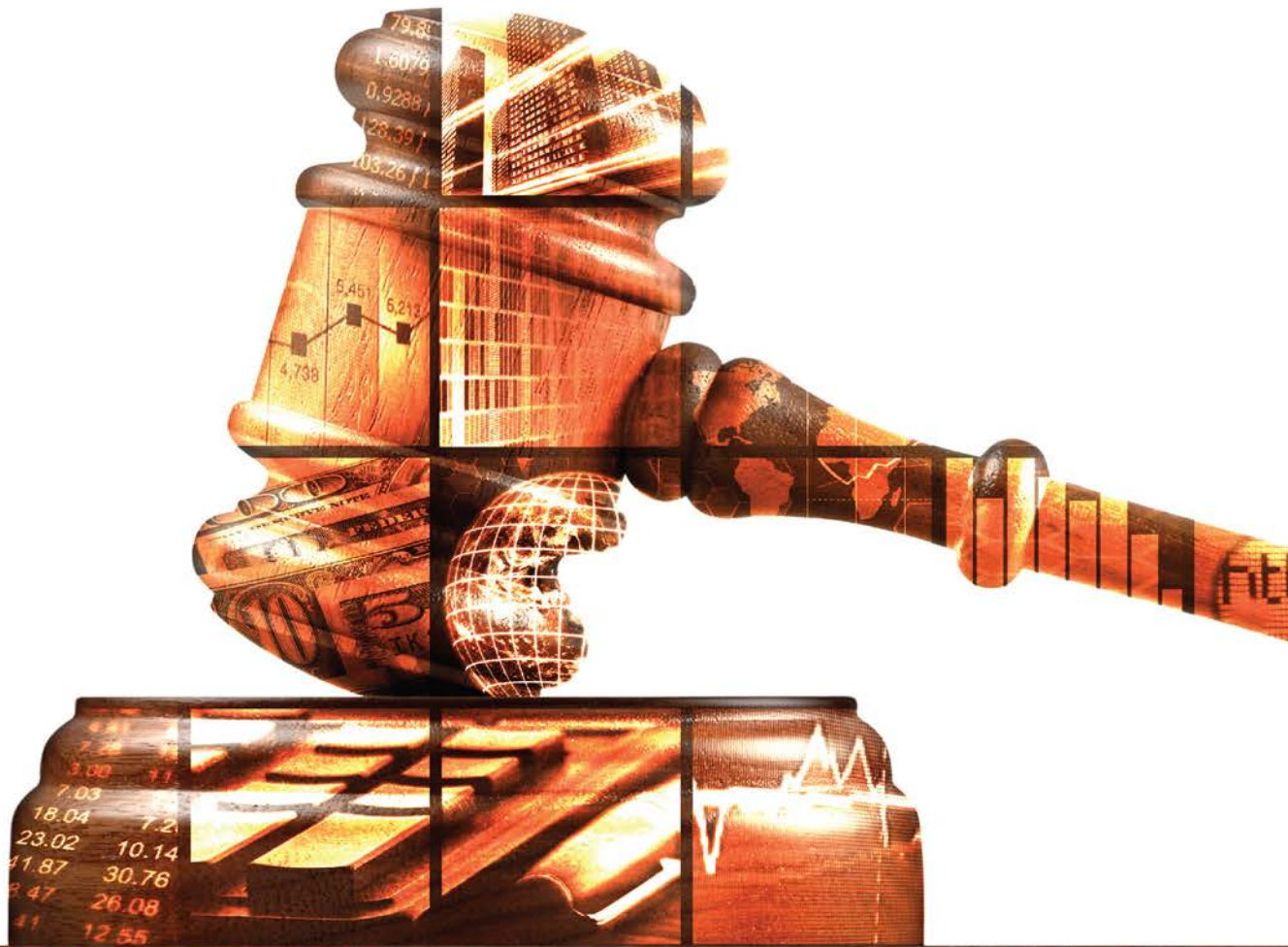


11th Edition

ROGER LEROY MILLER

Business Law Today

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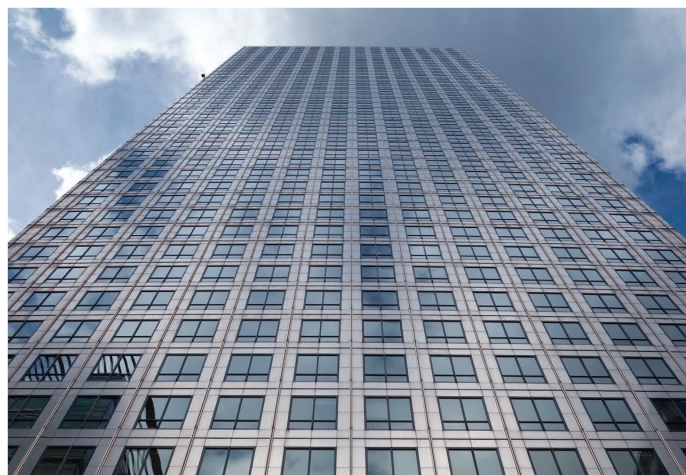
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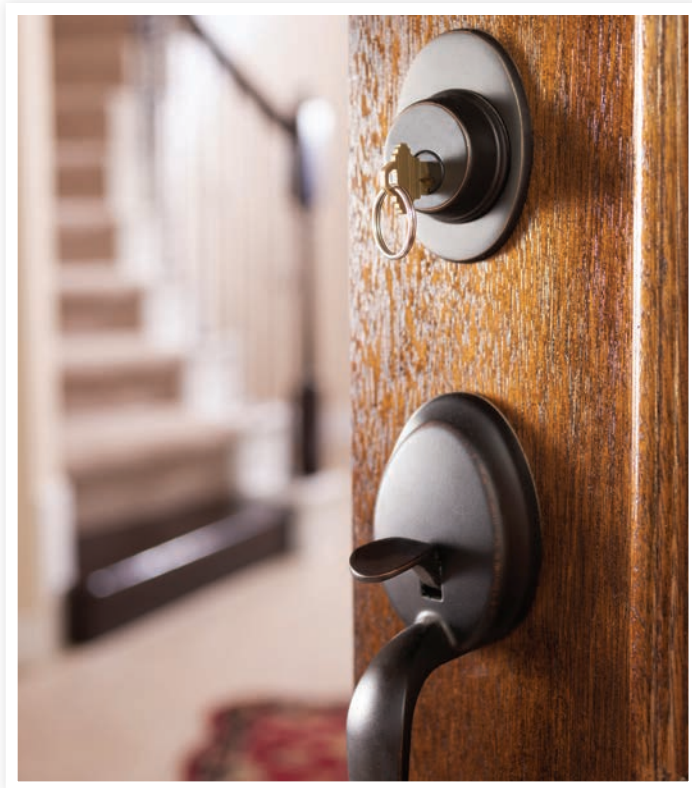
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The study of business and the legal environment has universal applicability. A student entering any field of business must have at least a passing understanding of business law in order to function in the real world. *Business Law Today*, Eleventh Edition, provides the information in an interesting and contemporary way. The Eleventh Edition continues its established tradition of being the most up-to-date text on the market.

Instructors have come to rely on the coverage, accuracy, and applicability of *Business Law Today*. This best-selling text engages your students, solidifies their understanding of legal concepts, and provides the best teaching tools available. I have spent a great deal of effort making this edition more contemporary, exciting, and visually appealing than ever before. Special pedagogical devices within the text focus on legal, ethical, global, and corporate issues, while addressing core curriculum requirements.

The Eleventh Edition incorporates the latest legal developments and United States Supreme Court decisions. It also includes more than fifty new features and seventy new cases, hundreds of new examples and case examples, new exhibits, learning objectives, margin definitions, and case problems.

New Chapter on Internet Law, Social Media, and Privacy

For the Eleventh Edition, I have included an entirely new chapter (Chapter 7) entitled **Internet Law, Social Media, and Privacy**. Social media have entered the mainstream and become a part of everyday life for many businesspersons. Throughout the text, I recognize this trend by incorporating the Internet and social media as they relate to the topics under discussion.

New Features

The Eleventh Edition of *Business Law Today* is filled with exciting new features including the following:

- Twenty-three **Adapting the Law to the Online Environment** features examine cutting-edge cyberlaw issues. Seventeen of these are new and cover topics such as Facebook poker, hacking, patent trolls, paying with smartphones, revenge porn, and social media.
- I have included twenty new **Ethical Issues** that focus on the ethical aspects of a topic being discussed in order to emphasize that ethics is an integral part of a business law course.
- I have also added six new **Beyond Our Borders** features (for a total of twenty-four) that focus on the global legal environment and illustrate how other nations deal with specific legal concepts being discussed.
