

McINNES KERR VANDUZER FIFTH EDITION

# MANAGING THE LAW

THE LEGAL ASPECTS OF DOING BUSINESS



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# Preface

*Managing the Law: The Legal Aspects of Doing Business* aims to equip students with the conceptual tools and intellectual skills needed to identify, assess, and manage the risks that arise in the course of doing business. Students who study this text will achieve the following:

- A basic understanding of the function of law.
- A basic understanding of the structure of the Canadian legal system.
- A basic understanding of legal sources, concepts, and principles.
- A sound understanding of the specific areas of the law that are especially important to business.
- The ability to identify legal problems that arise in business contexts.
- The ability to formulate opinions on important socio-legal issues that affect business.
- The ability to apply basic legal principles to problems that arise in business contexts.
- The ability to critically evaluate legal arguments put forth by others.
- The ability to devise arguments and present them persuasively.

Training students “to think like lawyers” (to use a favourite phrase of law professors) has long been the main purpose of law courses, even those designed for business students. But although this book provides valuable insight into legal thought processes, we have written this text to address a different primary goal. With *Managing the Law*, we aim to help students learn how “to think like successful business people.” The key concept here is **risk management**. Business people should know enough about the law to identify legal issues and the options for arranging their affairs so as to avoid difficulties. Moreover, they should know enough about the law to recognize when it is appropriate to obtain expert advice from a legal professional. Success in the business world often depends on thoughtful delegation.

This book was written with these considerations firmly in mind. As a result, *Managing the Law* differs from other books on the market in two important ways. First, it is a book for business students, not law students. *Managing the Law* provides a thorough and current picture of the legal rules that are relevant in the business world. It does not sacrifice important information for the sake of simplicity. At the same time, however, it does not overwhelm the business student with unnecessary detail or impenetrable jargon. The tone is intelligent and student-friendly. The text is accessible and comprehensible, regardless of the reader’s background.

Second, the text’s recurring theme is *risk management*. That focus is reflected in both the choice and the presentation of material. Legal topics are chosen for their relevance to the commercial context. Furthermore, they are presented in a manner that fosters the development of effective risk-management skills. Through the extensive use of discussion boxes, review exercises, cases and problems, and the like, the text draws students into the business law world and requires them to actively resolve practical problems. Sometimes, of course, the proper resolution of a problem involves recognition of the need for a lawyer’s assistance.

Canadian business students, like Canadians in general, are an increasingly diverse group. They come from a variety of backgrounds in terms of personal characteristics, past qualifications, and professional aspirations. Some are new Canadians; others have long-established roots. Some are embarking on post-secondary education for the first time; others are engaged in advanced degrees. Some have little experience in the business world; others are retraining after successful careers. Some are seeking a generalized education; others are more focused on a particular career. This book is appropriate for them all.

Law texts are typically dense and uninviting, not only in substance and language but also in appearance. Business law texts often suffer the same flaw. In contrast, *Managing the Law* has

been specifically designed with the full breadth of its target audience in mind. It is visually engaging. Its use of colour, boxes, icons, figures, and layout draws readers in and provides them with room to breathe intellectually.

*Managing the Law* has also been designed for use in any course that deals with legal issues in a “business context” (using that phrase broadly). Consequently, without limiting its scope, it is appropriate for students who are studying the legal aspects of any of the following areas:

- Accounting
- Business administration
- Commerce
- Finance
- Management
- Marketing
- Office administration

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## New to This Edition

While retaining the strengths of the previous editions of *Managing the Law*, this fifth edition introduces several important changes.

- **Risk Management.** The focus on the management of legal risks is strengthened throughout the book.
  - **Taxation.** A new section dealing with the power of taxation appears in Chapter 1.
- **Paralegals.** Chapter 2 is revised to reflect the evolving role of paralegals.
- **Administrative Law.** The discussion of administrative law has been updated and streamlined to better reflect the law’s impact on business.
- **Invasion of Privacy.** New developments in the emerging tort of invasion of privacy are explained in Chapter 4.
  - **Intentional Infliction of Emotional Distress.** A new section in Chapter 4 explains how the tort of intentional infliction of emotional distress may arise in the business world.
  - **Citizen’s Arrest.** Recent changes to the rules governing the power of citizen’s arrest are presented in Chapter 4.
- **Business Torts.** Chapter 5, dealing with business torts, has been updated and substantially re-written for greater accessibility. Figure 5.1 organizes the various torts to emphasize the roles they play in business.
  - **Unlawful Means Tort.** The new unlawful means tort that the Supreme Court of Canada recognized in *AI Enterprises v Bram Enterprises* is presented in Chapter 5.
- **Defamation.** Chapter 5 contains a new Case Brief that explains how online hosts may be liable for defamatory statements made by bloggers.
- **Contractual Acceptance.** The discussion of contractual acceptance in Chapter 7 has been re-written to reflect the growing importance of online commerce.
- **Consideration and Privity.** The sections in Chapter 8 that deal with the rules governing assignments and trusts have been substantially revised for greater accessibility and clarity.
- **Duty of honest performance.** A new Case Brief has been added to reflect the SCC decision in *Bhasin v Hrynew*, setting out a new duty to perform contracts honestly.

