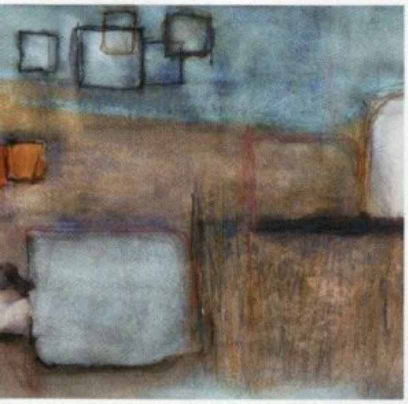

CHAPTER 9

Torts and Products Liability

earning Objectives

er studying this chapter, students who have mastered the material will be able to:

1 Articulate a basic definition of a tort and identify the source of law governing various types of torts.

2 Determine the classification of tort based on the conduct of the wrongdoer.

3 Give specific examples of how tort law applies in the business environment.

4 Apply the elements and defenses of the torts of defamation, trade libel, and product disparagement and discuss the applicability of each in the business environment.

5 Identify the differences in terms of liability for traditional print defamation and defamation in cyberspace.

6 Distinguish business competition torts from other intentional torts and understand their applicability in commercial relationships.

7 Recognize conduct that is classified as negligent and identify any potential defenses.

8 Provide alternate theories of liability and defense that can be applied when a product is the cause of an injury.

9 Articulate what must be proved in negligence and strict liability cases and appreciate how the levels of proof differ.

earning to recognize situations in which a business venture may have potential liability to another party is an important part of limit- k in business operations. Tort law and products ty law set out certain conduct and standards of ableness and provide legal recourse when a on of those standards results in an injury caus- sses. Because business owners are ordinarily sible for the intentional or accidental conduct ir employees who cause another party harm, it ntial for managers to understand ways in which to control risk and reduce liability. In this chapter, students will learn:

- The fundamental principles of tort law, types of torts, and how each applies in a business context.
- Rules governing intentional and business competition torts.
- How liability arises for negligent acts and the defenses to liability.
- Special rules governing strict liability and products liability.

OVERVIEW OF TORT LAW

A **tort**[1] is a civil wrong where one party has acted, or in some cases failed to act, and that action or inaction causes a loss to be suffered by another party. The law provides a remedy for one who has suffered an injury by compelling the wrongdoer to pay compensation to the injured party. Tort law is best understood as law that is intended to compensate injured parties for losses resulting in harm from some unreasonable conduct by another.[2] One who commits a tort is known as the **tortfeasor**. The tortfeasor's wrongful conduct is described as **tortious conduct**. Recall from Chapter 1, "Legal Foundations," that an individual may commit a criminal offense and a civil wrong in the very *same* act. While criminal statutes are intended to punish and deter the wrongdoer, the common law of torts is primarily intended to provide *compensation* for the victim. In some cases tort law also may be used to deter wrongful conduct in the future.

LO 9-1

Articulate a basic definition of a tort and identify the source of law governing various types of torts.

SOURCES OF LAW

For the most part, tort law is governed by state common law principles. Recall from Chapter 1, "Legal Foundations," that courts look to rules articulated by the American Law Institute (ALI) for guidance on applying common law legal principles. For tort law, these rules are known as the ***Restatement of Torts***. The ALI has amended the Restatements twice, and, therefore, these sources of law are called the *Restatement (Second) of Torts* and the *Restatement (Third) of Torts*. Remember that courts are not bound by any of the Restatements, but they do recognize them as widely applied principles of law. The Second Restatements have the benefit of volumes of case law and wide acceptance, and therefore references to the Restatements in this chapter refer to the Second Restatements unless otherwise noted.

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Laws that cover individuals who are injured by a product, known as *products liability laws,* may take the form of state common law or state statutes that expressly impose liability for injuries that result from products. These statutes are based primarily on the Restatements and are relatively uniform from state to state.

CATEGORIES OF TORTS

LO 9-2

Determine the classification of tort based on the conduct of the wrongdoer.

Torts fall into one of three general categories: *intentional torts, negligence,* and *strict liability.* An **intentional tort** is one in which the tortfeasor is *willful* in bringing about a particular event that causes harm to another party. **Negligence** is an accidental (without willful intent) event that causes harm to another party. The difference between the two is the mind-set and intent of the tortfeasor. For example, suppose that Pangloss is the delivery van driver for Cultivate Your Garden Flowers Inc. One day while on a delivery he spots his archenemy crossing the street, so he accelerates his truck and hits him. In this case, Pangloss has committed an intentional tort (battery). If, on the other hand, Pangloss is late for his delivery, carelessly speeds around a turn, and accidentally hits a pedestrian crossing the street, he has committed the tort of negligence.

LO 9-3

Give specific examples of how tort law applies in the business environment.

Strict liability torts, in which a tortfeasor may be held liable for an act regardless of intent or willfulness, applies primarily in cases of defective products and abnormally

Legal Speak >))

Willful Conduct Intentional behavior directed by the "will."

[1]The term *tort* originally derives from the Latin root *tortus,* meaning "twisted" or "wrested aside." As with many legal terms, Latin words were given a French twist in English common law via the Norman kings. Thus, the shortened term *tort* is a French root meaning "wrong."

[2]*Black's Law Dictionary.*

dangerous activities (such as major construction demolition). Owning a wild animal or even some breeds of dogs can result in strict liability should the animal harm an individual, regardless of the precautions taken by the animal's owner.[3]

LO 9-4

Apply the elements and defenses of the torts of defamation, trade libel, and product disparagement and discuss the applicability of each in the business environment.

INTENTIONAL BUSINESS-RELATED TORTS

While the law provides relief for injured parties in a variety of circumstances, there are some intentional torts that are more important to business owners and managers because they have the potential to impact business relationships and operations.

Defamation

The law recognizes an individual's or a company's reputation as a valuable asset by imposing liability on any party that makes false and defamatory statements affecting another party's reputation. In this context, the term *party* means an individual, business, or product. Just as in all civil lawsuits, the *untrue statements* must have caused the victim to suffer *damages*. Generally, we think of written defamation as **libel** and oral (spoken) defamation as **slander**. In order to recover for a defamation action, the plaintiff must prove four elements:

- *Defamatory statement:* A *false* statement concerning a party's reputation or honesty or a statement that subjects a party to hate, contempt, or ridicule. In order to qualify as defamatory, the statement must have a tendency to harm the reputation of the plaintiff.[4] Because many statements can be interpreted in more than one way, the law provides that the statement is defamatory so long as a defamatory interpretation is an objectively reasonable one and the plaintiff shows that at least one of the recipients did in fact make that interpretation. Note that the statement must be false, not merely unkind. Moreover, if a statement was *pure opinion,* that statement is not defamatory. That is, a defamatory statement is one that must be *provable as false.*
- *Dissemination to a third party:* In the Restatements, this requirement is referred to as *publication,* but in this context it does not literally require the statement to be published. Rather, this element requires that the statement must somehow reach the ears or eyes of someone other than the tortfeasor and the victim. For example, suppose a manager telephones one of his employees and says, "You are the one who stole $100 in petty cash, so you're fired." Even if the accusatory statement is false, the manager has not defamed the employee based on that action alone. No third party heard the statement, and, thus, the dissemination element is missing.
- *Specificity:* The statement must be about a particular party, business, or product. Thus, any general statement about a profession as a whole cannot constitute defamation, but a false statement about a specific company can be the basis of a reputation claim.
- *Damages:* In a business context, the aggrieved party must be able to prove that he or she suffered some *pecuniary* harm. Examples of damages in a defamation suit include situations in which the victim has lost a valuable client due to the tortfeasor's defamatory comment or the victim is unable to secure employment because of a tortfeasor's defamatory comment during a reference check.

Legal Speak >))

Pecuniary Harm
Lost revenue or profits, both actual and potential.

Legal Speak >))

Malice
The intent, without justification or excuse, to commit a wrongful act or inflict harm.

Public Figure Standard

If the victim is a public figure, such as a candidate for political office or a celebrity, the defamation must have been committed with *malice* or reckless disregard for the truth.

[3] Numerous cities and municipalities have declared certain breeds of dogs such as pit bulls, rottweilers, and mastiffs to be dangerous animals, and many have even banned the ownership of such animals. See, for example, *Tracy v. Solesky,* 25 A.3d 1025, 421 Md. 192 (2011).

[4] *Restatement (Second) of Torts,* § 559.

This "public figure" rule is based on the U.S. Supreme Court's landmark ruling in *New York Times v. Sullivan*.[5] The case involved a public official, the police commissioner of New York City, who sued *The New York Times* for defamation based on allegations printed in the newspaper that accused him of complicity in criminal activity. In announcing the public figure standard, the Court ruled that, in order for a public figure to prevail in a defamation case, the plaintiff must provide evidence that the defamer either had "actual knowledge" that the statement was false or made the defamatory statement with a "reckless disregard for the truth."

Defenses to Defamation

The second phase of a defamation analysis is an inquiry into whether the defendant may avail themselves to a statutory or judicially recognized defense.

Truth

Truth is an absolute defense to a charge of defamation. If the statement made is truthful, no defamation has occurred. To assert truth as a defense, the defendant must prove that the statement was either literally true or substantially true.

Privilege Defenses

If the injured party meets all of the requirements of a defamation claim, the defendant may still avoid liability if the defamatory statement falls into the category of ***privileged statements***. Privilege is a defense that recognizes either a legal or public policy–based immunity from a defamation claim. It is divided into two subcategories: **absolute privilege**, whereby the defendant need not offer any further evidence to assert the defense, and **qualified privilege**, whereby the defendant must offer evidence of good faith and be absent of malice to be shielded from liability.

Absolute Privilege

Courts generally recognize three types of absolute privilege:

- *Government officials:* The framers of the Constitution recognized the need for free debate among members of Congress and gave immunity in the Constitution via the Speech and Debate Clause, which shields members of Congress from liability for any statement made during a congressional debate, hearing, and so on, while in office. The U.S. Supreme Court later extended that protection to all federal officials.[6]
- *Judicial officers/proceedings:* All states now recognize some protection of participants of a judicial proceeding for statements made during the proceeding. This includes judges, lawyers, and, in some cases, witnesses.
- *State legislators:* Similar immunity has been extended by the states to protect state legislators for statements made in the course of carrying out their duties.

Qualified Privilege

Courts also recognize certain qualified privileges that are grounded in public policy:

- *Media:* Employees of media organizations (e.g., television, radio, periodicals) are afforded a qualified protection from defamation liability. So long as the media has acted in good faith, *absent of malice*, and without a reckless disregard for the truth, the media is protected from liability through privilege as a defense for unintentional mistakes of fact in their reporting.

[5] 376 U.S. 254 (1964).

[6] *Barr v. Matteo*, 360 U.S. 564 (1959).

me states provide statutory or common law munity from defamation claims for employers oviding references for ex-employees, so long as e information is factual. © Flying Colours Ltd/Getty ges

- *Fair report privilege:* If one relies on an official public document or a statement made by a public official and cites the document or public statement when making an allegedly defamatory statement, no cause of action for defamation occurs unless the speaker knows the statement is false.
- *Employers:* An increasing number of states have extended some liability protection for employers who are providing a reference for an ex-employee. In most cases, employers do not have liability if the employee's defamation claim is connected to a reference check. However, an employer may lose this privilege if it provides false information or acted with malice.

In Case 9.1, a state appellate court considers an employer reference privilege as a defense to defamation.

CASE 9.1. Nelson v. Tradewind Aviation, No. AC34625, Appellate Court of Connecticut (2015)

FACT SUMMARY Tradewind Aviation (TA) employed Nelson as a pilot for a small commercial airline that primarily flew from New York and New Jersey to Martha's Vineyard and Nantucket. Over the course of the summer of 2007, Nelson copiloted 137 flights without incident or complaint from passengers. Nelson was never removed from flying status for a performance-based reason or disciplinary reason. Although some senior pilots did complain about Nelson, he was never given a written warning, disciplined, or suspended. As the summer ended, TA announced that some pilots would be laid off due to a decrease in demand during the off-season. Nelson committed to working during the first part of the off-season; however TA informed Nelson it would be unable to continue his employment. TA's human resources office completed necessary paperwork indicating that Nelson was laid off due to "lack of work."

In December 2007, Nelson was offered a job by Republic Airways (Republic). As part of his initial interview, Nelson signed authorizations that gave TA permission to verify his employment with TA and to release all of his employment records to Republic. This authorization also required TA to send copies of these records to Nelson so that he had an opportunity to submit written comments to correct any inaccuracies. TA completed the reference forms and indicated (1) that Nelson had been involuntarily terminated from TA and (2) Nelson had been involuntarily removed from flying status based on poor performance. Responding to Republic's request for more details, TA faxed Republic a letter stating that Nelson was terminated "after he failed to perform to company standards." Prior to that date he was given several opportunities to discuss the need for improvement as well as additional training to help him perform at the levels we needed." TA never sent the records or letter to Nelson. Republic subsequently revoked its job offer. Nelson sued TA for, among other claims, defamation. The jury awarded the plaintiff a total of $307,332.94 in damages. TA appealed asserting the employer reference privilege.

SYNOPSIS OF DECISION AND OPINION The court affirmed the jury's verdict in favor of Nelson. The court reasoned that it was well settled that defamation is actionable if it charges improper conduct or lack of skill or integrity in one's profession or business and is of such a nature that it is calculated to cause injury to one in his profession or business. The court rejected TA's argument that Nelson had not proven that TA's statements rose to the level of malicious. The court held that a qualified privilege in a defamation case may be defeated if it can be

(continued)

established that the holder of the privilege acted with malice in publishing the defamatory material. Based on the facts in this case, the jury's conclusion that the statements were made with malice was reasonable.

WORDS OF THE COURT: Malice "A review of the evidence reveals that the jury reasonably could have concluded that the defendant's defamatory statements were made with knowledge that they were false and with an improper motive. The jury reasonably could have found that [Nelson] was laid off due to lack of work, that [TA supervisors] never removed the plaintiff from a flight for performance or professional competency reasons, that [Nelson] was never offered or sent for any additional training . . . Additionally, the jury reasonably could have found that the statements were made with an improper motive in light of the timing and manner in which the statements were made."

Case Questions

1. What statements by TA, specifically, do you consider to be malicious? Why?
2. How could TA's management have prevented the defamation from occurring?
3. *Focus on Critical Thinking:* What is the public policy behind the employer reference privilege? Is it fair to the employee who may have a different perspective on the circumstances of his or her termination? Have you ever heard an employer defaming an ex-employee?

Trade Libel and Product Disparagement Laws

In cases where a competitor has made a false statement that disparages a competing product, an injured party may sue for **trade libel**. This tort requires that the statement (1) be a clear and *specific* reference to the disparaged party or product (e.g., using the actual brand name of the product), (2) be made with either knowledge that the statement is false or reckless disregard for the truth, and (3) be communicated to a third party (similar to defamation).

Some states have passed **product disparagement statutes** intended to protect the interest of a state's major industries, such as agriculture, dairy, or beef.[7] In perhaps the most famous product disparagement case, the Texas Cattle Ranchers Association sued Oprah Winfrey under a Texas law allowing recovery for any rancher who suffers damages as a result of false disparagement. On her television show, Winfrey agreed with statements made by one of her guests that alleged certain U.S. market hamburger meat could cause mad cow disease, which is fatal to humans. At the end of the segment, Winfrey took the position that she would cease eating any hamburgers. The ranchers showed evidence that beef sales dropped precipitously immediately after the broadcast and alleged that Winfrey's statements were false and caused the ranchers lost revenue. The jury rejected the cattle ranchers' claim as too broad and without sufficient evidence that the remarks alone were the cause of the losses.[8]

Fraudulent Misrepresentation

Recall the discussion of misrepresentation and fraudulent misrepresentation in Chapter 7, "Contract Enforceability and Performance." It is important to note that there are some important overlapping legal principles of tort and contract law. For example, in some cases contract law allows a contract to be canceled if one party has made false representations concerning a *material fact.* This means that the misrepresented fact must involve an important aspect of the basis of the contract, such as a change in the value of the contract or an increase in one party's risk. Fraudulent misrepresentation (sometimes referred to simply as *fraud*) is *also*

[7]For example, disparagement of Idaho potatoes is covered in Idaho Code § 6-2003. For a list of many such laws, see *Of Banana Bills and Veggie Hate Crimes: The Constitutionality of Agricultural Disparagement Statutes,* 34 Harv. J. Legis. 135 (1997).

[8]Affirmed in *Texas Beef Group v. Winfrey,* 201 F.3d 680 (5th Cir. 2000).

KEY POINT

Fraudulent misrepresentation (in both contracts and torts) must center on a *material fact;* that is, a fact that is significant or would impact the parties' rights or obligations in a transaction as opposed to a minor and inconsequential detail.

