

---

# **BUSINESS LAW AND THE REGULATORY ENVIRONMENT**

**Concepts and Cases**

**Lusk Series**

**Metzger  
Mallor  
Barnes  
Bowers  
Phillips**

---

# **BUSINESS LAW AND THE REGULATORY ENVIRONMENT**

**Concepts and Cases**

**Lusk Series**

**Michael B. Metzger, J.D.**  
*Indiana University*

**Jane P. Mallor, J.D.**  
*Indiana University*

**A. James Barnes, J.D.**  
*Attorney at Law,  
Washington, D.C.*

**Thomas Bowers, J.D.**  
*Indiana University*

**Michael J. Phillips, J.D., LL.M., S.J.D.**  
*Indiana University*

Sixth Edition 1986

***IRWIN***

Homewood, Illinois 60430

© BUSINESS PUBLICATIONS, INC., 1935 and 1939

© RICHARD D. IRWIN, INC., 1946, 1951, 1955, 1959, 1963, 1966, 1970, 1974, 1978, 1982, and 1986

*All rights reserved.* No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without the prior written permission of the publisher.

ISBN 0-256-03334-X

Library of Congress Catalog Card No. 85-80612

*Printed in the United States of America*

1 2 3 4 5 6 7 8 9 0 K 3 2 1 0 9 8 7 6



---

# Preface

When the first edition of this text appeared in 1935, Harold F. Lusk could not have foreseen either the far-reaching developments that would reshape almost every area of the law he described, or the tremendous success that his book would have in the marketplace. Yet Harold's approach, a painstaking attention to the details of the "black letter" law coupled with an emphasis on emerging trends that promised to transform existing legal rules, was admirably well-suited to the needs of business students in a dynamic legal environment.

When John D. Donnell, Charles M. Hewitt, and A. James Barnes assumed authorship of the text in the late 1960s, they continued to employ Harold's approach with notable success. One constant in the changing legal environment of business over the past five decades has been that the textbook bearing Harold Lusk's name has always been among the leading texts in the business law field. The book must surely rank as one of the all-time success stories in the history of business publishing.

This latest edition of the book combines the efforts of A. James Barnes with those of four new authors: Thomas Bowers, Jane Mallor, Michael Metzger, and Michael Phillips. John

---

Donnell and Charlie Hewitt, like Harold Lusk before them, have decided to “pass on the baton” and retire from the rigorous business of textbook writing. We, like John and Charlie, approached our task with some trepidation, mindful of the high standards set by our predecessors. Like them, however, we assumed the challenge with confidence in the viability of the approach pioneered by Harold Lusk and in our own ability to meet the challenge. All of the new authors are tenured professors in the Business Law Department at Indiana University. We have all developed an intimate familiarity with the book through years of using it as a teaching tool. In addition, all of us are actively engaged in researching many of the topics that we were called upon to discuss.

Current adopters of the book will immediately note that a majority of the chapters in the new edition have undergone major revision. Wherever possible, we have tried to make a complex subject more understandable to students by adopting a more relaxed, almost conversational writing style. We have included many new cases exemplifying the latest legal developments and containing fact situations sure to stimulate high student interest. These cases have been edited in a way that we hope will aid student understanding.

In many chapters, current adopters will also notice an increased emphasis on the social forces that shape legal rules. Wherever feasible, we have attempted to identify both the historical factors that contributed to the evolution of the legal rules under discussion and the social function performed by those rules. We have done this because we believe that a complete understanding of the law requires an understanding of the origins, as well as the content, of legal rules.

In addition to these changes in approach, this new edition has been reorganized in a variety of ways. The discussion of legal rea-

soning has been expanded and moved from Chapter 2 to Chapter 1 due to its obvious affinity with the opening chapter’s expanded discussion of the nature of law. The chapters on agency law have been reorganized and reduced in number from three to two. The previously separate chapters on landlord-tenant and real property have been combined because of their common intellectual heritage and because many of the important legal trends relating to transactions for the sale of real property are having a similar impact on lease transactions. Finally, the material from the previously separate chapter on close corporations has been integrated into the other corporations chapters. Close corporations and publicly held corporations face many issues in common, and we believe that it is more efficient to confront those issues simultaneously. Also, we believe that an integrated treatment affords students a better understanding of both corporate forms.

Although it does not involve chapter consolidations, a similar integrative approach has been adopted in the contracts chapters of this edition. Rather than treating common law contract rules and their Uniform Commercial Code counterparts in separate sections of the chapters, we discuss these two converging bodies of law concurrently. In addition, we have incorporated many of the basic provisions of the *Restatement (Second) of Contracts* into the text because they exemplify the Code’s strong impact on modern contract rules, and because, given the influential nature of the first *Restatement*, they may represent the future of contract law.

Readers also will find that many chapters have been substantially expanded to reflect the latest legal developments, or to facilitate the inclusion of essential new topics. For example, the chapter on crimes now includes a more expansive treatment of criminal procedure, corporate criminal liability, and the controversy surrounding the application of

the RICO statute to corporate defendants. The chapter on employment law reflects a new emphasis on employment discrimination and the erosion of the employment "at will" doctrine. It also includes a topical discussion of current problem areas such as reverse discrimination, sexual harassment, and comparable worth. The contracts chapters now afford more expansive treatment to a variety of important topics, including promissory estoppel, unconscionability, liability for nondisclosure, and punitive damages as a remedy for breach of contract. The chapters on antitrust law now include a substantial discussion of the "Chicago School" challenge to traditional antitrust policy and its impact on recent antitrust enforcement. The corporations chapters also have been expanded to reflect the increasingly broad acceptance of the Revised Model Business Corporation Act. These examples are far from exhaustive.

