

Starting a Business

In This Unit You Will Find:

Chapter 16
Forms of Business

Chapter 17
Operating a Corporation

Chapter 18
Business and Regulations

Chapter 19
Cyberlaw and E-Commerce

.....▶
Be Your Own Boss An alternative to going to work for someone else is starting your own business. *What are the three main forms of business ownership?*



Thematic Project Preview

Protecting Social and Environmental Concerns

As you read this unit, use this checklist to prepare for the unit project:

- ✓ List the environmental laws the government requires businesses to obey.
- ✓ Differentiate between safe and unsafe business practices as they relate to environmental laws.
- ✓ Explain how laws protect the environment and society in general.
- ✓ Determine the impact environmental laws have on business and society.

Legal Portfolio When you complete the Unit Thematic project, you will have a guide of environmental protection law for your portfolio.



Entrepreneurship

Owning and operating your own business can be very exciting, and there are lots of federal agencies that can help to get you started. Log on to glencoe.com to find federal agencies that offer guidance to starting or buying a new business. Then, continue working on your WebQuest as you study Unit 6.



Find Unit 6 study tools such as **Graphic Organizers**, **Academic Skills Review**, and **Practice Tests** at glencoe.com.

Ask

STANDARD & POOR'S

Get Listed on a Stock Market

Q: How do shares of a company get traded on the New York Stock Exchange?

A: Suppose you run a successful company and want to start selling shares on the New York Stock Exchange (NYSE). The first thing you need to do is hire an investment banker to arrange an initial public offering (IPO), which is a company's first sale of stock to the public. After the government approves the sale, the stock is made available to investors. Then, the stock can be traded on a stock market. For your company's stock to be traded or listed on the NYSE, you must apply with the NYSE, which will review your company to determine if it meets certain requirements (such as having a minimum number of shareholders, a minimum market value, follows basic reporting procedures, has a board of directors, and has in place appropriate corporate governance rules). The NYSE's listing application and requirements are available online.

Language Arts/Reading Standard & Poor's is one of the world's main providers of credit ratings and financial-market indices. Go to glencoe.com and read more about the stock market and how it works.

Forms of Business

BusinessWeek News

A Sizzling Family Food Fight*By Ronald Grover*

Quintessential California drive-in chain In-N-Out Burger has built a cult-like following among fast-food gourmards for its juicy grilled patties and “secret” menu items. But the beef these days at the family-owned, 200-plus restaurant outfit isn’t its trademark Double-Doubles but allegations that the chain’s 23-year-old heir, Lynsi Martinez, and others are plotting to force out her 86-year-old grandmother, the wife of the founder. It’s a soap opera that includes allegations of fraud and a backroom power play. Matriarch Ester Snyder is alleged in court documents to have told ex-employee Richard Boyd that they “only want me dead.”

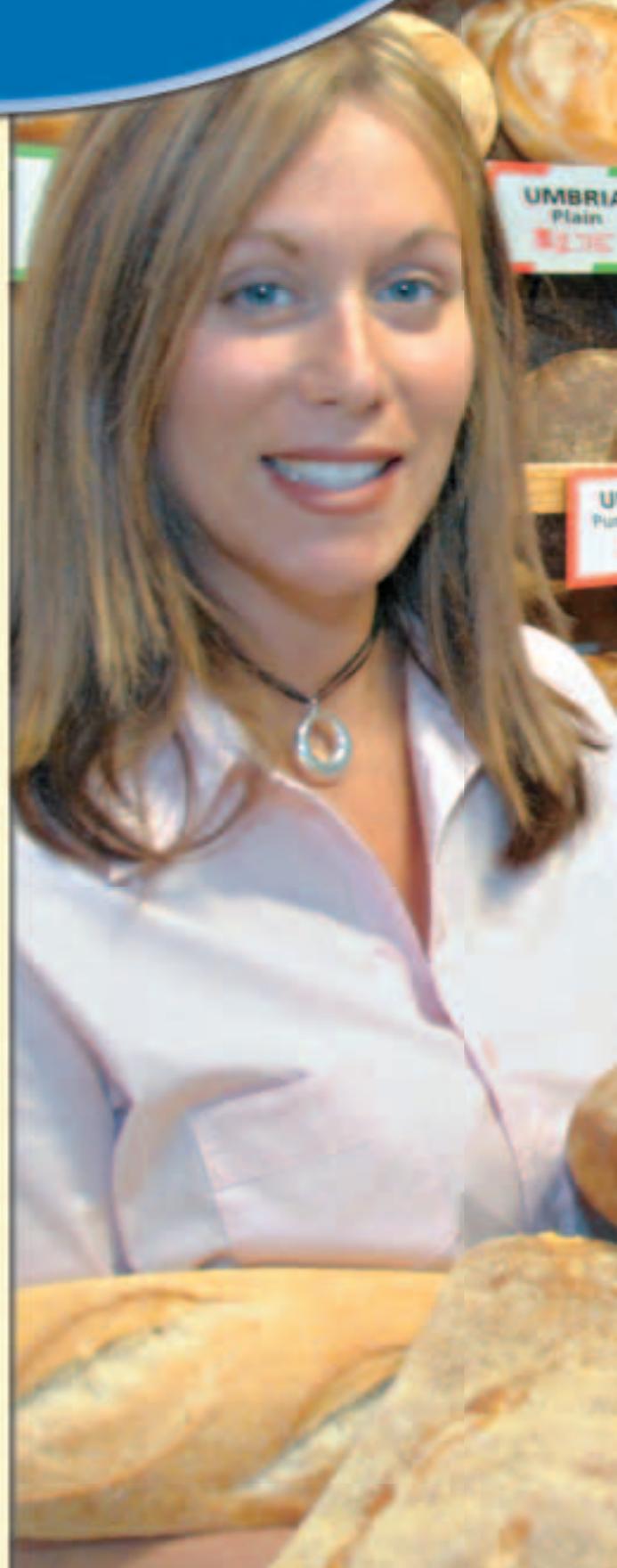
The saga is playing out in a state court in Los Angeles where Boyd, a former In-N-Out real estate vice-president and board member, claims Martinez and her stepsister’s husband, Vice-President Mark Taylor, maneuvered to oust Boyd and take over the chain.

Flex Your Reading

Efficient critical reading involves being flexible with speed and comprehension. There are several ways of reading critically, and you need to fit a reading style to your needs and to the material.



Go to glencoe.com for Flex Your Reading activities, more information on reading strategies for this chapter, and guided practice in reading about family-owned businesses and partnerships.





Paying Your Dues Running a business comes with responsibilities. *Who pays the taxes, and who is liable for debts in a partnership?*

Sole Proprietorships and Partnerships

What You'll Learn

- ◆ Describe how to form and run a sole proprietorship.
- ◆ List the advantages and disadvantages of a sole proprietorship.
- ◆ Explain the rights and responsibilities of partners.
- ◆ Identify the different types of partners.
- ◆ Explain how a partnership can be terminated.

Why It's Important

Knowing the differences between sole proprietorships and partnerships will help you decide which form of business is best for you.

Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

Social Studies (NCSS 7)
Study how people organize for the production, distribution, and consumption of goods and services.

English Language Arts (NCTE 3) Apply a wide range of strategies to comprehend, interpret, evaluate, and appreciate texts.

Reading Guide



Before You Read

Connect Have you ever tried to start your own business on the Internet or at school?

Focus on Ideas

Sole proprietorships and partnerships both have advantages and disadvantages.

Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to glencoe.com to find graphic organizers and tips on how to improve your note-taking skills.

	Sole Proprietorships	Partnerships
Advantages	_____ _____ _____	_____ _____ _____
Disadvantages	_____ _____ _____	_____ _____ _____



Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- sole proprietorship
- unlimited liability
- partnership
- joint liability
- dissolution
- dissociation
- limited partnership
- limited liability partnership (LLP)



Academic Vocabulary

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- perpetual
- dormant
- incompetence

Sole Proprietorships

If you start a babysitting service, what kind of business is it?

A **sole proprietorship** is a form of business that is **owned and operated by one person**. A sole proprietorship is the most common way to do business. It is also the easiest type of business to form. Common sole proprietorships are repair shops, small retail stores, and service organizations.

Advantages of a Sole Proprietorship

Sole proprietorships offer specific advantages. These advantages include ease of creation, total control, retention of profits, and one-time taxation of profits.

Ease of Formation There are only a few requirements to meet in forming a sole proprietorship. Some businesses, such as restaurants and motels, must get licenses to operate legally. Other businesses, such as barbers or plumbers, must have occupational licenses and liability insurance. Zoning ordinances which forbid the operation of businesses in residential neighborhoods can restrict the location of a sole proprietorship. If an owner plans to hire employees, he or she must obtain an employer identification number (EIN) from the Internal Revenue Service for tax purposes.

Total Control and Retention of Profits In a sole proprietorship, the owner has complete control of the business and makes all of the decisions. The proprietor also gets to keep all of the profits from the business. Proprietors, however, must still pay taxes on the profits that they make.

One-Time Taxation of Profits Sole proprietorships do not pay taxes as a business. The sole proprietor pays taxes based on his or her income. A full-time sole proprietor will pay income



 **Family Business** Many sole proprietorships are family-owned businesses passed down from one generation to the next. *About what percentage of businesses in the U.S. are sole proprietorships?*

taxes on all profits made in a year. If the business is a part-time venture, those profits plus all other income made by the sole proprietor are taxed.

Disadvantages of a Sole Proprietorship

Sole proprietorships have several disadvantages. These disadvantages include limited capital, unlimited liability, and limited lifetime.

Limited Capital An obvious shortcoming of a sole proprietorship is the fact that the business owner has limited access to capital. All money used to finance the business must come from the proprietor's savings or income, or from loans obtained by the proprietor.

Unlimited Liability Perhaps the biggest disadvantage of a sole proprietorship is unlimited liability. **Unlimited liability is a legal duty placed on a business owner that requires the owner to be responsible for all losses experienced by the business.** Even the personal property of a sole proprietor may be used to satisfy the debts of the business.

Limited Lifetime Unlike a corporation, which has **perpetual** existence, a sole proprietorship lasts only as long as the proprietor. When the proprietor dies or chooses to sell or close the business, the business ceases to exist.

General Partnerships

How can you start a business with some friends?

Partnership law is in a developmental stage. A new law called the Revised Uniform Partnership Act (RUPA) has been adopted by many states. However, many states still operate under the traditional Uniform Partnership Act (UPA). This chapter will discuss both laws and point out where the two acts are the same and where they differ. You will need to find out which partnership act your state follows.

Elements of a Partnership

A **partnership**, according to the RUPA, is an association of two or more persons to carry on as co-owners of a business for profit. This definition differs slightly from the definition in UPA, but both emphasize two essential elements:

- A partnership must involve at least two persons.
- A partnership must carry on a business for profit.

Advantages and Disadvantages of a Partnership

Partnerships have several advantages over sole proprietorships. More capital and credit is usually available to a partnership. The burden of all the work does not fall on one person. A partner does not have sole responsibility for any losses suffered.

A disadvantage to a partnership is that the partners must share the profits. Also, because all partners have a voice in running the

Vocabulary You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

business, bickering can cause problems. The biggest disadvantage is that the partners share in the liability. Each partner is responsible for the other partners' actions taken within the scope of the partnership. Partners share in two types of liability.

Contract Liability Partners have joint liability when a contract is made for the partnership. **Joint liability is liability shared by two or more people.** Every partner must be included in a breach of contract case against the partnership.

Tort Liability In a tort case against the partnership, partners have joint and several liability. Joint and several liability means that a tort case can be brought against all of the partners, one of the partners, or any combination of the partners. The partners named in the tort case must pay if they lose in court. If one partner settles the case on his or her own behalf, the rest of the partners are not released from the lawsuit. However, the partner who is actually responsible for the tort may be forced to pay the other partners back.



Forming a General Partnership

A general partnership can be formed in one of two ways: by agreement and by proof of existence.

Partnership by Agreement Forming a general partnership by agreement requires the valid assent of all parties. Such an agreement is usually express and may be written or oral. However, under the Statute of Frauds, if a partnership is to last more than a year, it must be in writing. A partnership formed to sell, buy, or lease real property must also be in writing. The partnership agreement is called the Articles of Partnership.

A partnership that is set to last for a certain period of time or to do a certain job is a term partnership. Partners cannot leave a term partnership until the time has passed or the job is done. A partnership at will means that the partners are free to leave the partnership any time that they want to. No liability follows a partner who leaves such a partnership.

Partnership by Proof of Existence A partnership can also be formed by the way two or more people conduct business together, regardless of what they label the business. For example, if two or more people share the profits of a business venture, it is likely that a partnership exists. This is called a partnership by proof of existence. Both the RUPA and the UPA provide a list of characteristics to show whether a partnership actually exists.

 **Partnerships** An advantage a partnership has over a sole proprietorship is the burden of all the work does not fall on one person. *What is the main disadvantage of a partnership?*

Types of Partners

The law recognizes five types of partners who may be involved in a partnership: general, secret, silent, dormant, and limited. They differ according to how active a role they play in the partnership, whether their role is known to the public, and the amount of liability they have.

General Partner A general partner plays an active role in the management of the partnership and is known to the public. Every partnership must have at least one general partner. A general partner has unlimited liability.

Secret Partner A secret partner is a general partner who has an active role in the management of the partnership, but whose connection with the partnership is kept a secret. A secret partner has unlimited liability.

Silent Partner A silent partner does not play an active role, but is known to the public. A silent partner has unlimited liability.



Case Study – Roach v. Mead



Critical Thinking *Is one partner liable for the actions of the other partner?*



Note key facts in the text below and look up words you do not understand. Restate difficult ideas in your own words. Go back and reread the text quickly to make sure you did not miss any important detail. Now, you are ready to formulate an opinion.

Bad Advice? On November 1, 1979, David Berentson and Kenneth Mead formed a law partnership. One of their clients was William Roach. Mr. Roach owned a meter repair business. Mr. Berentson and Mr. Mead assisted Mr. Roach with legal issues arising from his business, including preparing his tax returns. They also represented him on various traffic infractions.

In June 1980, Mr. Roach sold his business for \$50,000. In November 1980, he consulted with Mr. Mead about how to invest \$20,000 of the profits. At that time, Mr. Mead needed a loan. He offered to take the money from Mr. Roach and pay him 15% interest in return. Mr. Mead drafted a promissory note that stated Mr. Mead would pay Mr. Roach \$23,000 on or before November 25, 1982. Mr. Mead never paid Mr. Roach the \$23,000, and Mr. Mead eventually declared bankruptcy.

Mr. Roach then sued Mr. Berentson. Mr. Roach argued that since Mr. Berentson was Mr. Mead's partner, Mr. Berentson could be held liable for Mr. Mead's actions. Mr. Roach argued that Mr. Mead had negligently given him bad legal advice by: not advising Mr. Roach to consult with an uninterested attorney when Mr. Mead took the \$20,000; and not advising him that a 15% interest rate was unenforceable because it would be usury.

Roach v. Mead, 722 P.2d 1229 (Ore. 1986)



Go to glencoe.com for more case study practice.

Dormant Partner A **dormant** partner is a general partner who takes no active part in the management of the firm and whose connection with the firm is kept secret. A dormant partner, however, still has unlimited liability.

Limited Partner A limited partner is one whose liability does not extend beyond his or her investment. Limited partnerships are discussed later in this section.

Partnership Rights

Partners share certain rights. These rights include the right to use the property, the right to manage the firm, and the right to share in the profits.

Property Rights of the Partners It is important to distinguish between property that belongs to the partnership and property that belongs to individual partners. Property contributed directly to the partnership when the partnership is created is partnership property.

The UPA and the RUPA differ on the right to use property. According to the RUPA: “A partner is not co-owner of partnership property and has no interest in partnership property which can be transferred either voluntarily or involuntarily.” Partners are permitted to use partnership property, but the right to use the property is limited to partnership purposes. In contrast, the UPA states that partners are co-owners of all real and personal property included in the partnership. This co-ownership of property, called tenancy in partnership by the UPA, creates certain limitations. For example, a partner cannot personally transfer ownership of property. Also, the property cannot be taken by a partner’s personal creditors.

Right to Manage the Firm Unless otherwise stated in the partnership agreement, each partner has an equal voice in managing the firm. Each partner can bind the partnership on any matter within the scope of its business affairs. In a disagreement, the decision of the majority is final. If there is an even number of partners and the vote is split, no decision can be made. If a deadlock persists, the partners might consider ending their partnership.

Right to Share in the Profits Unless otherwise stated in the partnership agreement, partners share equally in the profits, regardless of their initial capital contribution or the time devoted by each partner to the business. This right can be assigned to others. Partners also have a right to reimbursement for any money they personally spend on behalf of the partnership.

Enforcement Rights Under the UPA, partners had three enforcement rights: the right to inspect the firm’s books; the right to an account; and the right to dissolve the partnership. The RUPA added a fourth right: a partner has the right to sue a partner or the partnership itself to enforce his or her rights as stated in the partnership agreement or in the RUPA.



Reading Check

Analyze What is the difference between limited and unlimited liability?

Partnership Duties

The RUPA states that partners have three duties: loyalty, obedience, and due care.

The Duty of Loyalty Loyalty is always the first duty because a partnership is a fiduciary relationship, or a relationship based on trust. The RUPA emphasizes loyalty more strongly than the UPA did. According to the RUPA, each partner must:

- tell the partnership about property, profits, or benefits that any partner receives for using partnership property
- avoid dealing with individuals who have any interest that somehow hurts the partnership
- avoid competing with the partnership

A partner does keep the right to look after his or her own interests before the partnership is actually formed.

The Duty of Obedience Once the partners have written the articles of partnership, the partners have the duty to obey those articles. The partners must follow the decisions made by the partners. If a partner disobeys the articles of partnership or partnership decisions, then that partner will be liable for any loss that results.

The Duty of Due Care The duty of due care means that a partner must work to the best of his or her ability, based on his or her talents, education, and experience, when that partner is working on partnership business.

Terminating a Partnership

A partnership may end in a number of ways. A partner may die, go bankrupt, become incapacitated, be expelled by the other partners, or simply wish to leave a partnership. Partners can leave a partnership any time they want to. However, they do not always have the legal right to do so. Whether a partner has the right to leave may depend on whether the partnership is a term partnership or a partnership at will. If the partner does not have the right, he or she may have to pay damages to the other partners.

Dissolution of a Partnership A **dissolution** is when a **partnership (or any legal entity) breaks up**. Dissolution is not the same as the termination of the business. Dissolution occurs at the moment one partner ceases to be associated with the firm. There are three ways dissolution can happen:

- **By the acts of the partners.** This arises when one partner decides to leave and the other partners agree; when the original agreement had a set time period or goal that has been reached; or when the majority of partners vote to expel a partner.
- **By operation of law.** This arises in cases of bankruptcy or death of a partner.

- **By a court order.** This arises when partners obtain a court order to end the partnership because of misconduct, **incompetence**, or incapacity of a partner.

Winding up a Partnership The dissolution of a partnership does not cause it to end immediately. The partnership must close down its business operations, called a winding up. During the winding up period, the business does not continue. The partners perform an accounting of the old firm's affairs, sell the partnership property, pay creditors, and divide what remains of the profits.

Dissociation of a Partnership Dissolution does not necessarily end a partnership. Other partners may want to continue the business. If so, a new agreement must be drawn up regarding the conduct of a new firm. There must be an accounting of the old firm's affairs and new financial arrangements must be made regarding the new firm. Public notice must be given to relieve retiring partners from liability for any new debts.

Under the UPA, a partnership ends automatically any time a partner leaves the partnership. The RUPA changed the law by adding a way for a partnership to continue even after a partner leaves, called a dissociation. **A dissociation, according to the RUPA, is when a partner is no longer associated with the firm.** A dissociation allows the business to continue doing business with the remaining partners or with a new partner.