- **Contractual Interpretation.** The section in Chapter 9 dealing with contractual interpretation have been enriched with a brief discussion of a new SCC decision: *Sattva Capital Corp v Creston Moly Corp.*
- **Rescission.** Chapter 11 includes a significantly revised discussion of rescission.
- **Strict Liability in Contract.** A new Case Brief in Chapter 11 highlights the fact that liability for breach of contract is strict.
  - **Exclusion Clauses.** Chapter 12 explains the new laws governing exclusion clauses that the Supreme Court of Canada formulated in *Tercon Contractors Ltd v British Columbia.*
  - **Land Registration.** The explanation of land registration systems in Chapter 15 is streamlined for easier understanding.
- **Business Patents.** Chapter 17 is expanded to include a discussion of the Amazon.com “one click” decision and the fledgling status of the patentability of business methods in Canada.
- **Patentable Subject Matter.** Chapter 17 now includes an important comparative analysis of the Harvard Mouse and Monsanto cases, expanding the discussion of patentable subject matter.
- **Electronic Commerce.** Chapter 18 has been significantly streamlined for the new edition.
- **Cryptocurrencies.** The automated transactions section of Chapter 18 has been expanded to include a new section on cryptocurrencies, including new material on Bitcoin and other automated payment systems.
- **Corporate Social Responsibility.** Chapter 21 is heavily revised to include an expanded discussion of corporate social responsibility, featuring real-world examples of companies that have failed or excelled.
- **Securities Law.** The discussion of securities law in Chapter 21 is expanded with a longer introduction and new material concerning environmental disclosure rules.
- **Taxation.** The taxation coverage in Chapter 24 is revised to include a new section on the taxation of corporations and shareholders, to discuss taxation of small businesses, and to provide a discussion of the legal basis for federal and provincial taxation
- **Contractors.** The section on contractors in Chapter 25 is expanded to include information on a new category of worker, the dependent contractor.
- **Discrimination.** The coverage of human rights and discrimination, in Chapter 25, is changes to include updates to the Human Rights Code of several provinces.
- **Boilerplate Contractual Clauses** is a new appendix that contains a variety of examples of clauses that are discussed in Chapter 9.

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## Organization

This text is divided into nine parts.

- **Part 1 (Introduction to Law)** consists of two chapters. The first chapter, dealing with risk management and sources of law, opens with an explanation of why business people should study law explaining the core concept of risk management. The chapter then sketches the essential features of the Canadian legal system, including:
  - The nature of law
  - Branches of law
  - Sources of law

The second chapter, dealing with litigation and alternative dispute resolution, explains various mechanisms for the resolution of legal disputes:

- The litigation process
- The court system
- Alternative dispute resolution
- **Part 2 (Torts)** is divided into four chapters. The focus throughout is on risk management in the business context. Here we introduce such key concepts as vicarious liability and liability insurance. And we examine business torts such as nuisance and defamation. The final chapter, which deals with the tort of negligence, places special emphasis on professional negligence as it arises in commercial matters.
- **Part 3 (Contracts)** consists of seven chapters dealing at length with the central concept of contracts. Because of the significance of enforceable agreements in the commercial context, separate chapters are devoted to each of the following:
  - Formation of contracts
  - Consideration and privity
  - Terms and representations
  - Contractual defects
  - Discharge and breach
  - Remedies

The final chapter focuses on a particularly important type of contract:

- Sales of goods

A chapter on negotiable instruments is available online.

- **Part 4 (Property)** consists of three chapters on the law of property. The discussion, as always, places the reader at the heart of practical business-law problems. The examination of personal property, for instance, centres on the institution of bailment and the means by which various forms of insurance can be used to manage legal risks.
- **Part 5 (Business Law in the Digital Age)**, consisting of two chapters, provides an unparalleled introduction to business law in the digital age. It deals with:
  - Intellectual property rights, challenging student to think about ideas as property through a survey of copyright, trademarks, patents, and industrial design law.
  - Electronic commerce, offering students an understanding of how to manage risk when acquiring a domain name, building a website, providing online services, transacting online and across jurisdictions. The chapter canvasses a number of core legal issues when doing business online, including: privacy policies, identity theft, dealing with privacy breaches and ensuring consumer protection.
- **Part 6 (Business Organizations)** deals with various types of business organizations. Its three chapters examine sole proprietorships, partnerships, corporations, agency relationships, joint ventures, and franchises. The principles of risk management as well as contemporary issues of corporate governance and corporate social responsibility are highlighted throughout.
- **Part 7 (Practical Business Decisions)** addresses specific decisions that affect business. Its two chapters focus on the following issues:
  - How creditors can use security interests in debtor's property to reduce risk in credit transactions
  - How creditors and debtors can protect their interests in the event of bankruptcy or insolvency
- **Part 8 (Sources and Forms of Public Law Regulation)** moves the discussion out of the purely private realm and into the world of public regulation and international relations. Its one chapter examines the various means by which Canadian governments regulate commercial conduct. It considers, for example, competition law and consumer protection laws. It also explains taxation in Canada.

- **Part 9 (Employment and Labour Law)** is divided into two chapters. The first focuses on individual employment. Risk management issues are highlighted at all stages of the employee/employer relationship, ranging from pre-employment matters (such as advertising and hiring) to post-employment matters (such as dismissal and severance packages). The second chapter focuses on organized labour. It includes a discussion of collective agreements, grievances, and industrial conflicts.

Taken together, those nine parts provide a thorough examination of the legal issues that generally affect Canadian businesses. At the same time, we have organized the material to offer instructors the utmost flexibility in matching the book to their course designs. We recognize that time is usually tight in business law courses. Therefore, we have adopted a modular approach in organizing the chapters and units. After covering the introductory Chapters 1 and 2 and the core material on contracts in Chapters 7–12, instructors can feel free to cover the remaining chapters in the order that best suits their needs.

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## Features

Students learn effectively when they are interested, enthusiastic, and engaged. As a result, we have designed this text to encourage students to participate actively, rather than merely read passively. A large number of features ensure that the materials are both accessible and stimulating.

**Objectives.** Each chapter opens with a list of 10 objectives that stress key issues and highlight risk-management skills that students should aim to develop. By providing a roadmap at the beginning of each chapter, the objectives help students to read and understand the material more efficiently and more effectively.

**Key Terms.** Key terms are boldfaced where they are defined in the body of the text. They are also restated with their definitions in the margins.

**Discussion Boxes.** Each chapter contains at least one instance of each of five distinct types of discussion boxes. These boxes provide instructors with additional opportunities to stimulate critical thinking and engage students in classroom debate. With the exception of the Case Briefs, each discussion box ends with Questions for Discussion. (Model answers appear in the *Instructor's Resource Manual*.) Each type of box fulfils a particular pedagogical goal.

