

8th EDITION

THE LEGAL ENVIRONMENT TODAY



Roger LeRoy Miller & Frank B. Cross

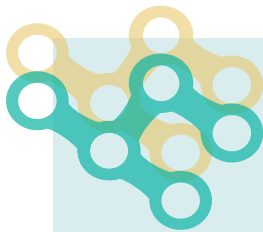


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Roger LeRoy Miller

Institute for University Studies, Arlington, Texas

Frank B. Cross

Herbert D. Kelleher
Centennial Professor in Business Law
University of Texas at Austin



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The Legal Environment Today

EIGHTH EDITION

Roger LeRoy Miller

Frank B. Cross

**Vice President and
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Social Sciences
& Qualitative Business:**
Erin Joyner

Product Director:
Michael Worls

Senior Product Manager:
Vicky True-Baker

Managing Developer:
Rebecca von Gillern

Product Assistant:
Ryan McAndrews

Marketing Director:
Kristen Hurd

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Cengage Learning
200 First Stamford Place, 4th Floor
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Preface

The study of the legal environment of business has universal applicability. A student entering any field of business must have at least a passing understanding of business law in order to function in the real world.

Additionally, students preparing for a career in accounting, government and political science, economics, and even medicine can use much of the information that they learn in a legal environment of business course. In fact, every individual throughout his or her lifetime can benefit from a knowledge of contracts, employment relationships, real property law, land-use control, and other legal topics. Consequently, we have fashioned this text as a useful “tool for living” for all of your students (including those taking the CPA exam).

For the Eighth Edition, we have spent a great deal of effort making this book more contemporary, exciting, and visually appealing than ever before. We have also added many new features and special pedagogical devices that focus on legal, ethical, global, and corporate issues, while addressing core curriculum requirements.

Unique New Digital Learning Systems

Before we discuss the many new aspects of this text, however, we wish to point out the exciting new digital products offered in conjunction with the text.

MindTap Legal Environment for The Legal Environment Today, Eighth Edition

MindTap™ Legal Environment is a fully online, highly personalized learning experience built upon authoritative Cengage Learning content. By combining readings, multimedia, activities, and assessments into a singular Learning Path, *MindTap* guides students through their course with ease and engagement. Instructors personalize the Learning Path by customizing Cengage Learning resources and adding their own content via apps that integrate into the *MindTap* framework seamlessly with Learning Management Systems.

Legal environment instructors have told us that it is important to help students **Prepare** for class, **Engage** with the course concepts to reinforce learning, **Apply** these concepts in real-world scenarios, and use legal reasoning and critical thinking to **Analyze** business law and legal environment content.

Accordingly, the *MindTap Legal Environment* product provides a four-step Learning Path designed to meet these critical needs while also allowing instructors to measure skills and outcomes with ease.

1. **Prepare**—Interactive worksheets are guided readings designed to prepare students for classroom discussion by ensuring reading and comprehension.
2. **Engage**—Real-world videos with related questions help engage students by displaying the relevance of business law in everyday life.
3. **Apply**—Brief hypotheticals help students practice spotting issues and applying the law in the context of short factual scenarios.
4. **Analyze**—Case-problem blueprints promote deeper critical thinking and legal reasoning by building on acquired knowledge to truly assess students’ understanding of legal principles.

Each and every item in the Learning Path is assignable and gradable. This gives instructors the knowledge of class standings and concepts that may be difficult. Additionally, students gain knowledge about where they stand—both individually and compared to the highest performers in class.

To view a demo video and learn more about *MindTap Legal Environment*, please visit www.cengage.com/mindtap.

CourseMate

CourseMate for *The Legal Environment Today* brings business law concepts to life with interactive learning, study, and exam preparation tools that support the printed textbook. Built-in engagement tracking tools allow you to assess the study activities of your students.

Additionally, *The Legal Environment Today* CourseMate includes an interactive online textbook, which contains the complete content of the print textbook enhanced by the many advantages of a digital environment.

Cengage Learning Testing Powered by Cognero

Cengage Learning Testing Powered by Cognero is a flexible, online system that allows you to do the following:

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- **Cross-compatible capability.** Import and export content into other systems.

What Is New in the Eighth Edition

Instructors have come to rely on the coverage, accuracy, and applicability of *The Legal Environment Today*. To make sure that our text engages your students, solidifies their understanding of legal concepts, and provides the best teaching tools available, we now offer the following items in the text.

New Chapter on Internet Law, Social Media, and Privacy

For the Eighth Edition, we have included an entirely new chapter (Chapter 9) entitled **Internet Law, Social Media, and Privacy**. Social media have entered the mainstream and become a part of everyday life for many businesspersons. Throughout the text, we recognize this trend by incorporating the Internet and social media as they relate to the topics under discussion.

We also give the legal issues and laws surrounding the Internet, social media, and privacy special emphasis in this new chapter. In addition, the chapter discusses recent legal developments concerning the protection of social media passwords and the use of social media by employers and law enforcement.

New Managerial Strategy Features

For the Eighth Edition, we have created a new feature entitled ***Managerial Strategy*** that focuses on the management aspects of business law. Special emphasis is given to sustainability, ethical trends, and changing managerial responsibilities.

Each feature includes a short section entitled ***Managerial Implications*** that provides concrete information for managers and connects the topic under discussion to operating a business. Each feature also concludes with two ***Business Questions*** that prompt students to further examine the issues discussed. **Suggested answers to all the Business Questions are included in the Solutions Manual for this text.**

Topics examined in these features include:

- Budget Cuts for State Courts Can Affect Businesses (Chapter 3).
- Marriage Equality and the Constitution (Chapter 4).
- Many Companies Have to Revise Their Social Media Policies (Chapter 17).

