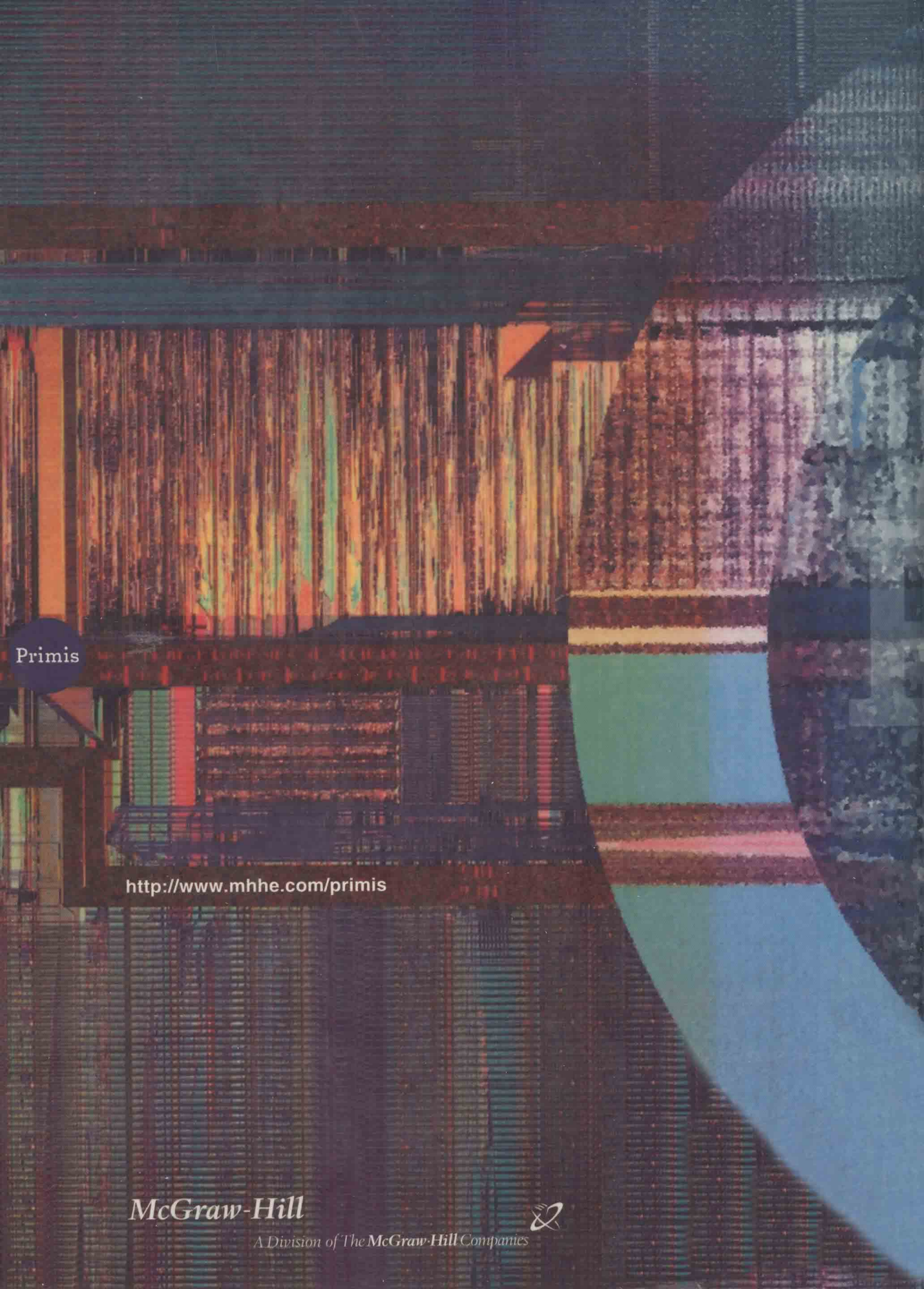

Primis
http://www.mhhe.com/primis
McGraw-Hill
A Division of The McGraw-Hill Companies

Business Law

Contents

Mallor et al. • *Business Law and the Regulatory Environment, Tenth Edition*

The cover photograph is courtesy of Intel® Corporation and was created from a color photograph of Intel's Pentium™ chip.*

* *Pentium™ is a trademark of Intel.*

This book was printed on recycled paper.

Business Law

http://www.mhhe.com/primis/

BLAW ISBN: 0-390-46661-1

The Nature of Law

Today, businesspeople confront the law at every turn. For example, business firms continually use the law of property, contract, and agency. Indeed, business could hardly function without these and other basic bodies of law. In addition to assisting business activity, the legal system restricts it as well. Today, government regulates most aspects of a firm's operations—for example, advertising, product safety, employee relations, the issuance of securities, and behavior toward competitors.

Thus, businesspeople constantly use, rely on, react to, plan around—and sometimes violate—innumerable legal rules (or laws). For this reason, managers should have a general knowledge of the legal system and the most important legal rules affecting their firms. This text discusses many such rules, often in detail. But your ability to use and apply the legal rules affecting business is incomplete unless you also understand law's general nature, its functions, and how judges interpret it. This understanding could go some way toward reducing business complaints about the law and lawyers.

To help provide such an understanding, this chapter examines law's nature from four different angles. First, it describes, classifies, and ranks the various kinds of rules that are regarded as law in the United States—the *types of law.* This discussion, however, only partly conveys law's general nature. Thus, the chapter's second section discusses a subject known as *jurisprudence* or legal philosophy. Jurisprudence tries to establish a general definition of law, and each of the competing definitions we examine highlights an important facet of law's many-sided nature. Shifting from the theoretical to the pragmatic, this chapter's third section examines some of the *functions* law serves—what it *does.* The chapter concludes by discussing *legal reasoning,* the set of techniques judges use when interpreting legal rules. This discussion should help dispel the common misconception that the law consists of clear and precise commands that judges merely look up and then mechanically apply.