LO 9-5

Identify the differences in terms of liability for traditional print defamation and defamation in cyberspace.

recognized as a tort in cases where the law provides a remedy to recover damages when the innocent party suffers a pecuniary loss as a result of the false representation. In cases of fraudulent misrepresentation, the law allows the innocent party to recover if (1) the misrepresentation was a material fact known to be false by the tortfeasor (or was a reckless disregard for the truth); (2) the tortfeasor intended to persuade the innocent party to rely on the statement, and the innocent party did, in fact, rely on it; and (3) damages were suffered by the innocent party. For example, Buyer asks Seller whether Seller's property is properly zoned for a manufacturing facility. In an effort to induce Buyer to purchase the property, Seller misrepresents that the property is zoned for manufacturing. Buyer then enters into a purchase agreement for the property with a 10 percent down payment, balance due in 30 days. Buyer then proceeds to spend money by hiring an architect to visit the site and draw plans for the new facility. The day after the agreement is signed, Seller applies to the zoning board for a change in zoning, hoping that it will be changed before Buyer completes the agreement by paying the balance owed. The zoning board does not change the status. In a case against Seller for fraud, Buyer would be entitled to cancel the contract *and* recover any losses in tort suffered as a result of Seller's fraudulent misrepresentation (such as the money spent on hiring the architect).

Every state has enacted a consumer fraud protection act. These acts severely punish those who commit fraud and, in many instances, allow victims of fraud to sue and collect treble damages.

LEGAL IMPLICATIONS IN CYBERSPACE

Protections for Online Content Providers

Along with holding the actual tortfeasor liable in a defamation case, the law imposes certain liability upon the publisher of libelous statements as well. However, the law does not impose liability on the *distributor* of the publication (such as a bookstore or newsstand). For example, suppose a famous movie star is the subject of a gossip feature in a hypothetical tabloid called the *American Tattler.* The feature implies that the movie star was seen at a local restaurant and was so intoxicated that she could not control her conduct. In a lawsuit for defamation, the movie star proves that the story was false and that it led to her being fired by her movie studio. In terms of liability, both the author of the defamatory feature and the publication *(American Tattler)* may be liable for damages.

However, the rules pertaining to publishers of online content in cyberspace are different. In our movie-star example, suppose that instead of the *American Tattler* publishing the defamatory feature, a gossip columnist hired by America Online (AOL) wrote the article for an AOL entertainment news board. There would be no doubt of the liability of the author, but would AOL be liable as the "publisher"?

As Internet accessibility increases rapidly, courts have struggled with this question. In the 1991 case, *Cubby Inc. v. CompuServe, Inc.,*[9] the plaintiffs filed a defamation action against CompuServe as a "publisher" of defamatory materials contained in an online publication called *Rumorville, USA. Rumorville* was composed, written, and edited by a third party who was not employed by CompuServe. The federal trial court in the southern district of New York held that CompuServe was *not* a publisher in the context of defamation law but rather was more akin to a bookstore and thus Internet service providers (ISPs) such as CompuServe were to be treated as "distributors." Consequently, CompuServe was not subject to liability for any defamatory statements so long as it did not "edit, review or reformulate" the publication.

However, not all courts have taken that view. A few years later, as the number of Internet service providers grew, a New York state trial court issued a very different ruling. In *Stratton v. Prodigy*

[9]776 F. Supp. 135 (S.D.N.Y. 1991).

Services Company, decided in 1995, the court ruled that an ISP could be held liable as a publisher of defamatory material. The case involved a Prodigy-maintained electronic bulletin board, available to its subscribers, called "Money Talk." Although Prodigy did not formally edit the postings, it had a policy that reserved the right to eliminate postings if they were objectionable. The plaintiff filed suit against Prodigy as a publisher of material that was allegedly libelous. In stark contrast to the *Cubby* court, a state trial court in New York ruled that Prodigy was a publisher in the context of a defamation claim and, therefore, could be liable for damages resulting from defamatory comments in its electronic bulletin board. The court held that Prodigy's "conscious effort to maintain editorial control" over the content was sufficient to qualify it as a *publisher* as that term is understood in defamation law.

In an apparent effort to address the pleas of ISPs for a uniform standard, Congress enacted the **Communications Decency Act (CDA) of 1996.**[10] This law extended immunity to the ISPs by protecting them from any defamation liability as a "publisher or speaker of any information provided by another information content provider." In effect, Congress made the policy choice that ISPs were to be treated as newsstand-like distributors.

One of the first cases to interpret this law was *Blumenthal v. Drudge and America Online, Inc.*[11] Although the case was decided by a trial court, the reasoning is often cited by appellate courts when applying the ISP safe harbor. The case involved a defamation lawsuit filed by a high-profile White House adviser (Blumenthal) against a controversial political journalist (Drudge) and America Online (AOL) because of spousal abuse and cover-up allegations in a column written by Drudge. The column was posted on an AOL news board as part of an agreement between Drudge and America Online. After Drudge posted a retraction and acknowledged that the allegations were false, Blumenthal sued Drudge and AOL for defamation. The trial court dismissed the case against AOL, citing the Communications Decency Act's safe-harbor provisions for ISPs. The court noted that even if AOL could conceivably be categorized as a *publisher* of defamatory material under previous cases, Congress specifically exempted ISPs such as AOL from civil suits for defamation.

Courts will also allow recovery for misrepresentations that are not intentional but are *negligent* misrepresentations. In most cases, the parties have to have some type of business relationship for the innocent party to recover. Any statement made by a party that turns out to be inaccurate may still allow the innocent party to recover if the tortfeasor's statement was negligent. In the Buyer-Seller case discussed earlier, suppose that Seller had no actual knowledge of the zoning status for the property but made a statement that it was zoned for manufacturing. Buyer would still be able to recover despite the fact that Seller did not know that the statement was false. Seller is still liable because he was negligent in his duty to know such an important fact (negligence is discussed in detail later in this chapter).

Legal Speak >))

Treble Damages
Treble damages are a remedy in fraud cases whereby the victim of fraud can collect triple the amount of actual damages.

False Imprisonment

The tort of false imprisonment is defined by the Restatements as the "intentional infliction of a confinement upon another party." In the business context, a merchant most commonly encounters these circumstances in cases of suspected retail theft. While the merchant has the right to briefly detain a suspected shoplifter, she must be cautious about giving rise to a false-imprisonment claim when detaining an individual or attempting to recover the merchandise. The Restatements provide for a **merchant's privilege**[12] to shield a merchant from liability for temporarily detaining a party who is *reasonably* suspected of stealing

[10] 18 U.S.C.A. § 1462. Note that some portions of the CDA, namely Congress's attempt to regulate Internet pornography, were struck down as unconstitutional by various federal courts. However, this section survived judicial scrutiny.

[11] 992 F. Supp. 44 (D.D.C. 1998).

[12] Also known as *shopkeeper's privilege.* See *Restatement (Second) of Torts,* § 120A.

merchandise. This privilege, however, is very narrow. In order to gain protection under the privilege, the merchant must follow certain guidelines:

- *Limited detention:* The privilege applies only for a short period of time under the circumstances. Some courts have limited this time period to as few as 15 minutes. However, most courts follow a case-by-case analysis with the general framework that the detention may last the time duration necessary to confront the accused party, recover any goods stolen, and wait for the authorities to arrive (if necessary).
- *Limited to premises:* Generally, the privilege applies only if the suspected party is confronted on the merchant's premises or an immediately adjacent area (such as a parking lot).
- *Seizure of property:* The merchant or merchant's agent may seize alleged stolen property in plain view but may not search the accused shoplifter.
- *Coercion:* The merchant or merchant's agent (such as a store security guard) may not attempt to coerce payment, purport to officially arrest the detained party, or attempt to obtain a confession.

Table 9.1 provides an overview of other types of intentional torts and examples of each.

TABLE 9.1 Other Intentional Torts

Tort	Definition	Example
Battery	Intentional touching of another person, without that person's consent, in a harmful or offensive manner.	An employee touches another employee, without consent, causing embarrassment, a feeling of harassment, or physical injury.
Intentional infliction of emotional distress	Extreme, outrageous, or reckless conduct that is intended to inflict emotional or mental distress (physical harm is not necessary).	A bill collector contacts a debtor's mother and threatens to physically harm and imprison the debtor son and to put a lien on the mother's house. The mother suffers two heart attacks after the threats persist.*
Trespass (land)	The act of entering another's land or causing another person or object to enter land owned by a private party without the owner's consent.	A survey crew mistakenly surveys the wrong property. While working, the crew damages landscaping. The landowner is entitled to compensation as a result of the crew's trespass.
Trespass (chattel†)	The act of interfering with another's use or possession of chattel (such as personal property).	An employee takes home his employer's drill for personal use without the employer's permission and with the intent to return it the next morning. The drill is broken while under the employee's control. The employee is liable for costs of repair/replacement and any lost profits resulting from the downtime.
Conversion	The civil counterpart to theft; intended to reimburse a party who suffers damages as a result of theft or any other substantial interference with the party's ownership, where fairness requires that the tortfeasor reimburse the injured party for the full value of the property.	The controller of a corporation embezzles corporate funds and covers up discrepancies on the financial statements. In addition to the controller's facing criminal charges, the controller's employer may sue her for conversion in an attempt to recover the embezzled funds.
Civil assault	The act of putting someone in fear and apprehension of immediate harmful or offensive contact (battery). No actual contact is required.	A worker yells at a customer and starts moving toward the customer in a hostile manner. If the customer reasonably believes that she is about to be struck, she has been civilly assaulted even if she runs away without being touched.

*Based on *George v. Jordan Marsh Co.*, 268 N.E.2d 915 (Mass. 1971).
†Chattel is the English common law term for personal property or equipment that is movable.

Business Competition Torts

LO 9-6

Distinguish business competition torts from other intentional torts and understand their applicability in commercial relationships.

Tort law also provides for the promotion of fairness in business dealings and for the reimbursement of a party that has suffered some damages as a result of a competitor's tortious acts. These common law torts arise when a tortfeasor (typically a competitor to the harmed party) interferes with an existing contract or hinders a prospective contract between two parties.

Tortious Interference with Existing Contractual Relationship

When one party *induces* another party to break an existing contract with a third party, the inducing party may be liable for any damages suffered by the innocent party as a result of breaking the contract. For the injured party to recover damages, the tortfeasor must have (1) had *specific knowledge* of the contract, (2) actively *interfered* with the contract, and (3) caused some *identifiable* damages (losses) to the injured party. Business owners and managers may encounter contract interference torts in the context of employment contract restrictions against working for competitors (known as a *restrictive covenant*[13]) or in defending an allegation of interference in the process of hiring a new employee away from a competitor. For example, Lee is a talented software programmer and signs a contract with Computer Researchers Inc. (CRI) for three years. The contract stipulates that Lee will not work for any of CRI's competitors during that time even if he is terminated or voluntarily resigns from CRI. After one year, one of CRI's competitors, MultiCom, contacts Lee and attempts to convince him to leave CRI and work for MultiCom. During the negotiations, Lee shows MultiCom his contract with CRI, and MultiCom's manager then offers a higher salary and a $1,000 signing bonus to Lee. Lee resigns from CRI with two years left on his contract and goes to work for MultiCom. CRI must then spend several thousand dollars recruiting and training a new programmer to finish Lee's projects. In this case, many courts would consider holding MultiCom liable for CRI's damages because CRI was injured as a result of MultiCom's tortious interference with the CRI-Lee contract. Of course, CRI would also be entitled to recover damages from Lee for breaking the contract.

Note that interference does not occur when a competitor merely offers a better price to a competitor's customer. For example, suppose that Chung is the owner of several self-service car washes and signs a two-year agreement with Mega Distributor for the supplying of snack vending machines in the lobby of each of Chung's car washes. Under the contract, Chung will receive 30 percent of the sales from the machines. Shortly thereafter, Chung is contacted by a sales rep from Start-Up Snacks and offered the same terms as the Mega contract except that Chung will receive 60 percent of the sales from the machines. Chung crunches the numbers and concludes that the increase in revenue will more than make up for any penalties incurred for breaching the Chung-Mega contract, so he breaks his contract with Mega and enters into a new contract with Start-Up. Despite the fact that Start-Up knew of the Mega contract, the level of interference is *not* sufficient to constitute a tort. In this case, Chung decided on his own to break the contract with Mega and was not *induced* to do so by Start-Up. It is important to note, however, that Mega could still sue Chung for failing to perform his obligations as agreed in the contract.[14]

Legal Speak >))

Induce
To bring about or give rise to. In the context of tortious interference, liability is triggered if interference causes the harm.

Tortious Interference with Prospective Advantage

In addition to providing protection against interference from third parties in existing contracts, the law also protects interference with *potential* contract (prospects) or other business relationships. The protections and definition of interference are similar to the existing contractual interference rules discussed earlier. However, because no contract actually exists, courts allow recovery for this tort only under limited circumstances in which the tortfeasor's conduct was highly anticompetitive. For example, assume that OldCo intends

[13]Restrictive covenants are covered in detail in Chapter 7, "Contract Formation."
[14]Based on *Restatement (Second) of Torts*, § 766, Illustration 3.

to sabotage NewCo's efforts to obtain a new customer through a competitive bidding process. An OldCo employee hacks into NewCo's computer and destroys the proposal forms. NewCo cannot submit the bid before the deadline and, thus, doesn't get the contract. Assuming that NewCo can prove it suffered damages, OldCo could be held liable for interference with prospective advantage.

Self-Check Intentional Torts

Which tort, if any, fits each of the following facts?

1. Jason and Elaine are both being considered for a promotion to VP of Sales. Jason starts a false rumor that Elaine doctored the books to make her accounts look better than they actually are. Because of the investigation and the need to fill the position, Elaine is dropped from consideration and Jason gets the promotion.
2. MOT Corporation does all of its banking with Second National Bank. MOT receives a 1 percent interest rate on its savings account and pays a fee of $.02 per check written. A representative of Third National Bank visits MOT's offices and tells the company that Third National pays 1.25 percent interest and has free corporate checking. MOT closes its accounts with Second National and moves all its banking business to Third National.
3. Wayne gets into his car after work, but it won't start. He returns to his office, and everyone has gone home. He takes the keys to a company vehicle and drives home intending to drive it back to the office in the morning. That night, a violent storm causes a tree branch to fall on the car, causing extensive damage.
4. Nancy has triplets attending eighth grade. Every once in a while she takes small quantities of paper, pens, paper clips, and other stationery supplies home from work and gives them to her kids for school use.
5. Frank is a used-car salesman. He is working with a customer who decides to buy a car. The price is agreed to, and the customer tells Frank that he will go to the bank to get a certified check. They shake hands. Frank then says, "You should know that this car used to be owned by Bill Gates!" The customer returns with the certified check, all paperwork is signed, and the customer drives the car home. The next day, the customer discovers that Bill Gates never owned the car.

Answers to this Self-Check are provided at the end of the chapter.

CONCEPT SUMMARY *Business-Related Intentional and Competition Torts*

- A tort is a civil wrong and can be classified as intentional, negligent, or strict liability.
- Defamation is a false statement that specifically concerns an individual, company, or product, is communicated to a third party, and results in pecuniary harm to the victim.
- A victim of fraud must show intentional misrepresentation by the tortfeasor of a material fact, reliance on that fact, and damages resulting from that reliance.
- False imprisonment is an intentional tort unless the tortfeasor is a merchant who temporarily and reasonably detains a suspected thief.
- When a business competitor's actions exceed standard competitive practices, that company may be liable for intentional interference with a contract by a third party if the company has specific knowledge of a contract and intentionally disrupts its proper execution.

NEGLIGENCE

LO 9-7

Recognize conduct that is classified as negligent and identify any potential defenses.

Tort law also applies when one party fails to act reasonably and harm occurs, even though that party did not intend to cause harm. The negligent party is liable for any injuries or damages suffered by another party as a result of his unreasonable conduct. This category of tort is called *negligence.* Recall from the first section of this chapter that the primary difference between intentional torts and negligence is the mind-set of the tortfeasor. When a tortfeasor causes harm to an injured party by creating an *unreasonable risk of harm,* the law provides the injured party a remedy regardless of the tortfeasor's intent. The Restatements also recognize certain defenses that may be asserted in a negligence case.

Elements of Negligence

The law requires that specific elements be proved in order to recover in a lawsuit against a tortfeasor for negligence. The injured party must prove five fundamental elements by answering certain questions about the conduct in question:

- *Duty:* Did the tortfeasor owe a duty of care to the injured party?
- *Breach of duty:* Did the tortfeasor fail to exercise reasonable care?
- *Cause in fact:* Except for the breach of duty by the tortfeasor, would the injured party have suffered damages?
- *Proximate (legal) cause:* Was there a legally recognized and close-in-proximity link between the breach of duty and the damages suffered by the injured party?
- *Actual damages:* Did the injured party suffer some physical harm that resulted in identifiable losses?