In addition to expanding the substance and scope of a majority of the chapters carried over from the fifth edition, we have added two new chapters. A chapter on computer law dramatically highlights the legal dilemmas associated with this important technology and the ways in which the law is responding to these new challenges. Like the franchising chapter it replaces, the computer law chapter is an integrative effort, embracing the law of contract, product liability, intellectual property, privacy, and crimes. A new chapter on corporate social responsibility has also been incorporated into this revision. While prior editions included a treatment of corporate social responsibility issues scattered throughout the text, a practice that we have continued to follow in this revision, we saw the need for a specific chapter that would address the basic issues in the field in a more integrative fashion. In treating this controversial subject we have attempted to avoid the temptation to be judgmental. Instead, we have tried to delineate the basic issues and the major argu-

ments of the parties on both sides of the debate, hoping to stimulate students to think independently about the subject after being properly informed of the complexity of the area and the trade-offs inherent in each of the contending policy positions.

This new edition also is accompanied by a variety of supplementary materials designed to enhance its effectiveness as a teaching tool. The teacher's manual includes suggestions for lecture preparation for each chapter and contains teaching hints, additional examples illustrating concepts introduced in the text and text cases, optional substantive material beyond that presented in the text, and suggestions for the discussion of text cases. A test manual containing multiple-choice, true-false, and essay questions is also available, and adopters are invited to use the Irwin Computerized Test Generator System. For students, a revised student workbook has been prepared by our colleague, Mary Jane Dundas, at Arizona State University.

As is usual with an effort of this magnitude, the final product reflects the contributions of a large number of people in addition to the named authors. Merritt Baker Fox of the Indiana University School of Law wrote the chapter on the international legal environment of business. Our other colleagues in the Business Law Department at Indiana University generously afforded us their counsel and guidance at various stages of the project. Our spouses tolerated the distraction, frequent absences, and irritability that inevitably accompany a project involving a year of night and weekend labor. We also had the assistance of able external reviewers, Mary Jane Dundas, Arizona State University; James E. Macdonald, Weber State College; Robert D. McNutt, California State University, Northridge; and Roscoe Shain, Austin Peay State University. These reviewers were drawn from the ranks of our colleagues in the business law field. In many cases we responded to their

comments. In some cases, after due consideration, we elected not to respond. The responsibility for any mistakes or errors of judgment thus remains our own.

By its nature, a basic text of this sort presents its authors with a variety of often perplexing choices. Practical constraints place effective limits on the subjects that can be addressed and the detail in which these subjects can be presented. Virtually any chapter in this text could serve as the proper subject for a book in its own right. A comprehensive effort such as ours thus inevitably poses the risk of distortion through oversimplification.

Reasonable persons can surely differ concerning the wisdom of many of the choices that we have made. We hope that knowledgeable readers will concur with our choices more often than not. As always, we solicit your comments and suggestions. Our goal is to make this text the best of its kind. With your help, we will be able to do so.

**Michael B. Metzger**  
**Jane P. Mallor**  
**A. James Barnes**  
**Thomas Bowers**  
**Michael J. Phillips**



# Contents

## PART I THE AMERICAN LEGAL SYSTEM

- 1 The Nature of Law . . . . . 2**  
Introduction. Types of Positive Law:  
*Constitutions. Statutes. Common Law. Equity.*  
*Administrative Regulations and Decisions.*  
*Treaties. Ordinances. Executive Orders. Priority*  
*Rules. Classifications of Positive Law.*  
Jurisprudence: *Introduction. Legal Positivism.*  
*Natural Law. American Legal Realism.*  
*Sociological Jurisprudence. The Schools*  
*Compared—An Example. The Approach of This*  
*Text. Legal Reasoning: Introduction. Case Law*  
*Reasoning. Statutory Interpretation.*
- 2 Court Structure, Jurisdiction, and  
Civil Procedure . . . . . 20**  
Introduction: *The Functions Performed by*  
*Courts. Limits on Courts. The Objectives of this*  
*Chapter. State Courts and Their Jurisdiction:*  
*Inferior Courts. Trial Courts. State Appeals*  
*Courts. State Court Jurisdiction. Federal*  
*Courts and Their Jurisdiction: District Courts.*  
*Specialized Courts. Courts of Appeals. The U.S.*  
*Supreme Court. Civil Procedure: Introduction.*  
*The Adversary System. The Summons. The*  
*Pleadings. Motion to Dismiss. Discovery.*  
*Summary Judgment. The Pretrial Conference.*



*The Trial. Appeal. Enforcing a Judgment. Class Actions. Procedure at Administrative Agency Hearings. Arbitration and Other Dispute Settlement Mechanisms: Arbitration. Other Methods.*

## **PART II CRIMES AND TORTS**

### **3 Crimes . . . . . 42**

Introduction. The Criminal Law: *Nature of Crime. Purpose of the Criminal Sanction. Essentials of Crime. Criminal Procedure: Criminal Prosecutions. Procedural Safeguards. White-Collar Crimes and the Dilemmas of Corporate Control: Introduction. Evolution of Corporate Criminal Liability. Corporate Criminal Liability Today. Individual Liability for Corporate Crime. New Directions.* Important White-Collar Crimes: *Regulatory Offences. Fraudulent Acts. Bribery. RICO. Civil RICO.*