- **Case Briefs** illustrate how the courts have formulated and applied legal rules in specific business contexts. They also introduce students to many of the leading cases in the common law system.
- **Business Decision** boxes ask students to respond as business people to common legal problems. They are designed to foster the development of sound commercial judgment. Accordingly, they focus less on purely legal concepts and more on practical matters that influence decisions in the commercial world in light of the material covered in the chapter.
- **You Be the Judge** boxes ask students to respond as judges to legal problems that commonly arise in the business world. They are designed to give students insight into legal thought processes and an opportunity to apply the material covered in the chapter.
- **Ethical Perspective** boxes ask students to assess morally contentious business-law scenarios. They compel students to place both business considerations and legal concerns into a larger social context, and to develop an appreciation of the fact that alternative solutions often pull in different directions. These boxes are particularly effective in generating classroom discussions.

**Concept Summaries.** Every chapter contains at least one Concept Summary; most chapters contain many more. Presented in tabular form, the Concept Summaries provide succinct and easily understood reviews of difficult concepts and rules. They are often used to compare and contrast related areas of law.

**Figures.** Every chapter contains at least one figure. Various diagrams and drawings are used to illustrate and clarify important concepts. Aside from their inherent pedagogic value, they contribute to the visual appeal of the book and therefore draw students into the material.

**Chapter Summaries.** Each chapter ends with a chapter summary that briefly reviews the important concepts of the chapter. These summaries help prepare students for the end-of-chapter exercises.

**Review Questions.** Twenty review questions appear at the end of each chapter. In some instances, students are required to define and explain key concepts and terms. In others, they are asked to respond to short problems. The review questions can be discussed in class or assigned to students for independent study. (Model answers are provided in the *Instructor's Resource Manual*.)

**Cases and Problems.** Each chapter concludes with 12 Cases and Problems (with the exception of the first and second chapters, which each contain six), at least two of which are new to this edition. These exercises vary in both length and difficulty. They are ideally suited to classroom discussion, but they too can be assigned to students for independent study. (Model answers are provided in the *Instructor's Resource Manual*.)

**Canadian Case Studies.** A special Canadian Case Study is provided at the end of each of Parts 2, 5, 8, and 9. Each of these cases provides an in-depth opportunity to apply the lessons learned from the text. Students are able to identify issues within practical business contexts and then propose possible solutions. The Canadian Case Studies readily lend themselves to both classroom discussion and independent study. (Model answers are provided in the *Instructor's Resource Manual*.)

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## Supplements

We have carefully prepared the following resources to aid instructors in presenting lectures, fostering class discussion, and administering examinations. These instructor supplements are available for download from a password-protected section of Pearson Canada's online catalogue ([catalogue.pearsoned.ca](http://catalogue.pearsoned.ca)). Navigate to your book's catalogue page to view a list of those supplements that are available. Speak to your local Pearson sales representative for details and access.

- **Instructor's Resource Manual.** The *Instructor's Resource Manual* is designed to enhance the organization and presentation of course materials. It includes **model answers** for all of the questions that appear in the discussion boxes, Review Questions, and Cases and Problems. Where appropriate, the answers explain the pedagogic purpose of their associated questions. The Manual also provides **case briefs** for every judicial decision that is mentioned in the text or its footnotes. In addition, the Manual includes **teaching tips and suggestions** that instructors might find useful in tailoring the materials in the textbook for their students.
- **Computerized Test Bank.** Pearson's computerized test banks allow instructors to filter and select questions to create quizzes, tests or homework. Instructors can revise questions or add their own, and may be able to choose print or online options. These questions are also available in Microsoft Word format.
- **PowerPoint® Presentation Slides.** The PowerPoint slides for each chapter can be used in electronic form to present materials in class or in printed form to guide the preparation of new lecture notes.

- **Image Library.** An electronic version of all the figures, tables, and concept summaries from the textbook.

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## MyBusLawLab

Pearson Canada's online resource, MyBusLawLab, offers instructors and students all of their resources in one place. With MyBusLawLab, you will be able to enliven your lectures with a variety of material. A powerful homework and test manager lets you create, import, and manage online homework assignments, quizzes, and tests that are automatically graded. You can choose from a wide range of assignment options, including time limits, proctoring, and maximum number of attempts allowed. The bottom line: MyLab means less time grading and more time teaching. MyBusLawLab also makes additional materials available to students. These materials include: topics of interest as they relate to business law practices in British Columbia, Alberta, Saskatchewan, Manitoba, the Atlantic Provinces, and Ontario; the *Charter of Rights and Freedoms*; and sample mortgage documents.

- **MyBusLawLab features:**
  - **Self-study questions** for extra practice and review (the questions do not duplicate any of those in the *Test Item File*)
  - **Provincially specific material** aimed at British Columbia, Alberta, Saskatchewan, Manitoba, the Atlantic Provinces, and Ontario.
  - **Additional materials** that could not be incorporated into the book such as the text of the *Charter of Rights and Freedoms*, sample mortgage documents, and a bonus chapter *Special Contracts: Negotiable Instruments*.
  - **Pearson eText.** The Pearson eText gives students access to their textbook anytime, anywhere. In addition to note taking, highlighting, and bookmarking, the Pearson eText offers interactive and sharing features. Instructors can share their comments or highlights, and students can add their own, creating a tight community of learners within the class.

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## **Mitchell McInnes, PhD (Cambridge), LLM (Cambridge), LLB (Alberta), BA (Alberta), of the Alberta Bar, Professor**

Professor McInnes joined the Faculty of Law at the University of Alberta in 2005. He previously taught at the University of Western Ontario, the University of Melbourne, and Deakin University. He has clerked at the Supreme Court of Canada and served as a Legal Research Officer with the Alberta Court of Appeal.

Professor McInnes' research focuses on Unjust Enrichment, Restitution, Remedies, Trusts, Contract, and Tort. He has published more than one hundred papers in leading journals, including the *Canadian Bar Review*, the *University of Toronto Law Journal*, the *Cambridge Law Journal*, and the *Law Quarterly Review*. His primary work is *The Canadian Law of Unjust Enrichment and Restitution* (LexisNexis). He has also co-authored leading works in four areas of law: *Oosterhoff on Wills* (Carswell), *Cases and Materials on the Law of Torts* (Carswell), *Oosterhoff on Trusts: Text, Commentary and Cases on Trusts* (Carswell), and *Cases and Materials on the Law of Restitution* (Emond Montgomery). His work has been relied upon by a number of courts, including the Supreme Court of Canada, the United Kingdom Supreme Court, the Supreme Court of New Zealand, and the High Court of Australia.