- For this edition, I have created a new feature entitled **Managerial Strategy** that focuses on the management aspects of business law. There are ten of these new features throughout the text, covering such topics as the commercial use of drones, marriage equality, and the use of company e-mail systems to organize a union.
- Fourteen **Business Application** features and eight **Linking Business Law to [one of the six functional fields of business]** features are included at the end of selected chapters.

The *Business Applications* focus on practical considerations and offer checklists related to the chapter's contents, whereas the *Linking Business Law* features underscore how the law relates to other fields of business.

- Eighteen **Landmark in the Law** features discuss a landmark case, statute, or other legal development that has had a significant effect on business law.

New Cases and Case Problems

The Eleventh Edition of *Business Law Today* has new cases and case problems from 2015 and 2014 in every chapter. The new cases have been carefully selected to illustrate important points of law and be of high interest to students and instructors. I have made it a point to find recent cases that enhance learning and are simple enough for business law students to understand.

Certain cases and case problems have been carefully chosen as good teaching cases and are designated as **Spotlight Cases** and **Spotlight Case Problems**. Some examples include *Spotlight on Apple*, *Spotlight on Beer Labels*, *Spotlight on Nike*, and *Spotlight on the Seattle Mariners*. Instructors will find these **Spotlight** decisions useful to illustrate the legal concepts under discussion, and students will enjoy studying these cases because they involve interesting and memorable facts. Other cases have been chosen as **Classic Cases** because they establish a legal precedent in the particular area of law.

Each case concludes with a question, which may be called *Critical Thinking*, *What If the Facts Were Different?* or *Why Is This Case Important?* **Classic Cases** conclude with an *Impact of This Case on Today's Law* section that clarifies how the case has affected the legal environment. *Suggested answers to all case-ending questions can be found in the Solutions Manual for this text.*

Many New Highlighted and Numbered Case Examples

Many instructors use cases and examples to illustrate how the law applies to business. For this edition of *Business Law Today*, I have added more than one hundred new highlighted and numbered **Examples**, and more than one hundred new highlighted and consecutively numbered **Case Examples**. **Examples** illustrate how the law applies in a specific situation. **Case Examples** present the facts and issues of an actual case and then describe the court's decision and rationale. The numbered **Examples** and **Case Examples** features are integrated throughout the text to help students better understand how courts apply the principles in the real world.

