

LAW FOR BUSINESS

Student Workbook

to accompany

Law for Business

Donnell, Barnes, and Metzger

Workbook prepared by

Jane P. Mallor

Michael J. Phillips

L. Thomas Bowers

Eric L. Richards

*All of the
School of Business
Indiana University*

1983

Revised Edition

IRWIN

**Richard D. Irwin, Inc.
Homewood, Illinois**

©Richard D. Irwin, Inc., 1980 and 1983

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 0-256-02805-2

Printed in the United States of America.

67890P09876

CONTENTS

Chapter 1	Law and Its Sources	1
2	Dispute Settlement	7
3	Crimes and Intentional Torts	13
4	Negligence and Strict Liability	19
5	The Nature and Origins of Contracts	25
6	Creating a Contract: Offers	31
7	Creating a Contract: Acceptances	37
8	Voluntary Consent	45
9	Capacity to Contract	51
10	Consideration	57
11	The Form and Meaning of Contracts	63
12	Illegality	69
13	Third Parties' Contract Rights	75
14	Performance and Remedies	81
15	Introduction to Sales	87
16	Title, Risk of Loss, and the Terms of Sales Contracts	95
17	Product Liability	101
18	Performance of Sales Contracts	109
19	Remedies for Breach of Sales Contracts	115
20	Introduction to Agency and Employment	121
21	Agency Authority and Termination	127
22	Liability of Principals and Agents to Third Persons	133
23	Duties of Principals and Agents to Each Other	141
24	Employment Laws	147
25	Introduction to Business Organizations	153
26	Formation and Operation of Partnerships	159
27	Dissolution of Partnerships	167
28	Limited Partnerships and Similar Forms	175
29	The Formation and Termination of Corporations	181
30	Management of the Corporate Business	189
31	Shareholder Functions, Rights, and Liabilities	197
32	Close Corporations	205
33	Which Form of Business Organization?	211
34	Legal Liability of Accountants	217
35	Personal Property	223
36	Bailments	229
37	Real Property	235
38	Landlord and Tenant	243
39	Estates and Trusts	249
40	Negotiable Instruments	255
41	Negotiation and Holder in Due Course	263
42	Liability of Parties	273
43	Checks and Bank Collections	281
44	Introduction to Secured Transactions	287
45	Secured Consumer Transactions	293
46	Secured Commercial Transactions	299
47	Bankruptcy	305
48	Insurance	311
49	Government Regulation of Business	317
50	The Antitrust Laws	323
51	Consumer Protection Laws	329

CHAPTER 1

LAW AND ITS SOURCES

Learning Objectives

1. You should understand the general concept of preventive law.
2. You should understand the basic functions law serves.
3. You should understand the difference between substantive law and procedural law.
4. You should understand the differences between civil law and criminal law.
5. You should understand the basic idea of checks and balances and be able to give some examples of its operation.
6. You should have a general idea of the more important constitutional provisions affecting business.
7. You should know what the Supremacy Clause of the Constitution is and the effect it has on state law.
8. You should be thoroughly familiar with the different sources of law.
9. You should understand the three ways in which courts make law.
10. You should be aware of the ways in which the law ensures predictability while still remaining adaptable to changing circumstances.
11. You should have some appreciation of the functions of the judge and of lawyers in the adversary system.

Learning Hints

1. Substantive law generally "looks outward" to set standards for organized social life. Procedural law "looks inward" to the internal operation of the legal system. It sets the rules which determine how substantive rules are enforced.
2. A civil action is a lawsuit between two private parties (one of whom may sometimes be the government). In a criminal action, the government is basically acting in a prosecutorial role and is enforcing the criminal law, a body of law set up to punish breaches of duty to society at large.