Professor McInnes has received a number of teaching awards and he has been recognized by *Maclean's* magazine as one of Canada's leading university teachers. In 2016, he received the *Alberta Law Society's Distinguished Service in Legal Scholarship Award*.

## **Ian R. Kerr, PhD (Western), MA (Western), LLB (Western), BA Hons (Alberta), BSc (Alberta), of the Bar of Ontario, Full Professor**

As Canada Research Chair in Ethics, Law, and Technology, Ian Kerr is Canada's leading authority on how legal and ethical issues intersect with electronic commerce. Ian plays a significant role in the development of national and international laws in e-commerce, privacy policy, and digital copyright reform. He has advised various Canadian agencies on legal policy for online activities, and has served as a Canadian delegate to the United Nations' Special Working Group on e-Commerce, a project of the United Nations Commission on International Trade Law. Ian teaches at the Faculty of Law, University of Ottawa, where he co-designed a new graduate program in law and technology. He holds cross-appointments to the Faculty of Medicine, the Department of Philosophy, and the School of Information Studies, and has won numerous awards for teaching excellence.

Ian's previous research projects include *On the Identity Trail*, a multi-disciplinary project supported by one of the largest-ever grants from the Social Sciences and Humanities Research Council, which studied the impact of information and authentication technologies on identity and anonymity. He also co-led *An Examination of Digital Copyright*, a large private sector grant from Bell Canada and the Ontario Research Network in Electronic Commerce examining the implications of copyright reform on Canadian values including privacy and freedom of expression. With his background in philosophy, technology, and private law, Ian has published numerous articles and papers and has edited and contributed to several books and journals on the legal implications of doing business online, including the *Canadian Business Law Journal* and the *Electronic Commerce Research Journal*. He has also contributed scholarly articles and chapters in several books on a range of other subjects, including cyberspace law, nanotechnology, bioethics, robo-ethics, contract law, information ethics, and the philosophy of law, and has lectured world-wide on these topics. His book, *Lessons From The Identity Trail*, published by Oxford University Press, is available for free download through a creative commons licence at [idtrail.org](http://idtrail.org). His most recent book, *Robot Law*, published by Edward Elgar Publishing, breaks new ground in the emerging field of robotics and artificial intelligence law and policy.

**J. Anthony VanDuzer, LLM (Columbia), LLB (Ottawa), BA (Queen's), of the Bar of Ontario, Professor**

Tony VanDuzer has taught and practised extensively in the area of corporate and commercial law for more than 25 years. Following five years in private practice, he joined the Faculty of Law at the University of Ottawa. He teaches a variety of advanced business law subjects, for which he has received several teaching awards. He has taught in the University of Ottawa's Executive MBA program as well as at universities in the UK, Germany and New Zealand. Since 2003, he has been an Adjunct Research Professor at the Norman Paterson School of International Affairs at Carleton University.

Tony has published over 70 articles and papers on subjects ranging from pharmaceutical patents and health care to corporate law. He has also written several significant books on business law, including *The Law of Partnerships and Corporations*, 3d ed. (Concord: Irwin, 2009); and *Merger Notification in Canada* (with Albert Gourley, Toronto: CCH Canadian, 1994). His work has been cited by the Supreme Court of Canada as well as provincial superior courts and courts of appeal.

Over the past decade, he has often been called on to advise Canadian government agencies and organizations on business and trade law issues. He completed a study for the Canadian Competition Bureau in 1999 on anti-competitive pricing practices. Many of his recommendations for reform of the *Competition Act* were included in amendments to the *Act* in 2009. His study for the Department of Foreign Affairs and International Trade of the impact of the WTO General Agreement on Trade in Services on the delivery of health, education, and social services in Canada was presented to the Standing Committee on Foreign Affairs and International Trade in 2005.

Tony has worked with international development agencies around the world, such as the Canadian International Development Agency and the World Bank, delivering workshops, drafting new laws, and providing other forms of technical assistance to foreign governments on issues related to business and trade. He played a key role in the drafting of Russia's foreign trade law and business registration law.

### *Dedication*

For Alkabesa, with all my love.

**M.M.**

In memory of my father, Morley Kerr, who taught me to see the goodness in things.

**I.K.**

For Heather.

**J.A.V.**

# Table of Statutes

- Act Respecting the Protection of Personal Information in the Private Sector*, RSQ 1993, c P-39.1 (Que), 458n
- Act to Amend the Criminal Code (Identity Theft and Related Misconduct)*, SC 2009, c 28, 481n
- Act to Establish a Legal Framework for Information Technology*, SQ 2001 c 32 (Que), 467n s 27, 467
- Age of Majority Act*, CCSM, c A7 (Man), s 1, 241n
- Age of Majority Act*, RSA 2000, c A-6 (Alta), s 1, 241n
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- An Act to Amend the Criminal Code (criminal liability of organizations)*, SC 2003, c 21 (Can), s 22.2, 553n
- An Act to Amend the Defamation Act*, SNB 1980, c 16 (NB), s 1, 119n
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*Zhu v Merrill Lynch HSBC* 2002 BCPC 0535, 469  
*Zippo Manufacturing Co v Zippo Dot Com Inc* 952 F Supp 1119 (WD Pa 1997), 472n

# Risk Management and Sources of Law

# 1

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## CHAPTER OVERVIEW

### Why Study Law?

Risk Management

### An Introduction to the Legal System

The Nature of Law

A Map of the Law

Sources of Law

## LEARNING OBJECTIVES

After completing this chapter, you should be able to:

- 1 Explain why it is important for business people to study law.
- 2 List four basic strategies for managing risks.
- 3 List three strategies for risk management that businesses often use in different situations.
- 4 Provide a general definition of the word “law.”
- 5 List four areas of public law and three areas of private law. Provide examples that demonstrate how each one of those areas is relevant to business people.
- 6 Outline one way in which tort and contract law are similar and two ways in which they are different.
- 7 Explain how federalism is related to the division of powers.
- 8 Describe the *Canadian Charter of Rights and Freedoms* and provide several examples of how it can help or hurt a business.
- 9 Explain two meanings of the term “civil law” and three meanings of the term “common law.”
- 10 Explain the historical development of equity. Briefly explain the relationship between law and equity today.