TYPES AND CLASSIFICATIONS OF LAW

The Types of Law

Constitutions **Constitutions,** which exist at the state and federal levels, have two general functions.[1] First, they set up the structure of government for the political unit they control (a state or the federal government). This involves creating the branches and subdivisions of the government and stating the powers given and denied to each. Through its **separation of powers,** for example, the U.S. Constitution establishes a Congress and gives it power to legislate or *make* law in certain areas, provides for a chief executive (the president) whose function is to execute or *enforce* the laws, and helps create a federal judiciary to *interpret* the laws. The U.S. Constitution also structures the relationship between the federal government and the states. In the process, it respects the principle of **federalism** by recognizing the states' power to make law in certain areas.

The second function of constitutions is to prevent other units of government from taking certain actions or passing certain laws. Constitutions do so mainly by prohibiting government action that restricts certain individual rights. The Bill of Rights to the U.S. Constitution is an example.

Statutes **Statutes** are laws created by Congress or a state legislature. They are stated in an authoritative form in statute books or codes. As you will see, however, their interpretation and application are often difficult.

Throughout this text, you will encounter state statutes that were originally drafted as **uniform acts.** Uniform acts are model statutes drafted by private bodies of lawyers and/or scholars. They do not become law until they are enacted by a legislature. Their aim is to produce state-by-state uniformity on the subjects they address. Examples include the Uniform Commercial Code (which deals with a wide range of commercial law subjects), the Uniform Partnership Act, the Revised Uniform Limited Partnership Act, and the Revised Model Business Corporation Act.

Common Law The **common law** (also called judge-made law or case law) is that law made and applied by judges as they decide cases not governed by statutes or other types of law. In theory, the common law exists at the state level only. The common law originated in medieval England. It developed from the decisions of judges in settling disputes. Over time, judges began to follow the decisions of other judges in similar cases. This practice became formalized in the doctrine of ***stare decisis*** (let the decision stand). As you will see later in the chapter, *stare decisis* has enabled the common law to evolve to meet changing social conditions. Thus, the common law rules in force today often differ considerably from the common law rules of earlier times.

The common law came to America with the first English settlers and was applied by courts during the colonial period. It continued to be applied after the Revolution and the adoption of the Constitution, and it still governs many cases today. For example, the rules of tort, contract, and agency discussed in this text are mainly common law rules. However, the states have codified (enacted into statute) some parts of the common law. They also have passed statutes superseding judge-made law in certain situations. As discussed in Introduction to Contracts, for example, the states have established special rules for contract cases involving the sale of goods by enacting Article 2 of the Uniform Commercial Code.

This text's torts, contracts, and agency chapters often refer to the *Restatement* (or *Restatement (Second)*) rule on a particular subject. The *Restatements* are collections of common law (and occasionally statutory) rules covering various areas of the law. Because they are promulgated by the American Law Institute rather than by courts, the *Restatements* are not law and do not bind courts. However, state courts often find *Restatement* rules persuasive and adopt them as common law rules within their states. Usually, the *Restatement* rules are the rules actually followed by a majority of the states. Occasionally, however, the *Restatements* stimulate changes in the common law by stating new rules that the courts later decide to follow.

[1] The chapter Business and the Constitution discusses constitutional law as it applies to government regulation of business.

Equity The body of law called **equity** has traditionally tried to do discretionary rough justice in situations where common law rules would produce unfair results. In medieval England, common law rules were technical and rigid and the remedies available in common law courts were too few. This meant that some deserving parties could not obtain adequate relief in the common law courts. As a result, the chancellor, the king's most powerful executive officer, began to hear cases that the common law courts could not resolve fairly.

Eventually, separate equity courts emerged to handle the cases heard by the chancellor. These courts took control of a case only when there was no adequate remedy in a regular common law court. In equity courts, procedures were flexible, and rigid rules of law were de-emphasized in favor of general moral maxims. Equity courts also provided several remedies not available in the common law courts (which generally awarded only money damages or the recovery of property). Perhaps the most important of these *equitable remedies* is the **injunction,** a court order forbidding a party to do some act or commanding him to perform some act. Others include the contract remedies of **specific performance** (whereby a party is ordered to perform according to the terms of her contract), **reformation** (in which the court rewrites the contract's terms to reflect the parties' real intentions), and **rescission** (a cancellation of a contract in which the parties are returned to their precontractual position).

Like the common law, equity principles and practices were brought to the American colonies by the English settlers. They continued to be used after the Revolution and the adoption of the Constitution. Over time, however, the once-sharp line between law and equity has become blurred. Most states have abolished separate equity courts, now allowing one court to handle both legal and equitable claims. Also, equitable principles have been blended together with common law rules, and some traditional equity doctrines have been restated as common law or statutory rules. An example is the doctrine of unconscionability. Finally, courts sometimes combine an award of money damages with an equitable remedy.

Administrative Regulations and Decisions Throughout this century, the *administrative agencies* established by Congress and the state legislatures have acquired considerable power, importance, and influence over business. A major reason for the rise of administrative agencies was the collection of social and economic problems created by the industrialization of the United States that began late in the 19th century. Because legislatures generally lacked the time and expertise to deal with these problems on a continuing basis, the creation of specialized, expert agencies was almost inevitable.