### **4 Intentional Torts . . . . . 77**

Introduction: *Nature and Function of Tort Law. Interference with Personal Rights: Battery. Assault. False Imprisonment. Defamation. Invasion of Privacy. Infliction of Emotional Distress. Misuse of Legal Proceedings. Evolving Concepts of Tort Liability. Interference with Property Rights: Nature of Property Rights. Trespass to Land. Nuisance. Trespass to Personal Property. Conversion. Business Torts.*

### **5 Negligence and Strict Liability . . . 100**

Negligence: *Origins and Elements. Duty. Breach. Causation. Res Ipsa Loquitur. Injury. Defenses to Negligence. Recklessness. Strict Liability: Introduction. Abnormally Dangerous Activities.*

## **PART III CONTRACTS**

### **6 Introduction to Contracts . . . . . 130**

The Nature of Contracts: *Definition. Elements. The Social Utility of Contract. The Evolution*

*of Contract Law: Classical Contract Law. Modern Contract Law Development. Basic Contract Concepts and Types: Bilateral and Unilateral Contracts. Valid, Unenforceable, Voidable, and Void Contracts. Express and Implied Contracts. Executed and Executory Contracts. Quasi Contract. Promissory Estoppel. The Uniform Commercial Code: Origins and Purposes of the Code. Scope of the Code. Nature of Article 2. Application of the Code. Restatement (Second) of Contracts: Nature and Origins. Impact.*

### **7 The Agreement: Offer . . . . . 145**

Introduction. What Is an Offer?: *Definition. Definiteness. Communication to Offeree. Special Offer Problem Areas: Advertisements. Rewards. Auctions. Bids. What Terms Are Included in Offers? Termination of Offers: Terms of the Offer. Lapse of Time. Revocation. Rejection. Death or Insanity of Either Party. Destruction of Subject Matter. Intervening Illegality.*

### **8 The Agreement: Acceptance . . . . 165**

What Is an Acceptance?: *Intention to Accept: Counteroffers. Acceptance in Unilateral Contracts. Acceptance in Bilateral Contracts. Acceptance of Ambiguous Offers. Who Can Accept an Offer? Communication of Acceptance: Necessity of Communication. Manner of Communication. When Is Acceptance Communicated?*

### **9 Reality of Consent . . . . . 182**

Introduction. Misrepresentation: *Nature of Misrepresentation. Elements of Misrepresentation. Fraud: Nature of Fraud. Nondisclosure. Duress: Nature of Duress. Elements of Duress. Undue Influence: Nature of Undue Influence. Mistake: Nature of Mistake. Mistake Caused by a Person's Negligence. Mistakes in Drafting Writings.*

### **10 Consideration . . . . . 202**

The Idea of Consideration. Legal Value: *Adequacy of Consideration. Illusory Promises. Preexisting Duties. Debt Settlement*

- Agreements. Forbearance to Sue. Bargained for Exchange: Past Consideration. Moral Obligation. Exceptions to the Consideration Requirement: Promissory Estoppel. Debts Barred by Statutes of Limitations. Debts Barred by Bankruptcy Discharge. Charitable Subscriptions.*
- 11 Capacity of Parties . . . . . 225**  
*Introduction. Minors' Contracts: Minor's Right to Disaffirm. Period of Minority. Emancipation. Time of Disaffirmance. Return of Consideration on Disaffirmance. Obligation to Pay Reasonable Value of Necessaries. Claims for Loss or Depreciation of Nonnecessaries. Misrepresentation of Age. Ratification. Capacity of Mentally Impaired Persons and Intoxicated Persons: Theory of Incapacity. Test for Mental Incapacity. The Effect of Mental Incapacity. The Right to Disaffirm.*
- 12 Illegality . . . . . 238**  
*Introduction: Meaning of Illegality. Determining whether an Agreement Is Illegal. Agreements Declared Void by Statute: Usury Statutes. Sunday Laws. Wagering Statutes. Agreements in Violation of Public Policy Manifested in Legislation: Agreements to Commit Illegal Acts. Agreements That Promote Illegal Acts. Agreement to Perform an Act for Which a Party Is Not Properly Licensed. Agreements in Violation of Public Policy Articulated by Courts: Agreements in Restraint of Competition. Exculpatory Clauses. Agreements Injurious to Public Service. Agreements to Influence Fiduciaries. Agreements That Impair Family Relationships. Agreements in Violation of Legislative and Judicial Public Policy against Unconscionability: Development of the Doctrine of Unconscionability. Meaning of Unconscionability. Procedure for Determining Unconscionability. Applicability of the Concept of Unconscionability. Consequences of Unconscionability. Effect of Illegality: General Rule. Excusable Ignorance of Facts or Legislation. Rights of Parties Not Equally*
- in the Wrong. Rescission before Performance of Illegal Act. Divisible Contracts.*
- 13 Writing . . . . . 262**  
*Introduction. The Statute of Frauds. Contracts within the Statute of Frauds: Collateral Contracts. Interest in Land. Contracts That Cannot Be Performed within One Year. Sale of Goods for \$500 or More. Meeting the Requirements of the Statute of Frauds: Nature of the Writing Required. Alternative Means of Satisfying the Statute of Frauds in Sale of Goods Contracts: Confirmatory Memo between Merchants. Part Payment or Part Delivery. Admission in Pleadings or Court. Specially Manufactured Goods. Promissory Estoppel and the Statute of Frauds. Effect of Failure to Comply with the Statute of Frauds. The Parol Evidence Rule: Explanation of the Rule. Scope of the Parol Evidence Rule. Admissible Parol Evidence. Interpretation of Contracts.*
- 14 Rights of Third Parties . . . . . 290**  
*Introduction. Assignments of Contracts: Nature of Assignment of Rights. Assignability of Rights. Limitations on Assignee's Right to Receive Performance. Necessity for Notifying Obligor of Assignment. Successive Assignments. Assignor's Warranty Liability to Assignee. Delegation of Duties: Nature of Delegation. Delegable Duties. Assumption of Duties by Delegate. Discharge of Delegating Party by Novation. Third Party Beneficiaries: Intended Beneficiaries versus Incidental Beneficiaries. Defenses against Beneficiary. Vesting of Beneficiary's Rights.*
- 15 Performance and Remedies . . . . . 305**  
*Introduction. Conditions: Nature of Conditions. Types of Conditions. Creation of Express Conditions. Excuse of Conditions. Performance and Breach: Degrees of Performance. Material Breach. Excuses for Nonperformance: Impossibility. Discharge: Nature of Discharge. Discharge by Mutual Agreement. Discharge by Waiver. Discharge by Alteration. Discharge by Statute of*