3. In a civil suit, the plaintiff is the party who is suing and the defendant is the party being sued. In a criminal suit, the party who is being prosecuted is the defendant. In criminal cases, however, the government is not usually referred to as a plaintiff.
4. The Constitution can limit Congress's law-making power in two ways: 1) by specifically listing Congress's powers and saying that Congress shall have these powers and no others; and 2) by imposing certain independent checks on Congress when it exercises its legitimate powers (e.g. due process). By now, the second sort of limitation on Congressional power is much more important than the first.
5. The Taxing Power is a source of regulatory power because of the effect that taxation can have on socially disfavored activities. "The power to tax is the power to destroy." Also, various tax deductions and tax credits can have a regulatory effect by encouraging certain kinds of activities.
6. Delegation is a process whereby the legislature effectively "hands over" some of its power to a subordinate body. The rules issued by the subordinate body are valid because the legislature has given that body power to issue them. Among the sources of law discussed in the text, administrative rules and decisions and executive orders clearly involve delegation.
7. Law and equity used to be dispensed in separate courts, and the test for obtaining equitable relief was whether the plaintiff lacked an adequate remedy at law. Today, law and equity are usually dispensed within the same courts. Also, equitable remedies and equitable concepts are sometimes applies in what seem to be "law" cases.
8. As the text stresses, the doctrine of stare decisis, while appearing to be very rigid, actually permits considerable change in the common law. This is because it is theoretically possible to distinguish every past case, or precedent. The power to determine what are "good" and "bad" distinctions of past cases rests with the courts.

True-False

Circle T (true) and F (false)

- | | | |
|---|---|---|
| T | F | 1. Preventive law means that business people should be able to manage their own legal affairs without the help of a lawyer. |
| T | F | 2. A legal rule which states what sorts of cases a court can hear is called a procedural rule. |
| T | F | 3. Civil law involves suits between private parties. |

- T F 4. The "checks and balances" concept works only between the states and the federal government, and not within the federal government.
- T F 5. Judicial review is the power of the state and federal courts to determine the meaning of statutes.
- T F 6. There is no federal common law.
- T F 7. Today, the Commerce Clause of the U.S. Constitution is a very broad source of Congressional authority to regulate society.
- T F 8. The Bill of Rights now applies only to the federal government, and not the states.
- T F 9. In case of a conflict, a treaty will defeat an inconsistent state constitutional provision.
- T F 10. Administrative agencies can issue rules and regulations, but they do not have the power to decide cases.

Multiple Choice

Circle the best alternative.

1. Executive orders:
- a. include decisions by an administrative body.
 - b. depend for their validity on the concept known as delegation.
 - c. are only good law at the federal level.
 - d. have to be ratified by two-thirds of the states in order to become law.
2. Which of the following is true of the common law?
- a. It will defeat an inconsistent statute.
 - b. It exists at both the state and federal levels.
 - c. It is one part of the power of judicial review.
 - d. In applying the common law, courts follow the doctrine of stare decisis.
3. The law helps ensure predictability by:
- a. permitting ex post facto laws.
 - b. giving courts no freedom when they interpret statutes.
 - c. requiring federal administrative agencies to publish notice of an intent to issue a regulation and the final text of a regulation in the Federal Register.
 - d. allowing judges to distinguish prior decisions in common law cases.

4. Substantive law may:
- set rules requiring notice and a fair hearing in criminal cases.
 - state how a trial is to be conducted.
 - permit the resolution of a lawsuit before it gets to trial.
 - impose duties on people in their day-to-day social life.
5. Which of the following is a source of Congressional power to regulate the economy?
- The Commerce Clause
 - The Due Process Clauses
 - The First Amendment right to free speech.
 - The Fourth Amendment protection against unreasonable searches and seizures.
6. If there is a conflict between a federal statute and one of the following sources of law, which will defeat the federal statute?
- A state constitution
 - An Executive Order
 - The federal common law.
 - None of the above.
7. Which of the following sources of law depends for its validity on the fact that Congress has given the person or body issuing it the power to make law?
- State constitutions
 - The common law
 - Administrative rules
 - State statutes
8. The doctrine of stare decisis:
- is a technique court use to discover the meaning of statutes.
 - compels a court in state X to follow the decisions of courts in state Y.
 - makes subsequent courts follow all dicta contained in an earlier case.
 - None of the above.
9. The federal courts:
- will never use state law to decide a case.
 - have the power to declare acts of Congress unconstitutional.
 - have the power to use the federal common law.
 - have the power to overturn administrative decisions whenever they feel that this is just, and do so frequently.

10. In order for federal legislation to be constitutional:

- a. the U.S. Constitution must give Congress the power to pass such a law.
- b. it must be based on Fifth Amendment due process.
- c. it must not be prohibited by anything in the Constitution.
- d. Two of the above.

Short Essay

1. Explain why a treaty will defeat an inconsistent state constitutional provision.

2. Of the sources of law described in the text, which exists at both the state and the federal levels?

3. Explain in general terms the difference between the adversary system used in Anglo-American law and the system generally used on the European continent.