Administrative agencies get the ability to make law through a *delegation* (or handing over) of power from the legislature. Agencies normally are created by a statute that specifies the areas in which the agency can make law and the scope of its power in each area. Often, these statutory delegations are worded so broadly that the legislature has, in effect, merely pointed to a problem and given the agency wide-ranging powers to deal with it.

The two kinds of law made by administrative agencies are **administrative regulations** and **agency decisions.** Like statutes, administrative regulations appear in a precise form in one authoritative source. However, they differ from statutes because the body enacting them is an agency, not the legislature. In addition, some agencies have an internal court structure that enables them to hear cases arising under the statutes and regulations they enforce. The resulting agency decisions are another kind of law.

Treaties According to the U.S. Constitution, **treaties** made by the president with foreign governments and approved by two-thirds of the U.S. Senate are "the supreme Law of the Land." As we note shortly, treaties invalidate inconsistent state (and sometimes federal) laws.

Ordinances State governments have subordinate units that exercise certain functions. Some of these units, such as school districts, have limited powers. Others, such as counties, municipalities, and townships, exercise various governmental functions. The enactments of municipalities are called **ordinances;** zoning ordinances are an example. The enactments of other political subdivisions may also be called ordinances.

Executive Orders In theory, the president or a state's governor is a chief executive who enforces the laws but has no law-making powers. However, these officials sometimes have the power to issue laws called **executive orders.** This power normally results from a legislative delegation.

Priority Rules

Because the different types of law conflict, rules for determining which type takes priority are necessary. Here, we briefly describe the most important such rules.

1. According to the principle of **federal supremacy,** the U.S. Constitution, federal laws enacted pursuant to it, and treaties are the supreme law of the land. This means that federal law defeats conflicting state law.
2. Constitutions defeat other types of law within their domain. Thus, a state constitution defeats all other state laws inconsistent with it, and the U.S. Constitution defeats inconsistent federal laws.
3. When a treaty conflicts with a federal statute over a purely domestic matter, the measure that is latest in time usually prevails.
4. Within either the state or the federal domain, statutes defeat conflicting laws that depend on a legislative delegation for their validity. For example, a state statute defeats an inconsistent state administrative regulation.
5. State statutes and any laws derived from them by delegation defeat inconsistent common law

C O N C E P T R E V I E W

The Types of Law Compared

	WHO ENACTS?	STATE AND/OR FEDERAL?	STATED IN ONE AUTHORITATIVE FORM?	REMARKS
Constitutions	U.S. Constitution originally ratified by states; complex amendment process. States may vary.	Both	Yes, but see constitutional decision making.	Defeat other forms of positive law within sphere (federal or state)
Statutes	Legislatures	Both	Yes, but see this chapter's discussion of statutory interpretation.	Normally defeat other forms of positive law within sphere (federal or state) except constitutions
Common Law	Courts	In theory, state only	No. See this chapter's discussion of legal reasoning.	Law of tort, contract, and agency mainly common law
Equity	Formerly, equity courts; now usually courts in general	In theory, state only. But equitable principles pervade federal law as well.	No	Traditional separation of law and equity now virtually gone
Administrative Regulations	Administrative agencies	Both	Yes	See the chapter entitled Administrative Agencies
Administrative Decisions	Administrative agencies	Both	No	See the chapter entitled Administrative Agencies
Treaties	President plus two-thirds of Senate	Federal	Yes	Defeat inconsistent state law
Ordinances	Usually, local government bodies	State (mainly local)	Yes	
Executive Orders	Chief executives	Both	Yes	Usually based on delegation from legislature

rules. For example, either a statute or a state administrative regulation defeats a conflicting common law rule.

Classifications of Law

Cutting across the different types of law are three common *classifications* of law. These classifications involve distinctions between: (1) criminal law and civil law, (2) substantive law and procedural law, and (3) public law and private law. One type of law might be classified in each of these ways. For example, a state homicide statute would be criminal, substantive, and public; a rule of contract law would be civil, substantive, and private.

Criminal and Civil Law **Criminal law** is the law under which the government prosecutes someone for committing a crime. It is said to create duties that are owed to the public as a whole. **Civil law** mainly concerns obligations that private parties owe to other private parties. It is the law applied when one private party sues another private party because the second party did not meet a legal duty owed to the first party. (For this purpose, the government may be treated as a private party and thus as a party to a civil suit; for example, a city may sue, or be sued by, a construction contractor.) Criminal penalties (e.g., imprisonment or fines) differ from civil remedies (e.g., money damages or equitable relief). Although most of the legal rules in this text are civil law rules, the chapter on Crimes deals specifically with the criminal law, and criminal provisions may appear in other chapters.

Even though the civil law and the criminal law are distinct bodies of law, the same behavior can violate both. For instance, if due to A's careless driving his car hits and injures B, A may face both a criminal prosecution by the state and B's civil suit for damages.

Substantive Law and Procedural Law **Substantive law** sets the rights and duties of people as they act in society. **Procedural law** controls the behavior of government bodies (mainly courts) as they establish and enforce rules of substantive law. A statute making murder a crime, for example, is a rule of substantive law. But the rules describing the proper conduct of a criminal trial are procedural. This text mainly discusses substantive law. However, the chapters entitled The Resolution of Private Disputes and Crimes examine some of the procedural rules governing civil and criminal cases, respectively.

Public and Private Law **Public law** concerns the powers of government and the relations between government and private parties. Examples include constitutional law, administrative law, and criminal law. **Private law** establishes a framework of legal rules that enables private parties to set the rights and duties they owe each other. Examples include the rules of contract, property, and agency.

JURISPRUDENCE

The types of law sometimes are collectively referred to as *positive law.* Positive law comprises the rules that have been laid down (or posited) by a recognized political authority. Knowing the types of positive law is essential for understanding the American legal system and the business law topics discussed in this text. But defining *law* by listing these different kinds of positive law is much like defining the word *automobile* by describing all the vehicles going by that name. To define law properly, some people say, we need a general description that captures its essence.