Law is essential to any society. It both shapes and reflects how people interact. As we will see in this text, it can affect a person even before birth (can you sue someone for injuries that you suffered as a fetus?) and even after death (what happens to your property after you are gone?). It also governs the most important issues that arise in between: the freedom to choose a lifestyle, the right to marry, the ability to create and raise children, the obligation to pay taxes, and so on.

Not surprisingly, the law is an enormous subject. As a whole, it cannot be studied in a single course. Indeed, as a whole, it cannot be mastered in an entire lifetime. Therefore, we have to make choices. We must examine some topics and leave others to the side. To a large extent, those choices depend upon our reason for studying law in the first place.

L.O. ① ② ③

## Why Study Law?

We therefore begin with the obvious question: Why study law? The answer depends upon who you are. As consumers, we all need to be aware of the rules that govern commercial transactions. In terms of employment, you may intend to work in the public sector. If so, you need to understand not only the nature of government organizations, but also the different types of laws that may affect you. Chances are, however, that you are a business student. And as you know, businesses exist primarily to make money. The goal is to maximize gains and minimize losses.

Of course, there are many factors in that equation: hard work, natural talent, good luck, and so on. But for the most part, success and failure are the results of choices. A business must choose, for example, a product, a price, a location, and a marketing strategy. And every one of those *business* choices has *legal* consequences. Some consequences are profitable; others are financially disastrous. The difference between winning and losing in the business world often depends upon the ability to make good choices from a legal perspective. That fact suggests, in general terms, both *why* you should study law and *which* parts of the law you should study.

It is important to realize that the law can both hurt *and* help. Many people think of laws only in terms of prohibitions and punishments. For example, if you break the rule against murder, you may be sent to jail. But the law can also allow you to do things that you could not otherwise do. Generally speaking, for instance, I am entitled to ignore my promises. I can stay home and read even if I agreed to meet you at the movies. Beyond the fear of making you angry, there is nothing that compels me to keep my word. In the business world, however, that sort of behaviour simply cannot be tolerated. If I promise to provide materials to your factory, you may act on the assumption that I will deliver. For instance, you may hire extra staff or promise to re-sell the materials to someone else. You therefore need some way of holding me to my word. Your best bet is to persuade me to enter into a *contract*. As we will see in a later chapter, a contract is a legal concept that allows people to create *enforceable* promises. In that situation, you would not have to worry (as much) that I might ignore my promise.

## RISK MANAGEMENT

Throughout this text, we will see a number of other ways in which businesses can positively benefit from the law. Much more often, however, we will be concerned about avoiding losses. The main theme of our discussion is that legal education plays a critical role in *risk management*. **Risk management** is the process of identifying, evaluating, and responding to the possibility of harmful events. Business Decision 1.1 provides a simple example.

**risk management** is the process of identifying, evaluating, and responding to the possibility of harmful events

## Business Decision 1.1

### Risk Management

One of your ex-employees is hoping to join another company. She has asked you to write a reference letter on her behalf. She obviously does not know that you have a very low opinion of her, largely because you believe that she stole money from your business. Furthermore, since the company that she wants to join is one of your best customers, you are tempted to write a candid letter.

### Questions for Discussion

1. Will you write a reference for your ex-employee? If so, what will it say?

Unless you know something about the law of torts, you are not in a position to answer these questions properly. You need to identify, evaluate, and respond to the legal risks involved.

- *Identification* If you accuse your ex-employee of theft, she may sue you for defamation because your statement would cause a reasonable person to think less of her.<sup>1</sup> More surprisingly, if you unreasonably refuse to write a letter, or if you write an unreasonably brief letter, you may be held liable for reducing the ex-employee's job prospects. In any event, you need to be concerned about *liability*, about actually being held legally responsible. But you also need to be concerned about the possibility of being sued. As we will see in the next chapter, litigation is time-consuming and expensive, even when you win.
- *Evaluation* Having identified the risk of being sued for defamation, you may decide that a candid letter would nevertheless be legally acceptable. Your allegations may be true. Even if they are not, you may be justified in sharing your suspicions with the other company. Furthermore, you may believe that the arguments in your favour are strong enough to discourage your former employee from suing you.
- *Response* Finally, having identified and evaluated the risks, you need to formulate a response. You have several options. You can refuse to write a letter. You can write a letter that does not mention your suspicions. Or you can write a letter that accuses your former employee of theft. The choice is still yours. Significantly, however, you are now in a position to make an informed decision. A basic understanding of the law makes you a better business person.

Business Decision 1.1 demonstrates risks that are largely legal and private in nature. While court cases are public events, very few cases ever go before a judge. Most are settled by the parties themselves. As a result, you are mainly concerned about being held liable to your ex-employee.

Quite often, however, extra-legal concerns may prove even more important. In addition to potentially leading to liability, an accident may generate bad publicity and damage consumer confidence. Canadians have seen many examples in recent years. In 2008, for example, contamination at a Maple Leaf meat packing plant in Ontario resulted in at least six deaths and dozens of injuries from listeriosis.

<sup>1</sup> The tort of defamation is discussed in Chapter 5. As we will see, a reference letter is protected by the defence of qualified privilege, meaning that an inaccurate and harmful statement will not trigger liability if the writer acted in good faith.

Although the company's response to the tragedy was considered by many to have been a textbook example of corporate responsibility, millions of dollars were lost to suspended operations, recalled products, and loss of consumer confidence. Those risks also need to be managed.

Notice that we have been talking about risk *management*. There are potential costs associated with nearly every form of behaviour, and that includes doing nothing at all. A business probably cannot exist, and certainly cannot profit, unless it is willing to take some chances. The goal therefore is not necessarily to eliminate risks; it is to *manage* them. The appropriate strategy depends upon the circumstances.

