leadership and the political structure are brought about by political actions such as elections, legislation, and referenda, rather than by revolution, sedition, and rebellion.

1-1c LEGAL SANCTIONS

A primary function of the legal system is to make sure that legal rules are enforced. **Sanctions** are the means by which the law enforces the decisions of the courts. Without sanctions, laws would be ineffectual and unenforceable.

An example of a sanction in a civil (noncriminal) case is the seizure and sale of the property of a debtor who fails to pay a court-ordered obligation, called a judgment. Moreover, under certain circumstances, a court may enforce its order by finding an offender in contempt and sentencing him to jail until he obeys the court's order. In criminal cases, the principal sanctions are the imposition of a fine, imprisonment, and capital punishment.

1-1d LAW AND MORALS

Although moral and ethical concepts greatly influence the law, morals and law are not the same. They may be considered as two intersecting circles, as shown in *Figure 1-1*. The area common to both circles includes the vast body of ideas that are both moral and legal. For instance, "Thou shall not kill" and "Thou shall not steal" are both moral precepts and legal constraints.

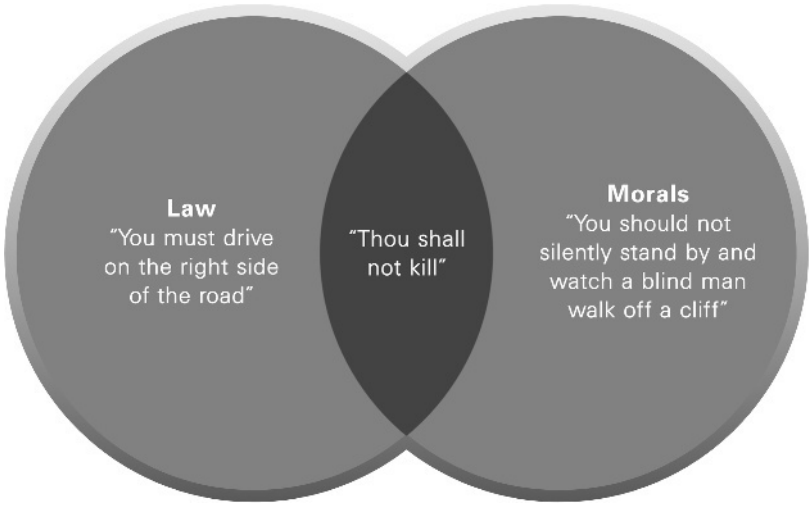
On the other hand, the part of the legal circle that does not intersect the morality circle includes many rules of law that are completely unrelated to morals, such as the rules stating that you must drive on the right side of the road and that you must register before you can vote. Likewise, the portion of the morality circle which does not intersect the legal circle includes moral precepts not enforced by law, such as the moral principle that you should not silently stand by and watch a blind man walk off a cliff or that you should provide food to a starving child.

◆ **SEE FIGURE 1-1:** ***Law and Morals***

1-1e LAW AND JUSTICE

Law and justice represent separate and distinct concepts. Without law, however, there can be no justice. Although justice has at least as many definitions as law does, justice may be defined as fair, equitable, and impartial treatment of the competing interests and desires of individuals and groups with due regard for the common good.

FIGURE 1-1 Law and Morals



On the other hand, law is no guarantee of justice. Some of history's most monstrous acts have been committed pursuant to "law." Examples include the actions of Nazi Germany during the 1930s and 1940s and the actions of the South African government under apartheid from 1948 until 1994. Totalitarian societies often have shaped formal legal systems around the atrocities they have sanctioned.