*Limitations. Remedies for Breach of Contract: The Theory of Remedies. Limitations of Recovery of Damages in Contract Cases. Compensatory Damages. Nominal Damages. Liquidated Damages. Punitive Damages. Enforcement of Damage Awards. Equitable Remedies.*

*Employees. Liability for Torts of Independent Contractors. Ratification. Tort Liability of the Agent: Exceptions. Actions against Principal and Agent. Criminal Liability. Subagents: Agent's Authority to Appoint Subagents. Liability to Third Parties for Acts of Subagents. Fiduciary Duties.*

## PART IV AGENCY LAW

- 16 The Agency Relationship . . . . 334**  
*Introduction: The Significance of Agency Law. Topic Coverage and Organization. Creation of the Agency Relationship and Related Matters: Formation. Capacity. Nondelegable Obligations. Agency Terminology. Duties of Agent to Principal: Introduction. Agent's Duty of Loyalty. Agent's Duty to Obey Instructions. Agent's Duty to Act with Care and Skill. Agent's Duty to Notify the Principal. Agent's Duty to Account. Remedies of the Principal. Duties of Principal to Agent: Introduction. Duty to Compensate Agent. Duties of Reimbursement and Indemnity. Remedies of the Agent. Termination of the Agency Relationship: Termination by Acts of the Parties. Termination by Operation of Law. Termination of Agency Powers Given as Security.*
- 17 Third-Party Relations of the Principal and the Agent . . . . 351**  
*Introduction. Contract Liability of the Principal: Introduction. Express Authority. Implied Authority. Apparent Authority. Liability for Agent's Misrepresentations. Incapacity of Principal or Agent. Effect of Termination of Agency. Ratification. Notice to or from Agent: Notification. Knowledge. Contract Liability of the Agent: Introduction. Disclosed Principal. Partially Disclosed Principal. Undisclosed Principal. Nonexistent Principal. Principal Lacking Capacity. Tort Liability of the Principal: Introduction. Direct Liability. Employees versus Independent Contractors. Employer Liability for Torts of*

## PART V PARTNERSHIP LAW

- 18 Introduction to Sole Proprietorship, Partnership, and Related Forms . . . . . 386**  
*Introduction. Sole Proprietorship. Introduction to Partnerships: History of Partnerships. Modern Partnership Law. Principal Characteristics of Partnerships. Entity and Aggregate Theories. Creation of Partnership: Introduction. Consequences of Being a Partner. No Formalities for Creation. Articles of Partnership. Absence of Articles of Partnership. UPA Definition of Partnership. Association of Two or More Persons. Carrying On a Business. Co-ownership. For Profit. Intent. Creation of Joint Venture and Mining Partnership: Joint Ventures. Mining Partnerships. Partnership by Estoppel: Introduction. Elements. Importance of Partnership by Estoppel. Ostensible Partnership. Partnership Property and Partners' Property Rights: Determining What Is Partnership Property. UPA Rule. Partners' Property Rights.*
- 19 Operation of Partnership and Related Forms . . . . . 409**  
*Introduction: Relations between Partners. Relation of Partners to Third Persons. Duties of Partners to Each Other: Duty of Loyalty and Good Faith. Duty to Act within Authority. Duty of Care. Duty to Inform. Duty to Account. Joint Ventures and Mining Partnerships. Compensation of Partners: Partners' Salaries. Profits and Losses. Effect of Partnership Agreement. Collective Management Powers of Partners: Introduction. Management Powers.*



*Right and Duty to Manage. Effect of Partnership Agreement. Individual Authority of Partners: Types of Authority. Special Transactions. Power to Convey Partnership Real Property. Borrowing Money and Issuing Negotiable Instruments. Admissions and Notice. Joint Ventures and Mining Partnerships. Liability for Torts and Crimes: Torts. Crimes. Lawsuits by and Against Partnerships and Partners: Suits by the Partnership and the Partners. Suits against the Partners. Suits against the Partnership.*