- *Risk Avoidance* Some risks are so serious that they should be avoided altogether. An automobile that regularly explodes upon impact should be removed from the market. Aside from issues of morality, the financial costs of being held liable will probably outweigh any sales profits.<sup>2</sup>
- *Risk Reduction* Some risks can be reduced to an acceptable level through precautions. For example, a bank that lends \$500 000 to a manufacturer realizes that the loan may not be repaid if the economy goes into recession. The bank can, however, protect itself by requiring the business to grant a *mortgage* over its factory. In that case, if the bank does not get its money, it may at least get the property.
- *Risk Shifting* Even if a risk cannot be avoided or reduced, it may be shifted onto another party. We will very shortly introduce two exceptionally important strategies for shifting risks: *insurance* and *exclusion clauses*. There are others.

Suppose, for example, that a construction company requires the temporary use of a crane. It has two options. First, it may rent a crane and have it operated by one of its own employees. Second, it may rent a crane and hire an *independent contractor* to operate it.<sup>3</sup> An independent contractor is a person who performs services on behalf of a company, but who is not a regular employee of that company. Although it is often difficult to distinguish between an employee and an independent contractor, there is a crucial difference in terms of risk management.

Suppose the worker operates the crane carelessly and injures a bystander. The bystander will certainly be able to sue the person who was actually in control of the equipment. Furthermore, if that person was an employee, then the bystander will also be entitled to sue the company. Even if it did not do anything wrong, a company is *vicariously liable* for the actions of its employees. (We will examine the doctrine of vicarious liability in Chapter 3.) A company is not, however, vicariously liable for an independent contractor. In some situations, it is therefore prudent to have work done by an independent contractor, rather than an employee.

- *Risk Acceptance* It is sometimes appropriate to simply accept a risk. Imagine a golf course that operates behind a factory. It is possible that a wild shot might hit a factory window, and that the golf course might be held responsible for the resulting damage. Nevertheless, if the likelihood of such an accident is small, the club might decide to do nothing at all. It certainly would not close the course to avoid the risk altogether. It might also find that the costs of reducing the risk by erecting a large safety net, or shifting the risk by buying an insurance policy, are too high. The most sensible approach might be to hope for the best and pay for any windows that are broken.

<sup>2</sup> *Grimshaw v Ford Motor Co* (1981) 119 Cal App (3d) 757.

<sup>3</sup> We will examine the difference between employees and independent contractors in Chapters 3 and 25.

## Concept Summary 1.1

### Risk Management

Risk Management Steps	
Identification	<i>What risks exist in a particular situation?</i>
Evaluation	<i>How serious are those risks?</i>
Response	<i>How will you react?</i>
Risk Management Strategies	
Avoidance	A risk should be <i>eliminated</i> altogether.
Reduction	A risk should be <i>decreased</i> to an acceptable level.
Shifting	A risk should be <i>transferred</i> to another party.
Acceptance	A risk should be <i>tolerated</i> as a cost of doing business.
Common Risk Management Techniques	
Insurance	A risk may be reduced and shifted by contracting for an <i>insurer's promise to pay</i> if a loss occurs.
Exclusion and limitation clause	A risk may be reduced or eliminated by contracting for a right to <i>limit or exclude liability</i> .
Incorporation	A risk may be reduced by <i>conducting business through a company</i> .

Concept Summary 1.1 summarizes the steps and strategies involved in the management of particular risks. It also reveals that certain basic strategies are broadly used to manage risks. Some of those techniques are fairly obvious. Businesses should, of course, ensure that employees are carefully selected and properly trained. Other strategies are more legal in nature. We will discuss those strategies in greater detail in later chapters. At this point, it is enough simply to introduce three important concepts.

- **Insurance** An insurance policy is a type of contract. One party, called the *insured*, promises to pay a price, called the *premium*. The other party, called the *insurer*, promises to pay a certain amount of money if the insured suffers a certain type of loss. There are many types of insurance. For now, we will mention two.

*Liability insurance* provides a benefit if the purchaser is held liable for doing something wrong.<sup>4</sup> *Property insurance* provides a benefit if the purchaser's property is damaged, lost, or destroyed. (We will examine property insurance in Chapter 16.) In either situation, insurance shifts the risk. For instance, while millions of Canadians buy liability insurance every year, only a fraction of those people are actually sued. Insurance works by spreading the cost of that liability over the entire group.

- **Exclusion Clauses** Many businesses make money by selling goods or services. Those sales are created by contracts. And those contracts very often contain exclusion or limitation clauses. (We will examine exclusion and limitation clauses

<sup>4</sup> Liability insurance also creates a *duty to defend*. That means that the insurance company is responsible for the litigation, including the costs of hiring lawyers, if its customer is sued by a third party. We will examine liability insurance in Chapter 3.

in Chapters 9 and 12.) Such a clause is a contractual term that changes the usual rules of liability. The clause may attempt to exclude all risk of liability, or it may exclude liability for certain types of acts or certain types of losses, or it may limit the amount of compensation that is available.

There are countless examples. A courier company's contract may say that it cannot be held liable at all, or for more than \$100, if it loses, damages, or destroys a package. In another example, if parties conducting business do not create a written contract, a company may attempt to exclude or limit liability by posting a notice somewhere on its premises. The entrance to a car park, for instance, may contain a large sign telling customers that they park at their own risk. While exclusion and limitation clauses are subject to certain rules and restrictions, the law generally allows people to sign away their right to sue.

- **Incorporation** There are many ways to conduct business. An individual who chooses to act in a personal capacity may be held personally liable for any debts or liabilities incurred by the business. To manage those risks, many businesses are set up as corporations or companies. (We will examine corporations, and others ways of carrying on business, in Chapter 20.)

The most significant benefit of incorporation is limited liability. That means that it is usually only the company itself, and not the directors or shareholders, that may be held liable for debts. The company may be lost, but the people behind it will be safe. It is important to realize, however, that the concept of limited liability does not protect individuals from *all* risks. For example, employees, directors, and officers may be held personally liable for the torts that they commit.