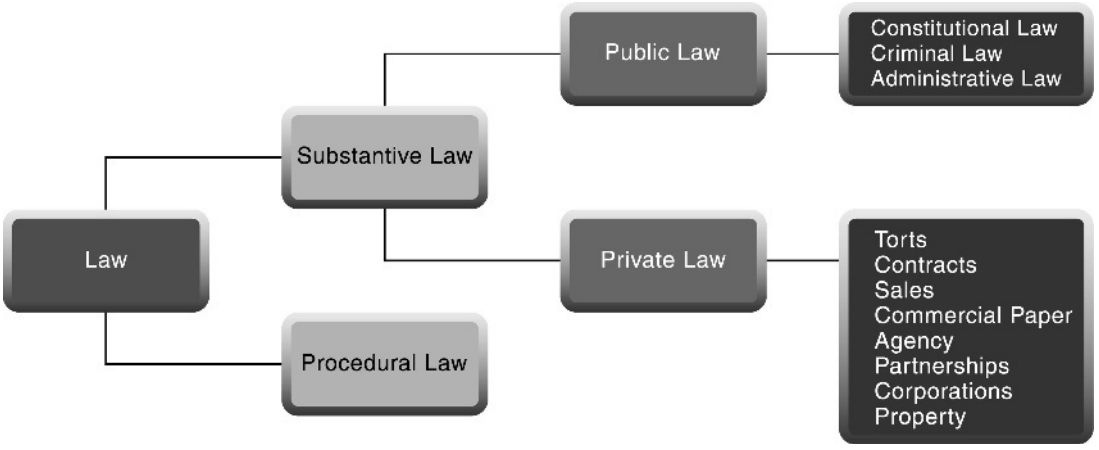
1-2 Classification of Law

Because the subject is vast, classifying the law into categories is helpful. Though a number of classifications are possible, the most useful categories are (1) substantive and procedural, (2) public and private, and (3) civil and criminal.

Basic to understanding these classifications are the terms *right* and *duty*. A **right** is the capacity of a person, with the aid of the law, to require another person or persons to perform, or to refrain from performing, a certain act. Thus, if Alice sells and delivers goods to Bob for the agreed price of $500 payable at a certain date, Alice has the capability, with the aid of the courts, of enforcing the payment by Bob of the $500. A **duty** is the obligation the law imposes upon a person to perform, or to refrain from performing, a certain act. Duty and right are correlatives: no right can rest upon one person without a corresponding duty resting upon some other person or, in some cases, upon all other persons.

◆ SEE FIGURE 1-2: *Classification of Law*

FIGURE 1-2 Classification of Law



1-2a SUBSTANTIVE AND PROCEDURAL LAW

Substantive law creates, defines, and regulates legal rights and duties. Thus, the rules of contract law that determine when a binding contract is formed are rules of substantive law. This book is principally concerned with substantive law. On the other hand, **procedural law** establishes the rules for enforcing those rights that exist by reason of substantive law. Thus, procedural law defines the method by which one may obtain a remedy in court.

1-2b PUBLIC AND PRIVATE LAW

Public law is the branch of substantive law that deals with the government's rights and powers in its political or sovereign capacity and in its relation to individuals or groups. Public law consists of constitutional, administrative, and criminal law. **Private law** is that part of substantive law governing individuals and legal entities (such as corporations) in their relations with one another. Business law is primarily private law.

1-2c CIVIL AND CRIMINAL LAW

The **civil law** defines duties the violation of which constitutes a wrong against the party injured by the violation. In contrast, the **criminal law** establishes duties the violation of which is a wrong against the whole community. Civil law is a part of private law, whereas criminal law is a part of public law. (The term *civil law* should be distinguished from the concept of a civil law *system*, which is discussed later in this chapter.) In a civil action the injured party **sues** to recover **compensation** for the damage and injury he has sustained as a result of the defendant's wrongful conduct. The party bringing a civil action (the **plaintiff**) has the burden of proof, which he must sustain by a **preponderance** (greater weight) of the evidence. Whereas the purpose of criminal law is to punish the wrongdoer, the purpose of civil law is to compensate the injured party. The principal forms of relief the civil law provides are a judgment for money damages and a decree ordering the defendant to perform a specified act or to desist from specified conduct.

A crime is any act or omission that public law prohibits in the interest of protecting the public and that the government makes punishable in a judicial proceeding brought (**prosecuted**) by it. The government must prove criminal guilt **beyond a reasonable doubt**, which is a significantly higher burden of proof than that required in a civil action. The government prohibits and punishes crimes upon the ground of public policy, which may include the safeguarding of the government itself, human life, or private property. Additional purposes of criminal law include deterrence and rehabilitation.