The field known as **jurisprudence** or legal philosophy tries to provide such a description. Over time, different schools of jurisprudence have emerged, each with its own distinctive view of law. The differences among these schools are not just academic matters. As Figure 1 suggests, their conceptions of law often affect their approach toward real-life issues.

Legal Positivism

One feature common to all types of positive law is their enactment by a recognized political authority such as a legislature or an administrative agency. This common feature underlies the definition of law adopted by the school of jurisprudence called **legal positivism.** Legal positivists define law as the *command of a recognized political authority.* To the British political philosopher Thomas Hobbes, for instance, "Law properly, is the word of him, that by right hath command over others."

The commands made by recognized political authorities can be good, bad, or indifferent in moral terms. But as Figure 2 demonstrates, to legal positivists such commands are valid law regardless of their goodness or badness. For positivists, in other words, legal validity and moral validity are different

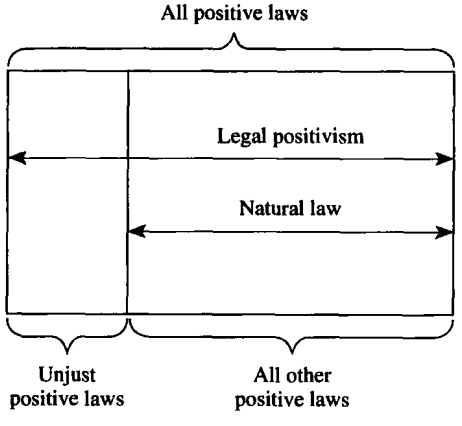
FIGURE 1

A Brief Sketch of the Jurisprudential Schools

	DEFINITION OF LAW	RELATION BETWEEN LAW AND MORALITY	PRACTICAL TENDENCY
Legal Positivism	Command of a recognized political authority	Separate questions: "law is law, just or not"	Valid positive law should be enforced and obeyed, just or not
Natural Law	All commands of recognized political authorities that are not unjust	"Unjust law is not law"	Unjust positive laws should not be enforced and obeyed
American Legal Realism	What public decisionmakers actually do	Unclear	"Law in action" often more important than "law in the books"
Sociological Jurisprudence	Process of social ordering in accordance with dominant social values and interests	Although moral values influence positive law, no way to say whether this is right or wrong	Law inevitably does (and should?) follow dominant social values and interests

FIGURE 2

The Positivist and Natural Law Definitions of Law



questions. Sometimes this view is expressed by the slogan: "Law is law, just or not." For this reason, some (but not all) positivists say that every properly enacted positive law should be enforced and obeyed, whether just or not. Similarly, positivist judges usually try to enforce the law as written, excluding their own moral views from the process.

Natural Law

At first glance, legal positivism's "law is law, just or not" approach may seem like perfect common sense. But it presents a problem, for it could mean that *any* positive law (no matter how unjust) is valid law and should be enforced and obeyed so long as some recognized political authority (no matter how wicked) enacted it. Here, the school of jurisprudence known as **natural law** takes issue with legal positivism by rejecting the positivist separation of law and morality.

The basic idea behind most systems of natural law is that some higher law or set of universal moral rules binds all human beings in all times and places. The Roman statesman Marcus Cicero described natural law as "the highest reason, implanted in nature, which commands what ought to be done and forbids the opposite." Because this higher law determines what is ultimately good and ultimately bad, it is a criterion for evaluating positive law. To Saint Thomas Aquinas, for example, "every human law has just so much of the nature of law, as it is derived from the law of nature." To be genuine law, in other words, positive law must resemble the law of nature by being good—or at least by not being bad. This suggests the practical natural law definition of law depicted in Figures 1 and 2—that it equals those commands of recognized political authorities that do not offend the higher law by being unjust.

Unjust positive laws, on the other hand, simply are not law. As Cicero put it: "What of the many deadly, the many pestilential statutes which are imposed on peoples? These no more deserve to be called laws than the rules a band of robbers might pass in their assembly." This view sometimes is

expressed by the slogan: "An unjust law is not law." Because unjust positive laws are not truly law, many natural law thinkers conclude that they should not be enforced or obeyed.

As compared with positivist judges, therefore, judges influenced by natural law ideas are more likely to read constitutional provisions broadly to strike down positive laws they regard as unjust. They also are more likely to let morality influence their interpretation of the law. Of course, neither judges nor natural law thinkers always agree about what is moral and immoral. This is a major difficulty for the natural law position. This difficulty allows legal positivists to claim that only by keeping legal and moral questions separate can we get any stability and predictability in the law.

American Legal Realism

To some people, the debate between natural law and legal positivism seems unreal. Not only is natural law pie-in-the-sky, such people might say, but sometimes positive law does not mean much either. For example, juries often pay little attention to the legal rules that are supposed to guide their decisions, and prosecutors frequently have discretion whether or not to enforce criminal statutes. In some legal proceedings, moreover, the background, biases, and values of the judge—and not the positive law—determine the result. As the joke goes, justice sometimes is what the judge ate for breakfast.

Remarks like these typify the school of jurisprudence known as **American legal realism.** Legal realists regard the positivist law-in-the-books as less important than the *law in action*—the conduct of those who enforce and interpret the positive law. Thus, American legal realism defines law as the *behavior of public officials (mainly judges) as they deal with matters before the legal system.* Because the actions of such decisionmakers—and not the rules in the books—really affect people's lives, the realists say, this behavior is what counts and what deserves to be called law.