CHAPTER 2

DISPUTE SETTLEMENT

Learning Objectives

1. You should know the differences between and among negotiation, mediation and arbitration as means of dispute settlement.
2. You must know the requirements for the two major forms of federal court jurisdiction: diversity jurisdiction and federal question jurisdiction.
3. You should be familiar with all the federal courts on the chart on page 22 of the text. You should be very familiar with the federal District Courts, Circuit Courts of Appeals, and U.S. Supreme Court.
4. You should know the various types of state courts discussed on pages 25-26.
5. You should be familiar with all the procedural steps in a civil action.
6. You should know the differences between the burden of proof in a civil case and the burden of proof in a criminal case.
7. You should know the general rules and procedures for appeals in civil cases.

Learning Hints

1. There are really two aspects to jurisdiction in most cases. The first is the ability of a court to hear a particular type of case (called "subject-matter jurisdiction" or "competence."). A state, for instance, may set up special courts to handle criminal, domestic relations or divorce cases, or set dollar limits for getting into a particular court. The other aspect of jurisdiction, mainly applicable to state courts, concerns the territorial reach of the court. This raises many problems beyond the scope of this book, as for instance the jurisdiction of a state trial court over an out-of-state corporation.

2. In federal court cases where jurisdiction is based on diversity of citizenship, the amount involved must be at least \$10,000. For federal question jurisdiction, there is no \$10,000 limit.
3. Many civil cases may be brought in a state trial court or in federal District Court. For instance, a suit against an out-of-stater for an amount exceeding \$10,000 might be brought in a state trial court (if there is jurisdiction) or in federal District Court. As the book suggests, this creates strategic questions an attorney will have to consider. Also, note the possibility that a state court case may be removed to federal court.
4. With a very few exceptions, cases do not originate in appellate courts and these courts are usually limited to correcting errors of law (not fact) made at the trial court level.
5. Each federal judicial circuit includes several states and each of these states has at least one District Court. Decisions appealed from such a District Court go to the Court of Appeals whose circuit includes that state. For instance, cases from the Southern District of New York (basically, Manhattan) are appealed to the Second Circuit Court of Appeals.
6. The U.S. Supreme Court's "appeal" jurisdiction is mandatory (for cases where it applies) and the Court's "certiorari" jurisdiction is discretionary. Most cases appealed to the Court fall into the second category and relatively few of these are actually heard by the Court, which, like most courts today, has severe caseload problems.
7. Note how the basic state court structure parallels the basic federal court structure.
8. The rules stating what is sufficient service of a summons and the rules governing jurisdiction are not the same.
9. The Summons and the Complaint, while often served together, are not the same, and in fact serve different functions.
10. Many cases are disposed of by the motion to dismiss described on page 28. The most common form of motion to dismiss goes to the legal sufficiency of the Complaint: it assumes the truth of its facts (but only for purposes of the motion) and effectively says that even if they are all true, the plaintiff still cannot recover, because there is no rule of law allowing recovery on those facts. You might say that the motion to dismiss says "So what?" to the plaintiff's Complaint.
11. The motion for a directed verdict and the motion for judgment notwithstanding the verdict are basically ways of "taking the case away from the jury." Basically, both assert that no reasonable jury could favor the party against whom the motion is made. Both express the U.S. legal system's ambivalence about the jury, since if all juries were reasonable, there would be little need for these motions.

12. Generally speaking, appellate courts review only legal errors made by the trial court. These can include at least the following: lack of jurisdiction, discovery rulings, the motion to dismiss, evidentiary rulings at trial, the motions for directed verdict and judgment notwithstanding the verdict, the instruction to the jury, and the trial court's findings of law (if there is no jury trial). Some of these matters look "factual," but technically they are not.

True-False

Circle T (true) or F (false).