New Spotlight Cases and Spotlight Case Problems

For the Eighth Edition of *The Legal Environment Today*, certain cases and case problems have been carefully chosen as exceptionally good teaching cases. ***Spotlight Cases*** and ***Spotlight Case Problems*** are labeled either by the name of one of the parties or by the subject involved. Some examples include *Spotlight on Apple*, *Spotlight on Beer Labels*, *Spotlight on Gucci*, *Spotlight on Macy's*, *Spotlight on Nike*, and *Spotlight on the Seattle Mariners*.

Instructors will find these ***Spotlight Cases*** useful to illustrate the legal concepts under discussion. Students will enjoy studying these cases because the parties are often familiar and the cases involve interesting and memorable facts. **Suggested answers to all case-ending questions and case problems are included in the Solutions Manual for this text.**

New Legal Reasoning Group Activities

For instructors who want their students to engage in group projects, each unit of the Eighth Edition concludes with a **special new Legal Reasoning Group Activity**. Each activity begins by describing a business scenario and then requires each group of students to answer a specific question pertaining to the scenario based on the information that they learned in the chapter. These projects may be used in class to spur discussion or as homework assignments. **Suggested answers to the Legal Reasoning Group Activities are included in the Solutions Manual for this text.**

New Insight into Ethics Features

For the Eighth Edition, we have created many **new Insight into Ethics features** that appear in selected chapters. These features provide valuable insights into how the courts and the law are dealing with specific issues. Each of these features ends with a **For Critical Analysis** question that explores some cultural, environmental, or technological aspect of the issue. The following are some of the topics explored in these features:

- The Emergence of Patent Trolls (Chapter 8)
- Boasting on Facebook Can Have Consequences (Chapter 9)

- Warning Labels for Video Games (Chapter 12)
- Appearance-Based Discrimination (Chapter 18)

Suggested answers to the *For Critical Analysis* questions are included in the *Solutions Manual* for this text.

New Debate This Feature

To encourage student participation and motivate students to think critically about the rationale underlying the law on a particular topic, a new feature has been created for the Eighth Edition. Entitled *Debate This*, it consists of a brief statement or question concerning the chapter material that can be used to spur lively classroom or small group discussions. It can also be used as a written assignment. This feature follows the *Reviewing . . .* feature at the end of each chapter.

Suggested pro and con responses to the *Debate This* features can be found in the *Solutions Manual* for this text.

New Cases and Case Problems

The Eighth Edition of *The Legal Environment Today* is filled with new cases and case problems. Every chapter features new cases and case problems from 2013 and 2014, and some chapters include three new cases. That means more than 85 percent of the cases are new to this edition.

The new cases have been carefully selected based on three criteria:

1. They illustrate important points of law.
2. They are of high interest to students and instructors.
3. They are simple enough factually for legal environment students to understand.

We have made it a point to find recent cases that enhance learning. We have also eliminated cases that are too difficult procedurally or factually.

Improved Ethics Coverage

For the Eighth Edition of *The Legal Environment Today*, we have significantly revised and updated the chapter on ethics and business decision making (Chapter 2). The chapter now presents a more practical, realistic, case-study approach to business ethics and the dilemmas facing businesspersons today. It also provides step-by-step guidance for making ethical business decisions.

The emphasis on ethics is reiterated in materials throughout the text, particularly the *Insight into Ethics* features and the pedagogy that accompanies selected cases and features. We also discuss **corporate governance issues** in Chapter 24. Finally, each chapter in the text includes *A Question of Ethics* case problem that provides a modern-day example of the kinds of ethical issues faced by businesspersons and explores the ways that courts can resolve them.

Additional Features of This Text

The Legal Environment Today, Eighth Edition, includes a number of pedagogical devices and special features, including those discussed here.

Linking Business Law to . . . Feature

The Eighth Edition also includes a special feature entitled *Linking Business Law to . . .* [one of the six functional fields of business]. As will be discussed in Chapter 1, the six

functional fields of business are *corporate management, production and transportation, marketing, research and development, accounting and finance, and human resources management*.

This feature appears in selected chapters to underscore how the law relates to other fields of business. Some of the new *Linking Business Law to . . .* features include:

- *Linking Business Law to Marketing*—Is Pretexting Illegal? (Chapter 4)
- *Linking Business Law to Accounting and Finance*—Protecting Your Company against Hacking of Its Bank Accounts (Chapter 6)
- *Linking Business Law to Marketing*—Trademarks and Service Marks (Chapter 8)
- *Linking Business Law to Corporate Management*—What Can You Do to Prepare for a Chapter 11 Reorganization? (Chapter 13)

Preventing Legal Disputes

The Eighth Edition of *The Legal Environment Today* continues the emphasis on providing practical information in most chapters through a special feature entitled **Preventing Legal Disputes**. These brief, integrated sections offer sensible guidance on steps that businesspersons can take in their daily transactions to avoid legal disputes and litigation in a particular area.

Online Developments

The Eighth Edition contains many new **Online Developments** features, which examine cutting-edge cyberlaw issues coming before today's courts. Here are some examples of these features:

- Corporate Reputations under Attack (Chapter 2)
- Facebook Uses Privacy Concerns to Smear Google (Chapter 5)
- Even Smartphones Are Vulnerable to Cyber Attacks (Chapter 6)
- The New Era of Crowdfunding (Chapter 15)
- Social Media in the Workplace Come of Age (Chapter 17)
- The Justice Department Goes after E-Book Pricing (Chapter 23)

Each feature concludes with a *Critical Thinking* question that asks the student to analyze some facet of the issues discussed in the feature. **Suggested answers to these questions are included in the Solutions Manual for this text.**

Emphasis on Business and on Critical Thinking

For the Eighth Edition, we have focused on making the text more business related. To that end, we have carefully chosen cases, features, and problems that are relevant to operating a business.

In addition, we recognize that today's business leaders must often think “outside the box” when making business decisions. For this reason, we have included numerous critical thinking and legal reasoning elements in this text. Almost all of the features and cases presented in the text conclude with some type of critical thinking question.