Courdy v. Paycom Billing Services, Inc.

2006 WL 847212 (Cal. Ct. App. 2006)

On July 1, 1997, Edward Courdy and Paycom Billing Services, Inc. (Paycom) entered into a general partnership called Internet Commerce Solutions (ICS). According to the written partnership agreement, the purpose of the partnership was “to engage in the business of Internet Commerce.” ICS provided check processing for Internet merchants by taking check information from the merchants and relaying that information to banks. After experiencing problems with the online check processing, Paycom decided to end the partnership. It gave notice on August 12, 1998, that it wished to dissolve the partnership. Six days later, Paycom then notified ICS's clients that it would be providing a new check-processing service plus a credit-card processing service. Courdy sued Paycom on a number of counts, including fraud, arguing that Paycom stole Internet Commerce from ICS when it dissolved the partnership.

Ruling and Resolution

The California Court of Appeals held that the partnership was at will; that is, it could be dissolved at any time. Courdy did not have a right to any damages from profits gained by Paycom from former ICS clients.

Critical Thinking Are partnerships at will a good thing?

 **Limited Partnerships** Limited partners have no right to manage a partnership, but have only limited liability if the partnership is sued or goes bankrupt. *What happens to a limited partner who gets involved in running a partnership?*



Other Types of Partnerships

The business world constantly adjusts to the changing needs of the marketplace. As a result, several types of partnerships that differ from general partnerships are now legally recognized.

Limited Partnerships Limited partnerships are controlled by provisions of the Revised Uniform Limited Partnership Act (RULPA). A **limited partnership is a partnership formed by two or more persons, with one or more general partners and one or more limited partners.** The general partners of a limited partnership have the same types of duties as a general partner in a general partnership. Limited partners are investors who have no right to manage the partnership.

Limited partnerships must meet stricter formalities than general partnerships. The names of the limited partners cannot appear in the partnership name. The partners must file a certificate of limited partnership with the appropriate state or county office. The business name must indicate that it is a limited partnership. This is to warn third parties that some partners have only limited liability.

In terms of liability, the limited partnership falls between the general partnership, in which all owners have unlimited liability, and the corporation, in which all owners have limited liability. When a limited partnership ends, the assets are first distributed to creditors of the firm, and then to the partners.

Registered Limited Liability Partnerships A **limited liability partnership (LLP)** is a registered partnership in which each partner is not liable for the acts of the other partners. Partners can escape joint and several liability for the torts, wrongful acts, negligence, or misconduct of other partners by registering with the appropriate state office. The registration statement usually includes the following information:

- the name of the partnership
- the purpose of the partnership
- the number of partners in the partnership
- a statement of the intent to form an LLP
- the address of the partnership's main place of business
- the name and address of a statutory agent for service of process

All the partners, or at least the partners holding a majority interest in the partnership, must file the statement. The registration statement must be updated annually. LLPs are taxed in the same way as general partnerships.

Partnership-Type Business Organizations

Other partnership-type business organizations include limited partnership associations and joint ventures.

Limited Partnership Associations A limited partnership association is like a corporation in that it is considered an entity having an existence all its own. The participants own shares in the association and can convey their shares to another individual as long as the other participants vote to accept the new individual. The participants can lose only the amount of their initial investment. Not every state has made statutory provisions for limited partnership associations.

Joint Ventures A joint venture is a business enterprise in which two or more participants combine in order to complete a single task. There is no ongoing relationship in a joint venture, unlike a partnership.



After You Read

Summarize What are the different types of partners?

SECTION 16.1 ASSESSMENT

Self Check

1. What is a sole proprietorship?
2. What is a partnership?
3. What is a limited partnership?

Academic Connection

English Language

Arts Get together with three other members of the class to form a partnership. Decide what kind of business you want to go into, what kind of

partnership to create, and how much each partner will invest. Then decide how the duties of managing the business might be divided, what kind of partner each person will be, and how the profits will be split. For example, one partner might want to be a secret partner and another a dormant partner. One partner might want to focus on running the day-to-day operations of the business and the other focus on bringing in

business. Write up a brief partnership agreement laying out what you decide.

Critical Thinking

Extent of Liability

Suppose you are running a sole proprietorship in a building that you have just purchased. The floor collapses and injures several customers. Will your losses be limited to the amount of money in your company's business accounts?



Go to glencoe.com to check your answers.

Corporations and Limited Liability Companies

What You'll Learn

- ◆ Characterize corporations.
- ◆ Explain the different types of corporations.
- ◆ Discuss the steps involved in forming a corporation.
- ◆ Explain what a limited liability company is.
- ◆ List the steps in forming a limited liability company.

Why It's Important

Knowing how to form a corporation or limited liability company will help you if you want to expand your business.

Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

Math (NCTM NOS 2a)
Judge the effects of such operations as multiplication, division, and computing powers and roots on the magnitudes of quantities.

Social Studies (NCSS 5)
Study interactions among individuals, groups, and institutions.

Reading Guide



Before You Read

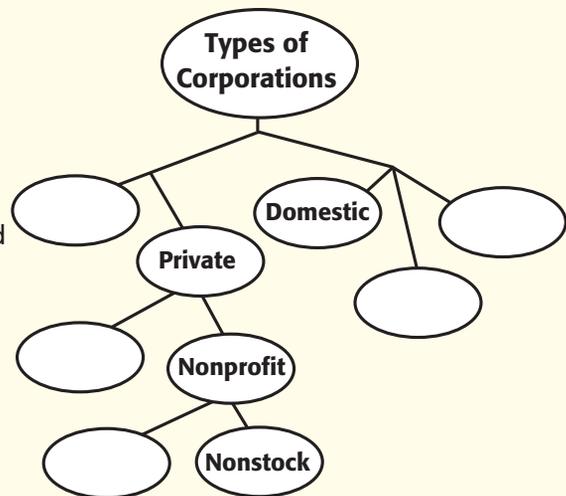
Connect How many different corporations can you name?

Focus on Ideas

A corporation is treated by law as a person.

Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to glencoe.com to find graphic organizers and tips on how to improve your note-taking skills.



Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- corporation
- share
- shareholder
- articles of incorporation
- certificate of incorporation
- limited liability company (LLC)
- expropriation



Academic Vocabulary

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- domestic
- process
- similar

Corporations

Are all corporations giant multinational companies?

A **corporation** is an entity with the legal authority to act as a single person, distinct from its owners. Unlike a sole proprietorship or partnership, a corporation is treated by law as if it is an individual person. It can make contracts, buy and sell goods, sue, and be sued.

All corporations have the same basic form. Ownership of a corporation is divided into shares. A **share** is a single unit of ownership of a corporation. A **shareholder** is an individual who owns shares of a corporation. Each shareholder has one vote for each share of stock that he or she owns in the corporation. Shareholders elect a board of directors who run the corporation.

Advantages and Disadvantages of a Corporation

Corporations have several advantages. A corporation can obtain a great deal of capital by selling shares, while general partnerships and sole proprietorships cannot. Each shareholder's liability is limited to the amount of money he or she paid for shares in the corporation. Corporations also have perpetual existence. This means that a corporation continues to exist after the founders, shareholders, managers, and directors are gone.

Corporations also have disadvantages. First, a corporation's income may be taxed more than once: the corporation is taxed on the profits it makes, and then the shareholders are taxed on the dividends (share of the profits) they receive. This is called double taxation. Second, corporations face numerous government regulations and are looked at very closely. Finally, the original founders of the corporation can lose control and ownership of the corporation to the shareholders or the board of directors.

Types of Corporations

Not all corporations are large. In fact, about 40 percent of all corporations have fewer than five employees. Corporations may be classified as public or private corporations, stock or nonstock corporations, and domestic, foreign, or alien corporations (see **Figure 16.1** on page 368).

Public Corporations Public corporations include incorporated political units, such as towns, villages, cities, and school districts. These entities often incorporate to obtain the protections of this form of business organization, such as limited liability.

Private Corporations Private corporations are owned by private individuals and may be for profit or nonprofit. For profit corporations are organized for the purpose of making money. A for profit corporation may be either a C corporation or an S corporation. A C corporation is a standard corporation and the type subject to double taxation: the corporation is taxed on its income and the shareholders are taxed on their dividends.



As You Read

Predict What are the disadvantages of a corporation?



De jure: *adj* Latin for as a matter of law.

De facto: *adj* Latin for as a matter of fact.

Vocabulary Builder In class, list as many words as you can think of in two minutes that come from the Latin root *jure*. Then, compare your list with the rest of the class.

Look It Up! Check definitions in *Black's Law Dictionary* or an online glossary. For direct links, go to glencoe.com to find more vocabulary resources.

Figure 16.1 Types of Corporations



Private Most corporations are privately held corporations. They are organized to make a profit and are usually owned by a small group of private individuals.



Public A public corporation is a corporation created by the federal, state, or local government for governmental purposes, or a large private corporation that sells its stock to the general public.



Nonprofit A nonprofit corporation, such as Habitat for Humanity, is formed for educational, religious, charitable, or social purposes. Membership is acquired by agreement, rather than by acquisition of stock, and no stockholder may share in the profits.

 There are different types of corporations, but they all have the same form. *What is the difference between a domestic and a foreign corporation?*

An S corporation is a special type of corporation that avoids double taxation. With an S corporation, the corporation itself does not pay income tax and the shareholders pay tax on their share of the income as if they were partners. However, an S corporation has limitations on the number of shareholders it can have.

Nonprofit corporations are formed for educational, religious, charitable, or social purposes. A nonprofit corporation in which membership is acquired by agreement, rather than by the sale and acquisition of stock, is called a nonstock corporation.

Domestic, Foreign, and Alien Corporations A corporation is considered a **domestic** corporation in the state in which it is incorporated. In any other state in which it operates, a corporation is considered a foreign corporation. An alien corporation is one that is incorporated in another country but does business in this country.

Forming a Corporation

Creating a corporation requires extensive paperwork according to each state's laws. Corporations can choose any state to incorporate in, even if they do not do business in that state. Despite differences, in the requirements of different states, there are many common procedures to the incorporation **process**.

Corporate Promoters A corporate promoter is someone who organizes the new corporation. The promoter may help assemble investors, lease office and warehouse space, purchase supplies and equipment, and hire employees. Promoters are personally liable for the contracts they make in the name of the corporation.

Choosing a Corporate Name The name of a corporation must include the word *corporation*, *incorporated*, or *company*, or the abbreviation for one of these words. A corporation cannot use the name of another corporation, foreign or domestic. In some states, the name cannot be **similar** to another business name in use.

Articles of Incorporation The **articles of incorporation** is a legal document filed with the state to establish a corporation. It describes the corporation's organization, powers, and authority. This can sometimes be done online. There may be a requirement to have a minimum amount of capital, such as \$500 to \$1,000. After the application is filed and fees are paid to the office of the secretary of state, the company will receive a certificate of incorporation. A **certificate of incorporation** is a corporation's official authorization to do business in a state. In some states, the certificate is called a charter.

Structure of the Corporation The shareholders of a new corporation elect a board of directors. The board elects a chairman and the top officers of the corporation. The officers manage the company and carry out the board's policies and decisions. Officers can be members of the board, or they may be hired employees.



Reading Check

Discuss What are the requirements for a corporate name?

Vocabulary You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.



Global Law

Brazilian Corporations

In 2002, the country of Brazil updated its corporation laws by passing the New Civil Code, Law 10.406. Under that system, there are many different business organizational structures. However, there are two main forms that make up the majority of businesses.

Limitadas

A *sociedade por quotas de responsabilidade limitada (limitada)* is similar to a limited liability company, limited partnership, or closely-held company in the United States. By law, a *limitada* must have at least two partners. Partners can be either individuals or legal entities.

The articles of association for a *limitada* must state the *limitada's* name and for what period of time the business has been created. It must also state the company's main activities and the location of its main place of business.

Finally, the *limitada* can be managed by all the partners, some of the partners, or by only one partner. The only requirement is that power to run the company must be in the hands of at least one legal resident of Brazil.

Sociedade anônima

The *sociedade anônima* is like a joint-stock company or corporation in the United States. Like a *limitada*, the *sociedade anônima* requires no less than two partners. However, there are additional requirements to forming one.

For example, all the documents relating to the formation of a *sociedade anônima* must be filed at the commercial registry. It must then be published in the *Official Gazette* and in a second major newspaper in the region where the company will be located.

Finally, shareholders of stock in *sociedade anônimas* have the following rights: the right to the company's profits; the right to distribution of the company's assets, if the company is dissolved; and the right to oversee the company's management.

Across Cultures: Ethanol Fuel

As the rest of the world is struggling to get enough oil for its energy needs, Brazil has shifted its focus from petroleum to ethanol. At least 20% of Brazilian cars run on pure ethanol, which is produced in Brazil from sugar cane. Many countries are looking to follow Brazil's lead in the future.

Critical Thinking: *Is publishing the documents for forming a new corporation in a newspaper a good idea?*

Incorporation Problems

If the incorporation process has been completed, the corporation legally exists and it is known as a *de jure* corporation. However, sometimes mistakes or problems interrupt the incorporation process. Although the corporation does not legally exist, some states will still recognize it as a *de facto* corporation as long as the incorporators made a good faith attempt to incorporate.

Piercing the Corporate Veil

The corporate entity can be seen as a veil protecting the shareholders from liability. Under some circumstances, however, the court will "pierce the corporate veil" and hold shareholders personally liable. This happens when a corporation is formed to avoid paying debt or is run like a sole proprietorship. The court will also hold shareholders liable if they use corporate assets for their own purposes or commit fraud in the corporation's name.

Limited Liability Companies

Are there any other ways you could set up your own company?

A **limited liability company (LLC)** is an entity with the legal authority to act as a single person, distinct from its owners, and combines the best features of a partnership and a corporation. Like a corporation, it offers limited liability to its owners. Like the partners in a partnership, the owners of an LLC escape double taxation.

The first step in forming an LLC is to draw up the articles of organization. The LLC must have a statutory agent within the state where it is organized. Filing fees must also be paid.

The dissolution of an LLC is similar to a partnership and can occur for any of the same reasons. It must also be followed by a winding up to put the LLC officially out of business. However, a winding up need not follow a dissolution if the remaining members want to continue the LLC.

Doing Business Internationally

What do you think you would need to do to create a company abroad?

Different countries have different tax codes and different laws regarding establishing a business. For example, many countries have favorable corporate tax laws designed to attract corporations there. On the other hand, the LLC form of business does not exist in most countries. Businesses in other countries are also subject to expropriation. **Expropriation** is when a government seizes a privately-owned business to be used for a public purpose.



After You Read

Summarize What are the different types of corporations?

SECTION 16.2 ASSESSMENT

Self Check

1. What is a corporation?
2. What is the difference between a public and a private corporation?
3. What is a limited liability company?

Academic Connection

Mathematics The Miller Metal Products Corporation manufactures hand-held can openers. It plans to manufacture

750,000 can openers to be sold at \$0.44 each. The fixed costs to make them are \$142,570. The variable costs to make them are \$0.19 each. How many can openers must Miller Metal Products sell to break even?

CONCEPT **Number and Operations:** To find the break-even point in units, use the following formula:

$$\text{Total Fixed Costs} \div (\text{Selling Price per Unit} - \text{Variable Costs per Unit})$$



For more math practice, go to the Math Appendix.

Critical Thinking

Changing Form Why might a sole proprietorship or a partnership want to incorporate?



Go to glencoe.com to check your answers.

Chapter 16 Review and Assessment

Summary

Section 16.1 Sole Proprietorships and Partnerships

- ◆ A sole proprietorship is a form of business that is owned and operated by one person.
- ◆ A partnership is an association of two or more persons to carry on as co-owners of a business for profit.
- ◆ General partnerships can be formed by agreement or by proof of existence.
- ◆ There are five types of partners: general, secret, silent, dormant, and limited.
- ◆ Partners have three duties: to be loyal to the firm; to be obedient to the arrangements made by the partnership agreement; and to act with due care in carrying out the business of the firm.
- ◆ Partnerships can end through dissociation and dissolution.

Section 16.2 Corporations and Limited Liability Companies

- ◆ A corporation is an entity with the legal authority to act as a single person, distinct from its owners.
- ◆ A shareholder is an individual who owns shares of a corporation.
- ◆ A share is a single unit of ownership of a corporation.
- ◆ Corporations may be classified as public or private corporations, stock or nonstock corporations, and domestic, foreign, or alien corporations.
- ◆ A limited liability company (LLC) is an entity with the legal authority to act as a single person, distinct from its owners, and combines the best features of a partnership and a corporation.



Vocabulary Builder

1 On a sheet of paper, use each of these terms in a sentence.

Key Terms

- sole proprietorship
- unlimited liability
- partnership
- joint liability
- dissolution
- dissociation
- limited partnership
- limited liability partnership (LLP)
- corporation
- share
- shareholder
- articles of incorporation
- certificate of incorporation
- limited liability company (LLC)
- expropriation

Academic Vocabulary

- perpetual
- dormant
- incompetence
- domestic
- process
- similar



Go to glencoe.com to play a game and improve your legal vocabulary.

Key Points Review

Answer the following questions. Refer to the chapter for additional reinforcement.

- | | |
|---|--|
| <p>2 What are the advantages and disadvantages of a sole proprietorship?</p> <p>3 What is unlimited liability?</p> <p>4 What are the advantages of forming a partnership?</p> <p>5 What is the difference between a term partnership and a partnership at will?</p> | <p>6 What are the advantages of a corporation?</p> <p>7 What are the steps in the formation of a corporation?</p> <p>8 What are the articles of incorporation?</p> <p>9 What is needed to form an LLC?</p> |
|---|--|

Standardized Test Practice

- 10** Read the following information about the concept of micro-enterprise development and complete questions 1 and 2.

The concept of micro-enterprise development has its roots in the recognition of a previously untapped market—skilled or motivated individuals who could provide desired services to the public but lacked access to traditional forms of credit and, in many cases, business and financial expertise. The micro-enterprise theory is simple. Loan these individuals small amounts of money for business start-up costs, make the loan terms affordable, and give them business training and support. This formula has proven to be a success.

Today the term micro-enterprise is commonly used to describe a business with up to five employees, which requires \$25,000 or less in start-up capital, and does not have access to the traditional commercial banking sector. Many aspiring micro-entrepreneurs have little formal business training and varying levels of education. Training and technical assistance can often be the biggest factor in the success of a new business.

1. Which statement best describes what a micro-enterprise is?

- A** a group of individuals who invest in small business concepts
- B** business counselors who work with entrepreneurs to start companies
- C** technical assistants who guide entrepreneurs with technology problems
- D** small businesses with few employees that need minimal start-up capital

2. Often the biggest factor to the success of a micro-enterprise is the

- A** ability to have an endless supply of funds
- B** ability to offer training and technical assistance
- C** ability to have new entrepreneurs be self-sufficient
- D** ability to provide raw materials and employees

**Test-Taking Strategies**

Notes that are complete and well organized, with key terms defined and highlighted, will make reviewing for a test easier.



Apply and Debate

Read the following scenarios. Get together with other students in pairs or groups of three and take a position on each scenario. Debate your position in class with students taking the opposite position or prepare a written argument justifying your position.

11 Who Owns a Name

Mark registered the business name Crazy Cookies, but did not open his bakery right away. When Ruth later opened Crazy Cool Cookies, Mark sued her for infringing on his registered business name.

You Debate *Should Ruth be allowed to use the business name? Why or why not?*

12 Disagreeing Partner

Ming was one of four general partners in a business. The other partners voted to terminate a contract. Ming disagreed, fearing they might be sued. They were.