Duty

The initial consideration in a negligence analysis is whether or not the tortfeasor owed the injured party a *legal* **duty**. The law imposes a general duty on all parties to act reasonably and not to impart unreasonable risk to others. In addition to having this general duty, some parties owe a special (heightened) duty of conduct to avoid liability for negligence.

General Duty of Reasonable Conduct

The law imposes a general duty on every party to act as a *reasonably prudent person* would under the circumstances. That is, everyone owes a duty to everyone else to act in a manner that does not impose unreasonable risk. The reasonably prudent person standard emphasizes that the conduct must be *objectively* reasonable. This means that at trial a fact finder (such as the jury) could conclude that a reasonably prudent person in the same circumstances should have realized that certain conduct would be risky or harmful to another person. In general, the scope of that duty is defined by *foreseeability.* In tort law, the term *person* in the reasonably prudent person standard is meant to be a generic term. The scope of duty is frequently defined by a particular industry or occupation. For example, the level of duty for a physician is defined by what a reasonably prudent *physician* would have done under the circumstances.

It is important to understand that duty is an element that *expands* and *contracts* based upon whether or not it was foreseeable that the conduct in question would cause an unreasonable risk of harm. For example, Cain is a guest on a shock-host television show. The owners of the show arrange to have Abel surprise Cain on the show with an embarrassing secret. Cain is embarrassed and runs off the stage, and no further incident ensues. Three days later, Abel persists in calling Cain and harassing him about this secret. Cain then shoots and kills Abel later that afternoon. Cain is sentenced to a life term, so Abel's heirs sue the owners of the shock-host television show for negligence, claiming they owed Abel a duty to protect him from Cain. In this case, a court will likely rule that due to the time period between the show and the shooting (three days) and the fact that no incident occurred on the show or immediately thereafter, the duty owed to Abel ended when the show ended and did not extend to the time of the incident. This is primarily because it was not reasonably foreseeable under the factual circumstances of this case that Cain would act in such a rash manner then or thereafter.[15]

No General Duty to Act

The duty of care, discussed above, does *not* include a general duty to act or to rescue another. Tort law allocates liability based on a fundamental difference between some *act* by one party that harms or endangers another party, known as **misfeasance**, and the failure to act or intervene in a certain situation, known as **nonfeasance**. While injured parties may generally recover for misfeasance, injured parties may not hold a defendant liable for failing to act *unless* the parties had a **special relationship** to each other. Special relationships that are set out in the Restatements include those of a common carrier (such as a bus company) to its passengers, innkeepers to guests, employers to employees, a school to students, and a landlord to tenants.[16] One important special relationship of interest to business owners and managers is a business's duty to *warn* and *assist* any business visitors or patrons in regard to potential danger or harm (such as a slippery floor) on business premises. Therefore, businesses have a special relationship with their visitors and patrons that would allow recovery even in a case of nonfeasance.

Landowners

Landowners owe a general duty to parties off the land from any unreasonable risks to them caused by something on the land. Courts use a reasonableness standard to determine the point at which the landowner should have acted. For example, the owner of GreenAcre plants several trees on the edge of his property, which is adjacent to a busy suburban street. One month later, one tree is dead, with no green vegetation and evidence of decaying bark and cracks in the roots. Eventually, the tree falls onto the road and injures a passerby. In this instance, a court may find that the landowner had a duty to inspect and remove the tree because it was foreseeable that the dead tree would be a risk to passersby if it fell.[17]

Landowners also owe a special duty to certain parties based on categories spelled out in the Restatements. It is important to understand that in a situation where a tenant is in possession of *leased space*, the tenant has the same special duties and level of liability that is imposed on landowners. Once a landlord/owner has given possession of the property to the tenant, the landlord is generally *not held liable* except for certain common areas (e.g., common stairwells, restrooms, or lobby).[18] The expected level of care varies by category. Table 9.2 sets out the categories of special relationship duties owed by landowners to licensees, invitees, and trespassers.

[15]Based on *Graves v. Warner Brothers*, 656 N.W.2d 195 (Mich. App. 2002).

[16]*Restatement (Second) of Torts*, § 314A.

[17]It should be noted that the Restatements do except "natural" conditions from the general duty. However, if a landowner planted shrubs or excavated land, this falls under the category of *artificial* and is not an exception to the landowner's general duty to persons off the property.

[18]There are exceptions to this rule, such as a situation in which the landlord transferred possession knowing of a certain defect but failed to warn the tenant about it.

TABLE 9.2 Special Relationship Duties Owed by Landowners

Special Relationship to	Definition	Example	Duties Owed
Licensee	Party has owner's consent to be on property for a nonbusiness purpose.	Social guest	Warn licensee of any known dangerous conditions on or about the premises. *No* duty owed to licensee to inspect for hidden dangers.
Invitee	Party is invited onto property by owner for business purposes or because landowner holds the premises open to the public.	Customer in a retail store	Warn invitee of any known dangerous conditions on or about the premises. Duty to inspect the premises for hidden dangers and take reasonable efforts to fix any defects.
Trespasser	Party enters premises without owner's consent.	Landscaping crew that accidentally mows wrong property	No duty to warn, inspect, or repair. Exception is a general duty of care when (1) owner has reason to know of regular trespass (such as a worn pathway) or (2) owner has reason to anticipate that young children might trespass on the property.

Assumption of Duty

Another exception to the no general duty to act/rescue is when one party voluntarily begins to render assistance even when there is no legal obligation to do so. This is known as *assumption of duty* and it requires that the party rendering assistance must proceed with reasonable care. This includes the duty to continue rendering aid and to take care not to leave the injured party in a worse position.[19] For example, suppose that Davis, a delivery truck driver, hears a call for help during one of his deliveries. He discovers that the call is coming from a nearby apartment that is on fire. Davis enters the building and rescues the caller. Although Davis has no legal duty to rescue, he undertakes the rescue and therefore assumes the duty to keep the caller safe. For example, if the caller is unconscious, Davis must use reasonable care to secure medical help and cannot abandon the caller.

In Case 9.2, a state appellate court considers a claim by a college student, injured as part of a fraternity prank that went awry, that he was owed a duty under both a landowner theory and an assumption of duty theory.

CASE 9.2 Yost v. Wabash College, Phi Kappa Psi Fraternity, et al., 969 3 N.E.3d 509 (Indiana 2014)

FACT SUMMARY Brian Yost (Yost) was an 18-year-old first-year student at Wabash College (Wabash) and a pledge at the local Phi Kappa Psi fraternity (Local Fraternity). Part of the Local Fraternity's traditions involve "creeking," meaning that a fraternity brother is thrown into a nearby creek. In September 2007, Yost and his pledge brothers confronted some of the Local Fraternity's member brothers in an attempt to toss one of these members, Yost's Pledge Father, into a nearby creek. Later that night, several Local Fraternity brothers retaliated by attempting to forcibly place Yost in the shower. This action was also a tradition of the Local Fraternity, and one in which Yost and his pledge brothers

(continued)

[19]*Restatement (Third) of Torts* § 43.

had previously participated two other times the evening of his injury. During this attempt, several Local Fraternity member brothers were carrying Yost to the shower when one of the fraternity members put him into a headlock that rendered Yost unconscious. The other member brothers panicked and dropped Yost to the ground.

Yost suffered significant physical and psychological injuries from the incident that caused him to withdraw from college. Yost filed suit alleging his injuries were a result of negligence and seeking damages from, among others: (1) Wabash College (the owner and landlord of the fraternity house), contending that a special relationship existed, and (2) the Local Fraternity on an assumption of duty theory. The trial court granted summary judgment to both Wabash and the Local Fraternity and Yost appealed.

SYNOPSIS OF DECISION AND OPINION The Indiana Supreme Court affirmed the summary judgment for Wabash but reversed the summary judgment for the Local Fraternity. In the case of Wabash, the court reasoned that a landlord has no liability to tenants or others for injuries on the property when the tenant is in full control of the leased premises. In the case of the Local Fraternity, the court held that there was sufficient evidence to reasonably conclude that Yost may be able to show that the Local Fraternity assumed a duty and that the actions of its members increased the risk of harm to him. This was especially true as the activity which led to the incident was a fraternity tradition.

WORDS OF THE COURT: Wabash College's Duty as Property Owner "Within the contours of this duty, we have held that landowners have a duty to take reasonable precautions to prevent foreseeable criminal acts against invitees. However, when the landowner is a lessor and the lessee is in operational control of the premises, such duty rarely exists . . . In the absence of statute, covenant, fraud or concealment, a landlord who gives a tenant full control and possession of the leased property will not be liable for personal injuries sustained by the tenant or other persons lawfully upon the leased property."

WORDS OF THE COURT: Local Fraternity's Assumed Duty "Here, Yost's argument is not that a conventionally recognized duty (such as a landowner's duty to an invitee or common carrier's duty to a passenger) existed, but rather that the local fraternity assumed a duty requiring the local fraternity to act with reasonable care. As the above facts show, Yost was living at the local fraternity, subject to the mentorship of a Pledge Father from the local fraternity, participating in traditions maintained at the local fraternity, was involved in the pledgeship program being run by local fraternity members, and, therefore, at least partially under the control and direction of the local fraternity . . . The undisputed designated evidence does not preclude the possibility that Yost may show at trial that the local fraternity undertook to render supervisory services intended to reduce the risk of harm to members like Yost, that upon which supervision Yost relied, and further that by failing to exercise reasonable care the local fraternity increased the risk of harm to Yost."

Case Questions

1. What factors did the court use to determine that the Local Fraternity may have assumed a duty here? Do you agree? Why or why not?
2. Why did the court find that Wabash College had no liability for this incident?
3. *Focus on Critical Thinking:* One of Yost's unsuccessful arguments against Wabash centered on a doctrine called *in loco parentis* (i.e., in place of the parent). The doctrine has largely disappeared from higher education since 1961. Yost claimed that the college had a duty to protect him and should have had a system in place to prevent fraternity pranks from becoming dangerous. Do you agree? Should an 18-year-old college student have full responsibility for his own safety while in a college-owned facility? Should colleges and universities have *in loco parentis* liability?

Breach of Duty

Once it has been established that one party owes another a general or special duty, the next factor in the analysis is whether or not the party has fulfilled her obligations. Failing to meet these obligations is known as a **breach of duty**. As discussed earlier, duties include (1) general obligations to act in a reasonable manner so as not to put another in harm's way, (2) special duties to certain parties, including the duty to inspect or the duty to warn of defects, and (3) assumption of duty. While the Restatements don't actually list events of breach, courts have traditionally looked to certain guideposts for determining whether a breach of duty has occurred.

Violation of Safety Statute

If the legislature has passed a statute intended to promote safety and one party violates the statute, there is a strong presumption that the party violating the statute has also breached her general duty to those who are protected by the law. Violations of safety statutes are sometimes referred to as *negligence per se*. For example, suppose the state legislature passes a law requiring that construction companies provide hard hats for all workers and visitors on a construction site. One day a prospective tenant visits an office building construction site to check on its progress, but there are not a sufficient number of hard hats available. The site manager allows the visitor on the site without a hard hat. The visitor is then injured by falling debris. In this case, the construction company has violated the state safety statute, and a court may find a breach of duty occurred without delving into a reasonably prudent person analysis.

States also pass statutes intended to establish specific liability standards in certain circumstances. For example, *dram shop laws,* enacted in most but not all states, impose liability on the owners and employees of a public establishment where alcohol is being served. These laws allow a third party who has been injured or harmed by an intoxicated tortfeasor to recover damages against the owner or employee who served the obviously intoxicated patron.[20]

Common Law Standards of Behavior

When the state legislature has been silent, appellate courts in each individual state have usually developed a fairly extensive body of cases in their common law so that certain standards of behavior may be used in judging whether or not a breach occurred. Standards related to maintenance of property (such as clearing ice from sidewalks) and safety measures (such as keeping one's car in good repair if driving on public roads) are examples of nonstatutory standards for reasonable behavior.

Res Ipsa Loquitur

The doctrine of *res ipsa loquitur* (a Latin phrase meaning "the thing or matter speaks for itself") is deep-seated in American tort law. This doctrine allows an injured party to create a presumption that the tortfeasor was negligent by pointing to certain facts that infer negligent conduct without showing exactly how the tortfeasor behaved.[21] An English judge first used this Latin phrase over a century ago in a case involving a pedestrian who was struck by a flour barrel that fell from a warehouse owned by the defendant. Although the injured party could not actually show how or why the barrel fell, the court held that the facts themselves were sufficient to impute a presumption of negligence.[22]

Assume that Ginsberg notices smoke coming out from under the hood of her car. She has the car towed to a mechanic, who determines that a valve cover gasket is leaking. She instructs him to make the necessary repairs. When she picks up the car, she pays the bill and drives off. One mile later, while stopped at a light, Ginsberg sees smoke coming from

[20]Note that an increasing number of state legislatures have also imposed similar liability for all social hosts, including the serving of alcohol in a private home.

[21]*Restatement (Second) of Torts,* § 328(D).

[22]*Byrne v. Boadle,* 159 Eng. Rep. 299 (Eng. 1863). The court wrote, "[A] barrel could not roll out of a warehouse without some negligence, and to say the plaintiff who is injured by it must call witnesses . . . is preposterous."

the hood again and gets out of the car just before it catches fire. The fire consumes the car, causing the engine to melt, and thus no specific cause for the fire can be determined. Ginsberg cannot prove exactly what the mechanic did wrong, but the car shouldn't have caught fire if the mechanic had repaired the car properly. She can use *res ipsa loquitur* to infer negligence.

Cause in Fact

After establishing that a breach of duty has occurred, the injured party must also prove that the tortfeasor's conduct was the **cause in fact** of the damages suffered by the injured party. In other words, there must be a *link* between breach of duty and damages. The overwhelming majority of courts use a simple test, known as the *but-for test,* to establish a link. Thus, the question that must be answered is this: "But for (except for) the breach of duty by the tortfeasor, would the injured party have suffered damages?" If the answer is no, then there is a link between the tortfeasor's conduct and the harm suffered by the injured party. The question can also be asked this way: "If the tortfeasor had complied with her legal duty, would the injured party have suffered damages?" Again, a no answer indicates a link and, thus, cause in fact. For example, suppose that Donald checks into Hotel's 20th-floor luxury suite. He watches a beautiful sunset while leaning on the balcony railing, but the railing snaps and Donald falls 20 stories. In a negligence analysis, one can reasonably conclude that Hotel owes Donald both a general duty and a special duty (innkeeper) and that the duty was breached because the rail was assumably defective in some way. To establish cause in fact, one would ask: But for the breach of duty by Hotel, would Donald have suffered damages? The answer is clearly no because if Hotel hadn't breached its duty (e.g., had inspected and kept the railing in good repair), Donald would not have suffered damages. Thus, the breach of duty by Hotel was the *cause in fact* of Donald's injuries.

Scope of But-For Test

One problem in applying the but-for test is its overreaching broadness. Its application may result in holding a tortfeasor liable for injuries that occurred well beyond the foreseeable scope of the wrongdoing. For example, in the Donald-Hotel case, suppose that after Donald's balcony rail snaps, Donald falls but the broken balcony rail also falls and penetrates the windshield of a car on the street below, injuring the driver. The injury causes the driver of the car to swerve, hit a pedestrian, and crash into an adjacent canal. A witness to the accident then attempts to rescue the driver of the car from the canal but drowns doing so. Five blocks away, a shopkeeper is so startled by the noise from the accident that she drops a priceless vase on her foot. In this set of accidental chain reactions, using the but-for test would impose liability on Hotel for each injury and damage, including those sustained by Donald, the driver of the car, the struck pedestrian, the drowned rescuer, and the shopkeeper who suffered foot injuries resulting from the destroyed vase. Nevertheless, a sense of fairness demands that the law cannot reasonably impose *all* of this liability on Hotel. At what point, if any, is the tortfeasor relieved from liability? The broad sweep of the but-for test requires a further step to establish liability. This step, known as **proximate (legal) cause**, is discussed next.

Proximate (Legal) Cause

In addition to showing that the tortfeasor's breach of duty was the cause in fact of the damages, the injured party must also prove that (1) the tortfeasor's conduct was also the closest-in-proximity cause of the damages and (2) the tortfeasor's liability wasn't canceled due to a superseding cause. These *proximate cause* concepts protect tortfeasors from liability for far-reaching and out-of-the-ordinary injuries resulting in damages from the tortious act.

Closest-in-Proximity

The majority of courts favor using *foreseeability* to define the scope of the risk. In the Donald-Hotel example discussed above, the jury would be charged with determining the scope of Hotel's liability. Liability would hinge on whether or not it was foreseeable that a faulty balcony railing would result in damages to be suffered by Donald (probable liability), the driver of the car (possible liability), the pedestrian (possible liability), the drowned rescuer (improbable liability), and the owner of the vase (very improbable liability). The Restatements define proximate cause as that which helps draw the line that determines when a tortfeasor is "not liable for harm different from harms whose risk made the [tortfeasor's] conduct tortious."