Cases may include one or more of the following critical thinking questions:

- *What If the Facts Were Different?*
- *The Ethical Dimension*
- *The E-Commerce Dimension*
- *The Global Dimension*
- *The Legal Environment Dimension*

Suggested answers to all questions following cases can be found in the Solutions Manual for this text.

Managerial Implications in Selected Cases

In addition to the critical thinking questions, we have included special case pedagogy at the end of selected cases that have particular importance for business managers. This section, called *Managerial Implications*, points out the significance of the court's ruling in the case for business owners and managers.

Highlighted and Numbered Examples and Case Examples

Many instructors use cases and examples to illustrate how the law applies to business. For this edition, we have expanded both our in-text examples and our discussion of case law by adding highlighted numbered *Examples* and *Case Examples* in every chapter.

These two features are uniquely designed and consecutively numbered throughout each chapter for easy reference. *Examples* illustrate how the law applies in a specific situation. *Case Examples* present the facts and issues of an actual case, and then describe the court's decision and rationale. The numbered *Examples* and *Case Examples* features are integrated throughout the text to help students better understand how courts apply the principles in the real world.

Two Issue Spotters

At the conclusion of each chapter, we include **two Issue Spotters related to the chapter's topics** that facilitate student learning and review of the materials. **Suggested answers to the Issue Spotters in every chapter are provided in Appendix D at the end of the text.**

Reviewing Features in Every Chapter

In the Eighth Edition of *The Legal Environment Today*, we continue to offer a *Reviewing* feature at the end of every chapter to help solidify students' understanding of the chapter materials. Each *Reviewing* feature presents a hypothetical scenario and then asks a series of questions that require students to identify the issues and apply the legal concepts discussed in the chapter.

These features are designed to help students review the chapter topics in a simple and interesting way and see how the legal principles discussed in the chapter affect the world in which they live. An instructor can use these features as the basis for in-class discussion or encourage students to use them for self-study prior to completing homework assignments. **Suggested answers to the questions posed in the Reviewing features can be found in the Solutions Manual for this text.**

Exhibits

When appropriate, we also illustrate important aspects of the law in graphic form in exhibits. In all, nearly fifty exhibits are featured in *The Legal Environment Today*, Eighth Edition. Several of these exhibits are new, and we have modified existing exhibits to achieve better clarity.

Case Problems

Every chapter includes a 2013 and 2014 case problem in the *Business Scenarios and Case Problems* that appear at the end of the chapter. These problems are designed to clarify how modern courts deal with the business issues discussed in the chapter.

At the request of instructors, we have given every business scenario and case problem a label that identifies the chapter topic to which the question relates. These labels make it easier for instructors who wish to assign only certain questions to their students. In

addition, for this edition, we have added references to the section in the text where the problem's answer can be found.

We have also included two special problems—the *Spotlight Case Problems* (in selected chapters, as mentioned earlier), which are based on good teaching cases with interesting facts, and the *Business Case Problem with Sample Answer* (discussed next).

Suggested answers to all *Business Scenarios and Case Problems* are included in the *Solutions Manual* for this text.

Business Case Problem with Sample Answer in Each Chapter

In response to those instructors who would like students to have sample answers available for some of the questions and case problems, we include a *Business Case Problem with Sample Answer* in each chapter. The *Business Case Problem with Sample Answer* is based on an actual case, and students can access a sample answer in Appendix E at the end of the text.

A Complete Supplements Package

This edition of *The Legal Environment Today* is accompanied by many teaching and learning supplements, which are available on the password-protected portion of the Instructor's Companion Web Site.

The complete teaching/learning package includes the supplements listed next. For further information on *The Legal Environment Today* teaching/learning package, contact your local sales representative or visit *The Legal Environment Today* Web site.

Instructor's Companion Web Site

The Instructor's Companion Web Site contains the following supplements:

- ***Instructor's Manual.*** Includes sections entitled “Additional Cases Addressing This Issue” at the end of selected case synopses.
- ***Solutions Manual.*** Provides answers to all questions presented in the text, including the questions in each case, feature, and unit-ending feature.
- ***Test Bank.*** A comprehensive test bank that contains multiple choice, true/false, and short essay questions.
- ***Case-Problem Cases.***
- ***Case Printouts.***
- ***PowerPoint slides.***
- ***Lecture Outlines.***
- ***Business Law Digital Video Library.*** Provides access to ninety videos, including the *Drama of the Law* videos and video clips from actual Hollywood movies. Access to our Digital Library is available in an optional package with each new text at no additional cost. You can access the Business Law Digital Video Library, along with corresponding *Video Questions* that are related to specific chapters in the text, at www.cengagebrain.com.

For Users of the Seventh Edition

First of all, we want to thank you for helping make *The Legal Environment Today* the best-selling legal environment text in America today. Second, we want to make you aware of the numerous additions and changes that we have made in this edition—many in response to comments from reviewers.

New Chapter and Special Pedagogy

For this edition, we have added more material on Internet law and social media throughout the text. We have also created an entire chapter (Chapter 9) on Internet law, social media, and privacy.

We have also added the following entirely new elements for the Eighth Edition:

- *Learning Objectives* in the margin.
- New *Managerial Strategy* features.
- New *Spotlight Cases* and *Spotlight Case Problems*.
- New *Debate This* features at the end of every chapter.
- New *Legal Reasoning Group Activities* for every unit.