You Debate *If you were one of the other partners, would you excuse Ming from being held liable in the lawsuit as partnership law requires since he had disagreed?*

13 Widow Partner

Tasha's husband was a partner in a store. When he died, the other partners continued to pay Tasha for his share of the profits. Tasha eventually decided to go into the store every day to help. One day, a patron tripped in the store and sued.

You Debate *If you were the lawyer for the suing patron, would you make a case that Tasha is also one of the partners?*

14 Lost Letter

Luca filed to incorporate his company. He was told that the charter was in the mail. He began his business. Later, when he was sued for an accident, he learned that the state had never mailed the incorporation charter and he was not protected.

You Debate *If you were the lawyer for Luca, would you defend him by saying that he was told that his business was incorporated?*

15 Putting on a Corporate Veil

Your sole proprietorship company has debts of \$200,000 but only \$27,000 in cash. You consider incorporating to protect yourself, in case your creditors sue you for failure to pay.

You Debate *Is it legal and valid to incorporate to get the protections under law, even though you know you may not be able to pay your debts?*



**Case Study Practice – Hurwitz v. Padden**

16 When Does a Partnership End? In September 1991, Thomas Hurwitz and Michael Padden formed a two-person law firm. They failed to enter into a written partnership agreement, but orally agreed to share all firm proceeds on a 50-50 basis. They also agreed to split all costs and fees on a 50-50 basis. In January 1993, Mr. Hurwitz and Mr. Padden changed their firm from a partnership to a limited liability company. On February 15, 1996, Mr. Padden notified Mr. Hurwitz that he wanted to dissolve the firm effective March 1, 1996. The two men resolved all the business issues involving their relationship except for a batch of attorneys' fees from several of the firm's cases, which Mr. Padden worked on after he gave notice of termination. Mr. Padden argued that since he worked on the cases after dissolution began, he was entitled to additional fees. Mr. Hurwitz argued that during dissolution, fees are split the same as they were prior to dissolution.

Source: Hurwitz v. Padden, 581 N.W.2d 359 (Minn. Ct. App. 1998)

Practice How should the fees be split?

17 Ethics Application

Conflict of Interest? Moesha Allen is co-owner of a small restaurant in a partnership at will. She is planning on leaving the partnership and opening her own restaurant in a couple of months. Her favorite customers keep asking her about her plans for the future.

- ◆ Is Moesha entitled to tell her customers about her new restaurant or will it appear as if she is trying to steal customers?

18 Internet Application

Read about Forming a Partnership Layla and Denyce both operate small gift shops in nearby shopping centers. They decide they might as well open one big gift shop by combining their resources and assets while lowering their monthly overhead costs.



Go to glencoe.com to access the Web site sponsored by QuickForms to see how to write up a partnership agreement. With a partner, discuss how you would handle creating a partnership agreement that Layla and Denyce could use for their gift shop.



Reading Connection

Outside Reading Go to glencoe.com for a list of outside reading suggestions about forming a business.

Operating a Corporation

BusinessWeek News

A Short History of Unpassed Torches

By Jena McGregor

There was an eerie sense of déjà vu about the management shakeup at Nike Inc. this week. Not only has the edgy shoemaker failed at earlier attempts to pass the baton, but business history is littered with the troubled successions of charismatic entrepreneurs and once and future kings. For visionary founders, the years of emotional investment, the inextricable melding of their own identity with the business, and the distancing from their creation can all pile up to create a transition that has classic corporate melodrama written all over it. "It's like Shakespeare or Greek tragedy or the Bible," says Jeffrey A. Sonnenfeld, senior associate dean at the Yale School of Management. "It's just such a predictable script."

"The core challenge of corporate governance is getting past the concept of the imperial CEO," says Ric Marshall, chief analyst at The Corporate Library, a research firm specializing in governance issues.

Flex Your Reading

Efficient critical reading involves being flexible with speed and comprehension. There are several ways of reading critically, and you need to fit a reading style to your needs and to the material.

Go to glencoe.com for Flex Your Reading activities, more information on reading strategies for this chapter, and guided practice in reading about how corporations operate.





Stock Exchange Shares in U.S. and global companies are publicly traded in marketplaces called stock exchanges. *What is the most famous stock exchange in the United States?*

What You'll Learn

- ◆ Distinguish the roles of corporate directors and corporate officers.
- ◆ List the rights shareholders have.
- ◆ Explain the business judgment rule.
- ◆ Explain the fairness rule.
- ◆ Describe the liability of corporate directors and officers.

Why It's Important

If you ever manage or buy stock in a corporation, you need to know how a corporation is run and what rights shareholders have.

Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

Social Studies (NCSS 5)
Study interactions among individuals, groups, and institutions.

English Language Arts (NCTE 7)
Conduct research on issues and interests by generating ideas and questions, and by posing problems.

Reading Guide



Before You Read

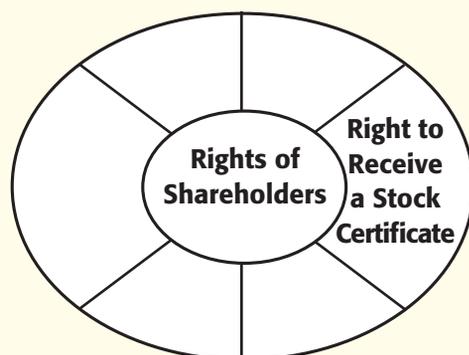
Connect You have probably heard of corporations such as Bank of America, Microsoft, and Coca-Cola. Who do you think actually owns these companies?

Focus on Ideas

Owners of stock in a corporation have certain rights.

Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to glencoe.com to find graphic organizers and tips on how to improve your note-taking skills.



Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- corporate director
- corporate officer
- direct suit
- derivative suit
- insider trading



Academic Vocabulary

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- proportionate
- preemptive
- exploit

Corporate Management

What is the difference between a corporate director and a corporate officer?

In a sole proprietorship or a partnership, power is concentrated in the hands of a few individuals. In a corporation, power is scattered among many individuals and institutions that make up the directors, corporate officers, and shareholders. Some key figures can also play more than one role. For example, directors can be officers and shareholders of the corporation.

Corporate Directors

Corporate directors are people elected by the shareholders to make broad policy decisions in the running of a corporation. Generally, directors do not have to meet any legal qualifications unless the corporation's certificate of incorporation or its bylaws specify. For example, the bylaws might require that a director be a shareholder or a state resident. Directors usually serve for a set number of years and must be reelected by the shareholders. Directors are subject to the duty of due care and the duty of loyalty to the corporation.

Corporate Officers

Corporate officers are people chosen by the directors to run the day-to-day affairs of a corporation. The officers include a president, several vice-presidents, a secretary, a treasurer, and assistant officers. Officers are agents of the corporation. This means that the rules of agency law apply. Like directors, officers are subject to the duties of loyalty and due care.

Corporate Shareholders

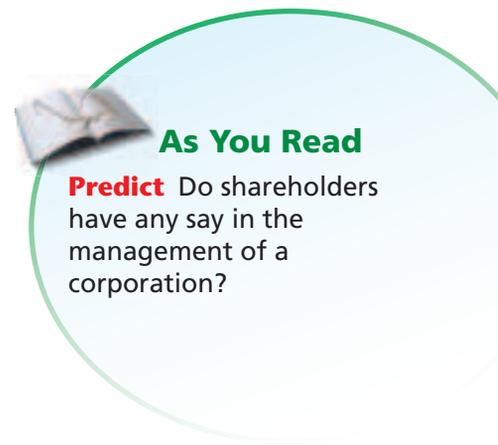
Corporate shareholders, or simply shareholders, are the owners of a corporation based on the number of shares they hold. Shareholders are also called investors, but in fact they are both the investors in and owners of a corporation. Shareholders are often individual people, but partnerships, labor union retirement funds, and other corporations can also be shareholders in a corporation.

The Rights of Shareholders

What rights do shareholders of a corporation have?

Owners of stock in a corporation acquire certain rights. These include the right to:

- receive a stock certificate
- receive dividends
- examine the corporate books and records
- transfer all shares
- maintain a proportionate share of stock
- exercise a vote for each share of stock owned
- sue



As You Read
Predict Do shareholders have any say in the management of a corporation?



Dividend: *n* Portion of a corporation's profits paid to shareholders.

Proxy: *n* Person authorized to vote on behalf of shareholders.

Vocabulary Builder List five synonyms for *dividend* and five synonyms for *proxy*. If you need help, you can find synonyms in a printed or online thesaurus.

Look It Up! Check definitions in *Black's Law Dictionary* or an online glossary. For direct links, go to glencoe.com to find more vocabulary resources.



Global Law

Businesses in South Africa

All companies in South Africa are governed by the Companies Act, which is based on the English system of company law. There are specific rules and regulations to follow for forming a business. The Act is governed by the Companies and Intellectual Property Registration Office (CIPRO).

Steps to Incorporation

There are three steps for a company to follow before it can be incorporated in South Africa.

- 1 The company must reserve a company name.
- 2 The company must file a memorandum and articles of association.
- 3 The company must provide a written consent of auditors to act for the company.

The first and third steps are straightforward. The second step, however, requires a few more steps.

Memorandum and Articles of Association

The memorandum and articles of association must include the following:

- 1 the name of the company
- 2 the primary purpose and business of the company
- 3 the number of shares and the amount of capital invested in the company

In addition to registering with CIPRO, new companies usually must register with other government offices, such as tax and unemployment offices. Finally, the number of shareholders needed depends on the type of company. A private company needs only one shareholder and a director, who may be the same person. In contrast, a public company must have at least seven shareholders and at least two directors.

Across Cultures: Three Capital Cities

South Africa has three capital cities. Pretoria is the administrative capital, where the president and his cabinet reside. Cape Town is the legislative capital, where the National Assembly meets. Bloemfontein is the judicial capital, where the Constitutional Court sits.

Critical Thinking: *What is a reason for requiring at least seven shareholders and two directors for a public company?*

Right to Receive a Stock Certificate

A stock certificate proves that the shareholder owns part of the corporation. The right to receive this document is an essential shareholder's right.

Right to Receive Dividends

Dividends are profits distributed to shareholders. When a corporation has made a profit, the board of directors may declare a dividend. Dividends must be distributed proportionately among shareholders. A dividend can be in the form of shares or cash.

Directors do not automatically have to declare a dividend when the corporation has made a profit. They may instead decide to keep the profit for the benefit of the corporation.

Right to Examine Corporate Books and Records

The law requires a corporation to keep records of its business affairs, including a list of shareholders, an accounting of all transactions, and the minutes of all directors' meetings. Shareholders have a statutory right to see these records.

Right to Transfer All Shares

Shareholders have the right to transfer or sell their shares. The person who sells or transfers stock is the transferor, and the person who receives it is the transferee.

Right to Maintain a Proportionate Share of Stocks

Shareholders have the right to purchase a **proportionate** share of every new stock issue before it is offered to the public. This right is called the shareholder's **preemptive** right. The purpose of this right is to prevent directors from taking control of the corporation by issuing more shares and buying them all themselves. However, this right can be limited or denied by the corporation's certificate of incorporation, by its bylaws or regulations, or by state law.

Right to Vote for Each Share of a Stock Owned

Shareholders have voting powers as part owners. They can, therefore, be involved in a corporation's management. The incorporation statutes of most states require that a meeting of shareholders be held annually to elect the board of directors and conduct other necessary business. Such meetings typically follow parliamentary procedure. Shareholders may vote on issues put up for a vote at the meeting. However, only holders of stock called common stock have full voting rights.

Shareholders who disagree with the decisions of the board of directors may be able to get more voting power than their own shares entitle them to have. One method is called proxy voting. A proxy vote is the right to vote on behalf of other shareholders. Proxy voting arises when shareholders who believe in one position solicit other shareholders and obtain their permission to vote for them. The shareholders may then win the majority votes they need to defeat the board on an issue.

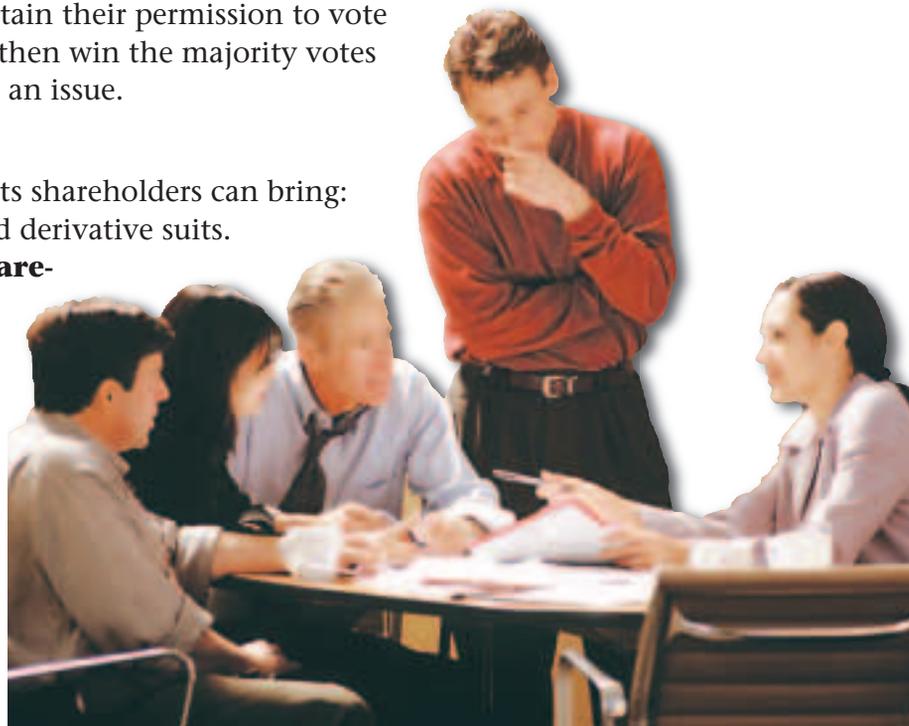
Right to Sue

There are three types of lawsuits shareholders can bring: direct suits, class action suits, and derivative suits.

A **direct suit** is a lawsuit a shareholder can bring against a corporation for denying his or her rights as a shareholder. Shareholders may also bring a class action lawsuit against a corporation on behalf of all shareholders in their position. A **derivative suit** is a lawsuit a shareholder can bring on behalf of the corporation to correct an injury to the corporation.

Vocabulary You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

 **Company Records** Shareholders have a statutory right to see all company records. *What kind of lawsuit could a shareholder bring if the company refuses to show its records?*



 **Insider Trading** It is illegal for corporate directors or officers to buy or sell stock based on inside information about a company not available to the public. *What kinds of outsiders could also be involved in insider trading?*



Liability of Directors and Officers

If you make a bad decision as the director of a corporation, can you be sued?

To test the decisions of corporate directors and officers, the courts have developed two standards: the business judgment rule and the fairness rule.

The Business Judgment Rule

The business judgment rule presumes that the decisions of corporate directors and officers are legal, made in good faith, with due care, and in the best interests of the corporation. However, a court will find against directors or officers if a decision involved fraud, lack of good faith, abuse of discretion, a conflict of interest, negligence, or illegality. The rule focuses not on whether a particular decision was the right decision but on how the decision was made. For example, a director who enters a deal with another corporation without doing any research could be considered negligent.

Directors and officers are not obligated to guarantee that the corporation makes a profit. If the corporation suffers a loss from a transaction the board authorized, the directors are not liable to the shareholders unless they violate the business judgment rule. Some states hold directors and officers liable only if they are grossly negligent in carrying out their duties, and some have even passed anti-liability statutes that limit the liability of directors.

The Fairness Rule

Directors and officers have a duty of loyalty to their corporation. They must not **exploit** their positions for personal gain at the expense of the corporation. Their main goal must be to act in the

Reading Check

Discuss *Is the business judgment rule too easy on corporate directors and officers?*

best interests of the corporation. They must not deliberately hurt the corporation. A director's or an officer's duty of loyalty may be questioned if he or she has a personal interest in a business decision. According to the fairness rule, if a manager profits in some way by a decision, the decision must be fair to the corporation.

Insider Trading One way directors or officers might exploit their position for personal gain is insider trading. **Insider trading is when a corporate director or officer buys or sells shares in a corporation based on firsthand information about the corporation that is not available to the public.** Insider trading gives an unfair advantage to people in a position of trust within a corporation. It also applies to passing valuable information to outsiders so they can profit from it. Under the insider trading rules, directors or officers who possess inside information must either refrain from acting on it or reveal it publicly before acting on it. Insider trading is legally considered a felony crime under the rules of the Securities and Exchange Commission (SEC).

Corporate Opportunity Doctrine The corporate opportunity doctrine is an extension of the duty of loyalty. According to this doctrine, directors and officers cannot take advantage of a business opportunity for themselves if they know that the corporation would want to take that opportunity for itself. The directors must first present the opportunity to the corporation. If the corporation turns it down, then the directors or officers can take the opportunity for themselves.

The only exception to this rule is if the director or officer knows that the corporation is financially incapable of taking the opportunity, despite its interest.



After You Read

Summarize Under the business judgment rule, for what reasons might a court find against a director for a bad decision?

SECTION 17.1 ASSESSMENT

Self Check

1. What are the differences between corporate directors and corporate officers?
2. What are the rights held by corporate shareholders?
3. What are the two standards courts have developed to test the decisions of corporate directors and officers?

Academic Connection

English Language Arts

Like corporate board meetings, many student organizations run their meetings using parliamentary procedure, also known as Robert's Rules of Order. Parliamentary procedure provides an approved and consistent format for holding meetings. It also protects majority and

minority rights. Research the history, purpose, and main rules of Robert's Rules of Order. Write a brief report outlining the basic procedure for conducting a meeting.

Critical Thinking

Insider Trading What are different ways a corporate director could engage in insider trading?



Go to glencoe.com to check your answers.

Financing, Expanding, and Dissolving a Corporation

What You'll Learn

- ◆ Describe the different types of corporate stock.
- ◆ Distinguish between a merger, a consolidation, and a conglomerate.
- ◆ Explain asset acquisition and stock acquisition.
- ◆ Identify the ways a corporation can be terminated.

Why It's Important

Knowing the laws that regulate corporate financing, expansion, and dissolution will prepare you for any dealings you might have with a corporation in the future.

Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

Math (NCTM CS1 2)
Communicate mathematical thinking coherently and clearly to peers, teachers, and others.

Social Studies (NCSS 6)
Study how people create and change structures of power, authority, and governance.

Reading Guide



Before You Read

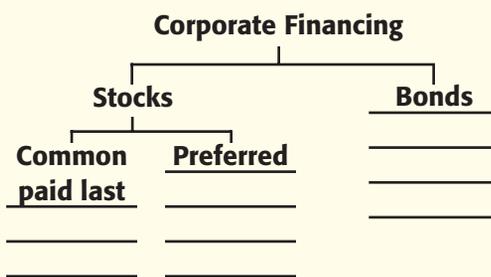
Connect Many of the corporations you come into contact with regularly are franchises. What are some franchises you can name?

Focus on Ideas

Corporations raise money by selling stocks and bonds.

Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to glencoe.com to find graphic organizers and tips on how to improve your note-taking skills.



Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- merger
- consolidation
- conglomerate
- asset acquisition
- stock acquisition
- franchise



Academic Vocabulary

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- subscription
- significant
- unanimous

Corporate Financing

How do you get money to finance a corporation?

Corporations need financing to pay for their business activities, such as research, product development, office space, marketing, and advertising. Corporations can finance their activities by raising money through the sale of stocks or borrowing money through the sale of bonds.

Corporate Stocks

Corporations raise money by selling stock. Shares of stock represent a shareholder's interest or investment in a corporation.

All stock is originally sold by the corporation. At the time a corporation is organized, the promoters seek **subscriptions** from investors. These stock subscriptions are contracts to buy stock once the corporation is authorized by the state to sell stock to the public. The subscribers do not become stockholders until the organization is completed and stock certificates are issued to them. The corporation may continue to sell shares after its incorporation is complete.