Critical Thinking and Legal Reasoning Elements

Critical thinking questions conclude most of the features and cases in this text. There is also a **Debate This** question at the end of each chapter that requires students to think critically about the rationale underlying the law on a particular topic.

Answers to all critical thinking questions, as well as to the **Business Scenarios and Case Problems** at the end of every chapter, are presented in the *Solutions Manual* for the text. In addition, the answers to one case problem in each chapter, called the **Business Case Problem with Sample Answer**, appear in *Appendix E*.

The chapter-ending materials also include a separate section of questions that focus on critical thinking and writing. This section always includes a **Business Law Critical Thinking Group Assignment** and may also include the following:

- **Critical Legal Thinking** questions require students to think critically about some aspect of the law discussed in the chapter.
- **Business Law Writing** questions require students to compose a written response to a business-oriented critical-thinking question.
- **Case Analysis Questions** require students to read through a case excerpt in *Appendix G*, brief the case, and then answer a series of questions relating to the case.

Other Pedagogical Devices within Each Chapter

- **Learning Objectives** (questions at the beginning of each chapter and in the margin of the text provide a framework for the student).
- **Preventing Legal Disputes** (integrated text sections offer practical guidance on how businesspersons can avoid legal disputes and litigation in a particular area).
- **Chapter Outline** (an outline of the chapter's first-level headings).
- **Margin definitions.**
- **Highlighted and numbered Examples and Case Examples** (illustrate legal principles).
- **Quotations and Know This** (margin features).
- **Exhibits.**
- **Photographs (with critical thinking questions) and cartoons.**

Chapter-Ending Pedagogy

- **Reviewing . . . features** (in every chapter).
- **Debate This** (a statement or question at the end of the *Reviewing* feature).
- **Key Terms** (with appropriate page references).
- **Chapter Summary** (in table format).
- **Issue Spotters** (in every chapter with answers in *Appendix D*).
- **Learning Objectives Check** (The *Learning Objectives* questions are presented again to aid students in reviewing the chapter. For this edition, answers to the even-numbered questions for each chapter are provided in *Appendix E*.)
- **Business Scenarios and Case Problems** (Every chapter includes a *Business Case Problem with Sample Answer* answered in *Appendix F*; *A Question of Ethics*, and a *Business Law Critical Thinking Group Assignment*. Selected chapters include a *Spotlight Case Problem*.)

Unit-Ending Pedagogy

Each of the seven units in the Eleventh Edition of *Business Law Today* concludes with the following features (which are answered in the *Solutions Manual*):

- **Business Case Study with Dissenting Opinion**—This feature presents a court case that relates to a topic covered in the unit. It opens with an introductory section, discusses the case background and significance, and then provides excerpts from the court's majority opinion and from a dissenting opinion as well. The case study portion ends with *Questions for Analysis*—a series of questions that prompt the student to think critically about the legal, ethical, economic, international, or general business implications of the case.
- **Business Scenario**—This feature presents a hypothetical business situation and then asks a series of questions about how the law applies to various actions taken by the firm. To answer the questions, the student must apply the laws discussed throughout the unit.
- **Group Project**—The final portion of the unit-ending pedagogy is a *Group Project* that requires students to work together to formulate answers based on materials they learned in the previous chapters.

Supplements

Business Law Today, Eleventh Edition, provides a comprehensive supplements package designed to make the tasks of teaching and learning more enjoyable and efficient. The following supplements are available for instructors.

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

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- **Instructor's Manual.** Includes sections entitled “*Additional Cases Addressing This Issue*” at the end of selected case synopses.
- **Solutions Manual.** Provides answers to all questions presented in the text, including the *Learning Objectives*, the questions in each case and feature, the *Issue Spotters*, the *Business Scenarios and Case Problems*, *Critical Thinking and Writing Assignments*, and the unit-ending features. New for this edition, we also provide a set of *Alternative Case Problems* for every chapter.
- **Test Bank.** A comprehensive test bank contains multiple-choice, true/false, and short essay questions.
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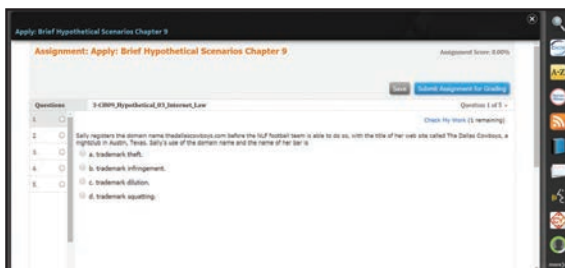
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-  eBook link back to the reading
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An eBook environment leads to more interaction with the material and a deeper learning of Business Law concepts. MindTap offers interactive cases, interactive exhibits, and video whiteboard explanations for the business law classroom.



Interactive Cases

Bring cases to life with an interactive environment that pulls students into the material. Instead of reading a boxed case feature, these interactive cases ask questions throughout, provide detailed answers, help guide students to a deeper understanding of the case, and enhance their legal reasoning skills. After reading the case, students are asked application questions to assess their understanding at a broader level.