It is doubtful whether the legal realists have ever developed a common position on the relation between law and morality or the duty to obey positive law. But they have been quick to tell judges how to behave. Many realists feel that the modern judge should be a kind of social engineer who weighs all relevant values and considers social science findings when deciding a case. Such a judge would make the positive law only one factor in her decision. Because judges inevitably base their decisions on personal considerations, the realists seem to say, they should at least do this honestly and intelligently. To promote this kind of decisionmaking, the realists have sometimes favored fuzzy, discretionary rules that allow judges to decide each case according to its unique facts.

Sociological Jurisprudence

The term **sociological jurisprudence** is a general label uniting several different jurisprudential approaches whose common aim is to examine law within its social context. Their outlook is captured by the following quotation from Justice Oliver Wendell Holmes:

> The life of the law has not been logic: it has been experience. The felt necessities of the time, the prevalent moral and political theories, intuitions of public policy, avowed or unconscious, even the prejudices which judges share with their fellow-men, have had a good deal more to do than the syllogism in determining the rules by which men should be governed. The law embodies the story of a nation's development through many centuries, and it cannot be dealt with as if it contained only the axioms and corollaries of a book of mathematics.[2]

Despite this common outlook, there is no distinctive sociological definition of law. If one were attempted, it might go as follows: *Law is a process of social ordering reflecting society's dominant interests and values.*

Different Sociological Approaches By examining a few examples of sociological legal thinking, we can put some flesh on the definition just offered. The "dominant interests" portion of the definition is exemplified by the writings of Roscoe Pound, an influential 20th-century American legal philosopher. Pound developed a detailed catalog of the social interests that press on government and the legal system and thus shape positive law. During his life, Pound's catalog changed along with changes in American society. An example of the definition's "dominant values" component is the *historical school* of jurisprudence identified with the 19th-century German legal philosopher Friedrich Karl von Savigny. Savigny saw law as an unplanned, almost unconscious, reflection of the collective spirit (*Volksgeist*) of a particular society. In his view, legal change could only be explained historically, as a slow response to social change.

[2]Holmes, *The Common Law* (1881).

By emphasizing the influence of dominant social interests and values, Pound and Savigny undermine the legal positivist view that law is nothing more than the command of some political authority. The early 20th-century Austrian legal philosopher Eugen Ehrlich went even further in rejecting positivism. He did so by distinguishing two different "processes of social ordering" contained within our definition of sociological jurisprudence. The first of these is "state law," or positive law. The second is the "living law," informal social controls such as customs, family ties, and business practices. By regarding both as law, Ehrlich blurred the line between positive law and other kinds of social ordering. In the process, he stimulated people to recognize that positive law is only one element within a spectrum of social controls.

The Implications of Sociological Jurisprudence Because its definition of law includes social values, sociological jurisprudence seems to resemble natural law. But most sociological thinkers are only concerned with the *fact* that moral values influence the law, and not with the goodness or badness of those values. In Product Liability, for instance, we note that laissez-faire economic values were widely shared in 19th-century America and strongly influenced the product liability law of that period. But we do not say whether this was good or bad. Thus, it might seem that sociological jurisprudence gives no practical advice to those who must enforce and obey positive law.

However, sociological jurisprudence has at least one practical implication—a tendency to urge that the law must change to meet changing social conditions and values. This is basically the familiar notion that the law should keep up with the times. Some might stick to this view even when society's values are changing for the worse. To Holmes, for example, "[t]he first requirement of a sound body of law is, that it should correspond with the actual feelings and demands of the community, *whether right or wrong.*"[3]

[3]The italics have been added for emphasis.

ROCHIN v. CALIFORNIA[4] 342 U.S. 165 (U.S. Sup. Ct. 1952)[4]

In 1949, three Los Angeles County deputy sheriffs heard that Antonio Rochin was selling narcotics. In search of evidence, they entered Rochin's home one morning and forced open the door to his bedroom. They spotted two capsules on a nightstand beside the bed on which the half-clad Rochin was sitting. After the deputies asked, "Whose stuff is this?" Rochin quickly put the capsules in his mouth. The deputies then jumped Rochin and tried to force the capsules from his mouth. When this proved unsuccessful, they handcuffed Rochin and took him to a hospital. Over Rochin's opposition, they had a doctor insert a tube into his stomach and force an emetic (vomit-inducing) solution through the tube. This stomach pumping caused Rochin to vomit. Within the material he disgorged were two capsules containing morphine.

Rochin then was tried and convicted for possessing a morphine preparation in violation of California law. The two morphine capsules were the main evidence against him, and the trial court admitted this evidence over Rochin's objection. An intermediate appellate court and the California Supreme Court affirmed the conviction. Rochin then appealed to the U.S. Supreme Court. The main issue before the Court was whether the methods by which the deputies obtained the capsules violated the Due Process Clause of the U.S. Constitution's Fourteenth Amendment, which states that "No state shall . . . deprive any person of life, liberty, or property, without due process of law."

Note: *At the time this case was decided, evidence obtained through a forced stomach pumping probably was admissible in a majority of the states that had considered the question. Also, the Supreme Court did not then require that state courts exclude evidence obtained through an illegal search or seizure.*

Frankfurter, Justice The requirements of due process impose upon this Court an exercise of judgment upon the proceedings resulting in a conviction to ascertain whether they offend those canons of decency and fairness which express the notions of justice of English-speaking peoples even toward those charged with the most heinous offenses. These standards of justice are not authoritatively formulated anywhere as though they were

[4]At this point, you may want to read the appendix, Reading and Briefing cases.

specifics. Due process of law is a summarized guarantee of respect for those personal immunities so rooted in the traditions and conscience of our people as to be fundamental, or implicit in the concept of ordered liberty.