Purchasers of stock may buy the stock from the corporation or from current owners who want to sell their shares. They may buy stock personally or through agents called brokers. A broker fills the purchaser's order in one of two ways. The broker may buy the stock on a stock exchange, which is a public auction in which stocks are bought and sold. The largest and best-known stock exchange is the New York Stock Exchange (NYSE). The broker may also purchase stocks over the counter, meaning outside the organized exchanges. Many stock trades today are done online, using a brokerage house that has a Web site where the public can place buy and sell orders.



As You Read

Predict Why do corporations sell stocks and bonds?

Vocabulary You can find vocabulary definitions in the **Key Terms** glossary and the **Academic Vocabulary** glossary in the back of this book.



Executive Pay

As President and CEO, Paul Krocker guided his company stock price from \$3.23 to \$81.00 per share. Now, Big Blue Technology wants to hire him away. They offer him \$50 million dollars per year. He accepts and begins by cutting some jobs and reducing salaries by 25 percent, which help to make Big Blue more profitable. The share price of Big Blue shoots up 35 percent in one month.

Critical Thinking *Is it ethical for an executive to earn a huge salary while the employees lose jobs or salaries, but the stock price increases to the benefit of thousands of shareholders?*

Types of Stock There are two types of corporate stock: common stock and preferred stock. Common stock is the basic form of corporate ownership. All public corporations issue common stock. Holders of common stock have voting rights in a corporation. As a group, they elect the corporation's board of directors. Common stock sometimes pays dividends to the shareholders based on how the corporation performs. Holders of common stock are the last shareholders to be paid.

The second type of stock a corporation issues is preferred stock. Holders of preferred stock cannot vote. However, they do have the right to receive a fixed dividend. Holders of preferred stock are the first shareholders to be paid.

Corporate Bonds

A corporation may also finance its activities through bonds. Bonds are notes issued for money that the corporation borrows. When a company makes bonds available, it is called a bond issue. Unlike stocks, bonds earn interest and must be repaid in the future. If a company files for bankruptcy, bondholders are paid before shareholders.

Corporate Expansion

How can you increase the size of a corporation?

A corporation might want to expand by acquiring new land, new manufacturing plants, new sales outlets, or entering new fields of business. A corporation can expand by buying or investing in another corporation through a merger or consolidation, by acquiring the assets or stock of another company, or by opening new franchises (see **Figure 17.1**).

Merger and Consolidation

A **merger** is when two companies join together, with one company keeping its corporate identity and the other company losing its corporate identity. A **consolidation** is when two or more companies join together to form a new corporation. There is no **significant** difference between a merger and a consolidation, and the terms are often used interchangeably. Most of the time, the term merger is used to describe both scenarios. The boards of directors and shareholders of the corporations being merged must give their approval.

In some cases, companies merge or consolidate to form a conglomerate. A **conglomerate** is a corporation that owns many different types of companies. These companies do business in a variety of separate marketplaces, such as clothing, food, and entertainment. General Electric, for example, owns financial services, plastics companies, and theme parks.

Asset Acquisition

An **asset acquisition** is when one corporation agrees to purchase the assets, such as property, buildings, and

Reading Check

Analyze Why do bonds pay interest but stocks do not?

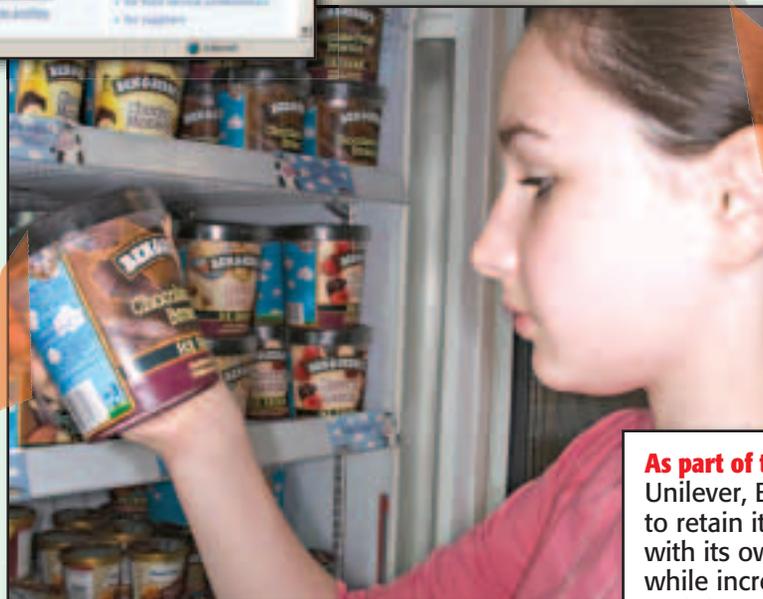
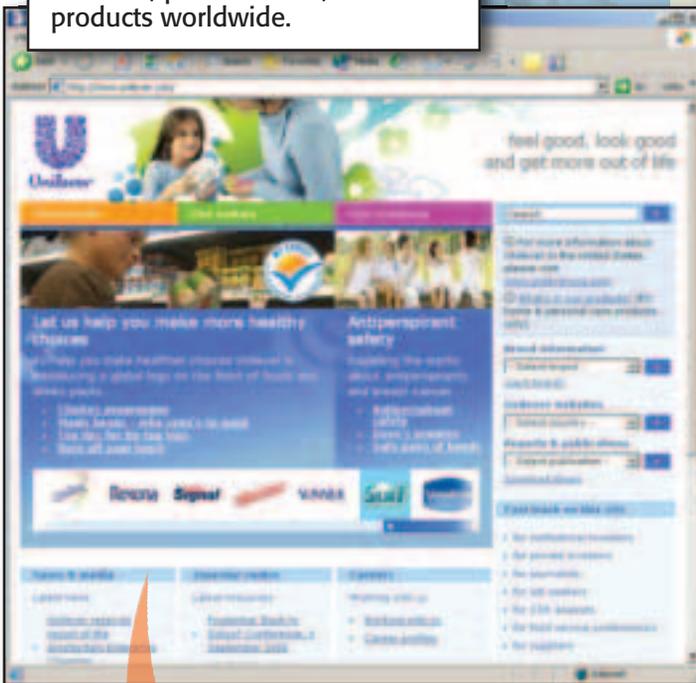


Figure 17.1 Ben & Jerry's

In 2000, Ben & Jerry's was acquired by the corporate giant Unilever, which sells 400 different brands of home, personal care, and food products worldwide.



Ben & Jerry's started out as a small partnership formed by Ben Cohen and Jerry Greenfield in 1978. When demand for its innovative line of ice cream soared, Ben & Jerry's became a public corporation.



As part of the agreement with Unilever, Ben & Jerry's was able to retain its corporate identity, with its own board of directors, while increasing its global sales and the value of its stock.

 Not all mergers are bad for a smaller company taken over by a larger company. *What kind of corporation is Unilever?*



Case Study – Unocal Corporation v. Mesa Petroleum Company



Critical Thinking *Who do you think should win this case and why?*



Note key facts in the text below and look up words you do not understand. Restate difficult ideas in your own words. Go back and reread the text quickly to make sure you did not miss any important detail. Now, you are ready to formulate an opinion.

Interests of the Company Mesa was the owner of about 13 percent of the stock of Unocal. Mesa made a tender offer to buy an additional 37 percent of the stock of Unocal at \$54 per share. The eight outside directors and six inside directors of Unocal fought this takeover bid. They offered a deal to Unocal shareholders in which the corporation itself would repurchase its own shares at \$72 per share. This offer, however, was not open to Mesa. In reaction to this tactic, Mesa filed suit. In the suit, Mesa argued that the repurchase deal was unfair and represented an attempt by the board of directors to keep themselves in power.

Unocal Corporation v. Mesa Petroleum Company, 493 A.2d 946 (Delaware)



Go to glencoe.com for more case study practice.

equipment, of a second corporation. A corporation will buy the assets of another corporation rather than the corporation itself to avoid taking on the debts and liabilities of the other corporation. The shareholders and directors of the corporation selling the assets must approve the transaction.

Stock Acquisition

A **stock acquisition** is when an individual or a corporation buys enough shares of stock in another corporation to take over control of it. A stock acquisition often begins when a prospective buyer makes a tender offer. A tender offer is an offer to buy a specific number of shares at a specific price.

Tender offers are often referred to as takeover bids. The party making the offer is called the suitor. The corporation the suitor wants to take over is called the target. The suitor does not need to buy all the stock of the target. The suitor only needs to buy enough stock to control the election of directors.

Franchises

A **franchise** is a license a company grants to a business or individual for the right to use its name and sell its products or services. The business buying the franchise benefits from the trade name and expertise of the parent company. The corporation benefits by expanding its business without spending money or building new stores itself. McDonald's, Blockbuster, and Holiday Inn are well-known franchises.

Dissolution of a Corporation

Can shareholders end a corporation?

As with partnerships and LLCs, the end of a corporate entity is referred to as a dissolution. The dissolution of a corporation can come about in two ways: voluntarily or involuntarily.

Voluntary Dissolution

A corporation can end voluntarily through a **unanimous** vote of its shareholders. The directors can vote for its end, provided they get the support of two-thirds of the shareholders. After the decision to end the corporation has been made, a statement of intent to dissolve must be filed with the secretary of state's office. The dissolution must be reported to the government, to creditors, and to the public.

Involuntary Dissolution

An involuntary dissolution occurs when the government itself terminates a corporation. If a corporation was formed by fraud, conducted business illegally, or exceeded its authority, the secretary of state can ask the state attorney general to bring a *quo warranto* action against it. If such an action is taken, the corporation could lose its charter and would no longer be authorized to do business in the state. Grounds for bringing such an action also include failure by the corporation to file annual reports, or pay franchise taxes.

A shareholder can also seek the involuntary dissolution of a corporation. However, the shareholder must have appropriate grounds to do this. Such grounds include evidence of fraud, waste of corporate assets, and that a dissolution is necessary to protect the shareholders' rights.



After You Read

Summarize List the ways a corporation can expand its business.

SECTION 17.2 ASSESSMENT

Self Check

1. What are the differences between stocks and bonds?
2. What is a tender offer, and what else is it called?
3. On what grounds might the government bring an action to dissolve a corporation?

Academic Connection

Mathematics You bought 80 shares of Netmark

Associates stock at \$24 per share last year. The company had a good year and paid all of its stockholders annual dividends of \$0.72 per share. How much is your total annual dividend?

CONCEPT **Number and Operations:** To calculate the dividend, multiply the annual dividend per share times the number of shares.



For more math practice, go to the Math Appendix.

Critical Thinking

Online Trading Buying and selling stock over the Internet has become a common way of playing the stock market. Why can this be risky for small investors?



Go to glencoe.com to check your answers.

Chapter 17 Review and Assessment

Summary

Section 17.1 Managing a Corporation

- ◆ Corporate directors are elected by shareholders to make broad policy decisions. Corporate officers are chosen by the directors to run the day-to-day affairs of a corporation. Corporate shareholders are the owners of a corporation based on the number of shares they hold.
- ◆ Shareholders rights include: (1) to receive a stock certificate; (2) to receive dividends; (3) to examine the corporate books and records; (4) to transfer all shares; (5) to maintain a proportionate share of stock; (6) to exercise a vote for each share of stock owned; and (7) to sue.
- ◆ The courts hold corporate directors and officers to two standards: the business judgment rule and the fairness rule.

Section 17.2 Financing, Expanding, and Dissolving a Corporation

- ◆ Corporations raise money by selling stocks or bonds.
- ◆ The public can purchase stock personally or through a stock broker.
- ◆ The two types of stocks corporations sell are common stock and preferred stock.
- ◆ Bonds are notes issued to those who lend money to the corporation. Bonds earn interest.
- ◆ A corporation can expand through a merger, a consolidation, an asset acquisition, a stock acquisition, or by opening new franchises.
- ◆ A corporation can be dissolved either voluntarily by the directors or shareholders, or involuntarily by the government.

Vocabulary Builder

1 On a sheet of paper, use each of these terms in a sentence.

Key Terms

- corporate director
- corporate officer
- direct suit
- derivative suit
- insider trading
- merger
- consolidation
- conglomerate
- asset acquisition
- stock acquisition
- franchise

Academic Vocabulary

- proportionate
- preemptive
- exploit
- subscription
- significant
- unanimous



Go to glencoe.com to play a game and improve your legal vocabulary.

Key Points Review

Answer the following questions. Refer to the chapter for additional reinforcement.

- 2 What are the two duties corporate directors and officers owe a corporation?
- 3 What is the difference between a direct suit and a derivative suit?
- 4 What is insider trading?
- 5 What is the corporate opportunity doctrine?
- 6 What are the differences between common and preferred stock?
- 7 What are corporate bonds and how are they different from corporate stocks?
- 8 What are the differences between a merger, an asset acquisition, and a stock acquisition?
- 9 What are the ways a corporation can be dissolved voluntarily?

Standardized Test Practice

- 10 Read the excerpt below about buying a franchise and complete questions 1 and 2.

Anyone who thinks about buying an existing business should know the phrase *caveat emptor*, which is Latin for let the buyer beware. It is in the seller's best interest to paint the prettiest possible picture of the business. It is in the prospective buyer's best interest to investigate the accuracy of the seller's statements. This means asking both technical and social questions.

Technical questions usually require the help of professionals such as accountants or lawyers. Are the financial records accurate? Are the legal requirements of the business in order? Was the business sued in the past?

Asking social questions means talking to the present owner, the employees, and the customers. Why is the owner selling? What is the business's reputation? How does the company compare to its competition? All of these questions need to be answered before deciding to purchase an existing business.

1. What does *caveat emptor* mean?

- A Let the seller beware.
- B Let the buyer beware.
- C Ask questions.
- D The truth is out there.

2. Which is an example of a technical question?

- A Why is the owner selling?
- B What is the business's reputation?
- C Was the business sued in the past?
- D How does the company compare to its competition?



Test-Taking Strategies

Choose a good seat to take the test. To avoid distractions, do not sit near a door or near friends.



Apply and Debate

Read the following scenarios. Get together with other students in pairs or groups of three and take a position on each scenario. Debate your position in class with students taking the opposite position or prepare a written argument justifying your position.

11 Insider Trading

Cyrus is an executive assistant at GenCom. His boss asks him to type a press release announcing that Gencom will soon merge with Billcom. That night, he discusses the merger with his aunt, who is a business journalist. She then buys 1,000 shares of GenCom, and, after the news is released, makes \$20,000 in stock price gains.

You Debate *Did Cyrus engage in insider trading by discussing the merger?*

12 Conflict of Interest?

Lakefront Craft, Inc. manufactures boats. To expand the company, the board of directors decided to purchase Paddle Canoes, Inc. for \$3.5 million. Lakefront's stock price rose with this news. A reporter later discovered that a cousin of Lakefront's chairperson was the owner of Paddle Canoes, and made \$1 million on the sale.

You Debate *Is there a conflict of interest in this situation?*

13 Hurricane Loss

Scott, a shareholder, brought suit against Big Trucking, Inc. when the company lost \$2 million because the senior executives failed to move 200 trucks out of the path of a hurricane that was forecast. The trucks and their contents were destroyed.

You Debate *Are executives responsible for losses arising out of natural disasters?*

14 Missed Market

Jackson was a shareholder in Life Pharmaceuticals, Inc. The company announced its plans to launch a new cancer drug. Jackson's stock soared. After the company delayed the drug's release due to complications in the research, his stock dropped. Jackson sued the company for mismanagement.

You Debate *Are stockholders right to sue for product delays?*

15 Merger Pros and Cons

Linda often shops at PayDown. When PayDown was bought out by a chain called High Quality Clothing, Inc., Linda was joyful because it carries nicer merchandise. Later, she learned her friend Sharon lost her job at PayDown.

You Debate *Is it important for a community to have better stores even though it may create job losses for some people?*



**Case Study Practice****Hoschett v. TSI International Software, Ltd.**

16 Shareholders' Meeting TSI International Software, Ltd. (TSI) was incorporated in the state of Delaware in 1993, but its headquarters is in Wilton, Connecticut. The company is a privately-held corporation. Less than 40 stockholders hold all the shares in the corporation. Fred Hoschett owns 1,200 shares of common stock, which is much less than 1% of all the stock. Since its incorporation, TSI has never had an annual meeting to elect its directors. Mr. Hoschett, as a shareholder, sued the corporation to make it hold an annual meeting. Under the Delaware Code, a Delaware corporation must have an annual meeting to elect directors, unless the by-laws of the corporation say otherwise. TSI argued that on November 16, 1995, the company received written consent from a majority of shareholders who chose five individuals as directors of TSI. Since a majority of shareholders had provided written consent, TSI argued that an annual meeting was unnecessary.

Source: Hoschett v. TSI International Software, Ltd., 683 A.2d 43 (Del. Ct. Chan. 1996)

Practice Does TSI have to hold an annual meeting?

17 Ethics Application

Nonprofit Monica Edwards and Javier Perez formed a political watchdog group as a nonprofit corporation. Because of political changes, income from donations and membership dues soared in the first year. Monica and Javier gave themselves huge bonuses and took lavish, fact-finding trips because, as a nonprofit corporation, there was no need to show a profit.

- ◆ Are Monica and Javier entitled to do this? Why or why not?

18 Internet Application

Find out about Stocks Your aunt and uncle give you 100 shares of ComTech stock for your birthday. You follow the stock and notice that after one week it has increased in value by \$2.00, and the next week it has gone down by \$1.37. You want to understand what makes a company's stock price go up and down. Why does it fluctuate?



Go to glencoe.com to find out where you can learn about the stock market, how stocks are traded, and why stock prices fluctuate.



Reading Connection

Outside Reading Go to glencoe.com for a list of outside reading suggestions about corporate management.

Business and Regulations

BusinessWeek News

Diesel Gets Cleaner and Greener

By Gail Edmondson

For years diesel engines have been the rage in Europe. They're powerful, use relatively cheap fuel, and can propel a car 40 miles on a single gallon. But they've never really caught on in the U.S., where memories of the 1970s-era soot-belching diesel cars still linger. Now, DaimlerChrysler is trying to clear away that old image. The company has engineered a new emissions technology that promises to make diesel as clean-burning as gasoline. Daimler also has just announced plans to unveil its clean-diesel exhaust system in the U.S. in the latest Mercedes E-class sedans.

Mercedes clean-diesel cars will cost less than an equivalent hybrid while offering greater power and acceleration, plus up to 40% better mileage over conventional gas engines. That's a lure for Americans who love big cars and off-road vehicles. And diesels can go 500 miles without a fill-up.

Flex Your Reading

Efficient critical reading involves being flexible with speed and comprehension. There are several ways of reading critically, and you need to fit a reading style to your needs and to the material.

Go to glencoe.com for Flex Your Reading activities, more information on reading strategies for this chapter, and guided practice in reading about new energy technology.





Environmental Impact The federal government has passed laws to conserve energy and protect the environment. *Which government agency was created to deal with pollution and toxic waste?*

What You'll Learn

- ◆ Explain the source of federal power in the regulation of business.
- ◆ Identify the laws that regulate the sale of securities.
- ◆ Distinguish between the laws that regulate antitrust activity.
- ◆ Describe what laws regulate corporate takeovers.

Why It's Important

Once you understand the background for governmental regulations, you will appreciate why the government plays a regulatory role to ensure competition and fairness.

Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

English Language Arts (NCTE 11) Participate as knowledgeable, reflective, creative, and critical members of a variety of literacy communities.

Social Studies (NCSS 6) Study how people create and change structures of power, authority, and governance.

Reading Guide**Before You Read**

Connect If you have ever been someplace where you could only buy goods at one store, you are familiar with a monopoly. Name an instance where you experienced a monopoly.