Significantly Revised Chapters

Every chapter of the Eighth Edition has been revised as necessary to incorporate new developments in the law or to streamline the presentations. Other major changes and additions for this edition include the following:

- **Chapter 2 (Business Ethics)**—This chapter has been thoroughly revised with all new cases, business scenarios, and many new case problems. It includes a new section on business ethics and social media, as well as an in-depth discussion of stakeholders and corporate social responsibility. The chapter also provides step-by-step guidance on making ethical business decisions and includes materials on global business ethics. An *Online Developments* feature examines Corporate Reputations under Attack.
- **Chapter 4 (Business and the Constitution)**—The chapter has been revised and updated to be more business oriented. It has numerous new *Examples* and *Case Examples*, many of which are based on United States Supreme Court decisions. The chapter includes an updated discussion of privacy rights and the equal protection clause. We have added two new cases and four new features, which discuss computers and free speech, Facebook photos and the First Amendment, same-sex marriages, and pretexting.
- **Chapter 5 (Torts and Strict Liability)**—This chapter has been thoroughly revised and updated. It includes a new defamation case example involving soccer player David Beckham. All of the cases presented in the chapter are new to this edition, including a *Spotlight on the Seattle Mariners*. An *Online Developments* feature involves Facebook and privacy concerns.
- **Chapter 6 (Criminal Law and Cyber Crime)**—The chapter includes many new examples and case examples. There is a new subsection and 2014 case on the reasonable expectation of privacy, and a new *Linking Business Law to Accounting and Finance* addresses Protecting Your Company against Hacking of Its Bank Accounts.
- **Chapter 7 (International Law in a Global Economy)**—The chapter now discusses international dispute resolution and includes a feature on border searches of electronic devices. There are three new cases, including a new *Spotlight on International Torts* that involves Mercedes-Benz Argentina, and several new examples, such as one concerning the 2014 Russian takeover of Crimea.
- **Chapter 8 (Intellectual Property Rights)**—The materials on intellectual property rights have been thoroughly revised and updated to reflect the most current laws and trends. Two of the cases are new, and a United States Supreme Court decision is presented as a *Spotlight Case*. There is a discussion of the dispute between Apple, Inc., and Samsung Electronics Company over smartphones, and many new examples, including one on Sherlock Holmes to illustrate how works fall into the public domain. There are numerous new features. An *Insight into Ethics* discusses The Emergence of Patent Trolls. A *Beyond Our Borders* discusses a 2013 United States Supreme Court decision on the resale on eBay of textbooks purchased abroad. The case problems include a *Spotlight on Macy's*.
- **Chapter 9 (Internet Law, Social Media, and Privacy)**—This chapter is all new and

was created for the Eighth Edition to explore timely topics. It discusses legal issues that are unique to the Internet, such as spam, domain name disputes, cybersquatting, digital copyright laws, and file-sharing. It also discusses social media, company-wide social media networks, state legislation on social media, the Electronic Communications Privacy Act, and password protection. The chapter also covers online defamation, data collection and cookies, and online privacy, and includes several features.

- **Chapters 10 and 11 (the contracts materials)**—The materials on contracts have been substantially revised and updated to include numerous new examples and case examples. Five of the six cases are new, and they include a new *Spotlight on Nike*. Both of the chapters have new *Online Developments* features—one concerns the validity of e-signatures in contracts with online schools and another discusses catfishing and online friends. There are also new *Insight into Ethics* features in both chapters, a *Spotlight on Taco Bell* case problem in Chapter 10, and a new *Preventing Legal Disputes* in Chapter 11.
- **Chapter 12 (Sales, Leases, and Product Liability)**—This chapter includes two new cases, and a *Spotlight on Baseball Cards*. Three new features have been added, one on how local governments are attempting to levy taxes on online travel companies, another on warning labels for video games, and another on imposing product liability in China. A *Spotlight on Apple* case problem is included.
- **Chapter 13 (Creditor-Debtor Relations and Bankruptcy)**—This chapter has been revised to be more up to date and comprehensible. We have streamlined the materials to focus on those concepts that students need to know and included updated dollar amounts of various provisions of the Bankruptcy Code. There are three new cases, several new features, and a new section and *Spotlight Case* on Mortgages.
- **Chapter 14 (Small Business Organizations)**—This chapter now provides more practical information and recent examples. There are two new cases and a *Classic Case*, new *Managerial Strategy* and *Insight into Ethics* features, and a *Spotlight on Liberty Tax* case problem.
- **Chapter 15 (Corporations)**—The chapter has been streamlined and revised to be more up to date. It includes a new subsection and discussion of benefit corporations, two new features, including one on crowdfunding, and a new *Spotlight on Smart Inventions* case problem.
- **Chapter 16 (Agency Relationships)**—Many new case examples have been added to this chapter, as well as three new cases, including a *Spotlight Case*. The chapter also includes two new features and several new case problems.
- **Chapter 17 (Employment, Immigration, and Labor Law)**—This chapter discusses many legal issues facing employers today, and includes updated minimum wage figures and Social Security and Medicare percentages. We have also included a discussion of the Affordable Care Act (Obamacare) and a new *Preventing Legal Disputes*. The materials on immigration law have been streamlined and updated, and include a discussion of state immigration legislation and its constitutionality. A *Managerial Strategy* feature covers how many companies are changing their social media policies, and an *Online Developments* feature discusses social media in the workplace. A *Spotlight on Coca-Cola* case problem is included.
- **Chapter 18 (Employment Discrimination)**—We have added *Examples* and *Case Examples* throughout this chapter, as well as new numbered lists of elements, and two new cases. A new *Insight into Ethics* feature examines appearance-based discrimination. We discuss relevant United States Supreme Court decisions affecting employment issues throughout this chapter, including a 2014 decision on affirmative action.
- **Chapter 20 (Consumer Protection)**—This chapter has been streamlined and updated. The chapter also includes a *Spotlight on Honda* case and a *Spotlight on McDonald's* case problem.
- **Chapter 22 (Real Property and Land-Use Control)**—Parts of this chapter have been significantly revised. Several new terms and new *Case Examples* were added. The discussion of eminent domain for economic development was updated. A *Spotlight Case*

covers whether the buyer of an allegedly haunted house can seek rescission of the sale. The discussion of zoning laws has been reworked, and several numbered lists explain permissible uses of land and requirements for variances.