The vague contours of the due process clause do not leave judges at large. We may not draw upon our merely personal and private notions and disregard the limits that bind judges. These limits are derived from considerations that are fused in the whole nature of our judicial process. These are considerations deeply rooted in reason and in the compelling traditions of the legal profession. The due process clause places upon this Court the duty of exercising a judgment upon interests of society pushing in opposite directions. Due process thus conceived is not to be derided as a resort to the revival of "natural law."

Applying these general considerations to the present case, we conclude that the proceedings by which this conviction was obtained do more than offend some fastidious squeamishness or private sentimentalism about combatting crime too energetically. This is conduct that shocks the conscience. Illegally breaking into the privacy of Rochin, the struggle to open his mouth and remove what was there, the forcible extraction of his stomach's contents—this course of proceeding is bound to offend even hardened sensibilities. They are methods too close to the rack and the screw to permit of constitutional differentiation.

Judgment reversed in favor of Rochin.

Comparing the Schools

The *Rochin* case helps illustrate the differences among the schools of jurisprudence. To highlight those differences, consider the following questions. Do you believe Justice Frankfurter when he says that the Court's decision is not based on natural law? Is that decision closer to positivism's law-is-law-just-or-not approach, or to natural law's an-unjust-law-is-not-law approach? Do you think that a positivist would like this case? On the other hand, how would a legal realist look at *Rochin?* Specifically, what would such a person probably say about both the Court's decision and the police behavior here? With the benefit of hindsight, finally, it looks as if *Rochin* was a precursor of the many liberal criminal procedure decisions of the 1960s—decisions that probably had their roots in changed social values. If so, what might an exponent of sociological jurisprudence say about *Rochin?*

THE FUNCTIONS OF LAW

In traditional societies, people often viewed law as a set of unchanging rules that deserved obedience because they were part of the natural order of things. By now, however, most lawmakers treat law as a flexible *tool* or *instrument* for the accomplishment of chosen purposes. For example, the law of negotiable instruments discussed later in this text is designed to stimulate commercial activity by promoting the free movement of money substitutes such as promissory notes, checks, and drafts. Throughout the text, moreover, you see courts manipulating existing legal rules to get the results they desire. One strength of this *instrumentalist* attitude is its willingness to adapt the law to further the social good. One weakness is the legal instability and uncertainty those adaptations often produce.

Just as individual legal rules advance specific purposes, *law as a whole* serves many general social functions. Among the most important of those functions are:

1. *Peacekeeping.* The criminal law rules discussed in Crimes best further this basic function of any legal system. Also, as The Resolution of Private Disputes suggests, one major function of the civil law is the resolution of private disputes.
2. *Checking government power and thereby promoting personal freedom.* Obvious examples are the constitutional restrictions on government regulation.
3. *Facilitating planning and the realization of reasonable expectations.* The rules of contract law discussed help fulfill this function of law.
4. *Promoting economic growth through free competition.* The antitrust laws discussed are among the many legal rules that help perform this function.
5. *Promoting social justice.* Throughout this century, government has intervened in private social and economic affairs to correct perceived

injustices and give all citizens equal access to life's basic goods. One example is the collection of employer–employee regulations treated in Employment Law.

6. *Protecting the environment.* The most important federal environmental statutes are discussed in Environmental Law.

Obviously, the law's various functions can conflict. The familiar clash between economic growth and environmental protection is an example. The *Rochin* case illustrates the equally familiar conflict between effective law enforcement and the preservation of personal rights. Only rarely does the law achieve one end without sacrificing others to some degree. In law, as in life, there generally is no such thing as a free lunch. Where the law's ends conflict, lawmakers can only try to strike the best possible balance among those ends. This suggests limits on the law's usefulness as a device for promoting particular social goals.

LEGAL REASONING

This text's main aim is to describe the most important legal rules affecting business. Like most other business law texts, it states those rules in what lawyers call "black letter" form, using sentences saying that certain legal consequences will occur if certain events happen. Although it enables a clear statement of the law's commands, this black letter approach can be misleading. It suggests definiteness, certainty, permanence, and predictability—attributes the law frequently lacks. To illustrate this, and to give you some idea how lawyers think, we now discuss the two most important kinds of legal reasoning: **case law reasoning** and **statutory interpretation.**[5] However, we first must examine legal reasoning in general.

Legal reasoning is basically deductive, or syllogistic. The legal rule is the major premise, the facts are the minor premise, and the result is the product of combining the two. Suppose a state statute says that a driver operating an automobile between 55 and 70 miles per hour must pay a $50 fine (the rule or major premise) and that Jim Smith drives his car at 65 miles per hour (the facts or minor premise). If Jim is arrested, and if the necessary facts can be proved, he will be required to pay the $50 fine. As you will now see, however, legal reasoning often is more difficult than this example would suggest.

Case Law Reasoning

In cases governed by the common law, courts find the appropriate legal rules in prior cases or *precedents.* The standard for choosing and applying prior cases to decide present cases is the doctrine of *stare decisis,* which states that like cases should be decided alike.[6] That is, the present case should be decided in the same way as past cases presenting the same facts and the same legal issues. If a court decides that an alleged precedent is not like the present case and should not control the decision in that case, it *distinguishes* the prior case.[7]

Because every present case differs from the precedents in *some* respect, it is always theoretically possible to distinguish those precedents. For example, one *could* distinguish a prior case because both parties in that case had black hair, while one party in the present case has brown hair. Of course, such distinctions are usually ridiculous, because the differences they identify are insignificant in moral or social policy terms. In other words, a good distinction of a prior case involves a widely accepted ethical or policy reason for treating the present case differently from its predecessor. Because people disagree about moral ideas, public policies, and the degree to which they are accepted, and because all these factors change over time, judges may differ on the wisdom of distinguishing a prior case. This is a significant source of uncertainty in the common law. But it also gives the common law the flexibility to adapt to changing social conditions.