Focus on Ideas

The federal government regulates corporations to make sure they do business fairly.

Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to glencoe.com to find graphic organizers and tips on how to improve your note-taking skills.

Antitrust Laws

Act	Purpose
Sherman Antitrust Act	

**Key Terms**

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- Commerce Clause
- security
- registration statement
- prospectus
- monopoly

**Academic Vocabulary**

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- commerce
- administer
- certify

Business and the Constitution

What gives the federal government the right to regulate businesses?

The federal government gets its power to regulate business from the Commerce Clause of the United States Constitution.

The Commerce Clause is a statement in Article I of the Constitution giving Congress the power to regulate commerce among the states. Over the last two hundred years, the U.S. Supreme Court has enlarged the government's power to regulate business. Now the federal government can regulate any business activity that affects interstate **commerce**, even one that occurs completely within the borders of a single state.

The individual states also have laws to regulate commerce. However, all state laws must abide by the Constitution. For example, the U.S. Supreme Court has ruled that a state violates the Commerce Clause when it creates a law that treats in-state and out-of-state businesses differently when the different treatment hurts the out-of-state business.

There are three major areas in which governments regulate commerce:

- securities (sale of stocks)
- antitrust (unfair competition)
- corporate takeovers

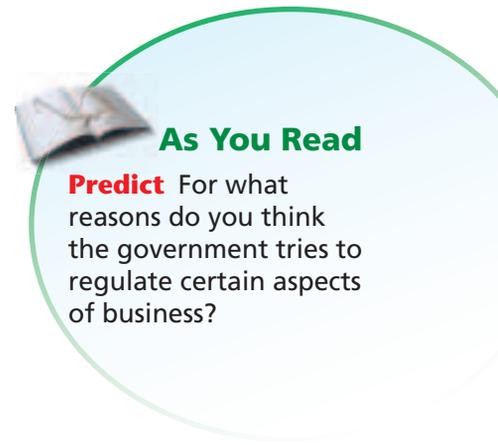
Securities Regulation

In October 1929 the stock market collapsed in what became known as the Great Crash or the Crash of '29. The crash led to a severe worldwide economic depression. Experts identified the sale of worthless securities as a major cause of the collapse. **A security is a monetary investment that seeks to make a profit solely because of another's efforts.** Corporate stocks, interests in savings and loans, interests in racehorses or sports teams, and even the sale of coins are types of securities.

The Securities Act of 1933 To prevent another stock market crash, Congress passed the Securities Act of 1933. The Securities Act is designed to protect investors by making sure they can learn about the securities they buy. It also provides a way to uncover fraud and unfair practices.

The Securities and Exchange Commission The Securities Exchange Act of 1934 created the Securities and Exchange Commission (SEC). The SEC is an independent federal agency set up to **administer** federal securities law. It consists of five commissioners appointed by the President. The SEC also employs lawyers, accountants, and securities analysts who oversee the sale of securities and the brokers, dealers, and bankers who sell them.

The Registration Requirement One way the SEC ensures that investors know what they are buying is through the registration



As You Read

Predict For what reasons do you think the government tries to regulate certain aspects of business?

Vocabulary You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.



requirement. This requires companies to file a registration statement and a prospectus with the SEC before they offer securities for sale. **The registration statement is a general description of the securities and of the company making the offer. The prospectus is a document that contains a detailed explanation of the stock offering for potential investors.** These documents further prevent the sale of fraudulent securities. A firm caught selling securities without SEC approval can be punished with fines or imprisonment.

Sarbanes-Oxley Act Following a series of corporate failures in the 1990s, Congress passed the Sarbanes-Oxley Act. The Act requires all chief executive officers (CEOs) and chief financial officers (CFOs) to **certify** periodic company reports filed with

the SEC. It prohibits most corporate loans to directors and executive officers. The law also places an affirmative duty on the board of directors to make certain that their company is conforming to all legal requirements.

Antitrust Law

In the nineteenth century a popular way for someone to gain control of several companies was to form a trust. In a trust, the voting power of the stock for all the companies was given to one person, or trustee. Today, this type of trust is usually called a monopoly. **A monopoly is a business situation in which one person, company, or group of companies controls the market for a product or service.** Antitrust laws were created to prevent monopolies.

The Sherman Antitrust Act In 1890 Congress passed the Sherman Antitrust Act, which made monopolies illegal. However, a Supreme Court ruling that said contracts or combinations were illegal only if they formed an “unreasonable restraint of trade” undermined the Sherman Act.

The Clayton Antitrust Act In 1914 Congress passed the Clayton Antitrust Act. The Clayton Act makes specific business practices illegal. For example, a business cannot sell goods to one company for less than the price it charges another company if it harms competition. It also makes it illegal to sell goods on the condition that a buyer cannot buy products from a competitor.

Antitrust In 1911 the Supreme Court ruled that Standard Oil had violated the Sherman Antitrust Act by using devious means to drive its competition out of business.

What did the Supreme Court make Standard Oil do?

Reading Check

Analyze How does the Williams Act control takeover bids to ensure fairness to shareholders?

The Federal Trade Commission Act Congress passed the Federal Trade Commission Act in 1914 to protect businesses from the wrongful acts of other businesses. It allows the courts to determine unfair methods of competition. The act also created the Federal Trade Commission (FTC). The FTC prevents businesses from violating the Federal Trade Commission Act.

The Robinson-Patman Act The Robinson-Patman Act is an amendment to the Clayton Act. It says companies cannot sell goods at lower prices to large purchasers without offering the same discount to smaller purchasers. It also outlaws unfair behavior, such as setting up a delivery schedule that helps one seller but hurts another.

Regulation of Corporate Takeovers

Starting in the 1980s, many large corporations took over smaller corporations in what became known as merger mania. The deals were often valued in the billions of dollars and created huge conglomerates and multinational corporations. As a result, Congress, state legislatures, and the courts became involved in regulating the corporate takeover process.

Federal Regulation The Williams Act strictly controls takeover bids. Under this act, when a suitor offers to acquire more than five percent of a target's stock, the suitor must file a statement with the SEC indicating where the money for the takeover is coming from, why the suitor is purchasing the stock, and how much of the target the suitor owns. The goal is to make certain shareholders know the qualifications and the intentions of the suitor.

State Regulation State legislatures have passed anti-liability statutes to protect corporate directors whose companies are



Prospectus: *n* Latin for *view, outlook*.

Monopoly: *n* From Greek *mono* = one + *polein* = seller: one seller.

Vocabulary Builder The prefix *mono* means one in Greek. List and define five words that begin with this prefix in terms of its meaning. For example, *monochrome* means one color.

Look It Up! Check definitions in *Black's Law Dictionary* or an online glossary. For direct links, go to glencoe.com to find more vocabulary resources.



Case Study - Centex-Winston v. Edward Hines Lumber Co.



Critical Thinking *Is Centex-Winston right in this case? Why or why not?*



Note key facts in the text below and look up words you do not understand. Restate difficult ideas in your own words. Go back and reread the text quickly to make sure you did not miss any important detail. Now, you are ready to formulate an opinion.

Preferential Treatment After being hired to build homes, the Centex-Winston Corporation contracted to purchase lumber, for resale, from Edward Hines Lumber Company. Hines consistently failed to deliver orders on time due to its preferential treatment of several Centex-Winston competitors. Centex-Winston sued Hines, claiming the preferential delivery violated the Robinson-Patman Act.

Centex-Winston v. Edward Hines Lumber Co., 447 F.2d 585 (7th Circuit)



Go to glencoe.com for more case study practice.

involved in takeovers. Several state legislatures have also enacted anti-takeover statutes to discourage suitors from targeting companies within their states.

Judicial Scrutiny Sometimes, a corporation's directors and officers who successfully resist a takeover bid are sued by dissatisfied shareholders who may complain that the suitor's takeover would have been more profitable for them. In such lawsuits, the courts must evaluate the decisions made by the corporation's directors and officers. One question courts must ask is whether the business judgment rule should apply. Recall that the business judgment rule (Chapter 17) presumes a director acts with due care. However, the business judgment rule does not apply if the director acts illegally or if there is a conflict of interest.

Operating a Business Internationally

Several organizations regulate international business dealings. The International Law Commission (ILC) is an agency within the United Nations responsible for the codification of international law dealing with relations among countries. The U.N. Commission on International Trade Law (UNCITL) codifies a set of international laws that regulate international trade among private businesses. The World Trade Organization (WTO) is not a U.N. agency, but a separate international organization that drafts rules dealing with trade among member nations. The WTO tries to limit or remove trade barriers. The rules drafted by all three organizations are enacted in the United States through the treaty process, and if Congress approves the rules, they become valid laws on par with Federal statutes.

After You Read

Summarize List the three major acts passed by Congress to help regulate unfair business practices.

SECTION 18.1 ASSESSMENT

Self Check

1. What is the federal government's authority to regulate business based on?
2. What are securities and what are some examples of them?
3. What is a monopoly?

Academic Connection

English Language Arts

Economist Alan Greenspan argues that the very existence of antitrust laws discourages

businessmen from some activities that might be socially useful out of fear that their business actions will be determined illegal and dismantled by government. In his essay entitled "Antitrust," Greenspan says: "No one will ever know what new products, processes, machines, and cost-saving mergers failed to come into existence, killed by the Sherman Act before they were born. No one can ever compute the price that all of us have paid for that

Act which, by inducing less effective use of capital, has kept our standard of living lower than would otherwise have been possible."

Write a one-to-two-page essay explaining why you agree or disagree with Alan Greenspan.

Critical Thinking

Monopoly Why is it a bad thing if one company controls the entire market for a particular product?



Go to glencoe.com to check your answers.

Reading Guide



Before You Read

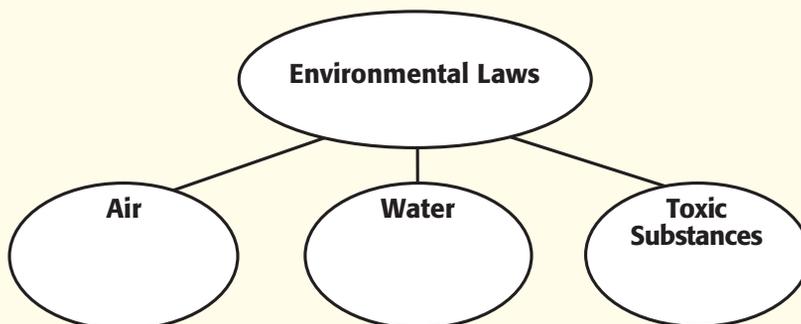
Connect Have you ever noticed days when the sky is brown with smog? Name some of the sources that you think might be responsible for the smog.

Focus on Ideas

To ensure a higher quality of life for its citizens, federal and state governments have passed laws to protect the environment and conserve energy.

Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to glencoe.com to find graphic organizers and tips on how to improve your note-taking skills.



Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- Environmental Protection Agency (EPA)
- Federal Energy Regulatory Commission (FERC)
- Nuclear Regulatory Commission (NRC)



Academic Vocabulary

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- comply
- emissions
- proactive

What You'll Learn

- ◆ Describe the laws that regulate the environment.
- ◆ Identify the federal and state agencies that regulate the environment.
- ◆ Identify the federal and state agencies that are responsible for regulating energy.
- ◆ Describe the impact of international law on energy regulation and conservation.

Why It's Important

If you ever go into business, you need to know that there are environmental and energy laws you have to obey.

Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

Social Studies (NCSS 3) Study people, places, and environments.

English Language Arts (NCTE 7) Conduct research on issues and interests by generating ideas and questions, and by posing problems.

As You Read

Predict When were the first environmental laws created?



Environmental Protection

What does the federal government do to make sure our air and water are not polluted?

In the nineteenth century, the rapid rise of industrialism led to an increase in factory-produced waste which polluted the land, air, and water. The only environmental laws that existed were based on common law, such as nuisance claims. For example, if a farmer had a feed lot that was a nuisance to its neighbors, the matter could be taken to court. By the mid-twentieth century, as the damage caused by industrialization to the environment and human health became apparent, the government recognized the need to pass laws specifically designed to protect the environment (see **Figure 18.1**).

The Environmental Protection Agency

In 1969 Congress passed the National Environmental Policy Act, which established the Environmental Protection Agency. **The Environmental Protection Agency (EPA) is the federal agency responsible for protecting the environment.** It is an independent agency that is a part of the executive branch. The EPA was set up to establish a national policy to combat pollution.

Regulatory Responsibilities The EPA can make regulations involving environmental policies, including laws that deal with air, water, solid waste, toxic substances, and noise pollution. Such regulations must be written in clear and unambiguous language to give fair notice of the regulations to individuals and institutions affected by them.

Research, Administrative, and Support Responsibilities

The EPA can do research, create and administer pollution control guidelines, and support programs designed to make sure that pollution standards are met. The agency can also administer grants to help eliminate pollution under state-run programs.

Enforcement The EPA prefers that businesses voluntarily **comply** with its standards. However, if businesses do not comply, the EPA can bring action against them for polluting the environment, even if the pollution is unintentional.

Current Legislation Congress has continued to increase the EPA's power to deal with new environmental challenges. For instance, the EPA was given the authority to deal with major oil spills using funds provided under the Oil Pollution Act. This allowed the EPA to compel oil storage plants to be built and to fund the development of strategies for dealing with oil-related accidents.

The Clean Air Act

There are actually several Clean Air Acts, each of which was an attempt to improve upon the preceding act. The first clean air act, the Air Pollution Control Act, was passed by Congress in 1955 to provide funds for research into the problems of air pollution. It also recognized that air pollution was a national problem.

Vocabulary You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

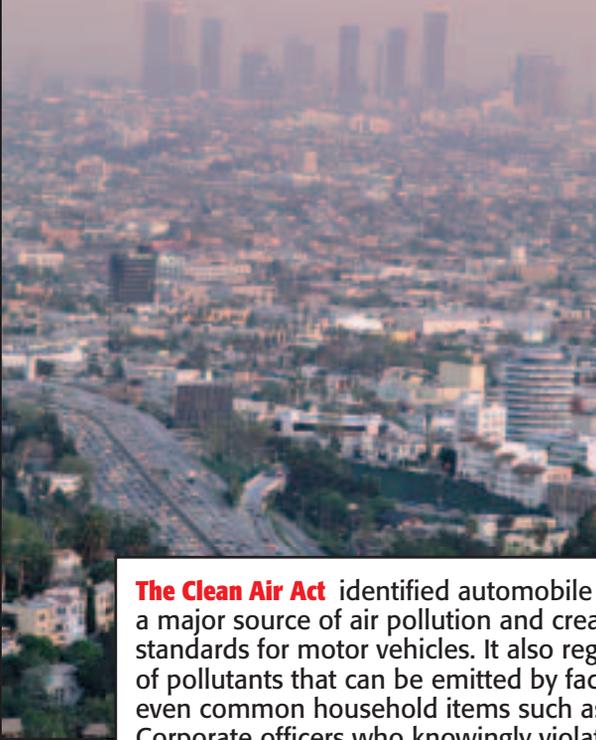
Figure 18.1 Environmental Regulations



The Environmental Protection Agency was created by the federal government in response to the growing public demand for cleaner water, air, and land. The EPA's tasks include repairing the damage already done to the environment, creating guidelines for controlling pollution, and promoting the use of more environmentally friendly sources of green energy, such as wind and solar power.



The purpose of the Clean Water Act is to protect the nation's waterways, wetlands, and drinking water. One of the biggest environmental problems is the illegal or negligent dumping of waste materials into lakes and rivers by mining operations.



The Clean Air Act identified automobile emissions as a major source of air pollution and created emission standards for motor vehicles. It also regulates the level of pollutants that can be emitted by factories and even common household items such as house paints. Corporate officers who knowingly violate the Clean Air Act are subject to criminal penalties, including imprisonment.



 Before laws such as the National Environmental Policy Act were passed, the federal government was not equipped to deal with pollutants that harm human health and the environment. *What are some of the problems businesses have with environmental laws?*



Global Law

Environmental Law in Cambodia

In 1992, the country of Cambodia created a new constitution. Since that time, a system of laws has been created to provide for peaceful resolutions. This system is not too different from the one in the United States and consists of five levels of laws:

- 1 The Constitution
- 2 Laws passed by the National Assembly
- 3 Decrees issued by the Council of Ministers
- 4 Implementing legislation enacted by the Ministries
- 5 Decree Laws, or laws passed before the 1992 Constitution

Constitutional Environmental Protections

Cambodia passed a series of laws to permanently protect the environment. Article 59 of the Constitution states:

The State shall protect the environment and balance of abundant natural resources and establish a precise plan of management of land, water, air, wind, geology, ecologic system, mines, energy, petrol and gas, rocks

and sand, gems, forests and forestial products, wildlife, fish and aquatic resources.

In November 1996, the Cambodian National Assembly passed the Law on Environmental Protection and Natural Resource Management. This law's goals are:

- Reduce and control pollution
- Establish the Environmental Impact Assessment system
- Ensure the sustainable use of resources
- Make the public aware and eager to participate
- Stop activities that are detrimental to the environment

Across Cultures: Civil War

In the 1970s and 1980s, the economy of Cambodia was destroyed by civil war. In the 1990s, however, the economy began to recover as Cambodia began to export rice, rubber, and timber.

Critical Thinking *Should the United States amend the Constitution to provide for environmental protections?*

The Clean Air Act of 1963 The Clean Air Act of 1963 was the first statute passed by Congress to use the words *clean air*. The act set aside funds that state and local programs could use to fight air pollution. The act also identified automobiles as a major source of air pollution and set automobile **emissions** standards.

The Clean Air Acts of 1970 and 1977 The Clean Air Act of 1970 set up the National Ambient Air Quality Standards to further improve air quality. Unfortunately, the standards were difficult, if not impossible, to meet. As a result, the act was amended once again in 1977 to establish more practical guidelines.

The Clean Water Act

The Clean Water Act is also known as the Federal Water Pollution Control Act. It was passed by Congress to guard against water pollution in the United States. The act set up guidelines for dealing with the risks involved in dumping pollutants into the nation's waterways. The act also provides money to help cities develop sewage treatment plants. The act encourages state and national cooperation in the effort to clean up the waterways.

The Toxic Substance Control Act

The Toxic Substance Control Act authorizes the EPA to police the production, use, and importation of industrial chemicals. The act gives the EPA the power to order the assessment of certain chemical agents and to outlaw the development of harmful chemical substances. Under the act, the EPA has authority over the production and use of existing chemical agents and over the introduction and use of newly developed chemical substances.

State Legislation and Regulation

The EPA encourages state and local governments to enforce actions in their own regions. Many states have passed their own state laws and standards to deal with environmental concerns. Massachusetts, for example, has established its own Department of Environmental Protection, which enforces air and water quality standards within the state. California has passed vehicle emissions standards that are stricter than the federal standards.

International Influences on Environmental Regulation

Environmental concerns are among the most serious problems facing the global community today. In response to these problems, the nations of the world have held a variety of international conferences over the last two decades. Some of these conferences have produced protocols or procedures for dealing with these concerns. For instance, a United Nations conference held in Kyoto, Japan, produced a set of protocols for the gradual reduction of greenhouse gases such as carbon dioxide. Many countries have passed the Kyoto Protocol into law; however, the United States has not.



Reading Check
Discuss Can environmental laws be too strict?



 **Solar Energy** The government offers tax breaks to individuals and businesses who install solar panels. *What are some of the advantages and disadvantages of using solar energy?*

Qwest Communications Corp. v. The City of Berkeley

146 F.Supp.2d 1081 (N.D. Cal. 2001)

Qwest Communications Corp. (Qwest) is a telecommunications company authorized to do business in the state of California. The California Public Utilities Commission granted Qwest the power to do public projects using public rights-of-way. In December 1999, Qwest was contracted to provide faster telecommunications, including higher-speed Internet, to the Lawrence Berkeley National Laboratory. To complete the project, Qwest needed to lay new fiber optic cable in the City of Berkeley's right-of-way. The City of Berkeley refused to let Qwest use the right-of-way. Qwest sued to use the right-of-way. Among the reasons Berkeley refused permission was that Qwest had to be certified under the California Environmental Quality Act to create the 4,300-foot trench needed for the cable.