- **Chapter 23 (Antitrust Law and Promoting Competition)**—We have added a new exhibit, several new *Examples* and *Case Examples*, and expanded coverage of leading cases. An *Online Developments* feature discusses price fixing and e-books. Updated thresholds for interlocking directorates have been incorporated.
- **Chapter 24 (Investor Protection and Corporate Governance)**—This chapter has been substantially revised, updated, and simplified. It includes new numbered lists of elements, two new cases, and a *Classic Case*. A new *Insight into Ethics* feature covers shareholder “say-on-pay” provisions.

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Since we began this project many years ago, a sizable number of legal environment of business professors and others have helped us in various phases of the undertaking. The following reviewers offered numerous constructive criticisms, comments, and suggestions during the preparation of the previous editions.

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As in all past editions, we owe a debt of extreme gratitude to the numerous individuals who worked directly with us or at Cengage Learning. In particular, we wish to thank Vicky True-Baker and Michael Worls for their helpful advice and guidance during all of the stages of this new edition. We extend our thanks to Rebecca von Gillern, our content developer, for her many useful suggestions and for her efforts in coordinating and ensuring the timely and accurate publication of all supplemental materials. We are also indebted to Katie Jergens for her excellent marketing advice.

Our content project manager, Ann Borman, and our art director, Michelle Kunkler, made sure that we came out with an error-free, visually attractive Eighth Edition. We appreciate their efforts. We are also indebted to the staff at Parkwood Composition, our compositor. Their ability to generate the pages for this text quickly and accurately made it possible for us to meet our ambitious printing schedule.

We especially wish to thank Katherine Marie Silsbee for her management of the entire project, as well as for the application of her superb research and editorial skills. We also wish to thank William Eric Hollowell, who co-authored the *Solutions Manual* and the *Test Bank* for his excellent research efforts. We were fortunate enough to have the copyediting services of Beverly Peavler and the proofreading services of Jeanne Yost. We are grateful for the efforts of Vickie Reiersen and Roxanna Lee for their proofreading and other assistance, which helped to ensure an error-free text. Finally, we thank Suzanne Jasin of K & M Consulting for her many special efforts on this project.

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Through the years, we have enjoyed an ongoing correspondence with many of you who have found points on which you wish to comment. We continue to welcome all comments and promise to respond promptly. By incorporating your ideas, we can continue to write a business law text that is best for you and best for your students.

FB.C.
 R.L.M.

Dedication

To my parents and sisters.

FB.C.

To Sophie and Philippe,

Writing is life.

Let's continue forever.

R.L.M.

UNIT 1



(BackyardProduction/iStockphoto.com)

The Foundations



UNIT CONTENTS

1. Business and Its Legal Environment
2. Business Ethics
3. Courts and Alternative Dispute Resolution
4. Business and the Constitution
5. Torts and Strict Liability
6. Criminal Law and Cyber Crime
7. International Law in a Global Economy

Business and Its Legal Environment

CONTENTS

- Business Activities and the Legal Environment
- Sources of American Law
- The Common Law Tradition
- Classifications of Law

LEARNING OBJECTIVES

The five learning objectives below are designed to help improve your understanding of the chapter. After reading this chapter, you should be able to answer the following questions:

1. What are four primary sources of law in the United States?
2. What is the common law tradition?
3. What is a precedent? When might a court depart from precedent?
4. What is the difference between remedies at law and remedies in equity?
5. What are some important differences between civil law and criminal law?



(JustASCI/Shutterstock.com)



“Laws should be like clothes. They should be made to fit the people they are meant to serve.”
—Clarence Darrow, 1857–1938 (American lawyer)

In the chapter-opening quotation, Clarence Darrow asserts that law should be created to serve the public. As you are part of that public, the law is important to you. Those entering the world of business will find themselves subject to numerous laws and government regulations. A basic knowledge of these laws and regulations is beneficial—if not essential—to anyone contemplating a successful career in today’s business environment.

Although the law has various definitions, they all are based on the general observation that **law** consists of *enforceable rules governing relationships among individuals and between individuals and their society*. In some societies, these enforceable rules consist of unwritten principles of behavior, while in other societies they are set forth in ancient or contemporary law codes. In the United States, our rules consist of written laws and court decisions created by modern legislative and judicial bodies. Regardless of how such rules are created, they all have one feature in common: *they establish rights, duties, and privileges that are consistent with the values and beliefs of a society or its ruling group*.

Law A body of enforceable rules governing relationships among individuals and between individuals and their society.

In this introductory chapter, we look first at an important question for any student reading this text: How do business law and the legal environment affect business decision making? Next, we describe the basic sources of American law, the common law tradition, and some schools of legal thought. We conclude the chapter with a discussion of some general classifications of law.

Business Activities and the Legal Environment

As those entering the business world will learn, laws and government regulations affect all business activities—hiring and firing decisions, workplace safety, the manufacturing and marketing of products, and business financing, to name just a few. To make good business decisions, a basic understanding of the laws and regulations governing these activities is essential. Moreover, in today's setting, simply being aware of what conduct can lead to legal **liability** is not enough. Businesspersons must develop critical thinking and legal reasoning skills so that they can evaluate how various laws might apply to a given situation and determine the potential result of their course of action. Businesspersons are also under increasing pressure to make ethical decisions and to consider the consequences of their decisions for stockholders and employees (as will be discussed in Chapter 2).

Liability The state of being legally responsible (liable) for something, such as a debt or obligation.

Many Different Laws May Affect a Single Business Transaction

As you will note, each chapter in this text covers a specific area of the law and shows how the legal rules in that area affect business activities. Although compartmentalizing the law in this fashion facilitates learning, it does not indicate the extent to which many different laws may apply to just one transaction. This is where the critical thinking skills that you will learn throughout this book become important. You need to be able to identify the various legal issues, apply the laws that you learn about, and arrive at a conclusion on the best course of action.

EXAMPLE 1.1 Suppose that you are the president of NetSys, Inc., a company that creates and maintains computer network systems for other business firms. NetSys also markets software for internal computer networks. One day, Janet Hernandez, an operations officer for Southwest Distribution Corporation (SDC), contacts you by e-mail about a possible contract involving SDC's computer network. In deciding whether to enter into a contract with SDC, you need to consider, among other things, the legal requirements for an enforceable contract. Are the requirements different for a contract for services and a contract for products? What are your options if SDC **breaches** (breaks, or fails to perform) the contract? The answers to these questions are part of contract law and sales law.