The proximate cause concept was first enunciated in Landmark Case 9.3, which is perhaps the most famous case in American tort law.

LANDMARK CASE 9.3 Palsgraf v. Long Island Railroad Co., 162 N.E. 99 (N.Y. Ct. App. 1928)

FACT SUMMARY Palsgraf bought a railroad ticket for Rockaway Beach, New York, and was waiting on the platform for her train. A different train arrived on a platform 100 yards away, allowed passengers to board, and began to depart from the station. Running to catch the departing train, two commuters grabbed onto the side and tried to hoist themselves up and into the moving car. To aid one of the men, the conductor on the train pulled him onto the train but dislodged a package covered in newspaper that the passenger was carrying. The package, which turned out to be fireworks, fell to the platform and exploded. The blast shook the station with sufficient force that large iron scales (used to weigh freight on various trains) hanging over Palsgraf fell on her, resulting in a severe injury. Palsgraf sued the Long Island Railroad for the conductor's negligent conduct of pulling the commuter onto the train, which eventually caused the explosion and her injury from the falling scales.

SYNOPSIS OF DECISION AND OPINION In a famous opinion written by Judge Benjamin Cardozo (who would later serve on the U.S. Supreme Court), the New York Court of Appeals ruled in favor of the Long Island Railroad. Cardozo reasoned that because the conductor *could not have known* that the man he was helping onto the train had a box full of fireworks, the action of the conductor was not a proximate-enough cause to incur liability for Palsgraf's injuries.

WORDS OF THE COURT: Proximate Cause "[T]he orbit of the danger as disclosed to the eye of reasonable vigilance would be the orbit of the duty. One who jostles one's neighbor in a crowd does not invade the rights of others standing at the outer fringe when the unintended contact casts a bomb upon the ground. The wrongdoer as to them is the man who carries the bomb, not the one who explodes it without suspicion of the danger. Life will have to be made over, and human nature transformed, before prevision so extravagant can be accepted as the norm of conduct, the customary standard to which behavior must conform. . . . The risk reasonably to be perceived defines the duty to be obeyed, and risk imports relation; it is risk to another or to others within the range of apprehension."

Case Questions

1. Are all the other elements of a negligence tort satisfied in this case?
2. Who else might Palsgraf have sued? For what?
3. *Focus on Critical Thinking:* Context is always important. This case was decided before any federal or state benefits for health care or lost time from work. The dissenting opinion in this case argued that public policy demanded that the Railroad pay for the injury because they were in the best position to pay and that some correlation existed between conduct and injury. In the 1928 context, does that strike you as a convincing argument? Why or why not?

Self-Check Proximate Cause

Is proximate cause met in these situations?

1. A truck driver crashes into a guardrail. During the accident, a defective steering wheel rapidly spins around, breaking the driver's arm. The driver sues the maker of the steering mechanism.
2. A tenant hurts herself falling down defective steps. The tenant sues the landlord's insurance company, alleging that it knew the steps were defective but insured him anyway, thus discouraging him from fixing them.
3. An employer burns down his warehouse for the insurance money. An employee is arrested and falsely imprisoned by the police for the crime. The employee sues the employer for negligence.
4. A passenger is injured in an automobile accident. The passenger sues the liquor store that sold alcohol to the driver of the car, who was already visibly intoxicated.

Answers to this Self-Check are provided at the end of the chapter.

Superseding Cause

Sometimes an *intervening* event takes place after the tortfeasor's negligent act. The intervening act may also contribute to the negligence by producing additional damages to the injured party. Some (but not all) intervening acts may be the basis for limiting a tortfeasor's liability. These acts are called *superseding causes* (i.e., they supersede the tortfeasor's liability) and they are also defined by *foreseeability*. For example, in the Donald-Hotel case, suppose that Donald falls only one story and sustains a broken wrist. While being driven to the hospital, a freak tornado hits the car that Donald is in and the wrist injury is made worse. In a case for damages related to the injury, even though the but-for test would impose liability on Hotel even for the aggravated broken wrist, Hotel's liability is discontinued (though not eliminated for the original injury) once the tornado hits the car. The tornado is a superseding cause and thus Hotel is not liable for the aggravated injury. This limit applies because it was not reasonably foreseeable by Hotel that Donald would be injured by a tornado en route to the hospital.

Legal Speak >))

Estate
In addition to land, assets, and personal property, a person's *estate* also consists of legal rights and entitlements after death, including the right to sue for the tortious conduct that caused the death.

Actual Damages

In order to recover in a negligence case, the tortfeasor must have caused another party **actual damages.** This means that the party alleging injury must prove that she has suffered some type of physical harm derived from an injury caused by the tortfeasor. An injured party may not prevail if the injuries are limited to mental and/or emotional harm alone. However, once a party has proved some *physical* harm, she is eligible for a variety of other types of damages, including out-of-pocket economic losses (such as medical bills), pain and suffering, lost time from employment, and similar categories. Punitive damages may be awarded but are rare because they can be awarded only when the tortfeasor's conduct has been extremely reckless or willful and wanton.[23]

[23]Punitive damages were sought in 12 percent of the estimated 25,000 tort and contract trials concluded in state courts in 2005. Punitive damages were awarded in 700 (5 percent) of the 14,359 trials in which the plaintiff prevailed. Among the trials in which punitive damages were requested by plaintiff winners, 30 percent received these damages. The median punitive-damage award among the 700 trials that resulted in punitive damages was \$64,000 in 2005, and 13 percent of these cases had punitive awards of \$1 million or more. (*Punitive Damage Awards in State Courts, 2005,* Special Report, U.S. Department of Justice, Office of Justice Programs, 2011.)

Many states allow a spouse or children of an injured party to recover damages related to the negligence. This includes loss of companionship or marital relations (known as *loss of consortium*). Moreover, if the injured party dies, his *estate* may sue for the damages that the injured party would have recovered if he had survived. Spouses and children may also recover damages for losses sustained by virtue of the death of an injured party.

Defenses to Negligence Claims

Once the elements of negligence are met, the analysis then shifts to potential defenses available to the tortfeasor. The two primary defenses to claims of negligence are **comparative negligence** and **assumption of the risk.**

Legal Speak >))

Punitive Damages
Monetary damages, generally a multiple of the actual damages, that are awarded partly to punish the tortfeasor and partly to deter others from acting in a similar manner.

Comparative Negligence

In cases where the injured party's conduct has played a factor in the harm suffered, the Restatements allow the tortfeasor to assert the defense of *comparative negligence*. This defense requires a jury to allocate the proportion of negligence committed by each party in terms of percentage (see Table 9.3). Ultimately, successfully asserting comparative negligence reduces (but does not eliminate) the final award to the plaintiff.

Note that comparative negligence is a cousin to the common law doctrine of *contributory negligence,* whereby even 1 percent of negligence on the part of the plaintiff is a complete bar to any plaintiff recovery. The overwhelming majority of states do not follow this standard because of its harshness on the injured party. Four states—Alabama, Maryland, North Carolina, and Virginia—along with the District of Columbia continue to recognize the contributory negligence defense. Indiana follows the contributory negligence rule in medical malpractice cases only.

Assumption of the Risk

When the injured party knows that a substantial and apparent risk is associated with certain conduct and the party goes ahead with the dangerous activity anyway, the Restatements allow the tortfeasor to assert the defense of *assumption of the risk* so long as (1) the injured party/plaintiff knows or should know (by virtue of the circumstances, warning signs, etc.) that a risk of harm is inherent in the activity and (2) the injured party/plaintiff voluntarily participates in the activity. Certain activities are considered to be "inherently dangerous" (such as bungee jumping or parachuting), and companies that are providers of these activities may have limited protection from liability if they act reasonably in minimizing the dangers and make full disclosures of the risks to participants.

TABLE 9.3 Comparative Negligence Formula

Suppose Abel is injured by Baker's conduct and suffers damages totaling \$100,000. A jury finds that Baker was 80 percent responsible for the injury but that Abel also contributed to his own injury and was 20 percent responsible for the harm. How much does Abel ultimately recover?

Damages suffered × Percentage of Baker's negligence = Recovery amount
\$100,000 × 80% = \$80,000

In Case 9.4, a state appellate court considers the assumption-of-the-risk defense in the context of leisure sports.

CASE 9.4 Zeidman v. Fisher, 980 A. 2d 637 (Pa. Super. Ct. 2009)

FACT SUMMARY Zeidman and Fisher were participants in a golf foursome at a charity tournament. On one hole where the view of the fairway was partially blocked, the foursome became concerned that they might inadvertently hit any players hidden by the blind spots on the fairway ahead of them. The group agreed that Zeidman would take a golf cart and ride ahead to see whether the course was clear for the group to hit. Zeidman made his observation and returned to his foursome in the cart. Because he intended on returning to his foursome to report that the group ahead was out of harm's way and because he never signaled to his group that it was safe to hit, Zeidman never entertained the possibility that one of his group would hit a shot. Before Zeidman returned, Fisher, becoming impatient, hit his shot while Zeidman was driving his cart back to the foursome. Fisher's shot was errant, and the ball struck Zeidman in the face, causing serious and permanent injuries. The trial court dismissed Zeidman's negligence lawsuit against Fisher on summary judgment, ruling that Zeidman had assumed the risk of participating in the golf match and this assumption of risk barred any recovery. Zeidman appealed.

SYNOPSIS OF DECISION AND OPINION The Pennsylvania Superior Court reversed the trial court's decision and ruled in favor of Zeidman. The court reasoned that the assumption-of-the-risk doctrine requires that the evidence show that the injured party (1) fully understood the specific risk, (2) voluntarily chose to encounter it, and (3) manifested a willingness to accept the known risk. In this case, an objectively reasonable person may have assumed that no risk existed because Zeidman's agreed-upon task was to check whether the fairway was clear and then report to his own foursome if it was safe to hit. Because he had not yet completed this task, Zeidman did not manifest a willingness to accept a known risk.

WORDS OF THE COURT: Assumption-of-the-Risk Doctrine "In the circumstances of the present case, it is obvious that Zeidman, on returning from his forward observer mission, did not consciously assume the risk of friendly fire when, to the contrary, he had every right to anticipate none of his playing partners would attempt a tee shot until his return to the tee box. To grant summary judgment on the basis of assumption of the risk it must first be concluded, as a matter of law, that the party consciously appreciated the risk that attended a certain endeavor. . . . Accordingly, whether Zeidman is able to convince a jury that his version of events is true remains to be seen, he, in any event is entitled to his day in court."

Case Questions

1. If Zeidman had signaled to his partners that all was clear from the fairway and was then hit while returning in the cart, would Fisher be entitled to a summary judgment based on assumption of the risk?
2. What duty did Fisher owe Zeidman in the first place? Was it a special-relationship duty?
3. *Focus on Critical Thinking:* What other leisure sports or activities might be covered under the assumption-of-the-risk doctrine? Is it good public policy to shield negilgent parties with the doctrine?

CONCEPT SUMMARY *Negligence Analysis*

- *Duty:* Did the tortfeasor owe a duty to the injured party?
- *Breach:* Did the tortfeasor breach the reasonably prudent person standard?
- *Causation:* Except for the tortfeasor's breach of duty, would the plaintiff have suffered the injury?

(continued)

- *Proximate (legal) cause:* Was the breach the closest in proximity? Were there any superseding causes? Was the harm foreseeable?
- *Damages:* Did the injury to person or property result in losses?
- *Defenses:* Did the injured party contribute to the injury (comparative negligence)? Did the injured party know of the risk but go ahead anyway (assumption of the risk)?

STRICT LIABILITY TORTS

The tort liability theories covered so far in this chapter are based on either intent or negligence. The Restatements also provide for liability in certain cases where neither intent nor negligence need be proved. This category of tort is known as *strict liability* and is recognized in the Restatements primarily for abnormally dangerous activities and for defective products (discussed in the next section).[24] Strict liability is a concept rooted in the notion that the general public benefits when liability is imposed on those who engage in certain activities that result in harm to another party, even if the activities are undertaken in the most careful manner possible (without negligence).

Abnormally Dangerous Activities

The Restatements set out a six-factor test to determine whether abnormally dangerous activities trigger strict liability for any harm caused by the activity:

- Does the activity involve a high degree of risk of some harm?
- Is there a likelihood that the harm that results will be great?
- Is it possible to eliminate the risk by exercising reasonable care?
- Is the activity relatively common?
- Is the location of the activity appropriate to the risk?
- Is there any community value that outweighs the dangerous attributes?

Strict liability is imposed on businesses engaged in abnormally dangerous operations such as the use of explosives in building demolition. © Image Source/Corbis

[24]Strict liability is also imposed under the common law for the keepers of wild or dangerous animals.

For example, suppose that ChemicalCo produces 100 pounds of plastic explosives for use in the demolition of a building. It leases a railroad car and ships the explosives to its storage warehouse until the buyer can pick them up. Before the buyer picks them up, thieves break in and inadvertently ignite the explosives. The explosion causes damage to several buildings and an injury to a party standing in the surrounding area. Using the six-factor test, a court will likely impose strict liability on ChemicalCo due to the nature of the abnormally dangerous activity of storing explosives. Other strict liability cases have involved the storage and use of toxic flammable liquids, nuclear power, and blasting for demolition or construction.

PRODUCTS LIABILITY

LO 9-8

Provide alternate theories of liability and defense that can be applied when a product is the cause of an injury.

Products liability refers to the liability of any seller (including the manufacturer, retailer, and any intermediary seller such as a wholesaler) of a product that, because of a defect, causes harm to a consumer. Note that modern products liability law protects not only the actual purchaser but also any ultimate users who are harmed by the product's defect. In a products liability case, the injured party may pursue a legal remedy against the seller under one of three theories: (1) negligence, (2) warranty, or (3) strict liability.

Negligence

The negligence analysis covered earlier in this chapter may also be applied to the seller of a product. Although historically negligence was severely limited as a remedy because the law protected only the actual purchaser, a revised rule announced in the landmark case of *MacPherson v. Buick*[25] has been adopted in every state. Under the *MacPherson* rule, one who negligently manufactures a product is liable for *any injuries to persons* (and, in some limited cases, property) proximately caused by the negligence. For example, suppose that Holmes purchases a motorcycle from a dealer and gives it to his son Wendell. Wendell is injured on the motorcycle and sues the manufacturer for negligence. So long as Wendell can prove negligence, the manufacturer will be liable for Wendell's injuries despite the fact that Wendell was not the one who entered into the purchase agreement with the dealer or the manufacturer.

Courts have found that manufacturers have the duty of care regarding proper design, manufacturing, testing, inspection, and shipping. Retailers do not have as comprehensive a duty as the manufacturer but still have a duty to warn consumers of any product they know or suspect to be unreasonably dangerous.

Warranty

Historically, warranty laws have been an important protection for purchasers because they impose liability even in the absence of negligence. When the seller makes a representation of fact about a product, this is known as an *express* warranty. If the seller has not made a specific representation about the product, the buyer may still be protected by a Uniform Commercial Code–imposed *implied* warranty. Warranties are set out in Article 2 (Sales) of the UCC and are discussed in detail in Chapter 21, "Consumer Protection Law."

Strict Liability

LO 9-9

Articulate what must be proved in negligence and strict liability cases and appreciate how the levels of proof differ.

The most appealing option for pursuing a products liability case is the doctrine of strict liability because the injured party need not prove the elements of negligence. In *Greenman v. Yuba Power Products, Inc.*,[26] the California Supreme Court decided a groundbreaking case that paved the way for adoption of a strict liability standard for product defects by ruling that "a manufacturer is strictly liable in tort when an article he places on the market, knowing that it is to be used without inspection for defects, proves to have a defect which causes injury to a human being." Two years after the *Greenman* case was decided, a similar doctrine of strict liability tort for the sellers of products was included in the *Restatement (Second) of Torts* in § 402A. The Restatements specifically indicate that liability still exists even if the seller has used all possible care. Note that the term *seller* means not only the product's manufacturer but also all business parties through the chain of commerce, including the retailer.

Section 402A is a bedrock for strict products liability because a substantial majority of states have adopted the section that imposes special liability on the seller of a product that could harm the user. Specifically, § 402A imposes strict liability on the seller so long as the injured party can show that the product was in a *defective* condition and that the defect rendered the product *unreasonably dangerous.* Liability under § 402A is triggered only when:

- The seller is engaged in the business of selling such a product, and
- The product is expected to and does reach the user or consumer without a substantial change in the condition in which it is sold.

Section 402A's strict liability is imposed on the seller even though:

- The seller has exercised all possible care in preparation and sale of the product, and
- The user or consumer has not bought the product from or entered into any contractual relationship with the seller (i.e., no *privity of contract* is required).

Defining "Defect"

For a party to recover for an injury caused by a product, the product must have been defective and must have created a danger that is outside the reasonable consumer's expectations. Courts have recognized several theories of unreasonably dangerous defects.