Interactive Exhibits

Select static exhibits from within the narrative are now interactive. Students can enjoy manipulating figures and exhibits to better solidify their understanding of key concepts in the text. These activities are sure to engage students in the learning process and encourage greater focus and participation.

Video Whiteboard Explanations

Bring key legal concepts to life, literally, with short, entertaining animations. Video whiteboard explanations help students remember and learn key concepts with fun, real-world examples. Each being 3 minutes or less, these videos are an exciting way to help students see how they'd encounter these concepts in their own lives or in the near future when entering the business world.



BUSINESS LAW TODAY SERIES

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Since I began this project many years ago, numerous business law professors and users of *Business Law Today* have been kind enough to help me revise the book, including the following:

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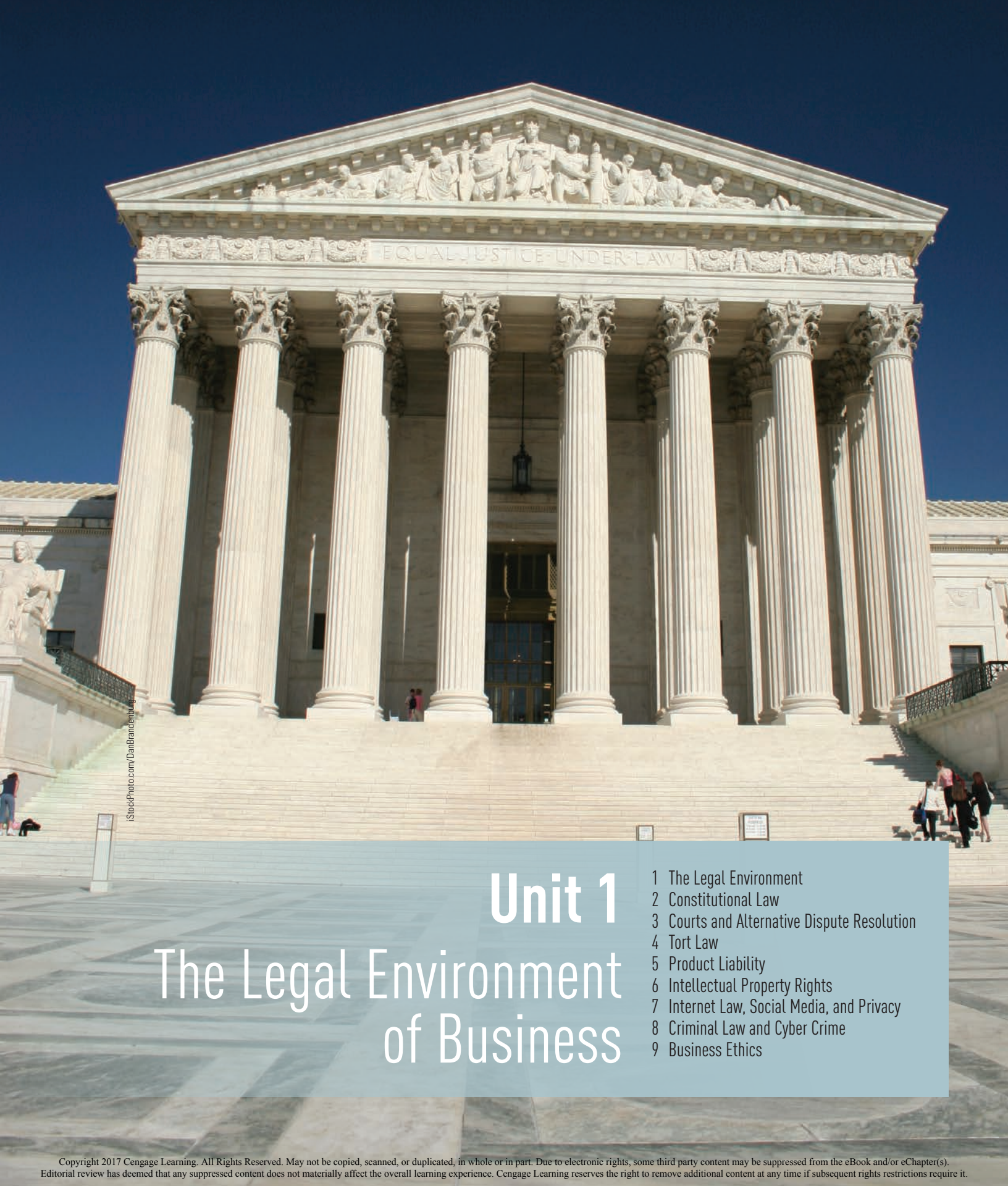
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Dedication

To John Allen,

The power of rational
analysis never weakens.

R.L.M.



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Unit 1

The Legal Environment of Business

- 1 The Legal Environment
- 2 Constitutional Law
- 3 Courts and Alternative Dispute Resolution
- 4 Tort Law
- 5 Product Liability
- 6 Intellectual Property Rights
- 7 Internet Law, Social Media, and Privacy
- 8 Criminal Law and Cyber Crime
- 9 Business Ethics

1

CHAPTER OUTLINE

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

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LEARNING OBJECTIVES

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

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

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

The Legal Environment

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

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

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

“Laws should be like clothes. They should be made to fit the people they are meant to serve.”