The following *MacPherson* case illustrates the common law's ability to change over time. In the series of New York cases *MacPherson* discusses, the **plaintiff** (the party suing) claimed that the **defendant** (the party being sued) had been negligent in manufacturing or inspecting some product, thus injuring the plaintiff, who later purchased or

[5]The reasoning courts employ in constitutional cases resembles that used in common law cases, but often is somewhat looser. For the way courts decide constitutional cases, see the chapter entitled Business and the Constitution.

[6]*Stare decisis* should be distinguished from the doctrine of *res judicata,* which says that a final judicial decision on the merits conclusively settles the rights of *the parties to the case.*

[7]Also, while they exercise the power infrequently, courts sometimes completely *overrule* their prior decisions.

used the product.[8] In the mid-19th century, such suits often failed due to the general rule that a seller or manufacturer was not liable for negligence unless there was *privity of contract* between the defendant and the plaintiff. Privity of contract is the existence of a direct contractual relationship between two parties. Thus, the no-liability-outside-privity rule prevented injured plaintiffs from recovering against a seller or manufacturer who had sold the product to a dealer who resold it to the plaintiff. Over time, however, courts began to allow injured plaintiffs to recover from sellers or manufacturers with whom they had not directly dealt. These courts were creating *exceptions* to the general rule; that is, they were distinguishing prior cases announcing the rule and creating new rules to govern the situations they distinguished. *MacPherson* describes the gradual enlargement of such an exception in New York. Eventually, the exception "consumed the rule" by covering so many situations that the original rule became insignificant.[9]

[8]Negligence law is discussed in Negligence and Strict Liability.

[9]The present status of the old no-liability-outside-privity rule in sale-of-goods cases is discussed in Product Liability.

MACPHERSON v. BUICK MOTOR CO. 111 N.E. 1050 (N.Y. Ct. App. 1916)

One wheel of an automobile manufactured by the Buick Motor Company was made of defective wood. Buick could have discovered the defect had it made a reasonable inspection after it purchased the wheel from another manufacturer. Buick sold the car to a retail dealer, who then sold it to MacPherson. While MacPherson was driving his new Buick, the defective wheel collapsed and he was thrown from the vehicle. He sued Buick for his injuries in a New York trial court, alleging that it had negligently failed to inspect the wheel. Buick's main defense was that it had not dealt directly with MacPherson and thus owed no duty to him. Following trial and appellate court judgments in MacPherson's favor, Buick appealed to the New York Court of Appeals, the state's highest court.

Cardozo, Justice The foundations of this branch of the law were laid in *Thomas v. Winchester* (1852). A poison was falsely labeled. The sale was made to a druggist, who sold to a customer. The customer recovered damages from the seller who affixed the label. The defendant's negligence, it was said, put human life in imminent danger. A poison, falsely labeled, is likely to injure anyone who gets it. Because the danger is to be foreseen, there is a duty to avoid the injury. *Thomas v. Winchester* became quickly a landmark of the law. In the application of its principle there may, at times, have been uncertainty or even error. There has never been doubt or disavowal of the principle itself.

The chief cases are well known. *Loop v. Litchfield* (1870) was the case of a defect in a small balance wheel used on a circular saw. The manufacturer pointed out the defect to the buyer. The risk can hardly have been an imminent one, for the wheel lasted five years before it broke. In the meanwhile the buyer had made a lease of the machinery. It was held that the manufacturer was not answerable to the lessee. *Loop v. Litchfield* was followed by *Losee v. Clute* (1873), the case of the explosion of a steam boiler. That decision must be confined to its special facts. It was put upon the ground that the risk of injury was too remote. The buyer had not only accepted the boiler, but had tested it. The manufacturer knew that his own test was not the final one. The finality of the test has a bearing on the measure of diligence owing to persons other than the purchaser.

These early cases suggest a narrow construction of the rule. Later cases evince a more liberal spirit. In *Devlin v. Smith* (1882), the defendant contractor built a scaffold for a painter. The painter's workmen were injured. The contractor was held liable. He knew that the scaffold, if improperly constructed, was a most dangerous trap. He knew that it was to be used by the workmen. Building it for their use, he owed them a duty to build it with care. From *Devlin v. Smith* we turn to *Statler v. Ray Manufacturing Co.* (1909). The defendant manufactured a large coffee urn. It was installed in a restaurant. The urn exploded and injured the plaintiff. We held that the manufacturer was liable. We said that the urn

was of such a character that it was liable to become a source of great danger if not carefully and properly constructed.

It may be that *Devlin v. Smith* and *Statler v. Ray Manufacturing Co.* have extended the rule of *Thomas v. Winchester.* If so, this court is committed to the extension. The defendant argues that things imminently dangerous to human life are poisons, explosives, deadly weapons—things whose normal function is to injure or destroy. But whatever the rule in *Thomas v. Winchester* may once have been, it no longer has that restricted meaning. A scaffold is not inherently a destructive instrument. No one thinks of [a coffee urn] as an implement whose normal function is destruction.

We hold, then, that the principle of *Thomas v. Winchester* is not limited to things which are implements of destruction. If the nature of a thing is such that it is reasonably certain to place life and limb in peril when negligently made, it is a thing of danger. If to the element of danger there is added knowledge that the thing will be used by persons other than the purchaser, then, irrespective of contract, the manufacturer is under a duty to make it carefully.