◆ SEE FIGURE 1-3: *Comparison of Civil and Criminal Law*

1-3 Sources of Law

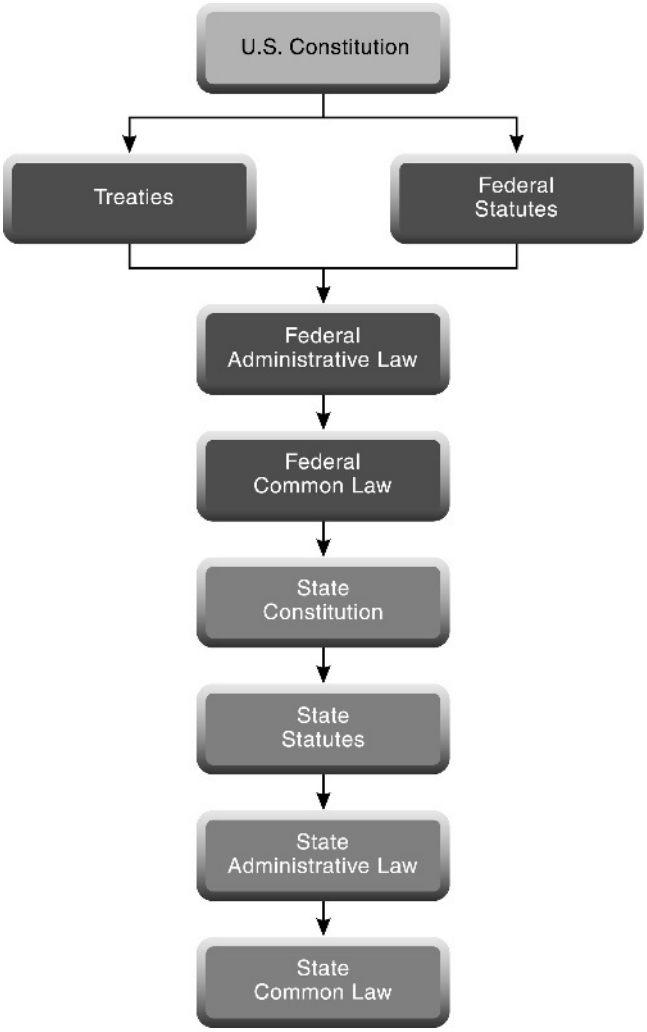
The sources of law in the U.S. legal system are the Federal and State constitutions, Federal treaties, interstate compacts, Federal and State statutes and executive orders, the ordinances of countless local municipal governments, the rules and regulations of Federal and State administrative agencies, and an ever-increasing volume of reported Federal and State court decisions.

The *supreme law* of the land is the U.S. Constitution. The Constitution provides that Federal statutes and treaties shall be the supreme law of the land. Federal legislation and treaties are, therefore, paramount to State constitutions and statutes. Federal legislation is of great significance as a source of law. Other Federal actions having the force of law are executive orders of the President and rules and regulations of Federal administrative officials, agencies, and commissions. The Federal courts also contribute considerably to the body of law in the United States.

FIGURE 1-3 Comparison of Civil and Criminal Law

	Civil Law	Criminal Law
Commencement of Action	Aggrieved individual (plaintiff) sues	State or Federal government prosecutes
Purpose	Compensation Deterrence	Punishment Deterrence Rehabilitation Preservation of peace
Burden of Proof	Preponderance of the evidence	Beyond a reasonable doubt
Principal Sanctions	Monetary damages Equitable remedies	Capital punishment Imprisonment Fines

FIGURE 1-4 Hierarchy of Law



The same pattern exists in every State. The paramount law of each State is contained in its written constitution. (Although a State constitution cannot deprive citizens of Federal constitutional rights, it can guarantee rights beyond those provided in the U.S. Constitution.) State constitutions tend to be more specific than the U.S. Constitution and, generally, have been amended more frequently. Subordinate to the State constitution are the statutes that the State's legislature enacts and the case law that its judiciary develops. Likewise, State administrative agencies issue rules and regulations having the force of law, as do executive orders promulgated by the governors of most States. In addition, cities, towns, and villages have limited legislative powers within their respective municipal areas to pass ordinances and resolutions.

◆ **SEE FIGURE 1-4:** ***Hierarchy of Law***

1-3a CONSTITUTIONAL LAW

A **constitution**—the fundamental law of a particular level of government—establishes the governmental structure and allocates power among the levels of government, thereby defining political relationships. One of the fundamental principles on which our government is founded is that of separation of powers. As detailed in the U.S. Constitution, this means that the government consists of three distinct and independent branches: the Federal judiciary, the Congress, and the executive branch.