## **20 Dissolution, Winding Up, and Termination of Partnerships . . . 437**

*Introduction. Dissolution: Dissolution Defined. Importance of Dissolution. Causes of Dissolution. Nonwrongful Dissolution. Wrongful Dissolution. Acts Not Causing Dissolution. Additional Effects of Dissolution. Joint Ventures and Mining Partnerships. Winding Up the Partnership Business: The Process. Fiduciary Duties. Who May Demand Winding Up? Who May Wind Up? Compensation during Winding Up. Partner's Authority in Winding Up. Disputes among Winding-Up Partners. When the Business is Continued: Advantages of Continuing. Successor's Liability for Prior Obligations. Outgoing Partner's Liability for Prior Obligations. Outgoing Partner's Liability for Obligations Incurred after Dissolution. Liability of Incoming Partners. Rights of Outgoing Partners. Distribution of Assets: Order of Distribution. Distribution of Assets of Insolvent Partnership. Example. Termination.*

## **21 Limited Partnerships . . . . . 463**

*Introduction: History. The Uniform Limited Partnership Act. Principal Characteristics of Limited Partnerships. Use of Limited Partnerships. Creation of Limited Partnership: Certificate of Limited Partnership. Defective Compliance with Limited Partnership Statute. Amendments to Certificate. Foreign Limited Partnerships. Application of Securities Laws. Rights and*

*Liabilities of Partners in Limited Partnerships: Common Rights and Liabilities. Other Rights of General Partners. Other Liabilities of General Partners. Other Rights of Limited Partners. Other Liabilities of Limited Partners. Dissolution and Winding Up of a Limited Partnership: Dissolution. Winding Up. Distribution of Assets.*

## **PART VI CORPORATIONS**

## **22 History and Nature of Corporations . . . . . 484**

*Introduction. History of Corporations. British Trading Companies. Early American Corporation Law. Principal Characteristics of Corporations. Classifications of Corporations: For-Profit Corporations. Not-for-Profit Corporations. Government-Owned Corporations. Regulation of Corporations: Federal versus State Incorporation. State Incorporation Statutes. State Common Law of Corporations. Regulation of Foreign Corporations: Definitions. State Jurisdiction over Foreign Corporations. Doing Business. Subjecting Foreign Corporations to Suit. Taxation. Health and Safety Regulations. Qualifying to Do Business. Regulation of Internal Affairs. Piercing the Corporate Veil: Domination. Improper Use. Defrauding Creditors. Circumventing a Statute. Evading an Existing Obligation.*

## **23 Organization, Dissolution, and Financial Structure of Corporations . . . . . 507**

*Introduction. Promoters: Role of Promoter. Relation of Promoter and Corporation. No Agency Relationship. Fiduciary Relationship. Promoter's Preincorporation Contracts. Corporation's Liability on Promoter's Contracts. Promoter's Liability on Preincorporation Contracts. Liability of Third Party. Reducing Promoter's Risk of Liability. Liability of Corporation to Promoter. Preincorporation Share Subscriptions.*

Incorporation: *Determining Where to Incorporate. Steps in Incorporation. Incorporators. Articles of Incorporation. Filing of Articles of Incorporation. Issuance of Certificate of Incorporation. The Organization Meeting. Bylaws of the Corporation. Defective Attempts to Incorporate: Consequences. De Jure Corporation. De Facto Corporation. Corporation by Estoppel. Liability for Defective Incorporation. Modern Approaches to the Defective Incorporation Problem. Close Corporation Election. Dissolution and Termination of Corporations: Voluntary Dissolution. Involuntary Dissolution. Dissolution of Close Corporations. Winding Up and Termination. Financing the Corporation: Sources of Funds. Equity Securities. Common Shares. Preferred Shares. Authorized, Issued, and Outstanding Shares. Options, Warrants, and Rights. Debt Securities. Convertible Debt Securities. Consideration for Shares: Quality of Consideration for Shares. Value of Consideration Received. Quantity of Consideration for Shares. Accounting for Consideration Received. Share Subscriptions: Nature of Share Subscriptions. Uses of Subscriptions. Payment of Subscription Price. Issuance of Shares: Function of Share Certificates. Liability for Overissuance under UCC. Transfer of Securities: Function of Securities Certificates. Restrictions on Transferability of Shares. Uses of Transfer Restrictions. Types of Restrictions on Transfer. Legality of Transfer Restrictions. Enforceability. Effect of Statutory Close Corporation Supplement. Corporation's Duty to Transfer Shares.*

## 24 Managing the Corporation . . . . 545

Introduction. Objectives of the Corporation: *Profit Objective. Other Objectives. ALI Corporate Governance Project. Corporate Powers: State Statutes. Limitations. The Ultra Vires Doctrine. The Ultra Vires Doctrine Today. The Board of Directors: Introduction. Major Functions of Modern Boards of Directors. Board Powers under*