CLARENCE DARROW
1857–1938
(AMERICAN LAWYER)

1-1 Business Activities and the Legal Environment

Laws and government regulations affect almost all business activities—from hiring and firing decisions to workplace safety, the manufacturing and marketing of products, business financing, and more. To make good business decisions, businesspersons need to understand the laws and regulations governing these activities.

Realize also that in today's business world, simply being aware of what conduct can lead to legal **liability** is not enough. Businesspersons must develop critical thinking and legal reasoning skills so that they can evaluate how various laws might apply to a given situation and determine the best course of action. Businesspersons are also pressured to make ethical decisions. Thus, the study of business law necessarily involves an ethical dimension.

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

1-1a Many Different Laws May Affect a Single Business Transaction

As you will note, each chapter in this text covers a specific area of the law and shows how the legal rules in that area affect business activities. Although compartmentalizing the law in this fashion facilitates learning, it does not indicate the extent to which many different laws may apply to just one transaction. Exhibit 1-1 illustrates the various areas of the law that may influence business decision making.

EXAMPLE 1.1 When Mark Zuckerberg started Facebook as a Harvard student, he probably did not imagine all the legal challenges his company would face as a result of his business decisions.

- Shortly after Facebook was launched, others claimed that Zuckerberg had stolen their ideas for a social networking site. Their claims involved alleged theft of intellectual property (see Chapter 6), fraudulent misrepresentation (see Chapter 13), partnership law (see Chapter 27), and securities law (see Chapter 30). Facebook ultimately paid a significant amount (\$65 million) to settle those claims out of court.
- By 2015, Facebook had been sued repeatedly for violating users' privacy (such as by disseminating private information to third parties for commercial purposes—see Chapters 4 and 7). In 2012 and 2014, lawsuits were filed against Facebook for violating users' privacy (and federal laws) by tracking their Web site usage and by scanning private messages for purposes of data mining and user profiling. Also in 2014, a suit was filed in Europe against Facebook alleging violations of EU laws governing privacy and data use.
- Facebook's business decisions have come under scrutiny by federal regulators, such as the Federal Trade Commission (FTC) and the Securities and Exchange Commission (SEC). The company settled a complaint filed by the FTC alleging that Facebook failed to keep "friends" lists and other user information private. ■

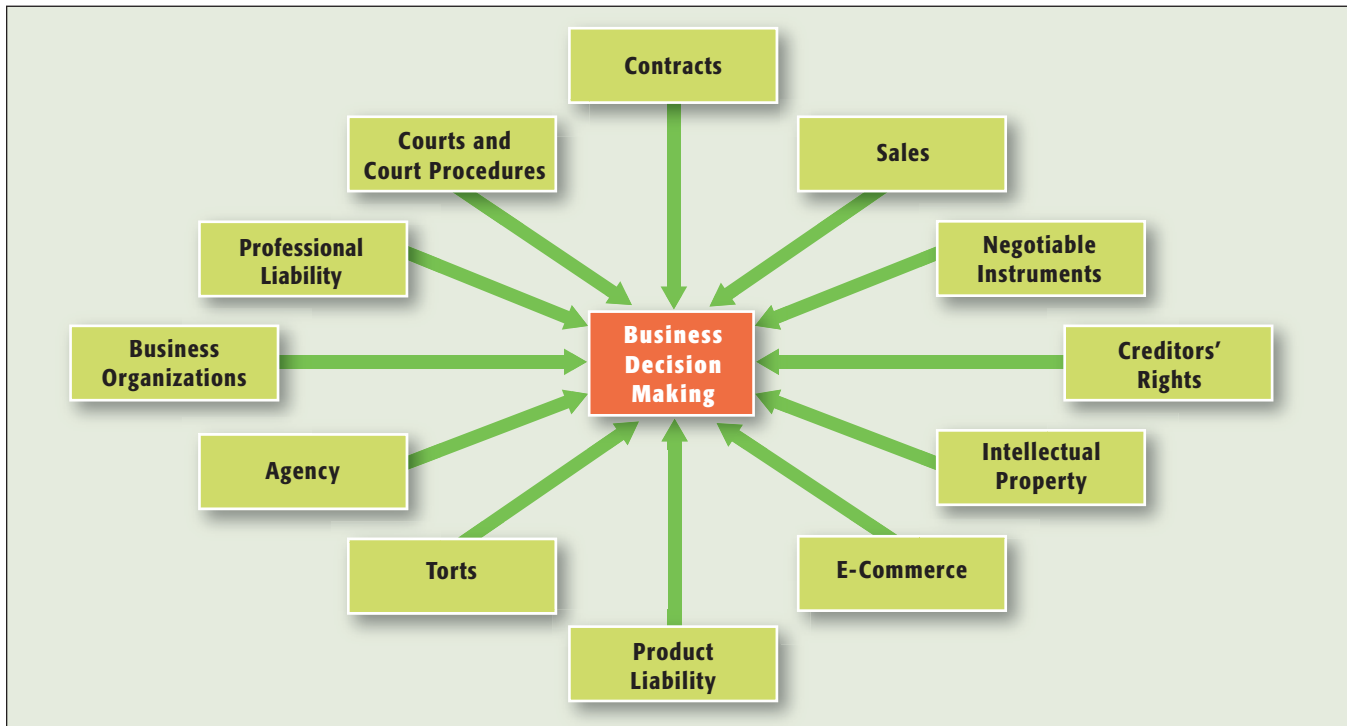


Mark Zuckerberg, founder of Facebook, has faced numerous legal challenges. These include privacy issues and the alleged theft of intellectual property. Can large Internet firms completely avoid such legal problems?