A constitution also restricts the powers of government and specifies the rights and liberties of the people. For example, the Constitution of the United States not only specifically states what rights and authority are vested in the national government but also specifically enumerates certain rights and liberties of the people. Moreover, the Ninth

Amendment to the U.S. Constitution makes it clear that this enumeration of rights does not in any way deny or limit other rights that the people retain.

All other law in the United States is subordinate to the Federal Constitution. No law, Federal or State, is valid if it violates the Federal Constitution. Under the principle of **judicial review**, the Supreme Court of the United States determines the constitutionality of *all* laws.

1-3b JUDICIAL LAW

The U.S. legal system is a **common law system**, first developed in England. It relies heavily on the judiciary as a source of law and on the **adversary system** for the adjudication of disputes. In an adversary system, the parties, not the court, must initiate and conduct litigation. This approach is based upon the belief that the truth is more likely to emerge from the investigation and presentation of evidence by two opposing parties, both motivated by self-interest, than from judicial investigation motivated only by official duty. Other English-speaking countries, including England, Canada, and Australia, also use the common law system.

In distinct contrast to the common law system are civil law systems, which are based on Roman law. **Civil law systems** depend on comprehensive legislative enactments (called codes) and an inquisitorial method of adjudication. In the **inquisitorial system**, the judiciary initiates litigation, investigates pertinent facts, and conducts the presentation of evidence. The civil law system prevails in most of Europe, Scotland, the State of Louisiana, the province of Quebec, Latin America, and parts of Africa and Asia.

Common Law The courts in common law systems have developed a body of law, known as "case law," "judge-made law," or "common law," that serves as precedent for determining later controversies. In this sense, common law is distinguished from other sources of law such as legislation and administrative rulings.

To evolve steadily and predictably, the common law has developed by application of *stare decisis* (to stand by the decisions). Under the principle of **stare decisis**, courts, in deciding cases, adhere to and rely on rules of law that they or superior courts announced and applied in prior decisions involving similar cases. Judicial decisions thus have two uses: (1) to determine with finality the case currently being decided and (2) to indicate how the courts will decide similar cases in the future. *Stare decisis* does not, however, preclude courts from correcting erroneous decisions or from choosing among conflicting precedents. Thus, the doctrine allows sufficient flexibility for the common law to change.

The strength of the common law is its ability to adapt to change without losing its sense of direction. As Justice Cardozo said, "The inn that shelters for the night is not the journey's end. The law, like the traveler, must be ready for the morrow. It must have a principle of growth."

Equity As the common law developed in England, it became overly rigid and beset with technicalities. Consequently, in many cases, the courts provided no remedies because the judges insisted that a claim must fall within one of the recognized forms of action. Moreover, courts of common law could provide only limited remedies; the principal type of relief obtainable was a monetary judgment. Consequently, individuals who could not obtain adequate relief from monetary awards began to petition the king directly for justice. He, in turn, came to delegate these petitions to his chancellor.

Gradually, there evolved a supplementary system of judicial relief for those who had no adequate remedy at common law. This new system, called **equity**, was administered by a court of chancery presided over by a chancellor. The chancellor, deciding cases on "equity and good conscience," afforded relief in many instances in which common law judges had refused to act or in which the remedy at law was inadequate. Thus, two systems of law administered by different tribunals developed side by side: the common law courts and the courts of equity.

An important difference between law and equity was that the chancellor could issue a **decree**, or order, compelling a defendant to do or refrain from doing a specific act. A defendant who did not comply with the order could be held in contempt of court and punished by fine or imprisonment. This power of compulsion available in a court of equity opened the door to many needed remedies not available in a court of common law.

Equity jurisdiction, in some cases, recognized rights that were enforceable at common law but for which equity provided more effective remedies. For example, in a court of equity, for breach of a land contract, the buyer could obtain a decree of **specific performance** commanding the defendant seller to perform his part of the contract by transferring title to the land. Another powerful and effective remedy available only in the courts of equity was the **injunction**, a court order requiring a party to do or refrain from doing a specified act. Still another remedy not available elsewhere was **reformation**, in which case, upon the ground of mutual mistake, contracting parties could bring an action to reform or change the language of a written agreement to conform to their actual intentions. Finally, an action for **rescission** of a contract allowed a party to invalidate a contract under certain circumstances.