*Corporation Statutes. Committees of the Board. Powers and Rights of Directors as Individuals. Compensation of Directors. Election and Removal of Directors: Qualifications of Directors. Number of Directors. Election of Directors. The Proxy Solicitation Process. Term of Office. Vacancies on the Board. Removal of Directors. Directors' Meetings: Formal Meetings. Notice of Meetings. Quorum Requirement. Voting. Corporate Governance Proposals: Traditional Corporate Governance Model. Corporate Governance in Practice. Improving Corporate Governance. Impact of Corporate Governance Proposals. Officers of the Corporation: Appointment of Officers. Authority of Officers. Officer Liability. Employees of the Corporation. Managing Close Corporations: Fewer Management Formalities. Preventing Domination. Directors' and Officers' Duties to the Corporation: Introduction. Acting within Authority. Duty of Care. Duties of Loyalty. Self-Dealing with the Corporation. Usurpation of a Corporate Opportunity. Oppression of Minority Shareholders. Trading on Inside Information. Federal Securities Law. Director Right to Dissent. The Business Judgment Rule: Elements of the Business Judgment Rule. Purpose of Business Judgment Rule. If Business Judgment Rule Is Inapplicable. Opposition to Acquisition of Control of the Corporation. Shareholder Derivative Suits. Liability for Torts and Crimes: Liability of the Corporation. Directors' and Officers' Liability. Violations of Corporation Statutes. Insurance and Indemnification: Indemnification of Directors. Indemnification of Nondirectors. Insurance.*

## 25 Shareholders' Rights and Liabilities . . . . . 587

Introduction. Shareholders' Meetings: *Annual Meeting. Special Meetings. Notice of Meetings. Conduct of the Meeting. Action without a Meeting. Election of Directors and Shareholder Control Devices: Election and Removal of Directors. Other Shareholder Control Devices. Voting Trusts. Shareholder Voting Agreements. Proxies. Other Matters*

Submitted to Shareholders: *Amendment of the Articles. Other Fundamental Transactions. Merger and Consolidation. Share Exchange. Sale of Assets. Dissolution. Procedures Required. Other Matters Submitted to Shareholders. Shareholder Proposals and Right to Speak: Corporate Governance Proposals. Shareholders' Right of Appraisal: Introduction. Actions Covered. Shareholders Covered. Shares Covered. Procedure to Exercise Right. Determination of Fair Value. Exclusivity of Remedy. Criticisms of the Appraisal Remedy. Distributions to Shareholders: Dividends: Introduction. Types of Dividends. Cash or Property Dividends. Share Dividends and Share Splits. Reverse Share Split. Other Corporate Distributions: Share Repurchases. Redemptions. Open-Market Purchases. Distributions from Capital Surplus. Partial Liquidations. Shareholders' Inspection and Information Rights: Inspection Right. Common Law. Statutory Inspection Rights. Eligible Shareholders. Information Rights. Preemptive Rights: Introduction. Scope of Preemptive Rights. Mechanics. Criticisms of Preemptive Rights. Shareholders' Lawsuits: Shareholders' Individual Lawsuits. Shareholder Class Action Suits. Shareholders' Derivative Suits. Defense of Corporation by Shareholder. Shareholder Liability: Introduction. Shareholder Liability on Illegal Distributions. Shareholder Liability for Corporate Debts. Sale of a Control Block of Shares. Oppression of Minority Shareholders. Close Corporation Statutes.*

## **26 Securities Regulation . . . . . 634**

*Introduction: Background. Disclosure Scheme. Securities Act of 1933. Securities Exchange Act of 1934. Securities and Exchange Commission. What Is a Security?: Investment Contract. Economic Realities Test. Sale-of-Business Doctrine. Securities Act of 1933: Introduction. Registration of Securities under the 1933 Act. Section 5: Timing, Manner, and Content of Offers and Sales. The Pre-filing Period. The Waiting Period. The Post-Effective Period. Exemptions from the*

*Registration Requirements of the 1933 Act: Types of Exemptions. Exempt Securities. Transaction Exemptions. Transaction Exemptions for Issuers. Private Offering Exemption. Intrastate Offering Exemption. Small Offering Exemptions. Integration of Offerings. Transaction Exemptions for Nonissuers. Sale of Restricted Securities. Liability Provisions of the 1933 Act: Introduction. Liability for Improper Offers and Sales. Liability for Defective Registration Statements. Other Liability Provisions. Jurisdictional Requirement. SEC Actions. Criminal Liability. Securities Exchange Act of 1934: Introduction. Registration of Securities under the 1934 Act. Periodic Reports. Short-Swing Trading by Insiders. Proxy Solicitation Regulation: Introduction. Proxy Statement. Proxy. False Statements. Proxy Contests. Shareholder Proposals. Liability Provisions of the 1934 Act: Manipulation of a Security's Price. Liability for False Statements in Filed Documents. Section 10(b) and Rule 10b-5. Elements of a Rule 10b-5 Violation. Conduct Covered by Rule 10b-5. Continuous Disclosure of Material Information. Trading on Inside Information. Criminal Liability. Tender Offer Regulation: History. The Williams Act. Definition of Tender Offer. Regulation of Tender Offers. Tender Offer Advisory Committee. Tender Offers versus Private Acquisitions of Shares. State Regulation of Tender Offers. The Foreign Corrupt Practices Act: Background. The Payments Prohibition. Record-Keeping and Internal Controls Requirements. State Securities Legislation: Purpose and History. Uniform Securities Act. Securities Fraud. Disclosure and Merit Registration. Broker-Dealer Registration.*

## **27 Legal Responsibilities of Accountants and Other Professionals . . . . . 682**

*Introduction: Bases of Professional Liability. General Standard of Performance. Deference to Professional Standards. Local versus National Standard. Accountants' Liability to*