Breach The failure to perform a legal obligation.

Other questions might concern payment under the contract. How can you guarantee that NetSys will be paid? For example, if SDC pays with a check that is returned for insufficient funds, what are your options? Answers to these questions can be found in the laws that relate to negotiable instruments (such as checks) and creditors' rights. Also, a dispute may arise over the rights to NetSys's software, or there may be a question of liability if the software is defective. There may even be an issue as to whether you and Hernandez had the authority to make the deal in the first place. Resolutions of these questions may be found in the laws that relate to intellectual property, e-commerce, torts, product liability, agency, business organizations, or professional liability. ●

Finally, if any dispute cannot be resolved amicably, then the laws and the rules concerning courts and court procedures spell out the steps of a lawsuit. Exhibit 1–1 that follows illustrates the various areas of the law that may influence business decision making.

To avoid potential legal disputes, be aware of the many different laws that may apply to a single business transaction. Become familiar with the laws that affect your business operations, but always consult an expert. Attorneys must keep up with the myriad rules and regulations that govern the conduct of business in the United States. When you need to choose an attorney, obtain recommendations from friends, relatives, or business associates who have had long-standing relationships with their attorneys. If that fails, contact your local or state bar association, or check FindLaw's online directory (at lawyers.findlaw.com).

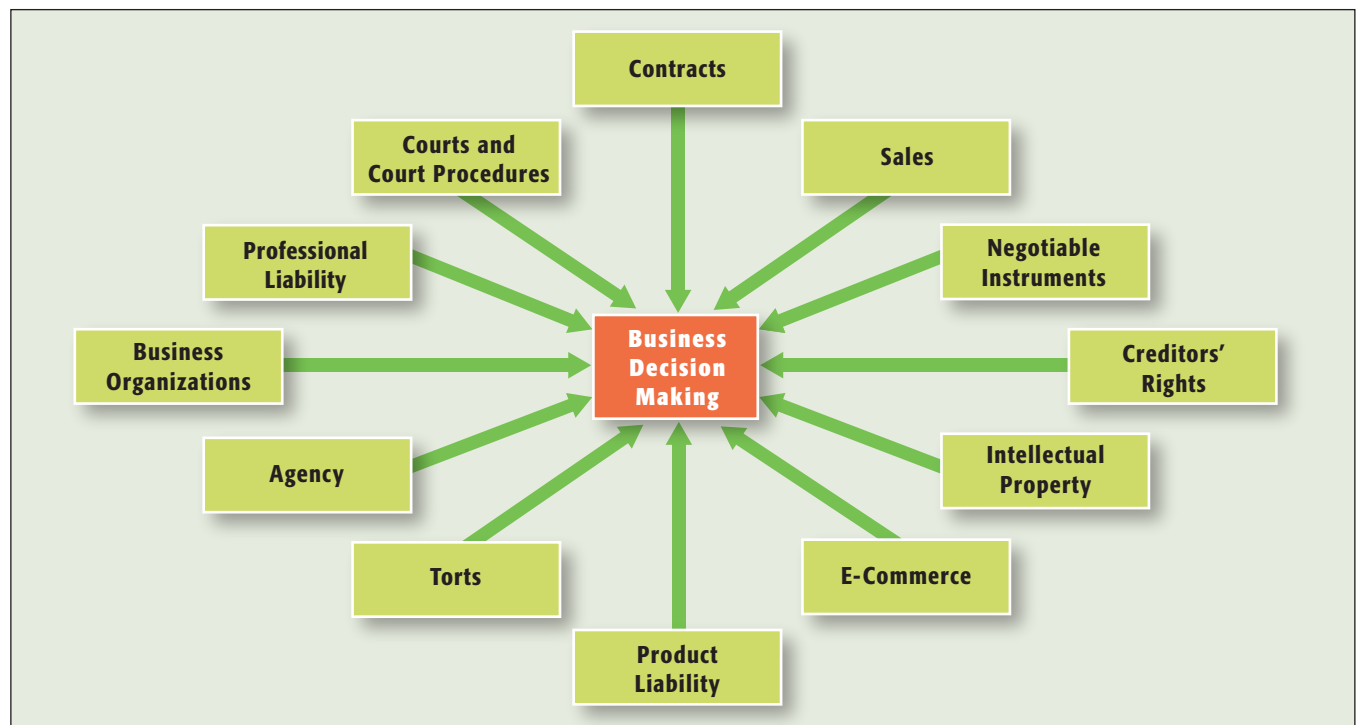
PREVENTING LEGAL DISPUTES

Linking Business Law to the Six Functional Fields of Business

In all likelihood, you are taking a business law or legal environment course because you intend to enter the business world, though some of you may also plan to become full-time practicing attorneys. Many of you are taking other business school courses and may therefore be familiar with the functional fields of business listed below:

1. Corporate management.
2. Production and transportation.
3. Marketing.
4. Research and development.
5. Accounting and finance.
6. Human resource management.

Exhibit 1-1 Areas of the Law That May Affect Business Decision Making





Every small-business person will at some time need to look up laws relating to his or her commercial activities.

Learning Objective 1

What are four primary sources of law in the United States?

Primary Source of Law A document that establishes the law on a particular issue, such as a constitution, a statute, an administrative rule, or a court decision.

Secondary Source of Law A publication that summarizes or interprets the law, such as a legal encyclopedia, a legal treatise, or an article in a law review.

Constitutional Law The body of law derived from the U.S. Constitution and the constitutions of the various states.

One of our goals in this text is to show how legal concepts can be useful for managers and businesspersons, whether their activities focus on management, marketing, accounting, or some other field. To that end, several chapters conclude with a special feature called “*Linking Business Law to* [one of the six functional fields of business].”