Although courts of equity provided remedies not available in courts of law, they granted such remedies only at their discretion, not as a matter of right. The courts exercised this discretion according to the general legal principles, or

maxims, that they formulated over the years. A few of these familiar maxims of equity are the following: Equity will not suffer a wrong to be without a remedy. Equity regards the substance rather than the form. Equity abhors a forfeiture. Equity delights to do justice and not by halves. He who comes into equity must come with clean hands. He who seeks equity must do equity.

In nearly every jurisdiction in the United States, courts of common law and courts of equity have united to form a single court that administers both systems of law. Vestiges of the old division remain, however. For example, the right to a trial by jury applies only to actions at law but not, under Federal law and in almost every State, to suits filed in equity.

Restatements of Law The common law of the United States results from the independent decisions of the State and Federal courts. The rapid increase in the number of decisions by these courts led to the establishment of the American Law Institute (ALI) in 1923. The ALI was composed of a distinguished group of lawyers, judges, and law professors who set out to prepare

> an orderly restatement of the general common law of the United States, including in that term not only the law developed solely by judicial decision, but also the law that has grown from the application by the courts of statutes that were generally enacted and were in force for many years. Wolk in, "Restatements of the Law: Origin, Preparation, Availability," 21 *Ohio B.A. Rept.* 663 (1940).

Currently the ALI is made up of more than 4,300 lawyers, judges, and law professors.

Regarded as the authoritative statement of the common law of the United States, the Restatements cover many important areas of the common law, including torts, contracts, agency, property, and trusts. Although not law in themselves, they are highly persuasive and frequently have been used by courts in support of their opinions. Because they state much of the common law concisely and clearly, relevant portions of the Restatements are frequently relied upon in this book.

1-3c LEGISLATIVE LAW

Since the end of the nineteenth century, legislation has become the primary source of new law and ordered social change in the United States. The annual volume of legislative law is enormous. Justice Felix Frankfurter's remarks to the New York City Bar in 1947 are even more appropriate in the twenty-first century:

> Inevitably the work of the Supreme Court reflects the great shift in the center of gravity of law-making. Broadly speaking, the number of cases disposed of by opinions has not changed from term to term. But even as late as 1875 more than 40 percent of the controversies before the Court were common-law litigation, fifty years later only 5 percent, while today cases not resting on statutes are reduced almost to zero. It is therefore accurate to say that courts have ceased to be the primary makers of law in the sense in which they "legislated" the common law. It is certainly true of the Supreme Court that almost every case has a statute at its heart or close to it.

This modern emphasis upon legislative or statutory law has occurred because common law, which develops evolutionarily and haphazardly, is not well suited for making drastic or comprehensive changes. Moreover, courts tend to be hesitant about overruling prior decisions, whereas legislatures frequently repeal prior enactments. In addition, legislatures are independent and able to choose the issues they wish to address, while courts may deal only with issues that arise in actual cases. As a result, legislatures are better equipped to make the dramatic, sweeping, and relatively rapid changes in the law that enable it to respond to numerous and vast technological, social, and economic innovations.

While some business law topics, such as contracts, agency, property, and trusts, still are governed principally by the common law, most areas of commercial law have become largely statutory, including partnerships, corporations, sales, commercial paper, secured transactions, insurance, securities regulation, antitrust, and bankruptcy. Because most States enacted statutes dealing with these branches of commercial law, a great diversity developed among the States and hampered the conduct of commerce on a national scale. The increased need for greater uniformity led to the development of a number of proposed uniform laws that would reduce the conflicts among State laws.

The most successful example is the **Uniform Commercial Code (UCC)**, which was prepared under the joint sponsorship and direction of the ALI and the Uniform Law Commission (ULC), which is also known as the National Conference of Commissioners on Uniform State Laws (NCCUSL). (Selected provisions of the Code are set forth in *Appendix B* of this book.) All fifty States (although Louisiana has adopted only Articles 1, 3, 4, 5, 7, and 8), the District of Columbia, and the Virgin Islands have adopted the UCC. The underlying purposes and policies of the Code are as follows:

1. simplify, clarify, and modernize the law governing commercial transactions;
2. permit the continued expansion of commercial practices through custom, usage, and agreement of the parties; and
3. make uniform the law among the various jurisdictions.

The ULC has drafted more than three hundred uniform laws, including the Uniform Partnership Act, the Uniform Limited Partnership Act, and the Uniform Probate Code. The ALI has developed a number of model statutory formulations, including the Model Code of Evidence, the Model Penal Code, a Model Land Development Code, and a proposed Federal Securities Code. In addition, the American Bar Association has promulgated the Model Business Corporation Act.