Client: *Contractual Liability. Tort Liability. Securities Law. Accountants' Liability to Third Persons: Common Law: Introduction. Negligence. Fraud. Correcting Erroneous Reports. Accountants' Liability to Third Parties: Securities Law: Securities Act of 1933. Errors in 1933 Act Registration Statements. Other 1933 Act Liability Sections. Securities Exchange Act of 1934. Errors in Filed Reports. Section 10(b) and Rule 10b-5. Aiding and Abetting. State Securities Law. Qualified Opinions and Disclaimers of Opinion: Qualified Opinion. Disclaimer. Adverse Opinion. Unaudited Financial Statements. Criminal, Injunctive, and Administrative Proceedings: Criminal Liability. Tax Law. Other Crimes. Injunctions. Administrative Proceedings. Ownership of Working Papers and Accountant-Client Privilege: Working Papers. Accountant-Client Privilege.*

## PART VII PROPERTY

### 28 Personal Property and Bailments 712

Introduction. Nature and Classification: *Property. Possession. Real and Personal Property. Tangible and Intangible Property. Public and Private Property. Acquiring Ownership of Personal Property: Possession. Production or Purchase. Lost and Mislaid Property. Gifts. Confusion. Accession. Bailments: Nature of Bailments. Elements of a Bailment. Creation of Bailment Relation. Custody. Types of Bailments. Special Bailments. Duties of the Bailee. Bailee's Duty of Care. Bailee's Duty to Return the Property. Limits on Liability. Right to Compensation. Bailor's Liability for Defects in the Bailed Property. Special Bailments: Common Carriers. Hotelkeepers. Safe-Deposit Boxes. Involuntary Bailments.*

### 29 Real Property . . . . . 736

Introduction. Scope of Real Property: *Fixtures. Rights and Interests in Real*

*Property: Estates in Land. Co-Ownership of Real Property. Interests in Real Property Owned by Others. Acquisition of Rights in Real Property: Acquisition by Purchase. Acquisition by Gift. Acquisition by Will or Inheritance. Acquisition by Tax Sale. Acquisition by Adverse Possession. Transfer by Sale: Steps in a Sale. Real Estate Brokerage. Contract for Sale. Financing the Purchase. Federal Disclosure Laws. Deeds. Form and Execution of Deed. Recording Deeds. Methods of Assuring Title. Warranties of Quality in the Sale of Houses. Duty to Disclose Latent Defects. Land Use Control: Introduction. Nuisance Law. Zoning and Subdivision Ordinances. Eminent Domain. Landlord and Tenant: Introduction. Types of Leases. Execution of a Lease. Rights, Duties, and Liabilities of the Landlord: Landlord's Rights. Traditional Duties of a Landlord. Landlord's Responsibility for the Quality of Leased Property. Landlord's Tort Liability. Rights, Duties, and Liabilities of the Tenant: Rights of the Tenant. Duties of the Tenant. Assignment and Subleasing. Tenant's Liability for Injuries to Third Persons. Termination of the Leasehold: Eviction. Abandonment.*

### 30 Estates and Trusts . . . . . 784

Introduction. Wills: *Right of Disposition by Will. Nature of a Will. Testamentary Capacity. Execution of a Will. Limitations on Disposition by Will. Revocation of Wills. Codicils. Intestacy: Characteristics of Intestacy Statutes. Example of Intestacy Statute. Special Rules. Administration of Estates: Determining the Existence of a Will. Selecting a Personal Representative. Responsibilities of the Personal Representative. Trusts: Nature of a Trust. Trust Terminology. Why People Create Trusts. Creation of Express Trusts. Charitable Trusts. Powers and Duties of the Trustee. Transfer of the Beneficiary's Interest. Termination and Modifications of a Trust. Implied and Constructive Trusts.*

## PART VIII SALES

### 31 Formation and Terms of Sales

#### Contracts . . . . . 804

Introduction: *Sale of Goods. Merchants. Code Requirements. Terms of the Contract: General Terms. Output and Needs Contracts. Time for Performance. Delivery Terms. Title: Passage of Title. Importance of Title. Title and Third Parties: Obtaining Good Title. Transfers of Voidable Title. Buyers in the Ordinary Course of Business. Entrusting of Goods. Risk of Loss: The Terms of the Agreement. Shipment Contracts. Destination Contracts. Goods in the Possession of Third Parties. Risk Generally. Effect of Breach on Risk of Loss. Insurable Interest. Sales on Trial: Sale on Approval. Sale or Return. Sale on Consignment.*

### 32 Product Liability . . . . . 826

Introduction. The Evolution of Product Liability Law: *The 19th Century. The 20th Century. The Current "Crisis" in Product Liability Law. The Organization of this Chapter. Express Warranty: Warranties in General. Creating an Express Warranty. Implied Warranty of Merchantability: The Merchantability Standard. Implied Warranty of Fitness. Negligence: Improper Manufacture or Inspection. Failure to Warn. Design Defects. Strict Liability: Introduction. Requirements of Section 402A. Applications of Section 402A. Other Theories of Recovery: The Magnuson-Moss Act. Section 402B. Industry-Wide Liability. Disclaimers: Introduction. Implied Warranty Disclaimers. Express Warranty, Negligence, and 402A Disclaimers. Limitation of Remedies. Damages in Product Liability Suits: The Types of Damages. Negligence and 402A Cases. Express and Implied Warranty Cases. The "No Privity" Defense: Introduction. In Negligence and 402A Cases. Privity under the UCC. Timing Problems: Statute of Limitations. Statutes of Repose. Notice. Defenses: Product Misuse. Assumption of*