The Role of the Law in a Small Business

Some of you may end up working in a small business or even owning and running one yourselves. The small business owner/operator is the most general of managers. When you seek additional financing, you become a finance manager. When you “go over the books” with your bookkeeper, you become an accountant. When you decide on a new advertising campaign, you are suddenly the marketing manager. When you hire employees and determine their salaries and benefits, you become a human resources manager.

Just as the functional fields of business are linked to the law, so too are all of these different managerial roles that a small-business owner must perform. See Exhibit 1–2, which shows some of the legal issues that may arise as part of the management of a small business. Large businesses face most of these issues, too.

Sources of American Law

There are numerous sources of American law. **Primary sources of law**, or sources that establish the law, include the following:

- The U.S. Constitution and the constitutions of the various states.
- Statutes, or laws, passed by Congress and by state legislatures.
- Regulations created by administrative agencies, such as the federal Food and Drug Administration.
- Case law (court decisions).

We describe each of these important primary sources of law in the following pages and discuss how to find statutes, regulations, and case law in the appendix at the end of this chapter.

Secondary sources of law are books and articles that summarize and clarify the primary sources of law. Legal encyclopedias, compilations (such as *Restatements of the Law*, which summarize court decisions on a particular topic), official comments to statutes, treatises, articles in law reviews published by law schools, and articles in other legal journals are examples of secondary sources of law. Courts often refer to secondary sources of law for guidance in interpreting and applying the primary sources of law discussed here.

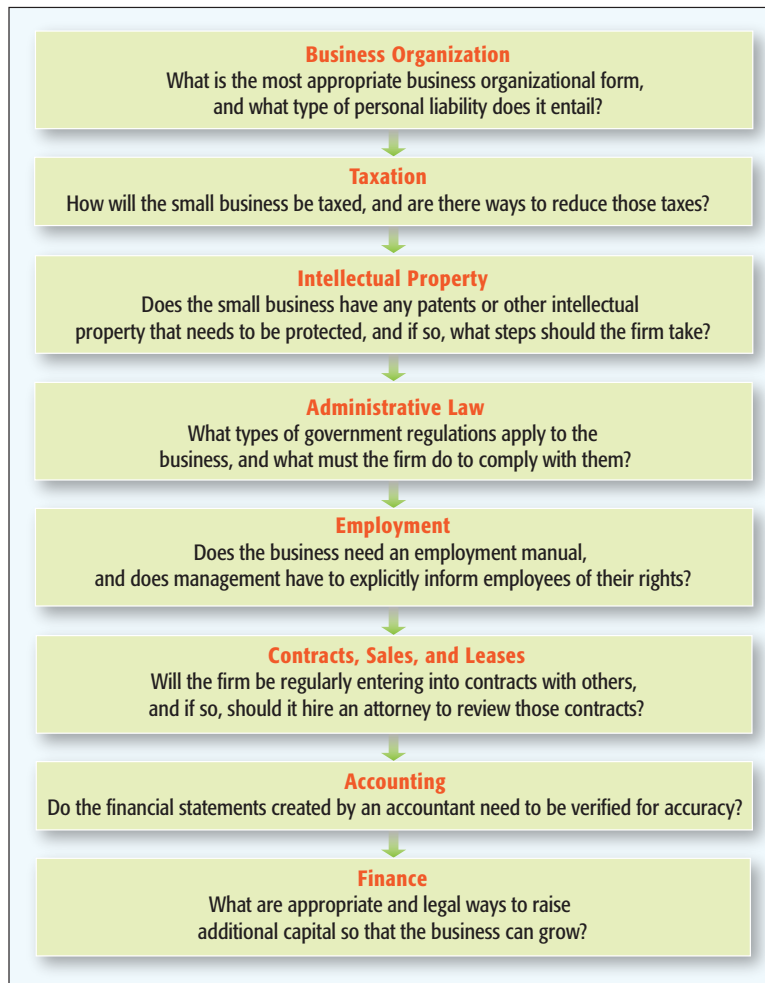
Constitutional Law

The federal government and the states have separate written constitutions that set forth the general organization, powers, and limits of their respective governments. **Constitutional law** is the law as expressed in these constitutions.

The U.S. Constitution is the supreme law of the land. As such, it is the basis of all law in the United States. A law in violation of the U.S. Constitution, if challenged, will be declared unconstitutional and will not be enforced, no matter what its source. Because of its paramount importance in the American legal system, we discuss the U.S. Constitution at length in Chapter 4 and present the complete text of the U.S. Constitution in Appendix B.

The Tenth Amendment to the U.S. Constitution reserves to the states all powers not granted to the federal government. Each state in the union has its own constitution. Unless

Exhibit 1–2 Linking Business Law to the Management of a Small Business



it conflicts with the U.S. Constitution or a federal law, a state constitution is supreme within that state's borders.

Statutory Law

Laws enacted by legislative bodies at any level of government, such as the statutes passed by Congress or by state legislatures, make up the body of law generally referred to as **statutory law**. When a legislature passes a statute, that statute ultimately is included in the federal code of laws or the relevant state code of laws. Whenever a particular statute is mentioned in this text, we usually provide a footnote showing its **citation** (a reference to a publication in which a legal authority—such as a statute or a court decision—or other source can be found). In the appendix following this chapter, we explain how you can use these citations to find statutory law.

Statutory law also includes local **ordinances**—statutes (laws, rules, or orders) passed by municipal or county governing units to administer matters not covered by federal or state

Statutory Law The body of law enacted by legislative bodies (as opposed to constitutional law, administrative law, or case law).

Citation A reference to a publication in which a legal authority—such as a statute or a court decision—or other source can be found.

Ordinance A regulation enacted by a city or county legislative body that becomes part of that state's statutory law.



(AP Photo/Craig Jensen Times, Marc Golden)

Many cities have passed local ordinances banning texting while driving.