Ruling and Resolution

The Federal District Court in California held that under the California Environmental Quality Act, construction projects must receive certification. A project is defined as any activity that causes direct physical change in the environment. However, the court was not persuaded that a single 4,300-foot trench could be considered a project under the law.

Critical Thinking How detailed should environmental regulations be?

Energy Regulation and Conservation

Why do we need laws to regulate energy?

Up until the early 1970s, Americans were accustomed to a seemingly endless supply of cheap gasoline. Then, in 1973, the oil-producing countries of the Mideast cut off the supply of oil to many nations in the West, including the U.S., creating a major gas shortage. As a result of the 1973 oil crisis, the U.S. government recognized the need to conserve and regulate its energy resources.

Federal Agencies

In 1977, the federal government created the Department of Energy (DOE). Although it was created in 1977, the roots of the DOE go back to World War II and the Manhattan Project, which developed the first nuclear weapons. To control this new form of energy, the government created the Atomic Energy Commission (AEC), the forerunner of the DOE.

The DOE has a dual function. First, the DOE develops and implements a national policy on energy resources. Second, the DOE has responsibility for the nation's nuclear energy program.

The Federal Energy Regulatory Commission (FERC), which is part of the DOE, regulates electricity and natural gas. FERC controls the wholesale price of natural gas and electricity sold for use in interstate (between states) commerce and the interstate transportation of electricity and natural gas. Intrastate (within a state) prices are regulated by state utility agencies. FERC is also responsible for regulating oil pipeline rates.

The Nuclear Regulatory Commission The **Nuclear Regulatory Commission (NRC)**, which is also part of the **DOE, regulates nuclear energy.** It regulates the licensing, constructing, and opening of nuclear power plants. The NRC also handles the possession, use, transportation, and disposal of nuclear material.

State Agencies

Every state in the United States now has an energy office to deal with energy-related concerns. Although the names of these agencies differ, the functions are the same. These functions are to improve energy regulation, to promote energy-efficient technologies, and to reduce the cost of energy development and production. Some states are more **proactive** than others in promoting and financing the development of alternative energy sources, such as solar power, wind power, and hydropower.

International Influences on Energy Regulation

The International Energy Agency (IEA) is the main worldwide group established to research energy conservation. The IEA is made up of 26 nations, including the United States. Originally, the IEA focused on planning for unanticipated oil shortages. Today, it has expanded its scope to include wide-ranging energy issues, including the development of alternate forms of energy and the creation of strategies for dealing with shifts in the Earth's climate.



After You Read

Summarize List the federal acts that deal with clean air and clean water.

SECTION 18.2 ASSESSMENT

Self Check

1. What federal agency is responsible for combating pollution?
2. What was the Federal Energy Regulatory Commission (FERC) created to do?
3. What are the goals of the International Energy Agency (IEA)?

Academic Connection

Social Studies The Resource Conservation and Recovery Act of 1976 (RCRA) gave the EPA the authority to control

hazardous waste from cradle to grave. This includes the generation, transportation, treatment, storage, and disposal of hazardous waste. The RCRA also set forth a framework for the management of non-hazardous wastes. The RCRA was amended in 1986 to enable the EPA to address environmental problems that could result from underground tanks storing petroleum and other hazardous substances. The RCRA focuses only on active and

future facilities and does not address abandoned or historical sites. Read about the Resource Conservation and Recovery Act. Then write an environmental act proposal to address a current environmental issue you are interested in.

Critical Thinking A Matter of Jurisdiction

What is the difference between interstate commerce and intrastate commerce and why is the distinction important?

➔ Go to glencoe.com to check your answers.

Chapter 18 Review and Assessment

Summary

Section 18.1 Corporate Regulations

- ◆ The federal government gets its power to regulate business from the Commerce Clause of the United States Constitution, which gives Congress the power to regulate commerce among the states.
- ◆ Congress passed the Securities Act of 1933 and the Securities Exchange Act of 1934 to protect investors in securities from fraud and unfair practices.
- ◆ Congress has passed a series of antitrust laws to prevent monopolies from controlling the market for a product or service.
- ◆ Congress, state legislatures, and the courts have created various laws to regulate the corporate takeover process.

Section 18.2 Environmental Laws

- ◆ Federal laws passed to protect the environment include the National Environmental Policy Act, the Clean Air Act, the Clean Water Act, and the Toxic Substances Control Act.
- ◆ Many states have created their own state laws and standards to deal with environmental concerns.
- ◆ The Department of Energy (DOE), the Federal Energy Regulatory Commission (FERC), and the Nuclear Regulatory Commission (NRC) were created to develop an energy policy and regulate the energy industry.
- ◆ Every state in the U.S. has an energy office to deal with energy-related concerns, such as improving energy regulation, promoting energy efficient technologies, and reducing the cost of energy development and production.

Vocabulary Builder

1 On a sheet of paper, use each of these terms in a sentence.

Key Terms

- Commerce Clause
- security
- registration statement
- prospectus
- monopoly
- Environmental Protection Agency (EPA)
- Federal Energy Regulatory Commission (FERC)
- Nuclear Regulatory Commission (NRC)

Academic Vocabulary

- commerce
- administer
- certify
- comply
- emissions
- proactive



Go to glencoe.com to play a game and improve your legal vocabulary.

Key Points Review

Answer the following questions. Refer to the chapter for additional reinforcement.

- 2 What is the function of the Securities and Exchange Commission (SEC)?
- 3 Why were antitrust laws created?
- 4 What was the Federal Trade Commission Act designed to do?
- 5 What is the goal of the Williams Act?
- 6 Why did Congress pass the National Environmental Policy Act?
- 7 What does the Toxic Substances Control Act do?
- 8 What is the role of the Department of Energy?
- 9 What is the difference between the Federal Energy Regulatory Commission (FERC) and the Nuclear Regulatory Commission (NRC)?

Standardized Test Practice

- 10 Read the following excerpt about energy law and complete problems 1 and 2.

Within the framework of energy laws, governments establish their policies, rules and regulations concerning ownership, exploitation, development, and use of energy resources within the boundaries of their jurisdiction. Some countries have comprehensive energy laws which regulate resource exploration, development, production, transport, purchase, and distribution of energy for one or more than one energy carrier. Other countries have issued separate laws for each type of fuel governing resource ownership, exploration rights, and trade regulations as well as supply and pricing rules. In most countries, energy supply systems, and electricity supply in particular, remain in the domain of the public sector. Due to the strategic and economic importance of energy, private sector activity in this field also remains highly regulated. However, conventional energy laws typically focus on the development and management of the energy resource and supply side, and do not normally provide specific guidelines concerning energy use or demand management.

1. In most countries, who controls the energy supply systems?

- A government agencies
- B public and private sectors
- C private corporations
- D the public sector

2. Conventional energy laws typically focus on

- A energy use
- B development and management of the energy resource
- C demand management
- D resource ownership

**Test-Taking Strategies**

Always pace yourself when taking a test and avoid spending too much time on a single passage or question.



Apply and Debate

Read the following scenarios. Get together with other students in pairs or groups of three and take a position on each scenario. Debate your position in class with students taking the opposite position or prepare a written argument justifying your position.

11 Downstream Pollution

Country A has a river running through it which flows into Country B. A lumber mill in Country A that makes plywood for needed housing is located on the river. When pollutants from the mill end up in Country B, it demands that it be closed down.

You Debate *Do you think that Country B has a right to ask Country A to close the lumber mill that supplies jobs and housing materials to the people in its country?*

12 Family History

The Jeffersons have owned a manufacturing company for over 100 years. They incorporated it in 2003. Now Merkson Industries is attempting a hostile takeover. But the board chairman, a descendant of the founder, refuses to sell.

You Debate *Do shareholders have a right to insist that the company be sold?*

13 Assessing a Primary Motive

After purchasing Italian eyewear company Ugo, Cambria Eye Glasses, Inc. lost money for years. The shareholders sued when they learned that Cambria's chairman had taken 12 lavish trips to Italy in two years and purchased a villa there.

You Debate *Does the evidence prove that the chairman acted solely in self-interest?*

14 Model Airplanes

Allied, Inc. manufactures model airplanes. Whenever their best customer, Flying Toys, calls to order 1,000 models, Allied ships them in 24 hours. But whenever Rich's Models places its usual 500 model order, Allied says it takes two weeks to ship.

You Debate *Could Rich's Models sue Allied for infringing on the Robinson-Patman Act guaranteeing them equal service?*

15 Grocery Store Fireplace

Dick Heeley has owned a cozy grocery store in Vermont for ten years. In the winter, hundreds of neighbors come in to sit by the wood-burning stove to chat. One day, a town resident complains to Dick that the stove pollutes the air. She insists that he halt its usage.

You Debate *Should the owner stop using the wood-burning stove?*



**Case Study Practice – Community Group v. City of San Diego**

16 Exempt from Environmental Laws? Developers in San Diego wanted to construct a 14-unit residential building with an underground parking garage. The site of the project was a 10,247-square-foot vacant lot. Across the street is Balboa Park, an 1,100-acre urban park that contains theaters, museums, restaurants, and other public facilities.

In January 2004, the City of San Diego issued a building permit for the parking garage. Banker's Hill, Hillcrest, Park West Community Preservation Group (Community Group) filed a petition to stop the construction project. The Community Group argued that the developers had not obtained an environmental review as required under California Environmental Quality Act (CEQA). Under CEQA, developers can be exempt from CEQA, if the project qualifies as urban in-fill. Urban in-fill is defined as an area that: is surrounded by urban structures; has no value to endangered species; would not result in significant traffic or noise; and would be adequately serviced by already installed utilities.

Source: Banker's Hill, Hillcrest, Park West Community Preservation Group v. City of San Diego, 2006 WL 1216918 (Cal. Ct. App. 2006)

Practice Can the City exempt the project from CEQA?

17 Ethics Application

Who Is Responsible? Margaret works for a furniture refinishing company. She notices that the chemicals used in the process are rinsed into the floor drains, which flow into the city's sewer system. She tells her boss he should dispose of the chemicals in a safe manner. He tells her that it is too costly, and the chemicals are not that dangerous.

- ◆ Does Margaret have an ethical duty to report the problem to the Environmental Protection Agency, or is it the responsibility of her boss or the company?

18 Internet Application

Find out about the Clean Air Act Five factories in your town have gigantic smokestacks and are clearly polluting the air. You and your friends want to find out what you can do about this.



Go to glencoe.com and research the Clean Air Act of 1970 and its amendments to find out what businesses are required to do. Research the steps that a community can take to encourage or force businesses to clean up their emissions.



Reading Connection

Outside Reading Go to glencoe.com for a list of outside reading suggestions about environmental laws.

Cyberlaw and E-Commerce

BusinessWeek News

E-Gold: Losing More Shine

By Brian Grow

Gold & Silver Reserve's tangle with the U.S. government is deepening. The company operates a bullion-backed "digital currency" unit called e-gold that U.S. law enforcement officials say has become a popular payment system for online criminals. On December 16, agents from the U.S. Secret Service and FBI raided Gold & Silver Reserve's offices in Melbourne, Fla., and took copies of documents and computer files. Now the U.S. Justice Department is demanding that the company forfeit more than \$800,000 in two of its bank accounts. The funds were seized on December 15 by the Secret Service, which declined to comment, citing ongoing investigations being conducted with the FBI.

Law enforcement officials worry that digital currency is becoming the money-laundering machine of choice for cybercriminals. At least a dozen such services allow users to deposit and transfer funds. Eight, including e-gold, claim to be backed by actual bullion.

Flex Your Reading

Efficient critical reading involves being flexible with speed and comprehension. There are several ways of reading critically, and you need to fit a reading style to your needs and to the material.



Go to glencoe.com for Flex Your Reading activities, more information on reading strategies for this chapter, and guided practice in reading about e-commerce and cybercrime.





Internet Insecurity The Internet has made doing business much faster and easier but has also brought with it the risk of Internet fraud and identity theft. *What are some of the things you can do to protect yourself online?*

What You'll Learn

- ◆ Explain the nature of a cybercrime.
- ◆ List different types of cybercrimes.
- ◆ Describe the nature of a cybertort.
- ◆ Distinguish between cyberdefamation and cyberinvasion of privacy.

Why It's Important

Learning how the law deals with computer-related crimes and torts will help you keep up with new technology.

Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

Social Studies (NCSS 9)
Study global connections and interdependence.

English Language Arts (NCTE 8) Use a variety of technological and information resources to gather and synthesize information and to create and communicate knowledge.

Reading Guide**Before You Read**

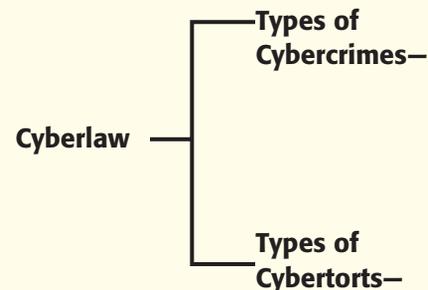
Connect If you have ever received an e-mail with a virus in it, you know what cybercrime is. What are some cybercrimes that you have experienced?

Focus on Ideas

Technology has created new areas of law to prosecute criminals who use computers to commit crimes.

Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to glencoe.com to find graphic organizers and tips on how to improve your note-taking skills.

**Key Terms**

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- cyberlaw
- cybercrime
- cybertrespass
- cyberspoofing
- cyberpiracy
- cyberblackmail
- identity theft
- cybervandalism
- cybertort
- cyberdefamation
- cyberinvasion of privacy

**Academic Vocabulary**

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- simulate
- infrastructure
- sabotage

The Development of Cyberlaw

Are there laws that control your use of a computer?

The interaction of the law and the world of computers is so new that new words have had to be invented. The field is now called cyberlaw. **Cyberlaw is the area of the law which concerns computers and computer-related crimes.** Some people also call it computer law, electronic law, or e-law. Cyberlaw merges concepts, doctrines, and principles from many legal fields—criminal law, tort law, intellectual property law, and contract law—and puts them into the context of computers. Cyberlaw is intended to deal with cybercrimes. A **cybercrime is any criminal activity associated with a computer.** Legal experts at the federal and state levels have developed two approaches for creating cyberlaws to deal with the new area of cybercrime.

The Cybertrespass Approach

Some states have dealt with the problem of covering cybercrimes by adding cybertrespass statutes to the traditional criminal code. **Cybertrespass, or computer trespass, is any illegal activity already in the criminal code committed by using a computer.** Under the cybertrespass approach, states do not define each individual cybercrime.

Rewriting of Criminal Code

Some state legislatures have dealt with cybercrime by writing individual statutes for every crime that can possibly be committed by using a computer. This approach is difficult because every new statute must be individually created. Some state legislators prefer this approach because criminal law statutes must be very specific



As You Read

Predict How does the government keep our laws current with new technology that is used to commit crimes?



Czech Investments

As a recent immigrant to the United States from the Czech Republic, you are trying to start a new life as a business owner. Back in the Czech Republic, you owned and operated a successful stock brokerage firm. Since moving to the U.S., you have realized that many people are interested in investing in Czech companies. The easiest thing for you to do is to set up an Internet investment company that would link American investors with the Czech stock market. U.S. law limits promoting stock for sale on the Internet, but Czech law does not. You want to send mass e-mails out to a lot of people promoting your new service.

Critical Thinking: *What kinds of issues should you be concerned about in using the Internet to link American investors with the Czech stock market?*



Trespass: *v* Unlawful act committed against a person or person's property. From Latin *trans* = beyond + *passer* = pass.

Extort: *v* To obtain from a person by force. From Latin *ex* = out + *tort* = twist: to twist out.

Vocabulary Builder List and define three words each that begin with the prefix *ex* and the prefix *trans*.

Look It Up! Check definitions in *Black's Law Dictionary* or an online glossary. For direct links, go to glencoe.com to find more vocabulary resources.

Vocabulary You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

Reading Check

Differentiate What is the difference between cyberpiracy and cyberspoofing?

in detailing an outlawed behavior. Otherwise, when the statute is used to prosecute a cyberdefendant, the court might decide that the statute is void because it is too vague.

Cybercrimes

What kinds of crimes can be committed using computers?

Cybercrimes include both crimes directed at people using a computer and crimes directed at other computers.

Cyberspoofing

Cyberspoofing is a crime in which a cybercriminal falsely adopts the identity of another computer user or creates a false identity on a computer Web site in order to commit fraud. One of the most common types of cyberspoofing is called *phishing*. This involves creating a phony Web site that **simulates** a real bank, credit card agency, or retail store. The criminals then broadcast false e-mails in the name of the business with a link to the phony Web site. They attempt to lure people into believing the Web site is real and attempt to obtain from the victims their private information such as credit card and bank account numbers, personal ID numbers (PINs), and passwords.

Cyberspoofers also use online auction sites, such as eBay, to deceive legitimate buyers. They pretend to have goods for sale that they do not actually have. After the consumers purchase the goods, the criminals pocket the money and do not deliver any goods.

Cyberpiracy

Cyberpiracy is a crime that involves using a computer to steal computer data stored in a digital format. Cyberpiracy often involves the theft of intellectual property, such as downloading software programs or transmitting them to others without payment or permission. To combat this, Congress passed the Digital Millennium Copyright Act (DMCA). The DMCA makes it illegal to pirate copyrighted computer programs using methods that bypass software copyright protection systems. The penalties for violating the DMCA are very severe, reaching as high as ten years in prison for second time offenders. The DMCA also allows individual plaintiffs to bring civil lawsuits against cyberpirates who violate its provisions.

Cyberblackmail

Cyberblackmail, sometimes called **cyberextortion**, is the use of information unlawfully obtained by computer to pressure a victim into granting a payoff to the blackmailer. Generally, the criminal threatens to reveal some sort of illegal or embarrassing conduct gathered about the person. Computer users who spend time in chat rooms are especially vulnerable to this type of crime. The cyberblackmailer often befriends a person, learns damaging information, then uses it to extort money from the victim.

Identity Theft

Identity theft is using a computer to steal financial, employment, educational, medical, and personal data.

Identity thieves attempt to obtain credit card numbers, financial data, passwords, PINs, Social Security numbers, and access codes. They then use the data to empty bank accounts, run up credit card bills, steal cash, and generally disrupt the target's personal life. It is important to be aware of all activity on your accounts to prevent identity theft because once your identity is stolen it can take years to fix the problem.



Cyberterrorism

Cyberterrorism is committed when someone operating a computer disrupts part of the national electronic **infrastructure**. This includes power grids, the air traffic control system, and the national defense system, among others. It also includes disrupting corporate computer systems, such as banks, brokerages, and telecommunications.

Cyber vandalism

Cyber vandalism is disrupting, damaging, or destroying a Web site or computer network. Cyber vandals, also called hackers, might attack a business or government computer system as an act of **sabotage** or revenge. Although many people commit cyber vandalism as a prank, to gain attention, or to show off, cyber vandalism is still a crime and cyber vandals are criminals.

Cybergerm Warfare

Cybergerm warfare involves transmitting computer viruses to people to destroy their computer system or files. Like cyber vandals, perpetrators transmit viruses as a prank or to show off, but others use viruses intentionally to commit crimes, such as cyberterrorism or cyber vandalism. Firewalls and anti-virus software can block many viruses.

Cybertorts

What is the difference between a tort and a cybertort?

A tort is a private wrong committed by one person against another. A **cybertort** is the invasion, theft, falsification, misuse, or deletion of data stored in a computer to commit a tort. The two most common cybertorts are cyberdefamation and cyberinvasion of privacy.