Risk management does not require you to become a lawyer. It may, however, require you to hire a lawyer. As a business person, you need to know enough about the law to recognize potential problems. In some situations, you will be able to resolve those problems yourself, preferably by taking steps to avoid them in the first place. But in other situations, it makes sense to call in an expert. Although lawyers' fees can be quite high, you may end up paying much more in the long run if you do not seek professional advice at the outset. Compared with the cost of losing a lawsuit or watching a deal collapse, a lawyer's bill is often a bargain.

In fact, many businesses have *in-house counsel*. Instead of hiring lawyers from time to time as the need arises, a company may create its own permanent legal department. While that option creates an additional expense, it also provides more efficient risk protection. Since in-house counsel have inside knowledge of their company, they are able to both prevent problems from arising and resolve disputes that do occur.

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## An Introduction to the Legal System

In the chapters that follow, we will examine various areas of law, including tort, contract, and property. But first, we must discuss the Canadian legal system as a whole. We can do so quite quickly. While it is important for business people to understand the basic structure of the courts, for instance, most of the details can be left to the lawyers.

### THE NATURE OF LAW

What are laws? Most people would say that they are rules. That may be true, but it is also clear that not every rule is a law. Sometimes that point is obvious. There is a rule against moving a bishop horizontally across a chessboard, but there certainly is not any

law to that effect. Sometimes, however, it is much more difficult to determine whether a rule is also a law. Consider Ethical Perspective 1.1.

## Ethical Perspective 1.1

### Rules and Laws

During the summer months, you operate a canoe rental business at a popular vacation spot. One of your customers has paddled to the middle of the lake, fallen into the water, and is frantically calling for help. He is in great danger of drowning. You hear his cries and you could easily paddle to his rescue. You would rather not get involved, however, partly because you are annoyed that he ignored your advice to wear a life jacket.

I have come to the lake to fish for the morning. I also hear the man's call for help and I know that I could easily bring him to shore in my motorboat. I would much prefer, however, to head in the other direction and start fishing.

Does either one of us have an obligation to rescue the man? If neither of us helps and he drowns, can either of us be held responsible? What sort of responsibility would we incur?

Most people would say that you and I should help the man, especially since we could do so easily and safely. An important distinction nevertheless needs to be drawn between *legal* obligations and *moral* obligations. According to an old American case, you could not be held legally responsible even if you knew that the man was drunk when he

rented the canoe.<sup>5</sup> That no longer is true in Canada.<sup>6</sup> Because you entered into a contract with the man, the law now says that you have a legal duty to rescue him.<sup>7</sup>

Since I do not have any relationship with the man, my situation is less clear. Judges traditionally drew a distinction between moral obligations and legal obligations, and have said that there is no general duty to rescue in law. The attitude of Canadian courts, however, is slowly changing. Consequently, although the current cases say that I am entitled to simply ignore the call for help, a court might decide differently some day soon. The law is always evolving. A moral obligation today may become a legal obligation tomorrow.

### Questions for Discussion

1. How would you, as a business person, decide when to follow a moral rule, even if you were not obligated to do so by a legal rule?
2. Does your answer depend entirely upon morality? Are there also important business consequences to acting morally or immorally?

Ethical Perspective 1.1 demonstrates that it is occasionally difficult to distinguish between moral obligations and legal obligations. However, it also helps us define the word “law.” Although philosophers have debated the issue for thousands of years, it is enough for us to say that a **law** is a rule that can be enforced by the courts. If I merely broke a moral obligation by refusing to rescue the canoeist, then I might be punished, but only through public opinion. Colleagues might stop talking to me, and newspapers might print unflattering articles. In contrast, if you broke a legal obligation by refusing to help, then you would have more serious things to worry about. Depending on the precise nature of the legal obligation, a court might put you in jail or require you to compensate the victim's family for his death.

Of course, moral issues may arise even if a rule is identified as a law. For instance, as a clothing manufacturer, you may be legally entitled to reduce production costs by using child labour in developing nations. If so, you may be faced with a difficult choice between your heart and your wallet. The Ethical Perspective boxes throughout this book provide many more examples.

a **law** is a rule that can be enforced by the courts

<sup>5</sup> *Osterlind v Hill* (1928) 160 NE 301 (Mass).

<sup>6</sup> Rescue sometimes is required by a statute. The *Canada Shipping Act 2001* states that the “master of a vessel in Canadian waters . . . shall render assistance to every person who is found at sea and in danger of being lost”: SC 2001, c C-26, c 132.

<sup>7</sup> *Crocker v Sundance Northwest Resorts Ltd* (1988) 51 DLR (4th) 321 (SCC). This case is discussed in Chapter 6 (Case Brief 6.5 on page 157).

## A MAP OF THE LAW

Even when distinguished from other types of rules, the law remains an enormous topic. To make sense of it all, we need to organize it into different parts. There are many ways of doing so. In Canada, for example, it is necessary to distinguish between *civil law* and *common law*.<sup>8</sup>

**civil law** systems trace their history to ancient Rome

a **jurisdiction** is a geographical area that uses the same set of laws

**common law** systems trace their history to England

**Civil law** systems trace their history to ancient Rome. Since the Roman Empire covered most of Europe, most countries on that continent are still *civilian*. The only civil law *jurisdiction* in Canada, however, is Quebec, which initially borrowed its law from France. (Although it has many different meanings, **jurisdiction** in this situation refers to a geographical area that uses the same set of laws.)

**Common law** systems trace their history to England.<sup>9</sup> Consequently, most jurisdictions that were settled by English colonists continue to use the common law. That is true of the rest of Canada, as well as jurisdictions such as Australia, New Zealand, and most of the United States.<sup>10</sup>

Since there are significant differences between civil law systems and common law systems, there are also significant differences between the laws that apply in Quebec and the laws that apply in the rest of this country.<sup>11</sup> It is for that reason that we will focus on Canadian laws that apply outside of Quebec. At the same time, however, it is important to recognize that some types of laws are the same across the entire country. That is true, for example, of criminal laws and constitutional laws. We will therefore occasionally consider cases from Quebec.

Within Canada's common law system, we can further organize legal rules on the basis of the topics they address. Although it does not cover every possibility, Figure 1.1 represents some of the most important areas that we will discuss in this text.