Uniform Law A model law developed by the National Conference of Commissioners on Uniform State Laws for the states to consider enacting into statute.

law. Ordinances commonly have to do with city or county land use (zoning ordinances), building and safety codes, and other matters affecting only the local governing unit.

A federal statute, of course, applies to all states. A state statute, in contrast, applies only within the state's borders. State laws thus may vary from state to state. No federal statute may violate the U.S. Constitution, and no state statute or local ordinance may violate the U.S. Constitution or the relevant state constitution.

Uniform Laws During the 1800s, the differences among state laws frequently created difficulties for businesspersons conducting trade and commerce among the states. To counter these problems, a group of legal scholars and lawyers formed the National Conference of Commissioners on Uniform State Laws (NCCUSL, online at www.nccusl.org) in 1892 to draft **uniform laws** (“model statutes”) for the states to consider adopting. The NCCUSL still exists today and continues to issue uniform laws: it has issued more than two hundred uniform acts since its inception.

Each state has the option of adopting or rejecting a uniform law. *Only if a state legislature adopts a uniform law does that law become part of the statutory law of that state.* Furthermore, a state legislature may choose to adopt only part of a uniform law or to rewrite the sections that are adopted. Hence, even though many states may have adopted a uniform law, those laws may not be entirely “uniform.”

The Uniform Commercial Code (UCC) One of the most important uniform acts is the Uniform Commercial Code (UCC), which was created through the joint efforts of the NCCUSL and the American Law Institute.¹ The UCC was first issued in 1952 and has been adopted in all fifty states,² the District of Columbia, and the Virgin Islands. The UCC facilitates commerce among the states by providing a uniform, yet flexible, set of rules governing commercial transactions. Because of its importance in the area of commercial law, we cite the UCC frequently in this text. We also present excerpts of the UCC in Appendix C.

Administrative Law

Another important source of American law is administrative law, which consists of the rules, orders, and decisions of administrative agencies. An administrative agency is a federal, state, or local government agency established to perform a specific function. Rules issued by various administrative agencies now affect almost every aspect of a business's operations, including the firm's capital structure and financing, its hiring and firing procedures, its relations with employees and unions, and the way it manufactures and markets its products. Because of its significance and influence on businesses, we discuss administrative law in detail in Chapter 19.

Case Law and Common Law Doctrines

Case Law The rules of law announced in court decisions. Case law interprets statutes, regulations, constitutional provisions, and other case law.

The rules of law announced in court decisions constitute another basic source of American law. These rules of law include interpretations of constitutional provisions, of statutes enacted by legislatures, and of regulations created by administrative agencies. Today, this body of judge-made law is referred to as **case law**. Case law—the doctrines and principles announced in cases—governs all areas not covered by statutory law or administrative law

1. This institute was formed in the 1920s and consists of practicing attorneys, legal scholars, and judges.

2. Louisiana has adopted only Articles 1, 3, 4, 5, 7, 8, and 9.

and is part of our common law tradition. We look at the origins and characteristics of the common law tradition in some detail in the pages that follow.

The Common Law Tradition

Because of our colonial heritage, much of American law is based on the English legal system. A knowledge of this tradition is crucial to understanding our legal system today because judges in the United States still apply common law principles when deciding cases.

Early English Courts

After the Normans conquered England in 1066, William the Conqueror and his successors began the process of unifying the country under their rule. One of the means they used to do this was the establishment of the king's courts, or *curiae regis*. Before the Norman Conquest, disputes had been settled according to the local legal customs and traditions in various regions of the country. The king's courts sought to establish a uniform set of rules for the country as a whole. What evolved in these courts was the beginning of the **common law**—a body of general rules that applied throughout the entire English realm. Eventually, the common law tradition became part of the heritage of all nations that were once British colonies, including the United States.

Courts developed the common law rules from the principles underlying judges' decisions in actual legal controversies. Judges attempted to be consistent, and whenever possible, they based their decisions on the principles suggested by earlier cases. They sought to decide similar cases in a similar way and considered new cases with care because they knew that their decisions would make new law. Each interpretation became part of the law on the subject and served as a legal **precedent**—that is, a court decision that furnished an example or authority for deciding subsequent cases involving identical or similar legal principles or facts.

In the early years of the common law, there was no single place or publication where court opinions, or written decisions, could be found. Beginning in the late thirteenth and early fourteenth centuries, however, portions of significant decisions from each year were gathered together and recorded in *Year Books*. The *Year Books* were useful references for lawyers and judges. In the sixteenth century, the *Year Books* were discontinued, and other reports of cases became available. (See the appendix to this chapter for a discussion of how cases are reported, or published, in the United States today.)

Stare Decisis

The practice of deciding new cases with reference to former decisions, or precedents, eventually became a cornerstone of the English and U.S. judicial systems. The practice forms a doctrine called **stare decisis**³ (“to stand on decided cases”).

The Importance of Precedents in Judicial Decision Making

Under the doctrine of *stare decisis*, once a court has set forth a principle of law as being applicable to a certain set of facts, that court and courts of lower rank must adhere to that principle and apply it in future cases involving similar fact patterns. *Stare decisis* has two aspects: (1) decisions made by a higher court are binding on lower courts, and (2) a court should not overturn its own precedents unless there is a strong reason to do so.

Controlling precedents in a *jurisdiction* (an area in which a court or courts have the power to apply the law) are referred to as binding authorities. A **binding authority** is any source of law that a court *must* follow when deciding a case. Binding authorities include

Learning Objective 2

What is the common law tradition?

Common Law The body of law developed from custom or judicial decisions in English and U.S. courts, not attributable to a legislature.

Learning Objective 3

What is a precedent? When might a court depart from precedent?

Precedent A court decision that furnishes an example or authority for deciding subsequent cases involving identical or similar legal principles or facts.

Stare Decisis A common law doctrine under which judges are obligated to follow the precedents established in prior decisions.

Binding Authority Any source of law that a court *must* follow when deciding a case.

3. Pronounced *stahree dih-sisis*.