A key to avoiding business disputes is to think ahead when starting or running a business or entering a contract. Learn what you can about the laws pertaining to that specific enterprise or transaction. Have some idea of the legal ramifications of your business decisions, and seek the advice of a licensed attorney. When you need to choose an attorney, obtain recommendations from friends, relatives, or business associates who have had long-standing relationships with their attorneys.

**PREVENTING
LEGAL
DISPUTES**



Exhibit 1–1 Areas of the Law That May Affect Business Decision Making**1–1b** Linking Business Law to the Six Functional Fields of Business

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



Why is basic knowledge of business law and the legal environment so important today?

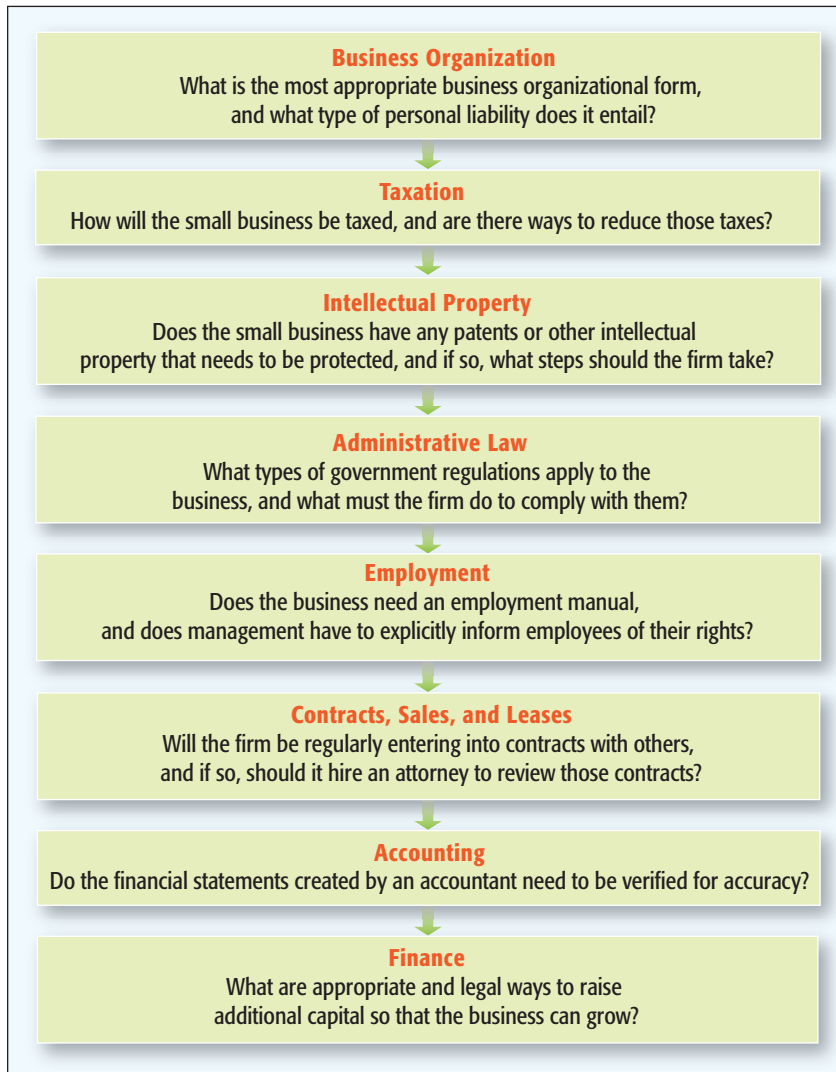
1. Corporate management.
2. Production and transportation.
3. Marketing.
4. Research and development.
5. Accounting and finance.
6. Human resource management.

One of our goals in this text is to show how legal concepts can be useful for managers and businesspersons, whether their activities focus on management, marketing, accounting, or some other field. To that end, numerous chapters, including this chapter, conclude with a special feature called “*Linking Business Law to* [one of the six functional fields of business].” The link between business law and accounting is so significant that we discuss it in detail in Chapter 33.

1–1c The Role of the Law in a Small Business

Some of you may end up working in a small business or even owning and running one. The small business owner/operator is the most general of managers. When you seek additional

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



financing, you become a finance manager. When you “go over the books” with your bookkeeper, you become an accountant. When you decide on a new advertising campaign, you are suddenly the marketing manager. When you hire employees and determine their salaries and benefits, you become a human resources manager.

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

1–2 Sources of American Law

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

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

LEARNING OBJECTIVE 1

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

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

We describe each of these important primary sources of law in the following pages. (See the appendix at the end of this chapter for a discussion of how to find statutes, regulations, and case law.)

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

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

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

1-2a Constitutional Law

The federal government and the states have written constitutions that set forth the general organization, powers, and limits of their respective governments. **Constitutional law**, which deals with the fundamental principles by which the government exercises its authority, is the law as expressed in these constitutions.

The U.S. Constitution is the basis of all law in the United States. It provides a framework for statutes and regulations, and thus is the supreme law of the land. A law in violation of the U.S. Constitution, if challenged, will be declared unconstitutional and will not be enforced, no matter what its source. Because of its paramount importance in the American legal system, we discuss the U.S. Constitution at length in Chapter 2 and present its complete text in Appendix B.