Treaties A **treaty** is an agreement between or among independent nations. Article II of the U.S. Constitution authorizes the President to enter into treaties with the advice and consent of the Senate, "providing two thirds of the Senators present concur."

Only the Federal government, not the States, may enter into treaties. A treaty signed by the President and approved by the Senate has the legal force of a Federal statute. Accordingly, a Federal treaty may supersede a prior Federal statute, while a Federal statute may supersede a prior treaty. Like statutes, treaties are subordinate to the Federal Constitution and subject to judicial review.

Executive Orders In addition to his executive functions, the President of the United States also has authority to issue laws, which are called **executive orders**. Typically, Federal legislation specifically delegates this authority. An executive order may amend, revoke, or supersede a prior executive order. An example of an executive order is the one issued by President Johnson in 1965 prohibiting discrimination by Federal contractors on the basis of race, color, sex, religion, or national origin in employment on any work the contractor performed during the period of the Federal contract.

The governors of most States enjoy comparable authority to issue executive orders.

1-3d ADMINISTRATIVE LAW

Administrative law is the branch of public law that is created by administrative agencies in the form of rules, regulations, orders, and decisions to carry out the regulatory powers and duties of those agencies. Administrative functions and activities concern matters of national safety, welfare, and convenience, including the establishment and maintenance of military forces, police, citizenship and naturalization, taxation, coinage of money, elections, environmental protection, and the regulation of transportation, interstate highways, waterways, television, radio, trade and commerce, and, in general, public health, safety, and welfare.

To accommodate the increasing complexity of the social, economic, and industrial life of the nation, the scope of administrative law has expanded enormously. Justice Jackson stated, "the rise of administrative bodies has been the most significant legal trend of the last century, and perhaps more values today are affected by their decisions than by those of all the courts, review of administrative decisions apart." *Federal Trade Commission v. Ruberoid Co.,* 343 U.S. 470 (1952). This is evidenced by the great increase in the number and activities of Federal government boards, commissions, and other agencies. Certainly, agencies create more legal rules and adjudicate more controversies than all the legislatures and courts combined.

1-4 Legal Analysis

Decisions in State trial courts generally are not reported or published. The precedent a trial court sets is not sufficiently weighty to warrant permanent reporting. Except in New York and a few other States where selected trial court opinions are published, decisions in trial courts are simply filed in the office of the clerk of the court, where they are available for public inspection. Decisions of State courts of appeals are published in consecutively numbered volumes called "reports." Court decisions are found in the official State reports of most States. In addition, West Publishing Company publishes State reports in a regional reporter, called the National Reporter System, composed of the following: Atlantic (A., A.2d, or A.3d), South Eastern (S.E. or S.E.2d), South Western (S.W., S.W.2d, or S.W.3d), New York Supplement (N.Y.S. or N.Y.S.2d), North Western (N.W. or N.W.2d), North Eastern (N.E. or N.E.2d), Southern (So., So.2d, or So.3d), Pacific (P., P.2d, or P.3d), and California Reporter (Cal.Rptr., Cal.Rptr.2d, or Cal.Rptr.3d). At least twenty States no longer publish official reports and have designated a commercial reporter as the authoritative source of State case law. After they are published, these opinions, or "cases," are referred to ("cited") by giving (1) the name of the case; (2) the volume, name, and page of the official State report, if any, in which it is published; (3) the volume, name, and page of the particular set and series of the National Reporter System; and (4) the volume, name, and page of any other selected case series. For instance, *Lefkowitz v. Great Minneapolis Surplus Store, Inc.,* 251 Minn. 188, 86 N.W.2d 689 (1957) indicates that the opinion in this case may be found in Volume 251 of the official Minnesota Reports at page 188; and in Volume 86 of the North Western Reporter, Second Series, at page 689.

The decisions of courts in the Federal system are found in a number of reports. U.S. District Court opinions appear in the Federal Supplement (F.Supp. or F.Supp.2d). Decisions of the U.S. Court of Appeals are found in the Federal Reporter (Fed., F.2d, or F.3d), and the U.S. Supreme Court's opinions are published in the U.S. Supreme Court Reports (U.S.), Supreme Court Reporter (S.Ct.), and Lawyers Edition (L.Ed.). While all U.S. Supreme Court decisions are reported,