The nature of an automobile gives warning of probable danger if its construction is defective. This automobile was designed to go 50 miles an hour. Unless its wheels were sound and strong, injury was almost certain. The defendant knew the danger. It knew that the car would be used by persons other than the buyer, a dealer in cars. The dealer was indeed the one person of whom it might be said with some certainty that by him the car would not be used. Yet the defendant would have us say that he was the one person it was under a legal duty to protect. The law does not lead us to so inconsequent a conclusion. Precedents drawn from the age of travel by stagecoach do not fit the conditions of travel today. The principle that the danger must be imminent does not change, but the things subject to the principle do change. They are whatever the needs of life in a developing civilization require them to be.

Judgment for MacPherson affirmed.

Statutory Interpretation

Because statutes are written in one authoritative form, their interpretation might seem easier than case law reasoning. However, this is not so. One reason courts face difficulties when interpreting statutes is the natural ambiguity of language. This is especially true when statutory words are applied to situations the legislature did not foresee. Also, legislators may deliberately use ambiguous language when they are unwilling or unable to deal specifically with each situation the statute was enacted to regulate. When this happens, the legislature expects courts and/or administrative agencies to fill in the details on a case-by-case basis. Other reasons for deliberate ambiguity include the need for legislative compromise and legislators' desire to avoid taking controversial positions.

Due to problems like these, courts need and use various techniques of statutory interpretation. As you will see shortly, different techniques can dictate different results in a particular case. Moreover, judges sometimes employ the techniques in an instrumentalist or result-oriented fashion, emphasizing the technique that will produce the result they want and downplaying the others. Thus, it is unclear which technique should control when different techniques yield different results. Although there are some "rules" on this subject, judges often ignore them or use them selectively.

Plain Meaning Courts begin their interpretation of a statute with its actual language. Where the statute's words have a clear, common, accepted meaning, some courts employ the *plain meaning rule.* This rule states that in such cases, the court should simply apply the statute according to the plain, accepted meaning of its words, and should not concern itself with anything else.

Legislative History Some courts, like the Supreme Court in the following *Weber* case, refuse to follow a statute's plain meaning when its legislative history suggests a different result. And almost all courts resort to legislative history when the statute's language is ambiguous. A statute's legislative history includes the following sources: the reports of investigative committees or law revision commissions that led to the legislation, the hearings of the

legislative committee(s) originally considering the legislation, any reports issued by such a committee, legislative debates, the report of a conference committee reconciling two houses' conflicting versions of the law, amendments or defeated amendments to the legislation, other bills not passed by the legislature but proposing similar legislation, and discrepancies between a bill passed by one house and the final version of the statute.

Sometimes a statute's legislative history provides no information or conflicting information about its meaning, its scope, or its purposes. Also, some sources are more authoritative than others. The worth of debates, for instance, may depend on which legislator (e.g., the sponsor of the bill or an uninformed blowhard) is quoted. Some sources are useful only in particular situations; prior unpassed bills and amendments or defeated amendments are examples. To illustrate those sources, consider whether mopeds are covered by an air pollution statute applying to "automobiles, trucks, buses, and other motorized passenger or cargo vehicles." If the statute's original version included mopeds but this reference was removed by amendment, it is unlikely that the legislature wanted mopeds to be covered. The same might be true if six similar unpassed bills had included mopeds but the bill that was eventually passed did not, or if one house had passed a bill including mopeds but mopeds did not appear in the final version of the legislation.

Courts use legislative history in two overlapping but distinguishable ways. They may use it to determine what the legislature thought about the specific meaning of statutory language. They may also use it to determine the overall aim, end, or goal of the legislation. In this second case, they then ask whether a particular interpretation of the statute is consistent with this purpose. To illustrate the difference between these two uses of legislative history, suppose that a court is considering whether our pollution statute's "other motorized passenger or cargo vehicles" language includes battery-powered vehicles. The court might scan the legislative history for specific references to battery-powered vehicles or other indications of what the legislature thought about their inclusion. However, the court might also use the same history to determine the overall aims of the statute, and then ask whether including battery-powered vehicles is consistent with those aims. Because the history probably would reveal that the statute's purpose was to reduce air pollution from internal combustion engines, the court might well conclude that battery-powered vehicles should not be covered.

General Public Purpose Occasionally, courts construe statutory language in the light of various *general public purposes.* These purposes are not the purposes underlying the statute in question; rather, they are widely accepted general notions of public policy. In one case, for example, the U.S. Supreme Court used the general public policy against racial discrimination in education as one argument for denying tax-exempt status to a private university that discriminated on the basis of race.[10]

Prior Interpretations Courts sometimes follow prior cases (and administrative decisions) interpreting a statute regardless of the statute's plain meaning or its legislative history. The main argument for following these prior interpretations is to promote stability and certainty by preventing each successive court that considers a statute from adopting its own interpretation. The courts' willingness to follow a prior interpretation depends on such factors as the number of past courts adopting the interpretation, the authoritativeness of those courts, and the number of years that the interpretation has been followed. Note that in *Weber,* the Supreme Court arguably did not follow one of its own prior interpretations.

Maxims Maxims are general rules of thumb employed in statutory interpretation. There are many maxims, and courts tend to use them or ignore them at their discretion. One example of a maxim is the *ejusdem generis* rule, which says that when general words follow words of a specific, limited meaning, the general language should be limited to things of the same class as those specifically stated. Suppose that the pollution statute quoted earlier listed 32 types of gas-powered vehicles and ended with the words "and other motorized passenger or cargo vehicles." Here, *ejusdem generis* probably would dictate that battery-powered vehicles not be included.

[10] *Bob Jones University v. United States,* 461 U.S. 574 (1983).