The Tenth Amendment to the U.S. Constitution reserves to the states all powers not granted to the federal government. Each state in the union has its own constitution. Unless it conflicts with the U.S. Constitution or a federal law, a state constitution is supreme within that state's borders.

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

1-2b Statutory Law

Laws enacted by legislative bodies at any level of government, such as the statutes passed by Congress or by state legislatures, make up the body of law generally referred to as **statutory law**. When a legislature passes a statute, that statute ultimately is included in the federal code of laws or the relevant state code of laws.

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

Whenever a particular statute is mentioned in this text, we usually provide a footnote showing its **citation** (a reference to a publication in which a legal authority—such as a statute or a court decision—or other source can be found). In the appendix following this chapter, we explain how you can use these citations to find statutory law.

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

Statutory law also includes local **ordinances**—regulations passed by municipal or county governing units to deal with matters not covered by federal or state law. Ordinances commonly have to do with city or county land use (zoning ordinances), building and safety codes, and other matters affecting only the local governing unit.

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

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

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

The Uniform Commercial Code (UCC) One of the most important uniform acts is the Uniform Commercial Code (UCC), which was created through the joint efforts of the NCCUSL and the American Law Institute.¹ The UCC was first issued in 1952 and has been adopted in all fifty states,² the District of Columbia, and the Virgin Islands.

The UCC facilitates commerce among the states by providing a uniform, yet flexible, set of rules governing commercial transactions. Because of its importance in the area of commercial law, we cite the UCC frequently in this text. We also present excerpts of the UCC in Appendix C. From time to time, the NCCUSL revises the articles contained in the UCC and submits the revised versions to the states for adoption.

1-2c Administrative Law

Another important source of American law is **administrative law**, which consists of the rules, orders, and decisions of administrative agencies. An **administrative agency** is a federal, state, or local government agency established to perform a specific function.

Rules issued by various administrative agencies affect almost every aspect of a business's operations. Regulations govern a business's capital structure and financing, its hiring and firing procedures, its relations with employees and unions, and the way it manufactures and markets its products. (See the *Linking Business Law to Management* feature at the end of this chapter.)

Federal Agencies At the national level, numerous *executive agencies* exist within the cabinet departments of the executive branch. The Food and Drug Administration, for example, is an agency within the U.S. Department of Health and Human Services. Executive agencies are subject to the authority of the president, who has the power to appoint and remove their officers.

There are also major *independent regulatory agencies* at the federal level, including the Federal Trade Commission, the Securities and Exchange Commission, and the Federal Communications Commission. The president's power is less pronounced in regard to independent agencies, whose officers serve for fixed terms and cannot be removed without just cause.

State and Local Agencies There are administrative agencies at the state and local levels as well. Commonly, a state agency (such as a state pollution-control agency) is created as a parallel to a federal agency (such as the Environmental Protection Agency).

Just as federal statutes take precedence over conflicting state statutes, so do federal agency regulations take precedence over conflicting state regulations. Because the rules of state and local agencies vary widely, we focus here exclusively on federal administrative law.

Agency Creation Because Congress cannot possibly oversee the actual implementation of all the laws it enacts, it delegates such tasks to agencies. Congress creates an administrative

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

Administrative Law The body of law created by administrative agencies in order to carry out their duties and responsibilities.

Administrative Agency A federal or state government agency created by the legislature to perform a specific function, such as to make and enforce rules pertaining to the environment.

“Laws and institutions, like clocks, must occasionally be cleaned, wound up, and set to true time.”

HENRY WARD BEECHER
1813–1887
(AMERICAN CLERGYMAN
AND ABOLITIONIST)

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

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



iStockPhoto.com/TerryJ

Which federal agency oversees worker safety?

Enabling Legislation A statute enacted by Congress that authorizes the creation of an administrative agency and specifies the name, composition, purpose, and powers of the agency being created.

Adjudicate To render a judicial decision. Adjudication is the trial-like proceeding in which an administrative law judge hears and resolves disputes involving an administrative agency's regulations.

Administrative Process The procedure used by administrative agencies in administering the law.

Rulemaking The process by which an administrative agency formally adopts a new regulation or amends an old one.

Legislative Rule An administrative agency rule that carries the same weight as a congressionally enacted statute.

Interpretive Rule A nonbinding rule or policy statement issued by an administrative agency that explains how it interprets and intends to apply the statutes it enforces.

agency by enacting **enabling legislation**, which specifies the name, composition, purpose, and powers of the agency being created.

EXAMPLE 1.2 The Federal Trade Commission (FTC) was created in 1914 by the Federal Trade Commission Act.³ This act prohibits unfair and deceptive trade practices. It also describes the procedures the agency must follow to charge persons or organizations with violations of the act, and it provides for judicial review (review by the courts) of agency orders.

Other portions of the act grant the agency powers to “make rules and regulations for the purpose of carrying out the Act,” and to conduct investigations of business practices. In addition, the FTC can obtain reports from interstate corporations concerning their business practices, investigate possible violations of the act, publish findings of its investigations, and recommend new legislation. The act also empowers the FTC to hold trial-like hearings and to **adjudicate** (resolve judicially) certain kinds of disputes involving its regulations. ■

Note that the powers granted to the FTC incorporate functions associated with the legislative branch of government (rulemaking), the executive branch (investigation and enforcement), and the judicial branch (adjudication). Taken together, these functions constitute the **administrative process**, which is the administration

of law by administrative agencies. The administrative process involves rulemaking, enforcement, and adjudication.