### Public Law

**public law** is concerned with governments and the ways in which they deal with their citizens

Figure 1.1 shows that the major division is between *public law* and *private law*. **Public law** is concerned with governments and the ways in which they deal with their citizens. It includes:

- constitutional law
- administrative law
- criminal law
- tax law

**constitutional law** provides the basic rules of our political and legal systems

**Constitutional law** provides the basic rules of our political and legal systems. It determines who is entitled to create and enforce laws, and it establishes the fundamental

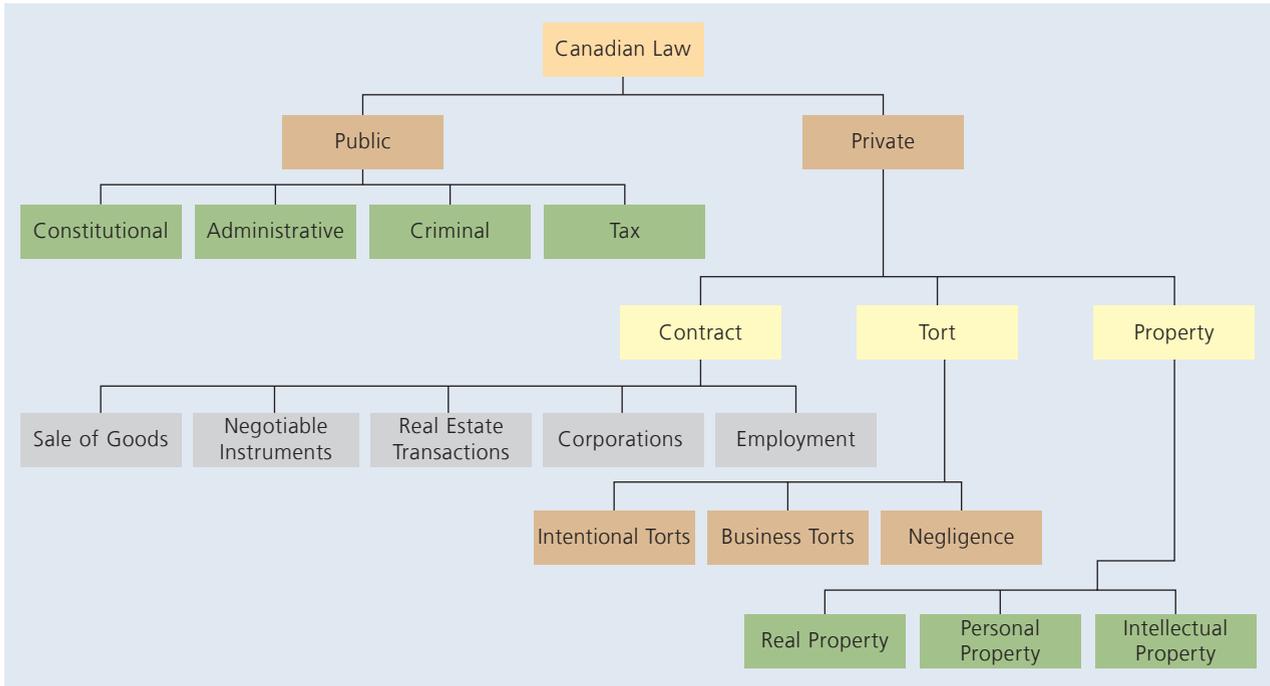
<sup>8</sup> There are other systems of law as well, such as Aboriginal law and Islamic law.

<sup>9</sup> The phrase “common law” refers to the fact that the rules in question were used throughout ancient England, in contrast to the various systems of localized rules that had developed over time.

<sup>10</sup> The exception in the United States is Louisiana. Like Quebec, it was settled by France and therefore uses a civil law system.

<sup>11</sup> “Civil law” is a confusing phrase. While it often refers to a legal system that can be traced to ancient Rome, later in this chapter we will encounter another definition of that phrase. Within a common law system, “civil law” may refer to private law rather than public law. For example, when Canadian lawyers talk about “civil litigation,” they are usually referring to cases involving contracts or torts. “Common law” is also a confusing phrase. While it often refers to a legal system that can be traced to England, later in this chapter we will see that it may also refer to rules that are made by judges, rather than by legislators. And within the context of rules made by judges, “common law” may refer to those made by judges who sat in the courts of law, as opposed to the courts of equity. (The concepts of “law” and “equity” are explained at the end of this chapter.)

FIGURE 1.1 A Map of the Law



rights and freedoms that Canadians enjoy. We will discuss the Constitution in more detail in a later part of this chapter.

Beginning in the second half of the twentieth century, Canadians have grown to expect more and more from their elected officials. To manage the workload, governments regularly *delegate* or *assign* responsibility to a variety of agencies, boards, commissions, and tribunals. **Administrative law** is concerned with the creation and operation of those bodies.

Administrative law has a profound impact on business. For instance, a human rights tribunal may decide that a corporation discriminated against women by paying them less than it paid men for work of similar value. If so, the company may be ordered to pay millions of dollars in compensation.<sup>12</sup> Even if a particular business never becomes involved in that sort of landmark case, it probably has to deal, in the normal course of operations, with a number of administrative bodies. There are literally hundreds. Figure 1.2 (on page 10) lists a sampling of federal, provincial (or territorial), and municipal bodies that regularly affect business.<sup>13</sup>

**Criminal law** deals with offences against the state. In other words, it is concerned with people who break rules that are designed to protect society as a whole. For instance, if you punch me, you have committed a *tort* because (as discussed below) you have done something wrong to me personally. However, you have also committed a *crime* because you have done something wrong to the entire community. Even if I am not particularly upset about being hit, society may want to discourage and punish your behaviour. Consequently, the police and the prosecutor may bring you to court even if I would prefer

**administrative law** is concerned with the creation and operation of administrative agencies, boards, commissions, and tribunals

**criminal law** deals with offences against the state

<sup>12</sup> *Bell Canada v Canadian Telephone Employees Association* (2001) 199 DLR (4th) 664 (FC CA).

<sup>13</sup> This list is not exhaustive. Some bodies serve more than one function. Note that, below the federal level, the name of a particular body may vary from place to place.