- | | | | |
|---|---|-----|--|
| T | F | 1. | Mediation is a means of dispute settlement in which the mediator has the power to issue a final decision binding on the parties. |
| T | F | 2. | Often, courts will decide cases that are moot, rule on hypothetical questions, or give advisory opinions on important constitutional questions. |
| T | F | 3. | All cases heard before federal courts must be for an amount greater than or equal to \$10,000. |
| T | F | 4. | The U.S. Supreme Court's certiorari jurisdiction is discretionary. |
| T | F | 5. | The Summons must state in numbered paragraphs the legal facts on which the plaintiff bases his case. |
| T | F | 6. | When the Answer includes an affirmative defense, the plaintiff must file a Reply. |
| T | F | 7. | Interrogatories are a form of discovery involving written questions submitted to a party. |
| T | F | 8. | In a civil case, the plaintiff must have a preponderance of the evidence on his or her side in order to win. |
| T | F | 9. | An appellate court will hold a new trial if it determines that the trial court's decision was erroneous, and will do so itself because of possible prejudice to the losing party if the case were returned to the trial court. |
| T | F | 10. | One of the functions of the pleadings is to inform each party about the other party's case. |

Multiple Choice

Circle the best alternative.

1. Which of the following is an advantage of arbitration as a means of dispute settlement?
 - a. Lawyers are not allowed in arbitration proceedings and thus there are fewer petty technicalities raised.
 - b. Arbitrators are, on the whole, more honest and capable than judges.
 - c. Arbitration proceedings are usually quicker than judicial proceedings.
 - d. Arbitration actually has no advantages over regular judicial proceedings.
2. Federal question jurisdiction:
 - a. is one of the types of jurisdiction possessed by state trial courts.
 - b. is the principal form of U.S. Supreme Court appellate jurisdiction.
 - c. requires that the amount in controversy be at least \$10,000.
 - d. None of the above.
3. A state's "inferior" courts:
 - a. usually keep no transcript of their proceedings.
 - b. decide cases which cannot be later heard in a court of record because the issues they deal with are so trivial.
 - c. always require that the parties be represented by an attorney.
 - d. provide each party with the right to a jury trial.
4. A Summons which is properly served:
 - a. requires the defendant to file an Answer.
 - b. requires the defendant to make an appearance.
 - c. is the same thing as a Complaint.
 - d. Two of the above.
5. The term "discovery" includes:
 - a. oral examinations under oath.
 - b. disclosure of trial strategy.
 - c. stipulations of agreed-upon facts.
 - d. the obtaining of affidavits from key witnesses.
6. A device by which a case might be taken away from the jury after all the evidence is presented is:
 - a. the motion to dismiss.
 - b. the opening statement.
 - c. sequestration of the jury.
 - d. the motion for a directed verdict.

7. Which of the following is a recognized basis for an appeal?
 - a. one party's failure to agree to arbitration before trial.
 - b. a legal error at trial.
 - c. a jury decision on a close question of fact.
 - d. All of the above.
8. Federal courts have exclusive jurisdiction over:
 - a. all cases where the amount in question equals or exceeds \$10,000.
 - b. all cases between citizens of two different states.
 - c. patent cases.
 - d. all cases presenting federal constitutional questions.
9. The U.S. Circuit Courts of Appeals:
 - a. are 15 in number.
 - b. hear appeals from state Supreme Courts.
 - c. are basically trial courts.
 - d. are mainly organized on a territorial basis.

1. State the tests for diversity jurisdiction in the federal District courts.
2. What is the difference between the Complaint and the Summons?

3. What is the main difference between the motion for a directed verdict and the motion for judgment notwithstanding the verdict?

CHAPTER 3

CRIMES AND INTENTIONAL TORTS

Learning Objectives

1. You should know the general difference between a felony and a misdemeanor.
2. You must know the three basic essentials of any crime.
3. You should know the rules surrounding the three major types of criminal incapacity: intoxication, infancy and insanity.
4. You should be familiar with the more important procedural protections our system gives defendants in a criminal case.
5. You should recognize the three broad categories of intentional torts: interference with personal rights, interference with property rights, and interference with economic relations.
6. You should understand the distinction between assault and battery.
7. In the area of defamation, you should understand the difference between libel and slander, when proof of specific damages is required in each case, and the various defenses and privileges to a defamation suit.
8. You should know the four types of invasion of privacy.
9. You should of course also be familiar with the intentional torts not specifically mentioned here but discussed in the text.

Learning Hints

1. The delay of trial or sentencing, or the acquittal of the defendant, on the basis of insanity does not necessarily mean that the defendant will be released from custody. In many such cases, the defendant will be placed in some sort of institution for treatment.
2. The same behavior can give rise to both criminal liability and civil (tort) liability. The penalties imposed for the civil wrong will, of course, differ from those imposed in the criminal action, as will the parties initiating the suit.