Design or Manufacturing Defect

A product may become dangerous if it is *designed* improperly in that foreseeable risks of harm posed by the product could have been reduced or avoided by some *alternative* design. Even products that are designed properly may still be rendered dangerously defective by some mistake made during the *manufacturing* process. For example, suppose CarCo designs a new car intended to have higher-than-average gas mileage. It achieves this by moving the gas tank to a different position on the car. The design, however, results in the gas tank rupturing during a rear-end crash. This is a classic *design* defect.[27] On the other hand, suppose CarCo designs the new car properly but one of the factory workers improperly installs the brakes and this eventually results in an injury. In this case the product has been rendered unreasonably dangerous via a *manufacturing* defect.

Inadequate Warning

Products that are ostensibly safe may carry risks unknown to a reasonable consumer. In such cases, the law requires the product to carry sufficient warnings and instructions. Failure to warn may render the product unreasonably dangerous even absent any manufacturing or design defect. One common category of inadequate-warning cases involves prescription drugs, but the theory of unreasonable danger applies to all products that carry some danger in use (such as a lawn mower or snow thrower).

[25] 111 N.E. 1050 (N.Y. 1916). The historical requirement that negligence suits could only be brought by the direct purchaser was known as *privity of contract.*

[26] 377 P.2d 897 (Cal. 1963).

[27] See Landmark Case 5.3 in Chapter 5, "Business, Societal, and Ethical Contexts of Law," for a case involving a design defect in an automobile that caused rear-end explosions.

In Case 9.5, an appellate court in California considers an inadequate-warning claim against the manufacturer of an above-ground pool.

CASE 9.5 Bunch v. Hoffinger Industries, 20 Cal. Rptr. 3d 780 (Cal. App. 2004)

FACT SUMMARY Bunch, an 11-year-old girl, dove into an above-ground pool that was only four feet deep. As a result, Bunch suffered a severe injury to her spine that rendered her quadriplegic. Bunch filed suit against Hoffinger as the manufacturer of the pool alleging, among other theories, that Hoffinger was liable for failing to provide adequate warnings which could have prevented the tragedy. Hoffinger argued that it did not owe any duty to warn consumers because the danger was "open and obvious." At trial, Bunch testified that she saw only a sticker that depicted a man doing a *pike* dive (knees straight and body bent at the waist) with the word "caution" and she thought that the caution referred only to pike diving. Bunch also called expert witnesses to testify that warnings to children between the ages of 7 and 12 must be concrete and spell out any consequences of diving into shallow water. Another of Bunch's experts testified that the risk of spinal paraplegia was not readily apparent to an 11-year-old and that it was difficult for someone in that age group to judge the depth of a pool. Hoffinger countered that (1) warning labels on pools were not feasible before it left the factory because the label would become distorted by the stretching of the liner, and (2) Bunch had assumed the risk because she had swum in that same pool prior to that occasion and ignored an adult present at the pool who warned against diving. The jury returned a verdict in Bunch's favor and awarded her $16,112,306. Hoffinger appealed.

SYNOPSIS OF DECISION AND OPINION The California Court of Appeals affirmed the judgment and verdict in favor of Bunch. The court rejected Hoffinger's contention that it owed no duty to warn Bunch of possible head injury from the open and obvious danger of diving headfirst into a shallow above-ground pool. Although the court acknowledged that some previous cases have held that no recovery was available for those who made a shallow dive into an above-ground pool because the danger was obvious, they distinguished those cases from the facts in this case because Bunch was only 11 years old. Age was one of the important factors in determining an awareness of open or obvious danger. It also rejected Hoffinger's assumption of the risk argument and ruled that any assumed risk by an injured party does not insulate equipment suppliers from liability for injury from providing defective equipment.

With respect to the failure-to-warn issue, the court held that the jury's conclusions were sound and in accord with expert testimony that pool industry standards require manufacturers to prominently display permanent warnings on their pools and that Hoffinger's sticker was below industry standards. Thus, the court concluded that the record supported the jury's determination that Hoffinger's warnings were inadequate.

WORDS OF THE COURT: Lack of Effective Warning "Given the testimony of Bunch and her two expert witnesses, we find sufficient evidence to support the conclusion that the lack of adequate warning label was neither a negligible nor theoretical contribution to Bunch's injury. The evidence presented at trial revealed that the lack for persuasive label outlining the consequences of diving into the pool was a substantial factor in causing the injury. As the [California] Supreme Court points out 'a very minor force that does cause harm is a substantial factor.' Here, at the very least, the lack of an effective warning was a minor force in bringing about the fateful dive."

Case Questions

1. Why is the injured party's age one of the most important factors in considering a failure-to-warn claim?
2. Do you agree with Hoffinger's contention that the injured party assumed the risk? Why or why not?
3. *Focus on Critical Thinking:* What other products can you think of that may require a more effective warning given the age of the average user? Should bicycles, skateboards, and snow boards fall into the same category? Why or why not?

Improper Packaging

A court found that Tylenol's packaging was not defective and thus the company was not liable for any injuries resulting from third- party tampering.

A product can be rendered unreasonably dangerous by a defect in the packaging. Cases that have recognized this theory of defect are primarily asserted against manufacturers of products that require safety-proof containers as well as food or beverage packages that clearly indicate whether the product is sealed or whether there is evidence of tampering (e.g., a seal on a bottle of juice). Perhaps the most famous case related to improper packaging involved the well-publicized Tylenol scare in 1986. In *Elsroth v. Johnson & Johnson,*[28] a federal court in New York held that Johnson & Johnson, the manufacturer of Tylenol, was not liable for the death of a consumer who was the victim of tampering by an unknown third party. The estate of the consumer brought suit, claiming that improper packaging had led to the tampering when an unknown third party removed a package of Tylenol from a supermarket shelf, laced it with cyanide, and then somehow resealed the container and box so the tampering was not readily detectable. However, the court pointed to the fact that the Tylenol bottle featured a foil seal glued to the mouth of the container, a shrink-wrap seal around the neck and cap of the bottle, and a box sealed with glue in which the bottle was placed. Because Johnson & Johnson went above and beyond existing standards by using three different methods to prevent consumption of a tampered product, the company could not be held liable under § 402A.

Unavoidably Unsafe

Some products are inherently dangerous. That is, some products are designed and manufactured correctly, and adequate warning has been given, but the product is still dangerous (such as a handgun). Courts have struggled to adjudicate strict liability standards in cases relating to prescription drugs, cigarettes, and guns. In each case, the product was properly manufactured and designed. The evolving view of products liability theories for cigarettes and guns is explored in more detail in *Legal/Ethical Reflection and Discussion.*

LEGAL/ETHICAL REFLECTION AND DISCUSSION

Products Liability and Guns

The prevalence of gun violence in America has led some victims to use products liability theories in an attempt to halt sales of certain guns used in mass shootings and hold gun manufacturers liable for damages suffered by the victims. The families of the victims in the 2012 Sandy Hook Elementary School massacre in Newtown, Connecticut, filed a products liability lawsuit against Remington Firearms International for, among other claims, wrongful death and pain and suffering. Remington is the parent company that manufactures and markets the Bushmaster XM15, a version of the notorious AR-15 semiautomatic rifle. The AR-15 has a bloody pedigree. In addition to the Sandy Hook murders, killers used an AR-15 style rifle in mass shootings at a nightclub in Orlando, Florida (2016), a workplace in San Bernardino, California (2015), community college campuses in Roseburg, Oregon (2015), and Santa Monica, California (2013), and a movie theater in Aurora, Colorado (2012).

The Sandy Hook lawsuit is a products liability claim based on both negligence and strict liability for

(continued)

[28]700 F. Supp. 151 (1988).

unsafe products. The suit alleged that the AR-15 is the "weapon of choice for shooters looking to inflict maximum casualties," and "American schools are on the forefront of such violence." The Sandy Hook plaintiffs drew on similar legal strategies used in the past to hold cigarette manufacturers liable for smoking-related deaths. As more than 40 states brought lawsuits against the tobacco industry by 1998, manufacturers agreed to an array of marketing and product use restrictions such as a ban on billboards, transit advertisements, and tobacco brand logos on clothing and merchandise. The tobacco settlement also required cigarette makers to pay $1.45 billion to finance advertisements deterring underage tobacco use. Despite the settlement, tobacco companies still faced increasingly successful lawsuits from individuals and were stung recently by a $51 million award of a California jury to a heavy smoker with inoperable lung cancer. The jury rejected big tobacco's standard defense, assumption of the risk, after finding substantial evidence that tobacco's manufacturers conspired to cover up the known dangers and addictions of cigarette smoking for decades. Tobacco companies are continuing to suffer heavy losses in courtrooms across America.

However, the Sandy Hook plaintiffs had to overcome a significant barrier that tobacco plaintiffs did not. The Protection of Lawful Commerce in Arms Act (PLCAA)[29] exempts gun manufacturers from products liability lawsuits brought by parties suffering damages as a result of a third party's criminal act. The law was a response to a wave of products liability lawsuits filed against gun manufacturers starting in 2002. Nonetheless, the law does contain important exceptions related to negligent entrustment and improper marketing. Therefore, the Sandy Hook plaintiffs strategically decided to focus primarily on Remington's marketing and sales strategies as reckless:

> Remington knowingly sold the AR-15 with no conceivable use . . . other than the mass killing of other human beings and unscrupulously marketed and promoted the assaultive qualities and military uses of AR-15s to a demographic of young civilians. . . . Invoking the unparalleled destructive power of the weapon, [Remington's] advertising copy read: "Forces of opposition, bow down. You are single-handedly outnumbered."
>
> *Soto v. Bushmaster Firearms, Conn. Superior Ct., Plaintiff's First Am. Compl. 72–74, (Oct. 29, 2015)*

Remington filed a motion to dismiss the lawsuit asserting immunity under the PLCAA. The trial court refused to dismiss the claims ruling that the Sandy Hook plaintiffs had asserted a legally cognizable theory that Remington's conduct fell into a PLCAA exception. The court ruled that the issue of whether the PLCAA exception applied was one for a jury and therefore the lawsuit could not be dismissed.[30]

Discussion Questions

1. Should gun manufacturers be held strictly liable for harm caused by their products? Why or why not? Is it good public policy?
2. Compare and contrast the theories used by tobacco plaintiffs versus gun manufacturing plaintiffs. How are they similar and how are they distinguishable?
3. Why did Congress opt to pass legislation to protect gun manufacturers when no other industry has similar protection? Was it pure politics or is there a policy justification? Was it ethical?
4. *The Wall Street Journal* reported that the sale of guns increased after the Sandy Hook and Orlando massacres. How do you account for that phenomenon?
5. According to CNBC, over 5 million Americans own an AR-15 style weapon.[31] As a practical matter, would an outright ban on the weapon be effective? What would be the commercial, social, and political impact of a government-imposed ban on semiautomatic rifles?
6. Use your favorite search engine to find "Sandy Hook Hoax" that will reveal a dark side of social media. Should the First Amendment cover such speech? What remedies are available to the families of the victims against the hoax theorists? Is the theory of Sandy Hook as a hoax proper subject matter to debate? Should Facebook or other social media sites take action against the hoax theorists?

[29] 15 USC §§ 7901 *et seq.*

[30] *Soto v. Bushmaster Firearms,* Conn. Superior Ct., Memorandum of Decision, Docket FBT-CV-15-6048103-S (April 14, 2016)

[31] http://www.cnbc.com/2016/06/13/owned-by-5-million-americans-ar-15-under-renewed-fire-after-orlando-massacre.html

Causation and Damages

Once it has been established that the product is unreasonably dangerous, the injured party must prove only that the defective product was the cause of the injuries and that the product caused an actual injury that resulted in damages.

Seller's Defenses

Although strict liability imposes a relatively onerous burden on the seller, the law recognizes several defenses for a seller even if the injured party has established all of the required elements for liability.

Substantial Change

The Restatements draw a line of liability based on the condition of the product at the time it leaves the seller's control. For strict liability to apply, the product must reach the end user without substantial change. Thus, if a product leaves the manufacturing plant in a reasonable condition (not dangerous) and then is contaminated or damaged in the next stage of the commercial chain of delivery, any resulting harm is outside the strict liability model. Depending on the circumstances, of course, the manufacturer may still be liable for negligence but not under strict liability.

Assumption of the Risk

Although courts apply this defense narrowly,[32] it is still recognized as a defense for sellers in a strict product liability case. An injured party has assumed the risk if the party knows or should have known about the risk and disregards this risk by continuing with the activity at issue for her own benefit. For example, suppose that WidgetCo owns a high-speed machine for producing widgets and a foreign object lodges in the machine while it is operating. The instructions warn to shut down the machine before removing the object, but the plant manager decides against a shutdown, fearing it will cost money from lost production time. If the plant manager is injured while removing the object from the operating machinery and sues the machine's manufacturer under a strict product liability theory, the manufacturer may successfully assert the assumption-of-the-risk defense.[33]

Sometimes a large quantity of goods is sold to the public before a dangerous defect in the product is discovered. That product may then be recalled. If a consumer is made fully aware of a product recall due to a design or manufacturing defect but continues to use the product, assumption of risk may be asserted if injury and a lawsuit result.

Misuse of Product

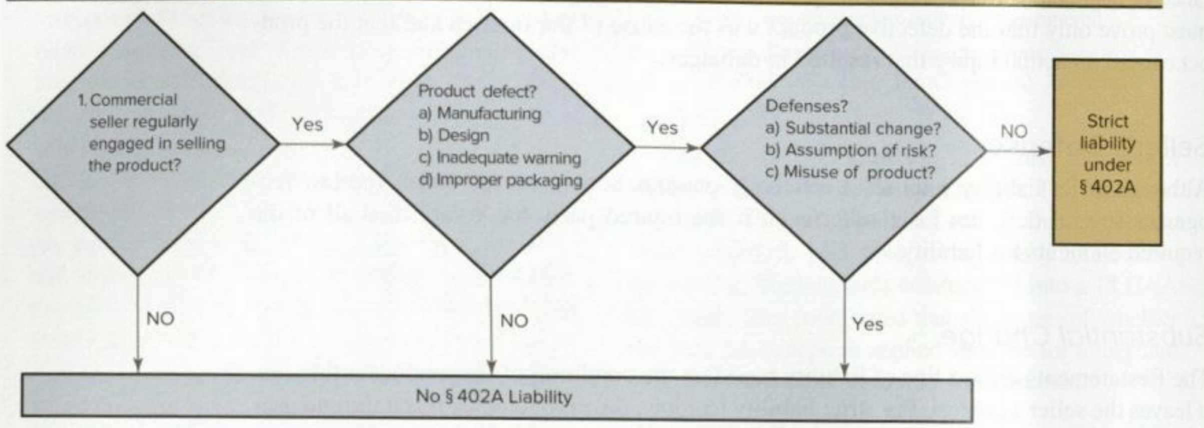
In a case where the injured party may not know of a certain risk and yet fails to use the product in a manner in which an ordinarily prudent person would, the seller may use product misuse as a defense. Courts have been reluctant to allow this defense unless the particular use of the product is so far from its ordinary use that it is not reasonably foreseeable by the seller.

Figure 9.1 provides an analysis of how liability is determined to apply or not apply under UCC § 402A.

[32] See *Assumption of Risk and Strict Products Liability,* 95 Harv. L. Rev. 872 (1982).

[33] Based on *Micallef v. Miehle Co.,* 348 N.E.2d 571 (N.Y. Ct. App. 1976).

FIGURE 9.1 Section 402A Liability



CONCEPT SUMMARY *Strict Liability and Products Liability*

Strict liability:

- Applies to abnormally dangerous activities.
- Applies in the absence of negligence.
- Applies regardless of the care exercised by the tortfeasor.

Products liability:

- Makes a company liable for design or manufacturing defects that cause harm.
- Applies in the absence of proof of negligent design or manufacture.
- Requires that injured parties prove only the defect and injuries; causation is not required.
- Can apply if a warning of a known danger or defect is not issued.

KEY TERMS

Tort p. 275 A civil wrong in which one party's action or inaction causes a loss to be suffered by another party.

Tortfeasor p. 275 One who commits a civil wrong against another that results in injury to person or property.

Tortious conduct p. 275 The wrongful action or inaction of a tortfeasor.

Restatement of Torts p. 275 An influential document issued by the American Law Institute that summarizes the general principles of U.S. tort law and is recognized by the courts as a source of widely applied principles of law. ALI has amended the Restatements twice, resulting in the *Restatement (Second) of Torts and* the *Restatement (Third) of Torts.*

Intentional torts p. 275 A category of torts in which the tortfeasor was willful in bringing about a particular event that caused harm to another party.

Negligence p. 275 A category of torts in which the tortfeasor was without willful intent in bringing about a particular event that caused harm to another party.

Strict liability p. 275 A category of torts in which a tortfeasor may be held liable for an act regardless of intent or willfulness; applies primarily to cases of defective products and abnormally dangerous activities.

Libel p. 276 Written defamation, in which someone publishes in print (words or pictures), writes, or broadcasts through radio, television, or film an untruth about another that will do harm to that person's reputation or honesty or subject a party to hate, contempt, or ridicule.