 **Cybercrime** The advent of computer technology and the Internet created new ways of communicating and doing business. Unfortunately, it also created new opportunities for criminals. *What crimes have computers and the Internet made it much easier to commit?*

Cyberdefamation

Cyberdefamation is the communication via computer or other electronic device of false data that damages a person's reputation. Cyberdefamation may involve sending out e-mails or text messages that contain false information about a company that ruins its name in the public. Congress recently passed the Communications Decency Act (CDA) that protects Internet Service Providers (ISPs) from being held liable for any cyberdefamation performed by users on these services.

Cyberinvasion of Privacy

Cyberinvasion of privacy is an unwelcome intrusion into the private matters of an individual carried out or sustained by a computer. Cyberinvasion of privacy often involves employees who, because of their jobs, work closely with confidential files, such as medical records, financial records, scholastic records, and employment records.

The government has passed several laws to protect the privacy of individuals and their computer records. The Fair Credit Reporting Act protects records kept by credit bureaus. The law says that credit bureaus must tell people about their files and must send corrections to anyone who might have been misled by false reports. The Right to Financial Privacy Act states that financial institutions cannot open customer records to a government official without the customer's permission, unless there is a court order. The Electronic Communications Privacy Act restricts the unauthorized access of e-mail and instant messaging. However, employers can monitor the e-mail transmissions of employees if the employees consent to it.

After You Read

Summarize List the four types of crimes in which the computer is the victim.



SECTION 19.1 ASSESSMENT

Self Check

1. What is a cybercrime?
2. What is a cybertort?
3. What is the difference between cyberdefamation and cyberinvasion of privacy?

Academic Connection

English Language Arts

You are a small business owner who conducts business internationally via the Internet. You are

concerned that this may expose your computer system to cybervandalism and cybergerm warfare. To combat this, you wish to upgrade your anti-virus software. Research three brands of anti-virus software, such as Norton and EZAntivirus. Create a chart comparing and contrasting the various features offered by each brand and determine which product best suits your needs. Write a brief report stating your

reasons for choosing this software application.

Critical Thinking Cyberterrorism

Since 9/11 the federal government has become much more involved in combating the threat of cyberterrorism. What are some of the concerns about what cyberterrorists could do?



Go to glencoe.com to check your answers.

Reading Guide



Before You Read

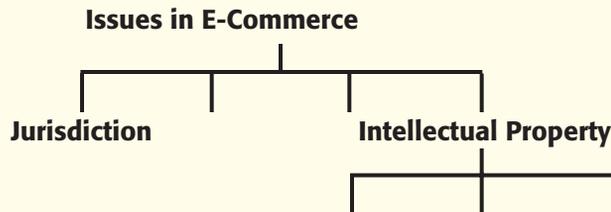
Connect What are some of the problems with doing business over the Internet you do not usually have doing business face-to-face, by phone, or by mail?

Focus on Ideas

The government has been very careful to balance the rights of the Internet buyer with those of the Internet seller.

Take Notes

Create a graph like the one shown and use it to take notes as you read this section. Go to glencoe.com to find graphic organizers and tips on how to improve your note-taking skills.



Key Terms

You will learn these legal words and expressions in this chapter. You can also find these terms in *Black's Law Dictionary* or in an online legal dictionary.

- e-commerce
- digital signature
- domain name



Academic Vocabulary

You will find these words in your readings and in your tests. Look them up in a dictionary and familiarize yourself with them.

- tangible
- broadcast
- duplicate

What You'll Learn

- ◆ Explain intellectual property and copyright for digital products.
- ◆ Explain the importance of trademarks.
- ◆ Identify the characteristics of a patentable invention.
- ◆ Recognize two unsettled issues in e-commerce law.
- ◆ Explain new laws regarding digital signatures and documents.

Why It's Important

Knowing the laws that affect e-commerce will help you whenever you download music or movies, or buy goods on the Internet.

Academic Standards

Reading and completing the activities in this section will help you practice the following academic standards:

Math (NCTM NOS 2)
Understand meanings of operations and how they relate to one another.

Social Studies (NCSS 8)
Study relationships among science, technology, and society.

As You Read

Predict Can a software program be copyrighted just like a book or song?



E-Commerce Laws

How does e-commerce save you time?

E-commerce, short for electronic commerce, is the process of conducting business using electronic means, especially the Internet. E-commerce includes purchasing products by using electronic credit or debit cards, extracting money from a checking account at the local ATM, and transferring funds electronically between financial institutions. These new electronic forms of business have raised jurisdictional issues, taxation issues, and authentication problems, as well as intellectual property rights issues (see **Figure 19.1**).

Jurisdictional Issues

Doing business over the Internet raises the question of which state has jurisdiction in a case when the user or buyer does not reside in the same state as the seller. The courts have recognized two principles on this matter:

- Just because a Web site can be accessed in a state does not, by itself, give jurisdiction to that state.
- A state may gain jurisdiction over an e-commerce transaction when a Web site allows users to purchase merchandise on that site. The merchandiser Amazon.com is an example. In such cases, the state in which the buyer resides has jurisdiction, even though the physical home of the seller is another state.

Tax Issues

The jurisdictional issue above is important because it plays a role in determining which state has the right to tax Internet sites that sell goods. The courts have ruled that sellers who do not have a store, office, or wholesale shop within a state cannot be taxed by that state. However, the buyer may be taxed at the buyer's location, such as a sales tax. At this time, Internet sales are governed by the Internet Tax Freedom Act.

Authentication Issues and the E-Sign Act

One difficulty with buying and selling on the Internet is making certain that the buyer and the seller really are who they claim to be. This is referred to as authentication. To manage this problem, Congress passed the E-sign Act, a short name for the Electronic Signatures in Global and National Commerce Act. This act ensures that any cybercontract is considered as legal as a paper equivalent if the parties have agreed to use digital signatures. A **digital signature is an encoded message that appears at the end of a contract created online**. The signature can be verified by a confidential password, by a special smart card, or by electronic equipment that can identify a person by scanning his or her fingerprints or retina.

WebQuest

E-Commerce and Computer Law

The world of e-commerce has quickly evolved in the last ten years. Log on to glencoe.com to see what types of regulations are being created to protect consumers.

List and explain three regulations you find in your WebQuest folder to share with your class.



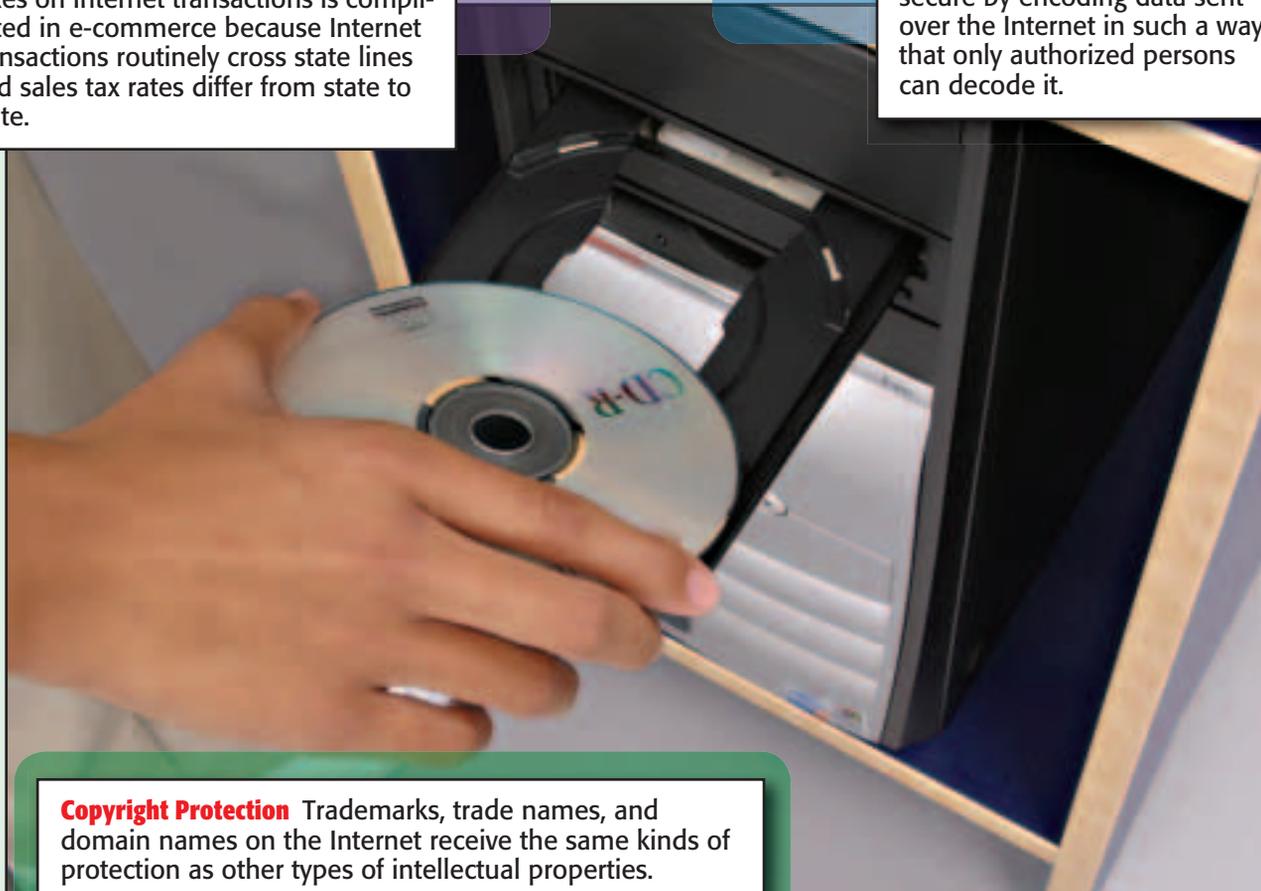
Figure 19.1 Issues in Cyberlaw



Taxation Charging and collecting sales taxes on Internet transactions is complicated in e-commerce because Internet transactions routinely cross state lines and sales tax rates differ from state to state.

A screenshot of a user login form titled "View Your Accounts". It includes the text "Log in to your account online:" followed by "User Name:" and a text input field containing "Enter user name". Below that is "Password:" and another text input field. There are two links: "Forgot password?" and "New user sign up". A red "GO" button is next to the "Forgot password?" link. At the bottom, there is a lock icon and the text "Why this is secure".

Internet Security Encryption makes Internet transactions secure by encoding data sent over the Internet in such a way that only authorized persons can decode it.



Copyright Protection Trademarks, trade names, and domain names on the Internet receive the same kinds of protection as other types of intellectual properties.

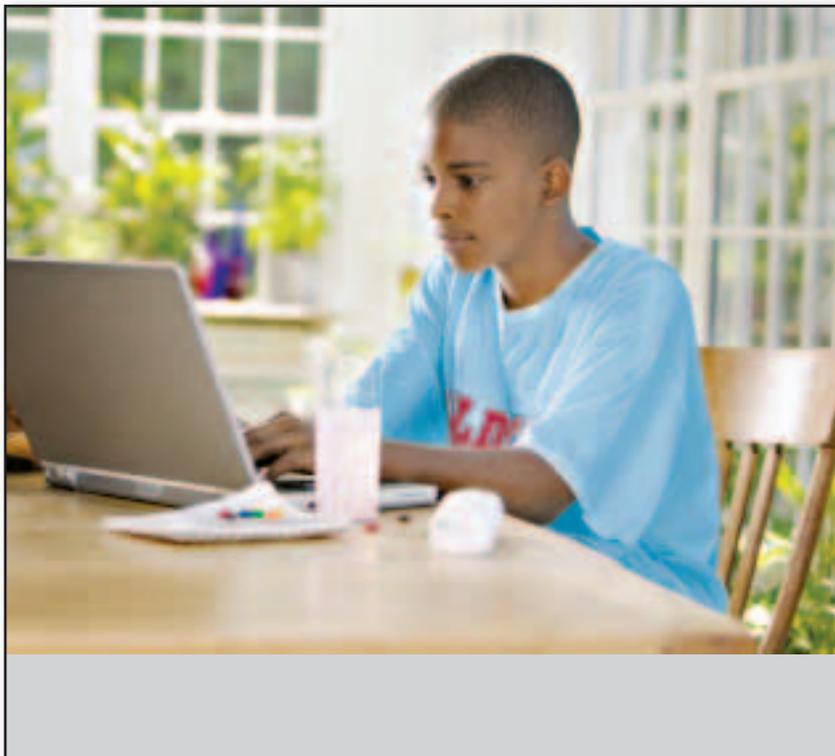
 E-commerce has made it easy for someone in Texas to buy something from a company in New York without ever leaving his or her chair, but it has raised questions regarding issues such as jurisdiction, security, and taxation. *What does a cybercontract require to be considered completely legal?*

Reading Check

Analyze How can an author or songwriter keep track of whether people are illegally copying their works on the Internet?

Vocabulary You can find vocabulary definitions in the **Key Terms** glossary and **Academic Vocabulary** glossary in the back of this book.

Electronic Copying Federal laws have given computer programs the same copyright protection as literary works and made it illegal to make electronic duplicates of them. *What exceptions are there to the law?*



Cyberlaw and Intellectual Property

Is there any way to protect intellectual property on the Internet?

Another new legal area is cyberprotection law. This involves laws that protect people and businesses that create or invent any of the following:

- products that can be distributed digitally using computers, such as music and movies
- new computer products and inventions, such as hardware devices
- products that use or work with computers, such as software

New cyberprotection laws have been created in three areas: copyrights, trademarks, and patents. These types of laws allow writers, artists, inventors, and businesses to protect their ideas, products, and trade names from having other people imitate, copy, use, or sell them without permission and/or payment.

Copyrights

A copyright is a legal protection that has been available in the United States for literary, artistic, and scientific works since 1790. Under the federal Copyright Act, the originator of a work in a “fixed **tangible** medium of expression” is granted the exclusive authority to publish, reproduce, and sell his or her work. The Computer Software Copyright Act of 1980 added computer software programs to the types of work to which copyright protection can be extended.

Copyrighting a work is done by registering it at the Copyright Office in Washington, D.C., although a formal registration is no longer required to obtain protection. As soon as a work exists in tangible form, the owner is protected. A copyright extends for the creator’s life plus 70 years. If the originator is a corporation, the copyright lasts 120 years from when it was first written or 95 years from its first publication. After the copyright period is over, the work goes into the public domain where it may be copied by others.

Another new area of copyright law concerns the **broadcast** of artistic works over the Internet. Millions of computer users can get free access to a protected literary or artistic work if just one person illegally publishes it on a Web site. As a result, Congress passed the No Electronic Theft Act (NET Act) in 1997. This statute provides prison terms and fines for anyone



Case Study – Medical Supply Chain, Inc. v. General Electric Co.



Critical Thinking *Can a corporation be sued for antitrust violations when the actions involve an Internet company it invested in?*



Your Reading

Note key facts in the text below and look up words you do not understand. Restate difficult ideas in your own words. Go back and reread the text quickly to make sure you did not miss any important detail. Now, you are ready to formulate an opinion.

Antitrust Violations? Medical Supply Chain, Inc. (MSC) provided an e-commerce marketplace for suppliers and purchasers of hospital supplies. Its two main competitors, Neoforma and GHX, controlled 80 percent of the hospital supply market. MSC looked for a location for its commercial offices and found a place in Blue Springs, Missouri. The office space, however, was already leased to GE Transportation Systems Global Signaling, LLC, a subsidiary of General Electric Co. (GE). MSC decided to buy the whole building. It sought financing from GE Capital Business Asset Funding Corporation (GE Capital), another GE subsidiary.

Everything seemed to be going fine, until GE Capital refused to provide financing to MSC. MSC discovered that GE was an investor in GHX and sued GE for antitrust violations. MSC argued that GE was trying to create or maintain a monopoly in hospital supply e-commerce by refusing to provide financing to MSC, thus preventing MSC from becoming a competitor of GHX.

Medical Supply Chain, Inc. v. General Electric Co., 144 Fed.Appx. 708 (10th Cir. 2005)



Go to glencoe.com for more case study practice.

who creates an electronic **duplicate** of a copyrighted work for commercial profit or private financial gain. The Digital Millennium Copyright Act (DMCA) also outlaws pirated copies of software made by disabling the internal protection system of the software.

Trademarks and Domain Names

A trademark is a distinctive name, word, symbol, image or slogan used by a business to identify and distinguish its goods from products sold by others. Trademarks are registered with the United States Patent and Trademark Office in Washington, D.C. Many hardware and software companies trademark their name and the name of their products.

A **domain name** is the Internet address of a business.

Domain name disputes arise when one party has registered a domain name that uses a famous person's name, a trademark, or a trade name that is registered by another user. In some cases, cybersquatters register a person's name, a trademark, or a trade name as a domain name with no intent to actually use it. Instead, the cybersquatter holds on to the name until the real holder of the name, the trademark, or the trade name appears to claim the name.



Global Law

Internet Privacy Laws in Taiwan

In 1995, the Taiwanese legislature passed the Computer-Processed Personal Data Protection Law 1995. This law covers the privacy of information collected over the Internet.

Who the Law Covers

The law only applies to the public sector and some industries within the private sector. The private sector categories only include:

- credit information organizations
- hospitals
- schools
- telecommunications businesses
- bank and financial institutions
- securities businesses
- insurance companies
- mass communications

Government Regulation

The law provides regulations for the transmission of private information from Taiwan to other

locations in the world. There are four reasons the government can block a transmission:

- 1 to protect Taiwan's national interest
- 2 where an international treaty or agreement prohibits the transfer
- 3 where the receiving country lacks sufficient laws or regulation to protect personal information
- 4 the indirect transmission of information to a third country to get around Taiwan's laws

Across Cultures: Convenience Store Culture

Taiwan boasts more convenience stores per person than any other country. There are over 8,000 convenience stores in Taiwan. Because they are so prevalent, the stores provide a number of services, such as collection of parking fees, utility bills, and credit card payments. Eighty percent of Taiwan's urban population visits a convenience store weekly.

Critical Thinking *How much should the government do to control private information sent over the Internet?*

The cybersquatter then asks for an enormous amount of money to sell the name back to the real owner.

To deal with this tactic, Congress passed the Anticybersquatting Consumer Protection Act. The object of the act is to provide a shield for the real owners of trademarks and trade names.

Patents

A patent is a property right that inventors can acquire to protect their right to make, use, and sell their inventions for a number of years as set by law. In order for an invention to be patentable, it must meet three requirements. The invention must fit within the statute as "patentable subject matter." The invention must consist of some nonobvious, new, and useful feature. The application designed for the invention must be so specific that, from its detail, the invention could be reproduced by experts in the field.

For many years, lawmakers debated whether stand-alone computer programs were patentable. Once lawmakers determined that software programs are indeed a process, or a means of doing something, they agreed that they qualify as patentable subject matter. Another software programmer must invent a different way to do the same thing as the one who owns the patent.

The patent application process requires documenting in detail the plans, structure, and operation of the invention. The document is then filed at the United States Patent and Trademark Office. If approved, the inventor is given a number that must be placed on the invention along with the word *patent* or the abbreviation *pat.*

Cybercontract Law

What is the difference between a contract and a cybercontract?

Cybercontract law deals with the buying and selling of computers and computer programs. One area of cybercontracts involves the sale of custom-programmed software. For example, a company might hire a programmer to come to its business to develop a new program. The legal issue in this matter is the question of who owns the source code, which is the actual code behind the software.

The Uniform Computer Information Transactions Act

The Uniform Computer Information Transactions Act (UCITA) governs the law for cybercontracts such as software agreements and licenses, software formulation contracts, and software maintenance contracts. Once the parties to a cybercontract have entered an agreement using electronic means, the agreement will be just as binding as a similar one negotiated outside of the Web. The UCITA is a default statute, which means that the parties can use it to resolve any issues not covered by their own contracts.