Rulemaking A major function of an administrative agency is **rulemaking**—formulating new regulations. When Congress enacts an agency's enabling legislation, it confers the power to make **legislative rules**, or substantive rules, which are legally binding on all businesses.

The Administrative Procedure Act (APA)⁴ imposes strict procedural requirements that agencies must follow in legislative rulemaking and other functions. **EXAMPLE 1.3** The Occupational Safety and Health Act authorized the Occupational Safety and Health Administration (OSHA) to develop and issue rules governing safety in the workplace. When OSHA wants to formulate rules regarding safety in the steel industry, it has to follow specific procedures outlined by the APA. ■

Legislative Rules. Legislative rulemaking under the APA typically involves the following three steps (referred to as *notice-and-comment rulemaking*).

1. *Notice of the proposed rulemaking.* The notice must be published in the *Federal Register*, a daily publication of the U.S. government.
2. *A comment period.* The agency must allow ample time for interested parties to comment in writing on the proposed rule. The agency takes these comments into consideration when drafting the final version of the regulation.
3. *The final rule.* Once the agency has drafted the final rule, it is published in the *Federal Register*. (See the appendix at the end of this chapter for an explanation of how to find agency regulations.)

Interpretive Rules. Administrative agencies also issue **interpretive rules** that are not legally binding but simply indicate how an agency plans to interpret and enforce its statutory authority. The APA does not apply to interpretive rulemaking. **EXAMPLE 1.4** The Equal Employment Opportunity Commission periodically issues interpretive rules indicating how it plans to interpret the provisions of certain statutes, such as the Americans with Disabilities Act. These informal rules provide enforcement guidelines for agency officials. ■

Enforcement and Investigation Agencies often enforce their own rules and have both investigatory and prosecutorial powers. Agencies investigate a wide range of activities, including coal mining, automobile manufacturing, and the industrial discharge of pollutants into the environment.

3. 15 U.S.C. Sections 45–58.

4. 5 U.S.C. Sections 551–706.

In an investigation, an agency can request that individuals or organizations hand over specified books, papers, electronic records, or other documents. In addition, agencies may conduct on-site inspections, although a search warrant is normally required for such inspections.⁵ Sometimes, a search of a home, an office, or a factory is the only means of obtaining evidence needed to prove a regulatory violation.

After investigating a suspected rule violation, an agency may decide to take action against an individual or a business. Most administrative actions are resolved through negotiated settlement at their initial stages without the need for formal adjudication. If a settlement cannot be reached, though, the agency may issue a formal complaint and proceed to adjudication.

Adjudication Agency adjudication involves a trial-like hearing before an **administrative law judge (ALJ)**. Hearing procedures vary widely from agency to agency. After the hearing, the ALJ renders a decision in the case. The ALJ can fine the charged party or prohibit the party from carrying on some specified activity.

Either the agency or the charged party may appeal the ALJ's decision to the commission or board that governs the agency. If the party fails to get relief there, appeal can be made to a federal court. Courts give significant weight (deference) to an agency's judgment and interpretation of its rules, though, and typically uphold the ALJ's decision unless it is unreasonable. If neither side appeals the case, the ALJ's decision becomes final.

Do administrative agencies exercise too much authority? Administrative agencies, such as the Federal Trade Commission, combine in a single governmental entity functions normally divided among the three branches of government. They create rules, conduct investigations, and prosecute and pass judgment on violators. Yet administrative agencies' powers often go unchecked by the other branches. Some businesspersons have suggested that it is unethical for agencies—which are not even mentioned in the U.S. Constitution—to wield so many powers.

Although agency rulemaking must comply with the requirements of the Administrative Procedure Act (APA), the act applies only to legislative, not interpretive, rulemaking. In addition, the APA is largely procedural and aimed at preventing arbitrariness. It does little to ensure that the rules passed by agencies are fair or correct—or even cost effective. On those rare occasions when an agency's ruling is challenged and later reviewed by a court, the court cannot reverse the agency's decision unless the agency exceeded its authority or acted arbitrarily. Courts typically are reluctant to second-guess an agency's rules, interpretations, and decisions. Moreover, once an agency has final regulations in place, it is difficult to revoke or alter them.

Administrative Law Judge (ALJ) One who presides over an administrative agency hearing and has the power to administer oaths, take testimony, rule on questions of evidence, and make determinations of fact.

ETHICAL ISSUE



1-2d Case Law and Common Law Doctrines

The rules of law announced in court decisions constitute another basic source of American law. These rules of law include *interpretations* of constitutional provisions, of statutes enacted by legislatures, and of regulations created by administrative agencies. Today, this body of judge-made law is referred to as **case law**. Case law—the doctrines and principles announced in cases—governs all areas not covered by statutory law or administrative law and is part of our common law tradition. We look at the origins and characteristics of the common law tradition in some detail in the pages that follow.

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

1-3 Common Law Tradition

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

LEARNING OBJECTIVE 2

What is the common law tradition?

⁵ In some heavily regulated industries, such as the sale of firearms or liquor, agencies can conduct searches without obtaining a warrant.