Slander p. 276 Oral defamation, in which someone tells one or more persons an untruth about another that will harm the reputation or honesty of the person defamed or subject a party to hate, contempt, or ridicule.

Absolute privilege p. 277 A defense to a defamation claim whereby the defendant need not proffer any further evidence to assert the defense; provided to government officials, judicial officers and proceedings, and state legislatures.

Qualified privilege p. 277 A defense to a defamation claim whereby the defendant must offer evidence of good faith and be absent of malice to be shielded from liability; provided for the media and employers.

Trade libel p. 279 A tort in which a competitor has made a false statement that disparaged a competing product.

Product disparagement statutes p. 279 Statutes intended to protect the interest of a state's major industries, such as agriculture, dairy, or beef.

Communications Decency Act (CDA) of 1996 p. 281 Federal legislation that extends immunity to Internet service providers (ISPs) by protecting them from any defamation liability as a "publisher or speaker of any information provided by another information content provider."

Merchant's privilege p. 281 A narrow privilege, provided for in the Restatements, that shields a merchant from liability for temporarily detaining a party who is reasonably suspected of stealing merchandise.

Duty p. 285 A fundamental element that must be proved to recover in a negligence lawsuit against a tortfeasor: The injured party must prove that the tortfeasor owed him a duty of care.

Misfeasance p. 286 An act by one party that harms or endangers another party.

Nonfeasance p. 286 The failure to act or intervene in a certain situation.

Special relationship p. 286 In tort law, a heightened duty created between certain parties, such as that of a common carrier to its passengers, innkeepers to guests, employers to employees, businesses to patrons, a school to students, and a landlord to tenants and landowners.

Breach of duty p. 288 A fundamental element that must be proved to recover in a negligence lawsuit against a tortfeasor: The injured party must prove that the tortfeasor failed to exercise reasonable care in fulfilling her obligations.

Cause in fact p. 290 A fundamental element that must be proved to recover in a negligence lawsuit against a tortfeasor: The injured party must prove that, except for the breach of duty by the tortfeasor, he would not have suffered damages.

Proximate (legal) cause p. 290 A fundamental element that must be proved to recover in a negligence lawsuit against a tortfeasor: The injured party must prove a legally recognized and close-in-proximity link between the breach of duty and the damages suffered.

Actual damages p. 292 A fundamental element that must be proved to recover in a negligence lawsuit against a tortfeasor: The injured party must prove that she suffered some physical harm that resulted in identifiable losses.

Comparative negligence p. 293 A defense to claims of negligence in which the injured party's conduct has played a factor in the harm suffered and, thus, the proportion of negligence should be divided.

Assumption of the risk p. 293 A defense to claims of negligence in which the injured party knew that a substantial and apparent risk was associated with certain conduct and the party went ahead with the dangerous activity anyway.

CHAPTER REVIEW QUESTIONS

1. Which of the following is *not* an element of defamation?

a. Specificity

b. Damages

c. Dissemination to a third party

d. Malice

2. A breach of duty may be established by showing:

a. Violation of a safety statute.

b. Breach of common law standards of behavior.

c. *Res ipsa loquiter* ("the thing/matter speaks for itself").

d. All of the above.

3. **Ginger uses the wrong type of cleaner fluid to clean out the deep fryer in her café and causes an explosion. The explosion causes the café's front window to shatter and injures a pedestrian walking on the public sidewalk in front of the café at the time of the explosion. In a suit against Ginger for negligence:**
   a. Ginger wins because she owed no duty to the pedestrian.
   b. Ginger wins because there is not sufficient proximate cause.
   c. Pedestrian wins because Ginger owes him a special duty.
   d. Pedestrian wins because Ginger's actions were the cause and proximate cause of the injury.
4. **Stuart attends a baseball game and, on his way to his seat, he is struck by a foul ball. He sues the stadium owner for negligence. What will be the owner's best defense?**
   a. Contributory negligence
   b. Comparative negligence
   c. Assumption of the risk
   d. Products liability
5. **A product may be unreasonably dangerous due to a _______ or _______ defect.**
   a. Risk, reward
   b. Risk, design
   c. Design, manufacturing
   d. Manufacturing, assumption

Answers and explanations are provided at the end of this chapter.

THEORY TO PRACTICE

Computer Installers (CI) Inc. is a company that sells, installs, and maintains computer networks for organizations that have large numbers of users. CI entered into a contract with Big Time Firm (BTF) to replace the firm's computer network. CI's contract included routine installation tasks such as laying network cable and wiring in the various offices to facilitate numerous network users simultaneously, installing new PCs in one-third of the network user stations, and setting up an appropriate network server with sufficient backup capability. CI arrived on March 1 and began work on rewiring BTF's office to facilitate the new computer system. In the process of installing the new cabling for the network, a CI technician accidentally rewired the system that controlled the fire sprinklers and rendered the sprinklers inoperable.

Office Cleaners (OC) Inc. was cleaning BTF's offices at night on March 2. One of OC's employees left a lit cigarette in one of BTF's restrooms. That night, as a result of the lit cigarette, a small fire began in the restroom. Because the sprinklers were inoperable, the fire spread and caused damage to the entire office and equipment in the amount of $50,000.

1. What level of duty does CI owe to BTF, and has CI breached that duty?
2. To what extent is the concept of cause in fact versus proximate cause important in regard to CI's liability?
3. At what point, if any, is CI's liability cut off? Does OC assume full liability for the fire?
4. Assume that BTF had fired its night security guard on February 1 and never refilled the position. Thus, no guard was present when the fire started. Articulate a possible defense for CI and OC based on this fact.
5. Suppose that after the incident the sales manager of Data Management Inc., one of CI's competitors, is having lunch with Sheldon, the chief information officer of City Hospital. City Hospital has an existing contract with CI to maintain City Hospital's network. During lunch, Data Management's sales manager tells Sheldon about the fire incident and also states that, based on his personal knowledge, CI is a shoddy outfit that has a poor reputation in the industry. The sales manager then proposes a new Data Management information system for City Hospital at a lower price than CI's. When Sheldon is reluctant to consider the offer, Data Management's sales manager offers to pay any penalty that City Hospital suffers as a result of canceling the CI contract. Sheldon cancels the contract with CI, citing customer service problems. What possible torts have been committed? What are the requirements for CI to recover damages?

LEGAL STRATEGY 101

Disclaimers

Jennifer Lawrence. © Gabe Ginsberg/WireImage/Getty Images

An essential legal strategy in the world of business is *legal risk management* or *prevention*. In brief, business firms work in tandem with their attorneys in order to anticipate legal problems before they occur and to take effective steps ahead of time to minimize such legal risks and potential civil liability exposure. This legal strategy identifies and minimizes future legal risks to the business.

A common method for minimizing legal risks in tort cases, for instance, is the use of disclaimers or "limitation of liability" clauses in business contracts. Although disclaimers are generally legally enforceable, courts may or may not enforce a particular disclaimer, depending on the facts of each case and the wording of the disclaimer. From a strategic perspective, however, disclaimers are designed to protect business firms from potential civil liability for negligence and other harms under tort law.

Thus a well-drafted disclaimer is a strategic or defensive measure, one that anticipates and attempts to reduce the risk of tort liability in certain situations. By way of example, consider the "terms and conditions" that computer users must agree to when installing a software update or when signing up for a free Internet service like Gmail or Facebook. Among the many provisions in the terms and conditions there may be a disclaimer, and by clicking "I Agree" in the dialogue box, users are agreeing to the disclaimer as a matter of contract.

To illustrate, let's take a look at an actual disclaimer. Apple operates a *cloud computing* or data-storage service called iCloud. This service provides iCloud users the ability to save and store their personal data on remote servers, including such electronic data as photos, documents, and music files. After the iCloud accounts of many celebrities (e.g., Jennifer Lawrence, pictured) were hacked, Apple inserted (in ALL CAPS and underlined) the following disclaimer language in its iCloud Terms and Conditions:

> APPLE DOES NOT REPRESENT OR GUARANTEE THAT [iCLOUD] WILL BE FREE FROM LOSS, CORRUPTION, ATTACK, VIRUSES, INTERFERENCE, HACKING, OR OTHER SECURITY INTRUSION, AND APPLE DISCLAIMS ANY LIABILITY RELATING THERETO. [*]

CRITICAL THINKING QUESTIONS

1. Based on what you have studied in this chapter, was Apple negligent for not taking stronger measures to protect the iCloud accounts of its users from third-party hackers?
2. What legal or nonlegal strategies could iCloud users employ against Apple to defeat or circumvent Apple's disclaimer?

*You can read the entire set of iCloud terms and conditions for yourself here: http://www.apple.com/legal/internet-services/icloud/en/terms.html.

MANAGER'S CHALLENGE

Another context in which managers encounter tort law is the area of employment checks and references. Suppose that the technician installer employed by CI in the Theory to Practice problem was suspended for incompetence. The installer was so enraged that he threatened his fellow employees with bodily harm and was subsequently fired. The installer sought new employment and listed several CI managers as

CHAPTER 22

Criminal Law and Procedure in Business

Learning Objectives

After studying this chapter, students who have mastered the material will be able to:

22-1 Explain the origins and sources of criminal law and procedure.
22-2 Distinguish between criminal law and criminal procedure.
22-3 Compare criminal law with civil law.
22-4 Articulate the underlying tenets of criminal law and the requirements for criminal liability.
22-5 Identify circumstances in which business managers and owners may be liable for criminal violations by a corporation.
22-6 Give specific examples of white-collar crime laws that may impact a business entity and/or its owners and managers.
22-7 Explain the steps in the criminal justice system.
22-8 Name and explain the various constitutional procedural protections afforded to those accused of a crime.
22-9 Understand the exclusionary rule and how it applies to business.

One way that the government regulates the practices and operations of business owners and managers is through **criminal law**. This chapter focuses on how criminal law, criminal procedure, and the criminal justice system impact the legal environment of business. In this chapter, students will learn:

- The origins and sources of criminal law.
- Elements and examples of criminal acts.
- The steps in the criminal justice system.
- Legal protections for those accused of committing a crime.

ORIGINS AND SOURCES OF CRIMINAL LAW AND PROCEDURE

Crime in the United States is ordinarily dealt with by state authorities, predominantly under state statutory law. While each state has its own system of criminal law, there is an increasing body of federal criminal law. Thus, the federal criminal justice system exists alongside (sometimes overlapping) the state systems. Much of American criminal law is derived from English criminal law, which existed primarily as common law with some statutory mandates. However, in the 1960s, state legislatures began to assemble various statutes addressing criminal culpability and integrating state common law to form more comprehensive criminal codes.

LO 22-1
Explain the origins and sources of criminal law and procedure.

MODERN CRIMINAL LAW: THE MODEL PENAL CODE

Nearly two-thirds of the states have enacted criminal codes based on the **Model Penal Code (MPC)** adopted by the American Law Institute (ALI) in 1962.[1] The vocabulary and formation of the MPC have been very influential in shaping criminal law notions, even in states where the MPC has not been formally adopted. However, many states have retained certain portions of their common law within their criminal codes as well.

In 1971, the congressionally appointed National Commission on Reform of Federal Criminal Laws issued a model federal criminal code that consolidated and clarified existing statutory law. However, it has long been settled that there are no federal common law crimes.[2] Although a state criminal statute and a federal criminal statute may outlaw identical or substantially identical conduct, state law and federal law may coexist unless the federal statute contains specific language that preempts state law.[3]

LO 22-2
Distinguish between criminal law and criminal procedure.

CRIMINAL LAW VERSUS CRIMINAL PROCEDURE

While *criminal law* defines the boundaries of behavior and prescribes sanctions for violating those boundaries, **criminal procedure** refers to the legal process and safeguards afforded to individuals (and in some cases business entities) during criminal investigations, arrests, trials, and sentencing. Criminal *law* consists of a body of law that, for the purposes of preventing harm to society, declares what conduct is criminal and prescribes the punishment to be imposed for such conduct. Criminal *procedure* sets limits on the government's authority in applying criminal law. Criminal procedure is covered in detail later in this chapter.

LO 22-3
Compare criminal law with civil law.

Legal Speak >))

Culpability
The quality of being blameworthy in criminal law; it is used to assess the guilt and determine whether he committed the crime purposefully, knowingly, recklessly, or negligently.

Criminal Law and Civil Law

Recall the distinctions between civil law and criminal law covered in Chapter 1, "Legal Foundations." Civil laws are designed to compensate parties (including businesses) for damages as a result of another's conduct. Criminal statutes are a protection of *society*, and the violation of a criminal law results in a penalty to the violator, such as a fine or imprisonment, based on the wrongdoer's level of culpability. It is important to remember that these categories are not mutually exclusive; one can violate a criminal law and commit a civil wrong in the very same act. For example, suppose that Mcduff is an accountant for Shakespeare Book Company (SBC) and steals $100,000 from the business by creating a fake employee on the company's books and secretly paying the fake employee's salary to himself. Upon discovery, SBC notifies the authorities, and Mcduff will likely be charged with various criminal offenses such as grand theft and fraud. If he is convicted, he will likely be incarcerated for an extended period of time. Although sometimes courts order restitution as part of a criminal sentence, SBC may also choose to file a civil lawsuit against Mcduff individually in

KEY POINT

Criminal *law* defines the boundaries of behavior and prescribes sanctions for violating those boundaries; criminal *procedure* refers to legal protections provided to citizens during criminal investigations, arrests, trials, and sentencing.

[1] Recall from Chapter 1, "Legal Foundations," that the ALI is an organization of attorneys, judges, and law professors that produces model statutes to promote consistency in the application of the law from state to state.

[2] *U.S. v. Hudson and Goodwin*, 11 U.S. 32 (1812).

[3] *Goldstein v. California*, 412 U.S. 546 (1973).

order to recover the losses due to Mcduff's commission of the tort[4] of conversion (the civil counterpart of theft). SBC may also be entitled to compensation from Mcduff for other incidental expenses it incurred as a result of the theft (such as costs of detecting the theft). If SBC is successful in obtaining a civil judgment against Mcduff, the company may then attempt to recover its losses by tapping Mcduff's personal assets.

Burden of Proof

One significant difference between a criminal case and a civil case is the **burden of proof**. In a civil case, the plaintiff needs to prove only by a **preponderance of the evidence** that the defendant committed a civil wrong. This means that the fact finder need not be completely convinced that the plaintiff's arguments in the case should prevail. Rather, the fact finder need be convinced only that the defendant's liability was *more likely than not* for the plaintiff to meet her burden of proof. In criminal cases, where the stakes may involve an individual's liberty, the standard of proof is much higher. In a criminal case, the government must prove its case **beyond a reasonable doubt**. Thus, a fact finder must be convinced that the defendant's criminal liability is not in doubt to a reasonable person.

LO 22-4

Articulate the underlying tenets of criminal law and the requirements for criminal liability.

General Principles of Criminal Law

There are two important underlying tenets to criminal law: *legality* and *punishment*. The principle of **legality** is a protection of individuals from being charged with some unspecified general offense. Legality simply requires that crimes be specifically proscribed by law in advance of the conduct sought to be punished. This includes the notion that the Constitution bars both Congress and state legislatures from enacting retroactive criminal statutes (known as *ex post facto* laws). Statutes that fail to give fair warning that a particular conduct is unlawful may be struck down by the courts as too vague. The principle of **punishment** is based on the concepts that (1) criminal law acts as a *deterrent,* (2) it *removes* dangerous criminals from the population, and (3) *rehabilitation* is an important part of the criminal justice system. Punishments are applied using a sentencing system that follows a general range of years prescribed by the legislature. After conviction, a sentence is imposed by the court based on the individual trial judge's discretion and assessment of the severity of the crime and mitigating circumstances. However, starting in the 1980s, public dissatisfaction with an actual or perceived view that courts were not imposing sufficiently stiff penalties spurred federal and state legislatures to pass laws requiring courts to assess penalties based on statutorily prescribed **sentencing guidelines**. These guidelines have had the impact of severely restricting judicial discretion. This same movement is also responsible for a spate of statutes that include mandatory minimum sentences for certain offenses as well as minimum sentences for repeat offenders (for example, some states adopted a "three strikes" law, which requires a 25-year sentence for a third felony conviction). Despite criticism by many prominent judges, attorneys, and legal scholars on various fronts, state and federal legislators continue to generally support the concept of sentencing guidelines and mandatory minimums.

Legal Speak >))

Mitigating Circumstances
Facts that do not excuse a crime but may lessen the punishment. For example, mitigating circumstances that might lessen the sentence for murder from death to life imprisonment include no prior criminal history, minor participation in the killing, mental illness, or young age at the time of the killing.