After You Read

Summarize List three issues of law that e-commerce has raised.

SECTION 19.2 ASSESSMENT

Self Check

1. What kinds of products and property do cyber-protection laws cover?
2. What is a domain name dispute?
3. What is the purpose of the No Electronic Theft Act?

Academic Connection

Mathematics Appleton Wholesale Grocers, Inc. plans to construct a new building at a cost of \$875,000 to house the new computer installation.

Appleton hires an architect, a systems analyst, and a computer programmer. The architect charges seven percent of the total cost of the building. The system analyst charges a flat fee of \$6,000. The computer programmer charges \$30 an hour and works 150 hours. What is the total cost of the professional services?

CONCEPT **Number and Operations:** To calculate the total cost of professional services, find the sum of consultants' fees using the formula:

$(\text{Cost of Building} \times 7\%) + \text{Systems Analyst Fee} + (\text{Computer Programmer Rate} \times \text{Total Hours})$



For more math practice, go to the Math Appendix.

Critical Thinking The Future of Cyberlaw

What are some of the legal challenges you can imagine facing lawmakers in the future?



Go to glencoe.com to check your answers.

Chapter 19 Review and Assessment

Summary

Section 19.1 Cyberlaw and Cybercrime

- ◆ Cyberlaw is the area of the law which concerns computers and computer-related crimes.
- ◆ A cybercrime is any criminal activity associated with a computer.
- ◆ Some states have dealt with cybercrimes by adding cybertrespass statutes to the traditional criminal code.
- ◆ Some states have dealt with cybercrimes by writing individual statutes for every crime that can be committed by using a computer.
- ◆ Cybercrimes include cyberblackmail, cyberspoofing, cyberpiracy, cyberterrorism, identity theft, cybervandalism, and cybergerm warfare.
- ◆ Cybertorts include cyberdefamation and cyberinvasion of privacy.

Section 19.2 Internet Transactions

- ◆ E-commerce is the process of conducting business using electronic means, especially the Internet.
- ◆ E-commerce has raised jurisdictional issues, taxation issues, and authentication problems.
- ◆ Cyberprotection laws protect intellectual property that can be distributed using computers, new computer products and inventions, and products that use or work with computers.
- ◆ No Electronic Theft Act provides prison terms and fines for anyone who creates an electronic duplicate of a copyrighted work for commercial profit or private financial gain.
- ◆ The Uniform Computer Information Transactions Act (UCITA) governs software agreements and licenses, software formulation contracts, and software maintenance contracts.

Vocabulary Builder

1 On a sheet of paper, use each of these terms in a sentence.

Key Terms

- cyberlaw
- cybercrime
- cybertrespass
- cyberspoofing
- cyberpiracy
- cyberblackmail
- identity theft
- cybervandalism
- cybertort
- cyberdefamation
- cyberinvasion of privacy
- e-commerce
- digital signature
- domain name

Academic Vocabulary

- simulate
- sabotage
- broadcast
- infrastructure
- tangible
- duplicate



Go to glencoe.com to play a game and improve your legal vocabulary.

Key Points Review

Answer the following questions. Refer to the chapter for additional reinforcement.

- 2 What two approaches have states used to cover cybercrimes?
- 3 What is cyberspoofing?
- 4 How do identity thieves work?
- 5 What is a cybertort?
- 6 What are the two principles courts use to decide jurisdiction in e-commerce sales?
- 7 What is a digital signature and how can it be verified?
- 8 What did the Computer Software Copyright Act of 1980 do?
- 9 What is the purpose of the Anticybersquatting Consumer Protection Act?

Standardized Test Practice

- 10 Read the following excerpt about efforts to combat cybercrime internationally and complete questions 1 and 2.

In May 2006, representatives of the Group of Eight (G8) industrialized nations, including France, Japan, and the U.S., met in Paris and agreed to boost cooperation to fight cybercrime. Participants there confirmed their support of the France-based Council of Europe's efforts to finalize a Convention on Cybercrime, which will be the first international treaty to deal with the different forms of criminal activity in cyberspace. The treaty would require countries to approve and enforce laws regarding interception of data, interference with computer systems, fraud, and forgery via the Internet. It also requires them to provide national law enforcement with the authority to carry out computer searches and seizures of computer data. "Everyone realizes that we are at a point where business is in transition, technology is in transition, and there is a legal transition as well," says Randy Picker, a law professor at the University of Chicago. "The reality is, the legal clock is a lot slower than the business or technology clock."

1. The first international treaty to deal with cybercrime will allow:

- A the G8 to represent the world in technology
- B laws to meet the needs of technology
- C methods to deal with cyberspace crimes
- D ability to search and seize computer data

2. The treaty would require countries to approve and enforce laws regarding:

- A fraud, forgery, interception of computer data, and overuse of the Internet
- B forgery, interception of data, fraud, and computer system interference
- C search and seizures, computer data, fraud, forgery, and cyberspace
- D cybercrime, technology, forgery, fraud, and computer system interference



Test-Taking Strategies

Do not cram the night before a test. Plan to get a full eight hours of sleep.



Apply and Debate

Read the following scenarios. Get together with other students in pairs or groups of three and take a position on each scenario. Debate your position in class with students taking the opposite position or prepare a written argument justifying your position.

11 Computer Hacker Dilemma

A computer hacker, Raoul, broke into computer systems at several businesses for fun. He did not do any damage, but he was caught and put on probation. After a year, he was hired to work at a computer security firm helping to stop hackers.

You Debate *Does it send the wrong message to computer hackers that they can get good jobs after committing crimes?*

12 Web Site with Music

Tina is a candle maker and sells her candles on a Web site. The site also contains photos of famous celebrities and the caption: "These stars would love my candles." Tina found the photos on the Internet.

You Debate *Is it fair that Tina uses photos of famous people to help sell her products?*

13 Online Purchase Fairness

To avoid paying sales tax, Jack buys his big purchases online from sellers located outside his state. Jack's friend's TV store loses sales because it must charge sales tax.

You Debate *Is it fair that some Internet-based companies are able to avoid charging sales tax when local stores must charge it?*

14 A Smart Programmer

Nick is a programmer. A company hired him to develop software that translates Web sites into French. While doing this, he also figured out how to translate the Web sites into Italian, German, and Russian. Nick claims he owns the extra programs.

You Debate *Do you think programmers own the rights to software programs they create that go beyond what they were hired to do?*

15 Fake Internet Order?

Juicy Oranges, Inc. received an e-mail from Alison Adams providing her credit card number and ordering five crates of oranges, worth \$272. When the shipment was delivered, Alison claimed she never sent the e-mail and refused to pay.

You Debate *If you were the judge in this case, would you rule in favor of Alison or Juicy Oranges, Inc.?*



**Case Study Practice –****See, Inc. v.
Imago Eyewear Party, Ltd.**

16 Does the Court Have Jurisdiction? See, Inc. is an American corporation that sells eyewear over the Internet on its Web site, seeeyewear.com, which it registered as a domain name in 1998. See, Inc. owns federal trademarks on SEE and SEE SELECTIVE EYEWEAR ELEMENTS. See, Inc. has also filed for a trademark on SEE EYEWEAR.

The Defendant, Imago Eyewear Party, Ltd., is an Australian company that also sells eyewear over the Internet. Imago uses the Web site “seeeyewear.com” to sell its products. This Web site domain name was registered in 2002. Imago has filed for a United States trademark on SEEYEWEAR. See, Inc. sued Imago Eyewear in Michigan Federal Court. See, Inc. claimed that Imago, by using the Web site seeeyewear.com, had violated Federal trademark law and Michigan’s unfair trade practices statutes.

Imago argued that there is no jurisdiction for See, Inc. to sue in Michigan. Imago argued that See, Inc. is an Australian corporation and that, although Michigan residents can access its Web site on the Internet, no Michigan resident has ever contacted See, Inc. via its Web site. Therefore, a U.S. Court does not have jurisdiction to hear this case.

Source: See, Inc. v. Imago Eyewear Party, Ltd., 167 Fed.Appx. 518 (6th Cir. 2006)

Practice Can See, Inc. sue Imago Eyewear in Michigan?

17 Ethics Application

Is It Ever Okay to Copy CDs? Five students from your school who graduated two years ago are in a band. They just cut a CD and began selling it. You love the music and buy a copy. Your two closest friends also love the music and ask you to make copies of the CD for them.

- ◆ Is it ethical for you to copy this CD and give it to other people? Explain your position.

18 Internet Application

Copyrighting Your Novel You have decided to write a novel. You learn that it is now easy to publish a book on your own, but you want to protect your copyright. You plan to sell both a print edition of the book and also an electronic book (e-book) that you will sell from your Web site.



Go to glencoe.com to research copyright law. Find out what you must do as an author to copyright your book and protect it in both print form and on the Internet.



Reading Connection

Outside Reading Go to glencoe.com for a list of outside reading suggestions about cyberlaw and e-commerce.

Patrick A. McNutt

Antitrust Consultant



What do you do at work?

“My job as a strategic antitrust consultant involves the preparation of advices for private clients, liaison with lawyers, and representations before competition agencies. On a larger scale it has involved the implementation of competition in a jurisdiction, drafting the legislation, and recruitment of staff. My work also involves quite a bit of travel, lecturing, and participating as a speaker at international conferences.”

What skills are most important to you?

“The skills set includes an ability to communicate effectively, an ability to understand the client’s problem from the client’s perspective, and an ability to work in teams or alone depending on the nature of the assignment. Up-to-date knowledge of the law is taken for granted.”

What kind of training do you recommend?

“I would recommend a primary degree in law and economics with an elective in antitrust economics and competition law. Early in one’s career, one could work as a paralegal in a law firm or join an economic consultancy firm in order to gain experience. Alternatively, one could gain experience as a case handler, either as a lawyer or economist with a national competition agency, and then move later in your career to the private sector as a consultant.”

What is your key to success?

“It is important to showcase a combination of hard work and dedication to the job without necessarily sacrificing a personal life. The key to this is developing good time management skills. Prioritizing and meeting deadlines reflects well on your professional image. Listening to clients and understanding the issue at hand from their idiosyncratic perspective also aid in the steps needed to move a successful professional relationship forward.”

Résumé Builder

Academic Skills

- Above average analytical skills
- Good speaking, listening, and negotiating skills

Education and Training

Obtain a bachelor’s degree in business administration, law, and economics as well as augment these with specifics in the industry of interest. The following high school and college courses will help develop the necessary background knowledge:

- Business Management
- Business law courses
- Communication
- English Language Arts (rhetoric and composition)
- Introduction to Business
- U.S. Government
- Social Studies

Critical Thinking

How can quality performance and time management skills impact your career?



Go to glencoe.com to find legal careers resources.

UNIT 6

The Writing Connection

Personal Essay Practice

The Particulars of a Dream Four college graduates come up with the dream of starting their own cultural magazine on music, literature, and art. They envision running the magazine full time and drawing salaries as the owners and editors of the magazine. One of the friends, a business major, brings up the real-world details of accomplishing their dream. They should form their business as a 501(c)(3) nonprofit corporation. They could then hold fundraisers, write grant proposals, and seek out funding from businesses, the government, and other sources. First, they will need to find out how to propose a budget, create an accounting system, and write a grant.

Assignments

Research Find out what it takes to form a nonprofit corporation in your state. Be sure to examine the federal laws as well as state laws.

Write Consider the situation above and write a personal essay about the nonprofit company you would want to start.

Writing Tips Before you start writing your personal essay, remember that it should:

- ✓ represent the writer's point of view
- ✓ reflect the writer's life and interests
- ✓ share a life lesson with the reader or talk about a relevant past experience

Discuss the specific details of how to start a nonprofit, and explain why you think there is a need in the marketplace for your idea. What makes you so passionate about your idea? Why would individuals, corporations, or organizations want to invest in your idea?

Essay Test Strategies CollegeBoard, a not-for-profit membership association, recommends the following tips on essay writing: read the entire assignment before writing; do not oversimplify; and support your idea with facts and figures.



Go to glencoe.com to find more writing resources.

Protecting Social and Environmental Concerns

For this project, you will use what you have learned to prepare an informational guide on an environmental law affecting society at large, as well as business. You can work on this project alone or with a partner.

Here is a checklist of the skills that you will need to complete this project. Your teacher will consider these skills when evaluating your work.

Evaluation Rubric	
Academic Skills	
1. Online and library research	1. 10 points
2. Reading for information	2. 10 points
3. Note-taking	3. 5 points
4. Estimation and computation of facts/figures you discover	4. 10 points
5. English composition to summarize findings	5. 15 points
Legal Skills	
6. Researching laws that protect the environment	6. 15 points
7. Knowledge of federal laws that set precedent for businesses	7. 15 points
8. Analysis of essential legislative acts governing businesses	8. 15 points
9. Use of technology	9. 5 points
	Total 100 Points



For more resources and for grading rubrics, go to glencoe.com.

Step 1: Preparation

- 1 Write a proposal for an area of environmental protection law you plan to research.
- 2 Use all you have learned in this unit and library or Internet resources as tools.
- 3 Complete this project in a format that is acceptable for adding to your portfolio.

Step 2: Procedure

- 1 **Review** the text in this unit and make a list of the environmental protection laws that pertain to your specific area of interest, such as air pollution, oil spills, global warming, disposing of nuclear waste, etc. Go to glencoe.com to find additional help and resources.
- 2 **List** all the legal terms you come across in your research. What laws protect the public and regulate business? How are these laws enforced?
- 3 **Write** an informational guide about the legal terms and documents that a business owner would need to know about the law you chose. Use the Internet to research and download important documents. Make enough copies so your classmates can review and annotate your guide.
- 4 **Describe** a real-world situation in which a business violated the laws in your area of interest. Explain the impact of the violation not only on the business, but on the public and on the environment as well. Present your guide and conclusion to your classmates.

Step 3: Create an Analysis Report

As a class, compare and contrast the information presented in each guide. See if any of the guides stand out, and if so what makes the information presented most interesting. After comparing the guides, answer the following questions:

- 1 How many and what areas of environmental laws were presented?
- 2 Did the guides presented include all the necessary information needed to understand the importance of federal environmental legislation?
- 3 If not, what should have been added to make the information easier to use?
- 4 How was your guide similar to and different from the other guides presented?



Community Connection

Research current environmental laws that are being debated by politicians, businesses, and environmental organizations either on a local, national, or international level. Decide who has the most to win and who has the most to lose if the law is passed. Go to glencoe.com to find resources.



Competitive Event Prep

New Business Venture

Situation: Assume the role of a high school business law student. A college student friend is a landscaping major who is planning to open a new landscaping and lawn service business. Your friend is concerned about the type of business ownership that should be established. Your friend has cared for lawns on a casual basis without a formally established business. This new venture will require the purchase of equipment and hiring help.

Activity: You must explain the different types of business ownership to your friend, with an emphasis on the pros and cons of each.



For more Competitive Event preparation, performance tips, and evaluation rubrics, go to glencoe.com.



Broz v. Cellular Information Systems, Inc.

Delaware Supreme Court 673 A.2d 148 (1996)

Read Critically As you read this case, ask yourself the following questions:

1. What companies did Mr. Broz have a responsibility to?
2. Why did CIS sue Mr. Broz?
3. What legal doctrine applies to his case?
4. What did the Delaware Supreme Court hold with regard to Mr. Broz?

Assignment Write a short summary of the situation. Include the court's decision and a couple of sentences about why or how the court reached its decision.

Facts Board Member Robert Broz was the president and sole stockholder of RFB Cellular, Inc. (RFBC), a Delaware corporation that provided cellular phone service. Mr. Broz was also a member of the board of directors of Cellular Information Systems, Inc. (CIS), a publicly-held Delaware corporation that was a competitor of RFBC.

License Availability Among the service areas it covered, RFBC had a license for service in the Michigan-4 area. In 1994, a license for service in the Michigan-2 area became available. This area was right next to Michigan-4. The owner of the Michigan-2 license, Mackinac Cellular Corp. (Mackinac) contacted Mr. Broz about selling the license to RFBC. Mackinac did not contact CIS to see whether it was interested in the license because CIS had just emerged from bankruptcy. At the same time, PriCellular, Inc. expressed an interest in buying the license from Mackinac. RFBC won a bidding war and bought the license.

CIS Financial Struggles At the time Mr. Broz was interested in buying the Michigan-2 license, CIS was going through financial problems. In fact, CIS was negotiating with PriCellular, Inc. for PriCellular to buy CIS. However, PriCellular was having trouble financing the purchase, and it took several months before it was able finally to do so. PriCellular finalized the purchase nine days after RFBC bought the Michigan-2 license.

Lawsuit Commencement After RFBC bought the license and PriCellular bought CIS, CIS sued Mr. Broz and RFBC. CIS argued that Mr. Broz should have notified the board of CIS about the availability of the Michigan-2 license to see if CIS was interested in buying the license. CIS argued that the actions of Mr. Broz constituted an "impermissible usurpation of a corporation opportunity" belonging to CIS.

Opinion Delaware Court of Chancery Proceedings The Delaware Court of Chancery held that the actions

of Mr. Broz did constitute a usurpation of a corporate opportunity that belonged to CIS. The Court found that CIS could have required Mr. Broz to abstain from the purchase out of deference to the CIS board, and that if Mr. Broz had notified the CIS board, the board could have notified PriCellular about the pending purchase.

Corporate Opportunity Doctrine In making its decision, the Delaware Supreme Court first had to define the law that applied. The Court had previously defined the corporate opportunity doctrine in the case *Guth v. Loft, Inc.* as follows:

A corporate officer or director may not take a business opportunity for his/her own if:

- (1) the corporation is financially able to exploit the opportunity;*
- (2) the opportunity is within the corporation's line of business;*
- (3) the corporation has an interest or expectancy in the opportunity; and*
- (4) by taking the opportunity for his own, the corporate fiduciary will thereby be placed in a position inimical to his duties to the corporation.*

A director or officer may take a corporate opportunity if:

- (1) the opportunity is presented to the director or officer in his individual and not his corporate capacity;*
- (2) the opportunity is not essential to the corporation;*
- (3) the corporation holds no interest or expectancy in the opportunity; and*
- (4) the director or officer has not wrongfully employed the resources of the corporation in pursuing or exploiting the opportunity.*

Applying the Corporate Opportunity Doctrine Under the doctrine, CIS must have been in a financial position to buy the license from Mackinac to keep Mr. Broz from pursuing the opportunity to do so himself. The testimony of board members was that CIS was emerging from bankruptcy and was not in a position to buy any additional licenses. Further, PriCellular had not yet

bought CIS, so even if PriCellular had the money it could not be considered by the court.

In addition, CIS must have an interest or expectancy in the opportunity. By the time CIS had emerged from bankruptcy, it no longer held cellular phone licenses in the area. The testimony of board members in court was that CIS's business plan after bankruptcy did not include getting any additional licenses.

Finally, CIS argued that, in applying the doctrine, it was an implicit requirement that Mr. Broz, as a board member, must present the opportunity to the full board of CIS so that the board can officially discuss the opportunity for its own benefit.

Holding The Delaware Supreme Court held that the Delaware Court of Chancery had improperly applied the corporate opportunity doctrine. The Supreme Court found that CIS was in no position to acquire or expect the license. The Court further held that board members are not required to present an opportunity to a full board, if such a presentation would result in the board's rejection of the offer, as was the case in this situation.

TRIAL PREP

The National High School Mock Trial Association organizes competitions at the local, regional, and national levels where teams of high school or college students prepare and argue fictional legal cases before practicing attorneys and judges. Mock Trial team members are each assigned a role as either an attorney or witness. Each team must develop a courtroom strategy, legal arguments, and a presentation style.



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