*Risk. Contributory Negligence. Comparative Fault. Federal Legislation? Relation to State Law. Liability of Manufacturers. Liability of Sellers. Defenses and Damages.*

### 33 Performance of Sales Contracts 859

*Course of Dealing. Usage of Trade. Modification. Waiver. Assignment. Delivery: Basic Obligation. Place of Delivery. Seller's Duty of Delivery. Inspection and Payment: Buyer's Right of Inspection. Payment. Acceptance, Revocation, and Rejection: Acceptance. Effect of Acceptance. Revocation of Acceptance. Buyer's Rights on Improper Delivery. Rejection. Right to Cure. Buyer's Duties after Rejection. Assurance, Repudiation, and Excuse: Assurance. Anticipatory Repudiation. Excuse.*

### 34 Remedies for Breach of Sales

#### Contracts . . . . . 883

Introduction: *Agreements as to Remedies. Statute of Limitations. Seller's Remedies: Remedies Available to an Injured Seller. Cancellation and Withholding of Delivery. Resale of Goods. Recovery of the Purchase Price. Damages for Rejection on Repudiation. Seller's Remedies Where Buyer Is Insolvent. Seller's Right to Stop Delivery. Liquidated Damages. Buyer's Remedies: Buyer's Remedies in General. Buyer's Right to Cover. Incidental Damages. Consequential Damages. Damages for Nondelivery. Damages for Defective Goods. Buyer's Right to Specific Performance. Buyer and Seller Agreements as to Remedies.*

## PART IX COMMERCIAL PAPER

### 35 Negotiable Instruments . . . . . 904

Introduction. Nature of Negotiable Instruments: *Uniform Commercial Code. Commercial Paper. Negotiability. Kinds of Commercial Paper: Promissory Notes.*

	<i>Certificates of Deposit. Draft. Checks. Benefits of Negotiable Instruments: Rights of an Assignee of a Contract. Rights of a Holder of a Negotiable Instrument. Formal Requirements for Negotiability: Basic Requirements. Importance of Form. In Writing and Signed: Writing. Signed. Unconditional Promise or Order: Requirement of a Promise or Order. Promise or Order Must Be Unconditional. Sum Certain in Money: Sum Certain. Payable in Money. Payable on Demand or at a Definite Time: Payable on Demand. Payable at a Definite Time. Payment to Order or Bearer. Special Terms: Additional Terms. Ambiguous Terms.</i>	
<b>36</b>	<b>Negotiation and Holder in Due Course . . . . .</b>	<b>919</b>
	<i>Introduction. Negotiation: Nature of Negotiation. Formal Requirements for Negotiation. Nature of Indorsement. Wrong or Misspelled Name. Indorsements by a Depository Bank. Transfer of Order Instrument. Indorsements: Effects of an Indorsement. Kinds of Indorsements. Rescission of Indorsement. Holder in Due Course: General Requirements. Holder. Value. Good Faith. Overdue and Dishonored. Notice of Defenses. Payee as Holder in Due Course. Shelter Provision. Rights of a Holder in Due Course: Importance of Being a Holder in Due Course. Personal Defenses. Real Defenses. Persons Not Holders in Due Course. Changes in the Holder in Due Course Rule: Consumer Disadvantages. State Legislation. Federal Trade Commission Rules.</i>	
<b>37</b>	<b>Liability of Parties . . . . .</b>	<b>947</b>
	<i>Introduction. Liability in General. Contractual Liability: Primary and Secondary Liability. Contract of a Maker. Contract of a Drawee. Contract of a Drawer. Contract of an Indorser. Contract of an Accommodation Party. Signing an Instrument. Signature by an Authorized Agent. Unauthorized Signature. Contractual Liability in Operation: Presentment of a Note. Presentment of a Check or a Draft. Time of</i>	

*Presentment. Effect of Unexcused Delay in Presentment. Warranty Liability: Transferor's Warranties. Rule of Finality of Payment. Presentment Warranties. Operation of Warranties. Other Liability Rules: Negligence. Impostor Rule. Fictitious Payee Rule. Conversion. Discharge of Negotiable Instruments: Discharge of Liability. Discharge by Cancellation. Discharge by Alteration. Discharge by Impairment of Recourse.*

## **38 Checks and Documents of Title 972**

*Introduction. The Drawer-Drawee Relationship: Bank's Duty to Pay. Bank's Right to Charge to Customer's Account. Stop Payment Order. Bank's Liability for Payment after Stop Payment Order. Certified Check. Cashier's Check. Death or Incompetence of Customer. Forged and Altered Checks: Bank's Right to Charge Account. Customer's Duty to Report Forgeries and Alterations. Electronic Banking: Electronic Funds Transfer Act. Documents of Title: Introduction. Warehouse Receipts. Bills of Lading. Negotiation of Document of Title. Rights Acquired by Negotiation. Warranties of Transferor of Document of Title.*

## **PART X CREDIT**

## **39 Credit and Secured Transactions 992**

*Introduction. Credit: Unsecured Credit. Secured Credit. Development of Security. Security Interests in Personal Property. Security Interests in Real Property. Liens on Personal Property: Common Law Liens. Statutory Liens. Characteristics of Liens. Foreclosure of Lien. Suretyship and Guarantee: Sureties and Guarantors. Creation of Principal and Surety Relationship. Defenses of a Surety. Creditor's Duties to Surety. Subrogation and Contribution. Security Interests in Real Property: Historical Developments of Mortgages. Form,*