Criminal Liability

From a legal perspective, a crime has two parts: (1) a physical part, in which the defendant committed an *act* or *omission,* and (2) a mental part, which involves the defendant's subjective *state of mind.* Thus, an analysis of criminal liability involves three fundamental questions: First, did the defendant actually commit the prohibited act? Second, did the defendant have a culpable state of mind? Third, does the law give the defendant a palpable defense (such as a self-defense claim to a homicide charge)?

[4]Torts were covered in detail in Chapter 9, "Torts and Products Liability."

Act Requirement

The **act requirement**, also called by its Latin name, *actus reus,* requires the government to prove that a defendant's actions objectively satisfied the elements of a particular offense. The act requirement is based on the fundamental criminal law tenet that evil thoughts alone do not constitute a criminal act. Rather, there must be some overt conduct (either an act or an omission), and it must be voluntary. Courts generally follow the rule that an act is voluntary unless it is demonstrated that the defendant acted based on physical compulsion, reflex, or certain physiological or neurological diseases. An act by omission occurs when a crime is defined in terms of *failure* to act. For example, if the chief financial officer fails to disclose data required by federal securities law, she has committed an omission that satisfies the act requirement.

Mental Requirement

The mental element, also called by its Latin name, *mens rea,* which translates literally into "guilty mind," requires that the defendant have a requisite degree of culpability with regard to each element of a given crime. The fundamental underpinning is that an act does not make a person guilty unless his mind is guilty.[5] The words contained in a criminal statute to express the guilty mind requirement include *intentionally, knowingly, maliciously, willfully,* and *wantonly.* However, some criminal statutes set the intent requirement at mere recklessness or negligence, rather than actual intent, in determining the level of culpability. Thus, an act or omission in which the defendant's conduct deviated from the standard of conduct so grossly that a reasonable person would judge it as criminal may also satisfy the mental element requirement.

Courts and legislatures have also established certain rules for applying the mental element requirement in cases of *mistake.* Certain statutes also impose *strict liability,* whereby the mental element is assumed by certain conduct so that the defendant's culpable state of mind need not be proved.

Figure 22.1 illustrates the typical language of the act requirement and the mental requirement, using an example from a Florida criminal statute prohibiting forgery.

FIGURE 22.1 Excerpt from a Florida Criminal Statute: F.S.A. § 831.02

Uttering forged instruments

"Whoever ***utters*** and ***publishes*** as true a false, forged or altered record, deed, instrument or other writing mentioned in § 831.01 (i.e., "letter of attorney, policy of insurance, bill of lading, bill of exchange or promissory note, or an order, acquittance, or discharge for money or other property") ***knowing*** the same to be false, altered, forged or counterfeited, with ***intent*** to injure or defraud any person, shall be guilty of a felony of the third degree."

Defenses

Even when the requisite mental state and criminal act standards are proved, the law provides for certain defenses based on unique circumstances of the crime. **Self-defense** is an example of a defense to a criminal charge of homicide in that the law recognizes that certain cases necessitate the use of deadly force to repel an attack in which the defendant reasonably fears that death or substantial harm is about to occur either to the defendant or to a third party. The rules governing self-defense are complex and vary from state to

[5]Expressed as the common law Latin maxim: *Actus not facit reum nisi mens sit rea* (Collins Latin, 2009).

state, especially on the question of whether the defendant is required to retreat before using deadly force. The defense afforded by the self-defense doctrine is at its height when it involves use of deadly force to repel an attack in the victim's home or place of business.

The other major category of defense is **mental incapacity**. As you may imagine, this defense is very controversial and is sometimes colloquially called the *insanity defense.* That term is potentially misleading because in certain jurisdictions incapacity covers a wide variety of conditions in addition to insanity. Although mental incapacity has a variety of definitions depending on the jurisdiction, the Model Penal Code (MPC) requires the defendant's actions to be related to some type of mental disease or defect.[6] The MPC also specifically rules out any sociopathic personality disorders as the basis for a mental incapacity case.

Less frequently asserted defenses include *duress,* in which a defendant has committed a crime in response to another person's threat to inflict personal injury (threats to property or reputation are insufficient), and *intoxication,* which generally depends on whether the intoxication was voluntary or involuntary. If voluntary, the criminal act is excused only if the defendant was so intoxicated that he could not form the requisite mental intent (guilty mind) to have criminal culpability. If involuntary, the defense is broader but still requires proof that the intoxication rendered the defendant unable to understand that his conduct constituted a crime.

Types of Crimes

Crimes may be classified in several different ways. **Felonies** are crimes that generally carry *one year or more* of incarceration as the penalty. **Misdemeanors** are crimes that carry *up to one year* of incarceration as the penalty. Frequently, states also have degrees (or grades) of crimes within each of those categories that further delineate the seriousness of the crime. Thus, a premeditated murder would be referred to as a first-degree felony, whereas shoplifting a shirt may be defined as a second- (or third-) degree misdemeanor. Many states also have a classification of crimes known as *summary offenses* or *infraction offenses,* which are minor crimes that carry no threat of jail (for first offenders), such as a charge of underage alcohol use.

Crimes are also sometimes classified based on the victim or result of the crime. Crimes in which the perpetrator has used force or violence, such as murder or sexual assault, are classified as *violent crimes.* Crimes that involve offensive or disorderly conduct in public are referred to as *public order crimes.* This category also includes crimes that have no direct victim but that society has judged to be detrimental to public well-being, such as crimes related to narcotics, prostitution, or obscenity. Crimes that involve damage to or stealing of property (such as theft, vandalism, or arson) are usually referred to as *property crimes.* When crimes take place in the business environment, they are classified as *white-collar crimes.*

CRIMINAL LAW AND BUSINESS ENTITIES

LO 22-5

Identify circumstances in which business managers and owners may be liable for criminal violations by a corporation.

While any discussion of criminal law necessarily focuses on the criminal culpability of individuals, business owners and managers should have a fundamental knowledge of how criminal law may be applied to business entities. This knowledge helps business owners and managers to reduce risk and add value to the business by taking affirmative steps to limit criminal culpability for the business and its principals.

The modern trend in criminal law is to expand the scope of criminal statutes to include criminal culpability for corporations and their principals. Courts have allowed liability to exist for corporations so long as the prosecutor can prove that the corporation's agents (not just executive management) were engaged in criminal conduct on behalf of the company. Recall from Chapter 15, "Corporations," that courts have recognized that corporations

[6]MPC § 4.01(1).

exist as a separate legal "person." Criminal statutes have embraced the concept that a corporation may be charged with a crime along with, or apart from, its principals or agents. The Model Penal Code (MPC) provides for criminal liability for business entities if any one of the following applies:

1. The criminal act by the business's agent is within the *scope of his employment* and the statute imposes liability on the business for such an act (e.g., the agent shreds documents related to potentially unlawful conduct, creating liability under obstruction of justice).
2. The criminal omission is the failure to perform a specific duty imposed by law (e.g., the agent fails to make important disclosures in a report to investors).
3. The crime was authorized by one of the corporation's top-level managers (e.g., a chief financial officer orders an internal accountant to file a false corporate tax return).

Congress has specifically included business entities in criminal statutes in areas that impact business, including fraud, obstruction of justice, health and safety requirements, sale of ownership interests (securities law), disclosure requirements, environmental regulations, and antitrust or other anticompetition laws.

Individual Liability for Business Crimes

Congress and state legislatures have also expanded criminal culpability for individual officers and directors (and sometimes majority owners) for corporate crimes committed within the scope of their employment. These principals are often included in criminal statutes that require officers and directors to act as responsible corporate officers in complying with statutes and being diligent about adhering to standards set out in statutes and regulations. Because of the inherent difficulties in terms of proof, most statutes do not require the specific mental intent (guilty mind) that is required for other crimes. Since the mid-1970s, legislative bodies have begun to impose what amounts to strict liability statutes for corporate officers even when the officer in question did not have any actual knowledge that a crime had taken place.

The *Park* Doctrine

The *Park* doctrine was developed by the U.S. Supreme Court in a famous 1975 case in which the court held that an individual corporate officer could be guilty of a misdemeanor crime under the Food, Drug and Cosmetic Act (FDCA) for allowing food to become adulterated while stored in a corporate warehouse. The case centered on John Park, the President of Acme Markets, Inc., a large national retail food chain with approximately 36,000 employees, 874 retail outlets, and 16 warehouses. In 1970, the Food and Drug Administration (FDA) observed and advised Park of unsanitary conditions, including rodent infestation, at Acme's Philadelphia warehouse. In 1971, the FDA found similar conditions at Acme's Baltimore facility. After the violations were not corrected, the government charged Acme and Park with misdemeanors under the FDCA. Although Acme pled guilty, Park argued that he could not have possibly had the requisite knowledge necessary to commit a crime. A jury convicted Park and eventually the U.S. Supreme Court affirmed the conviction. The Court pointed out the narrowness of the decision (i.e., limited to FDCA violations), but nonetheless affirmed that corporate agents have a high level of responsibility when it comes to the well-being of the public. The Court rejected Park's argument:

> The requirements of foresight and vigilance imposed on responsible corporate agents are beyond question demanding, and perhaps onerous, but they are no more stringent than the public has a right to expect of those who voluntarily assume positions of authority in business enterprises whose services and products affect the health and well-being of the public that supports them.
>
> *U.S. v. Park, 421 U.S. 658, 672 (1975).*

Case 22.1 provides an example of individual officer liability in the context of the *Park* doctrine.

CASE 22.1 U.S. v. LaGrou Distribution Systems, 466 F.3d 585 (7th Cir. 2006)

FACT SUMMARY LaGrou's warehouse in Chicago stored frozen meat for various food companies in the region. Its cold storage facility held more than 20 million pounds of poultry, pork, and beef. That building also had a severe rodent problem, as evidenced by rat droppings that could be found in every corner of the warehouse and nests found in boxes of meat. The company organized employee "rat patrols" that would catch up to 50 rats a day, but more would enter each night. Packing areas had puddles of beef blood mixed with rat hair and feces, and meat boxes showed rat trails with teeth marks. According to government investigators, employees would mark rat-infested boxes with "MM" for Mickey Mouse, but the boxes were not discarded. The warehouse was referred to by employees as an "amusement park for rats" and a "house of horrors for the City of Chicago." Evidence indicated that Stewart, president of LaGrou, knew of the rat infestation for a period of three years. Stewart told the employees to keep catching rats but refused to perform a full extermination because he determined that it would be too expensive. After notification that U.S. Department of Agriculture inspectors had scheduled a visit, Stewart had the employees work through the night to throw away boxes of rat-infested meat. Yet the USDA inspectors still found the rats, the filth, and the discarded meat. Stewart was charged with violating federal criminal laws prohibiting the sale of adulterated meat. At trial, Stewart defended that he did not have the requisite knowledge for criminal liability because he had no actual knowledge of any specific meat contamination.

SYNOPSIS OF DECISION AND OPINION The Seventh Circuit Court of Appeals ruled against Stewart and LaGrou. The court held that knowledge of *any* rat problem was sufficient and that Stewart was liable for all the violations that he was in charge of preventing. The court ruled that the government need not prove that Stewart had actual knowledge of specific meats that were contaminated. Stewart had a responsibility to install systems to ensure sanitation standards. The court affirmed the trial court's order that Stewart must contribute personal assets to the $8.2 million in fines and serve five years on probation.

WORDS OF THE COURT: Liability for Criminal Conduct of Others "The conditions at LaGrou's cold storage warehouse at 2101 Pershing Road in Chicago were enough to turn even the most enthusiastic meat-loving carnivore into a vegetarian. . . . In this case, the government needed to prove that agents of the LaGrou corporation knowingly stored meat, poultry, and food products under unsanitary conditions. LaGrou's president, Jack Stewart, and the Pershing Road warehouse manager, David Smith, were both well aware of the rodent infestation problem and other insanitary conditions at the warehouse, yet persisted in storing and distributing meat, poultry, and food products there."

Case Questions

1. Suppose Stewart was never told about the rat problem. Did he have a responsibility to find out?
2. What about the workers who shipped the contaminated meat each day? Should they be found guilty of some crime? What about the government inspectors who let the warehouse operate for three years? Who is most culpable?
3. *Focus on Critical Thinking:* Should Stewart have been sentenced to serve prison time? If there were evidence that a consumer suffered medical problems related to the infestation, would there be any tort claims against LaGrou? Against Stewart?

CONCEPT SUMMARY *Criminal Law*

- Criminal law is based on state and federal laws that started as common law crimes but were codified into statutes based on the Model Penal Code (MPC).
- While some actions involve both criminal and civil liability, civil laws protect individuals by redressing injuries and criminal laws protect society as a whole by punishing wrongdoers.
- Criminal liability requires both a bad act (*actus reus) and* a guilty mind (*mens rea*).
- Even when a requisite mental state and bad act are proved, the accused can offer a defense such as mental incapacity, duress, or self-defense to avoid criminal liability.
- Corporations and their managers can be guilty of the crimes of their employees if the crime was committed for some corporate advantage or benefit of the company.

WHITE-COLLAR CRIME

LO 22-6

Give specific examples of white-collar crime laws that may impact a business entity and/or its owners and managers.

White-collar crimes usually signify criminal violations by corporations or individuals, including fraud, bribery, theft, and conspiracy committed in the course of the offender's occupational duties. Typically, these crimes are set out in state and/or federal statutes.

Fraud

Perhaps the most common white-collar crime is fraud. *Fraud* is a broad general term used to describe a transaction in which one party makes false representations of a matter of fact (either by words or conduct) that are intended to deceive another. In certain cases, active concealment of a material fact (versus an affirmative false representation) may also constitute fraud. The basic elements of criminal fraud are (1) a false representation (or concealment) concerning a material fact and (2) another party that relies on the false misrepresentation of the fact and suffers damages as a result. A material fact is one that is essential to the agreement or one that affects the value of the transaction. For example, suppose that Rasputin applies for a loan to start his business. Because his finances are in dire straits, Rasputin submits a false set of tax returns to the bank loan officer. Based on this information, the bank lends Rasputin the money. Rasputin has committed a fraud upon the bank. Bank fraud of this nature is a felony punishable under state and, depending on the bank, federal criminal statutes.

In 1990, Congress passed the **Mail Fraud Act**[7] with the intent of giving federal prosecutors significant leverage in prosecuting white-collar criminals. The statute criminalizes any fraud in which the defrauding party uses the mail or any wire, radio, or television in perpetrating the fraud. This comprehensive approach to criminalizing fraud is based on Congress's authority to regulate mail and interstate commerce. It also covers any *organization* of a scheme to defraud by false pretenses. For example, in the Rasputin example discussed earlier, suppose that Rasputin sets up an elaborate scheme to fool investors into thinking that he has invented a new product that will bring in several millions of dollars of revenue. He designs a brochure and mails it to several wealthy individuals. At this point, Rasputin has committed mail fraud even though he has not actually induced any investors. The ease of prosecution for mail fraud has made it a primary tool used by prosecutors in white-collar crime investigations.

[7] 10 U.S.C. § 1341.

Another form of fraud is *embezzlement.* Embezzlement is appropriately categorized as fraud (and not as theft) because it involves fraudulent concealment of financial records to perpetrate theft. Embezzlement occurs when someone in a position of trust creates fraudulent records to disguise the theft. For example, suppose that Rasputin is the controller of WidgetCo. Over the period of a month, Rasputin transfers small amounts of WidgetCo's money to his personal checking account and adjusts the monthly financial statements to indicate that the money is in WidgetCo's account. This act constitutes embezzlement because of the cover-up aspect of the scheme. If Rasputin had come into his office one morning, stolen cash from the safe, and walked out never to return, this would likely constitute theft because no scheme was involved.

Ponzi Schemes

A *Ponzi scheme* is a fraudulent investment operation that pays returns to investors from their own money or money paid by subsequent investors rather than from any actual profit earned. The scheme is named after Charles Ponzi, who became notorious for using the technique in 1903. A Ponzi scheme usually offers returns that other investments cannot match in order to entice new investors. This is generally accomplished in the form of short-term returns that are either abnormally high or unusually consistent. The perpetuation of the returns that a Ponzi scheme advertises and pays requires an ever-increasing flow of money from investors in order to keep the scheme going. The system is destined to collapse because the earnings, if any, are less than the payments. The authorities uncover some schemes before they collapse if an investor suspects that she is a victim and reports the investments to authorities. As more investors become involved, the likelihood of the scheme coming to the attention of authorities increases.

For example, suppose that High Return Investments (HRI) prints advertising brochures that promise a 30 percent return on an investment in just one month—an extraordinary return by any measure. HRI states that it uses a "complex offshore investment strategy that is the result of years of study and testing." No matter how fancy the brochures are, it is difficult to attract any large initial investments without a track record. Thus, HRI convinces a few investors to take the risk with small amounts of money. Instead of investing the money, HRI then takes out a loan and repays the initial investors with the promised 30 percent return one month later. This is where HRI sets the trap: Initial investors now invest larger sums, and new investors want a piece of the action. It is no longer necessary to take out a loan because sufficient capital from eager new investors is flowing into HRI's hands. The cascading effect then allows HRI to pay back any loans used to perpetrate the scheme and take handsome bonus fees for managing the money. HRI covers its tracks by producing false investment statements for its investors showing high returns. When one or more investors request a withdrawal, there is sufficient cash to pay out. But HRI's scheme cannot last forever. Typically HRI's schemes will end up in one of two scenarios: (1) HRI disappears with the investment money, or (2) the scheme collapses because too many investors demand their returns at the same time. The second scenario typically happens when investor confidence in the equities markets deteriorates and investors withdraw money from market-based investments in favor of cash and other safer forms. For example, when the financial crisis of 2008 began to shake investor confidence, it unraveled the largest Ponzi scheme ever operated by a single person. Federal prosecutors claim that a 20-year scheme, operated by well-known investment manager Bernard Madoff, cost his investors billions of dollars. In March 2009, Madoff pleaded guilty to 11 felonies, including fraud and perjury. He was given the maximum sentence of 150 years of incarceration. Madoff's accountant was also charged and cooperated with authorities in exchange for leniency. The Madoff case is examined in more detail in Chapter 16's "Legal Strategy 101."

Conspiracy

Conspiracy is an agreement by two or more persons to commit a criminal act. It is itself a punishable offense: All parties to the agreement are subject to prosecution. Because the crime is complete upon agreement, there is a very low threshold for satisfying the criminal act requirement. Conspiracy requires a specific *intent* to achieve the object of the conspiracy but does not require that the act actually be carried out. The Model Penal Code (MPC) contemplates conspiracy as a crime that requires two guilty minds. Therefore, both parties must actually *manifest* intent to commit the criminal act for a conspiracy to occur.

Racketeer Influenced and Corrupt Organizations Act (RICO)

The federal Racketeer Influenced and Corrupt Organizations Act[8] (RICO) was enacted in 1970 with the objective of providing the government with a powerful tool to fight the rising tide of organized crime. One purpose of the RICO law was to prevent organized crime from infiltrating legitimate business operations. The statute makes it a criminal offense for anyone associated with an enterprise to conduct or participate in its affairs through a pattern of racketeering activity. Although racketeering is generally understood to mean an organized conspiracy to commit the crimes of extortion or coercion, state and federal legislatures have added to the definition by including conduct such as engaging in illegal gambling, narcotics trafficking, and prostitution.

The modern trend is for authorities to use the RICO statute in an expansive manner, including criminal conduct that is not traditionally related to organized crime. Because RICO laws define racketeering in such broad terms, including crimes such as wire fraud, mail fraud, and securities fraud, prosecutors have been increasingly willing to bring RICO cases in white-collar crime and political corruption cases. Although the penalties under RICO are stiff, the real teeth of the law are found in its forfeiture provisions. They allow prosecutors to seize the defendant's personal assets if the government can prove that the assets were obtained using profits from criminal activity. This is a powerful tool because it has the effect of bankrupting the racketeering enterprise while an individual convicted under the statute is incarcerated.

Insider Trading

In the wake of the financial crisis that began in 2008, the government has become increasingly aggressive about the enforcement of **insider trading laws**. These laws are federal securities statutes directed at corporate insiders who have access to certain information that is not available to the general investment public; the laws prohibit corporate insiders from trading their company's stock based on their insider knowledge. Insiders can be executives, managers, corporate counsel, consultants, certain employees, brokers, and even majority shareholders. In 1988, Congress passed the Insider Trading and Securities Fraud Enforcement Act, which raised the criminal and civil penalties for insider trading, increased the liability of brokerage houses for wrongful acts of their employees, and gave the government more authority to pursue insider trading violations. Insider trading laws and other laws regulate the issuance and trading of certain business ownership interests (such as stocks) and are discussed in detail in Chapter 16, "Regulation of Securities, Corporate Governance, and Financial Markets."

[8] 18 U.S.C. §§ 1961–1968.

BUSINESS ETHICS PERSPECTIVE

Enforcing Insider Trading Laws

Overview

In Chapter 16, "Regulation of Securities, Corporate Governance, and Financial Markets," we discussed insider trading under rule 10b-5 of the Securities Exchange Act. That rule prohibits investors in public markets from profiting by using nonpublic information to guide their investments. However, the rule does not explicitly define insider trading and therefore courts have struggled to apply uniform standards to insider transactions. Headlines filled with stories of insider trading involving celebrities, professional athletes, and entertainers have become increasingly common. In several cases that garnered substantial media attention, appellate courts have overturned the convictions of investors who profited from insider knowledge. The lack of uniformity in enforcement and interpretation has spawned significant uncertainty in the investment community and created both legal and ethical conundrums. As you learn more about the government's efforts to enforce insider trading laws, consider the following questions. First, the murkiness that surrounds insider trading laws contradicts the very purpose of federal securities regulation: promoting investor confidence in the markets. Second, is it fair to impose substantial prison sentences on those convicted of such a vaguely defined crime? Third, if the legal rules are not clear, how can an investor understand what the ethical boundaries are? Finally, are government prosecutors that pursue questionable insider trading cases driven more by politics than public good?

The SEC Unleashed

Beginning in 2013, the SEC stepped up its enforcement activity by pursing record numbers of insider trading cases. Consider the comments of SEC Chair Mary Jo White from a 2013 speech at the Securities Enforcement Forum where she made clear the SEC's new approach to enforcing securities laws:

> One of our goals is to see that the SEC's enforcement program is—and is perceived to be—everywhere, pursuing all types of violations of our federal securities laws, big and small . . . believe the SEC should strive to be that kind of cop—to be the agency that covers the entire neighborhood and pursues every level of violation. An agency that also makes you feel like we are everywhere. And we will do our best not to disappoint. . . . Over the last four years, we have filed an unprecedented number of insider trading actions—some 200 actions—against more than 450 individuals and firms charging illicit trading gains of nearly $1 billion. In these types of cases, one of the most challenging issues is establishing the relationship between tippee and tipper.[9]

After a number of high-profile losses, the SEC's aggressive enforcement actions became the subject of criticism by securities lawyers, commentators, and even courts. Still, the SEC continued to expand its enforcement division and set a record of 755 enforcement actions in 2014, approximately 10 percent higher than the previous year. Critics argued that the SEC had shifted its assets away from other important responsibilities to avoid political criticism that Wall Street bankers were not being held accountable for the financial crisis in 2008.

A Shift in Strategy

Despite aggressive enforcement and increased use of technology to detect insider trading, the SEC began to lose a string of enforcement actions (including insider trading cases) in federal courts. The SEC then shifted to a different tactic: It increased its use of in-house courts called Administrative Law Courts (ALCs). As part of the Dodd-Frank Act, the SEC's enforcement powers were expanded to allow the agency to pursue securities enforcement through administrative hearings rather than in federal courts. ALCs operate much differently than federal courts. There is no independent jury, no discovery, no rules of evidence, and only limited opportunity for appeals. ALCs are staffed by Administrative Law Judges (ALJs). ALJs are government attorneys selected, maintained, and funded by the SEC. Although they are theoretically impartial, some commentators have alleged that ALJs have a pro-SEC bias. For example, federal Judge Jed S. Rakoff warned about the loss of the securities laws' neutral character and pointed out the trend in which the SEC would essentially directly make, enforce, and adjudicate these laws. Despite these warnings, however, the SEC looks to continue its reliance on administrative proceedings unless prevented from doing so by the courts. One can understand Judge Rakoff's concern, especially in light of the statistics, which are a stunning commentary on the SEC's home-court advantage. According to a 2014 *Washington Post* article, the SEC's preference for home-court advantage in insider trading cases resulted in a 100 percent conviction rate, compared to a 66 percent conviction rate in federal courts.

[9]https://www.sec.gov/News/Speech/Detail/Speech/1370539872100

(continued)

Discussion Questions

1. The SEC responded to criticism of its ALCs with the rationale that ALJs are experts in securities law and therefore better at applying the law to various circumstances. It also cited the efficiency of ALCs in comparison with federal courts. Does that strike you as compelling? Why or why not? Should securities cases be decided by untrained jurors who may not fully understand the issues?
2. Does the SEC's shift toward ALCs comport with the ethical conduct that is expected of those who hold power?
3. Analyze the SEC's decision to shift toward ALCs under both a principles-based approach and a consequences-based approach to ethical decision making (see Chapter 5, "Business, Societal, and Ethical Contexts of Law," for a review of the approaches). What are the results?
4. According to the SEC's website, the mission of the U.S. Securities and Exchange Commission is to "protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation." Do the actions of the SEC comport with its mission?

Cuban the Critic

One of the SEC's most vocal critics is billionaire entrepreneur Mark Cuban, who battled the SEC over a period of eight years. In 2008, the SEC alleged that Cuban violated insider trading laws by selling shares of stock in Mamma.com Inc. after learning material, nonpublic information concerning a

Mark Cuban speaking to the press. © Mike Fuentes/Bloomberg/Getty Images

(continued)

planned private investment offering by the company. The SEC's case centered on an eight-minute telephone conversation between Mamma.com's CEO and Cuban in which the CEO reported to Cuban that an investment transaction was to take place in the near future. According to the CEO, Cuban reacted angrily to the news and agreed not to disclose or trade on the information and Cuban ended the conversation with the comment, "Now I'm screwed, I can't sell." Cuban denied that he ever agreed to keep the information confidential or that he ever agreed not to trade on that information.

Although the trial court dismissed the case against Cuban, the SEC was successful in convincing an appellate court that the case had enough to merit sending it to a jury trial. After a two-week trial in October 2013, the jury acquitted Cuban of all counts.

Discussion Questions

1. An important underlying objective of federal securities laws is to provide the public with confidence in the securities market. Did the SEC achieve that objective by bringing this case against Cuban?
2. Do the SEC and other government regulators target high-profile celebrities for enforcement under the theory that it deters lower profile illegal activity? Does the deterrent effect work? Is it ethical? Why or why not?
3. After the trial, Cuban was highly critical of the government's conduct in the case and accused the prosecutor of lying. The government's case took five years to get to trial at an enormous cost to taxpayers. Was it worth it even if Cuban had been found guilty? Should an entire case hinge on an eight-minute telephone call?

Bribery

Bribery generally involves a scheme to pay a government official money in order to obtain favorable treatment for a personal or business transaction. Bribery is covered in both federal and state statutes. Note that bribery is an offense that requires only the *offer* of a bribe. It is not necessary that the transaction actually takes place. For example, suppose that Whitaker is the owner of a construction company and bids on a contract to build a firehouse in the city. Whitaker promises a city councilman that she will pay him 10 percent of the total profit in the contract if the councilman will vote to give Whitaker the contract. The offer itself is unlawful even if the councilman does not go along with the scheme. Of course, if the councilman does go along with the bribe (known as a *kickback* in these circumstances), he too will be culpable for bribery (and perhaps several other *public trust* laws).

Obstruction of Justice

Prosecutors have been increasingly willing to prosecute white-collar criminals under federal laws prohibiting the obstruction of justice[10] for any conduct related to attempting to cover up evidence of wrongdoing. Cover-ups take many forms, including (1) lying to investigators, (2) altering documents, (3) shredding or concealing documents or any media such as videotape, and (4) inducing other witnesses to lie or influencing witnesses to refrain from cooperating with authorities. Note that an obstruction of justice charge may stand *independently,* and prosecutors need not charge or convict the defendant with the underlying crime. For example, suppose that prosecutors interview Rasputin during the criminal investigation of insider trading at Rasputin's firm. Rasputin lies about his involvement in the insider trading to the authorities. When it is discovered that Rasputin has lied, prosecutors may charge Rasputin with obstruction of justice. Rasputin may be convicted of the obstruction charge even if prosecutors do not have sufficient evidence to charge Rasputin with the underlying crime (insider trading).

[10] 18 U.S.C. § 1001 et seq.

In one of the most famous cases of a company being charged with obstruction, federal prosecutors charged the accounting firm Arthur Andersen with obstruction, alleging that individuals within the firm shredded documents related to the collapse and fraudulent practices of the Enron Corporation. A federal grand jury also indicted individual employees of Arthur Andersen for obstruction. However, as we shall see in Case 22.2, the U.S. Supreme Court made clear that there are certain requirements of culpability in an obstruction case.

CASE 22.2 Arthur Andersen LLP v. United States, 544 U.S. 696 (2005)

FACT SUMMARY As Enron Corporation's financial difficulties became public, Arthur Andersen, Enron's auditor, instructed its employees to destroy documents pursuant to its established document retention policy. Andersen was indicted under a federal statute that makes it a crime to "knowingly . . . corruptly persuad[e] another person . . . with intent to . . . cause" that person to "withhold" documents from, or "alter" documents for use in an "official proceeding." The jury returned a guilty verdict, and the Fifth Circuit Court of Appeals affirmed, holding that the district court's jury instructions properly conveyed the meaning of "corruptly persuades" and that the jury need not find any consciousness of wrongdoing in order to convict.

SYNOPSIS OF DECISION AND OPINION In a unanimous decision by the U.S. Supreme Court, Andersen's conviction was overturned. The Court reasoned that the instructions allowed the jury to convict Andersen without proving that the firm knew it had broken the law or that there had been a link to any official proceeding that prohibited the destruction of documents.

The Court specifically held that the jury's instructions—which stated that even if Andersen honestly and sincerely believed its conduct was lawful, the jury could still convict the firm—were improper. The statute under which Andersen was charged used the language "knowingly . . . corruptly persuade." Andersen managers did instruct their employees to delete Enron-related files, but those actions were within the firm's document retention policy. If the document retention policy was constructed to keep certain information private, even from the government, Andersen was not corruptly persuading its employees to keep the information private.

WORDS OF THE COURT: Improper Jury Instruction "The jury instructions failed to convey properly the elements of a 'corrup[t] persuas[ion]' conviction. . . . The jury instructions failed to convey the requisite consciousness of wrongdoing. Indeed, it is striking how little culpability the instructions required. For example, the jury was told that, even if petitioner honestly and sincerely believed its conduct was lawful, the jury could convict. The instructions also diluted the meaning of 'corruptly' such that it covered innocent conduct."

Case Questions

1. What are the words from the statute that establish the act requirement and the mental requirement?
2. Why did the Court hold that the jury instructions were improper?
3. *Focus on Critical Thinking:* By the time the Court reversed Andersen's conviction, the firm had collapsed from the weight of bad publicity. The government decided not to retry the case. Was it good public policy to destroy the world's largest professional service firm for the actions of a handful of employees? Why do you suppose the government chose not to retry the case?

LEGAL IMPLICATIONS IN CYBERSPACE

Computer Fraud and Abuse Act

There are three major classes of criminal activity through use of a computer: (1) engaging in unauthorized use of a computer, which might involve stealing a user name and password or accessing the victim's computer via the Internet through a backdoor created by a Trojan horse[11] program; (2) creating or releasing a malicious computer program (e.g., computer virus, worm, Trojan horse); and (3) harassing and stalking in cyberspace.

In a 1983 incident that received substantial media attention, a group of hackers managed to access the computer system at Sloan-Kettering and alter patient files. The incident led to passage the **Computer Fraud and Abuse Act (CFAA)**[12] which was amended in 2001 by the USA PATRIOT Act.[13] The law prohibits unauthorized use of computers to commit seven different crimes: (1) espionage; (2) accessing unauthorized information; (3) accessing a nonpublic government computer; (4) fraud by computer; (5) damage to computer; (6) trafficking in passwords; and (7) extortionate threats to damage a computer. The CFAA has stiff criminal penalties and also allows civil actions to be brought against an offender to recover damages.

The CFAA is the primary tool used by government to prosecute individuals who hack into computer systems of government and business entities. In 2016, the CFAA was in the headlines after a federal judge sentenced a former scouting director of Major League Baseball's St. Louis Cardinals to nearly four years in prison and to pay $279,038 in restitution for his involvement in a high-tech cheating case. Christopher Correa pled guilty to violating the CFAA for hacking into the player-personnel database and e-mail systems of the Houston Astros. Prosecutors alleged that Correa gained access to the Astros's database using a password similar to that used by a former Cardinals employee who left St. Louis to become the general manager of the Astros. Correa used the password to access hundreds of pages of confidential information about player trade discussions, evaluations, and draft pick alternatives.[14]

Foreign Corrupt Practices Act (FCPA)

The **Foreign Corrupt Practices Act (FCPA)**[15] of 1977 is a criminal statute that was enacted principally to prevent corporate bribery of *foreign officials* in business transactions. The law prohibits a company and its officers, employees, and agents from giving, offering, or promising anything of value to any foreign (non-U.S.) official with the intent of obtaining or retaining business or any other competitive advantage. This prohibition is interpreted broadly in that companies may be held liable for violating the antibribery provisions of the FCPA whether or not they took any action within U.S. borders. Thus, a U.S. company can be liable for the conduct of its overseas employees or agents even if no money was transferred from the United States and no U.S. citizen participated in any way in the foreign bribery.

A foreign official is any officer or employee of a foreign government, regardless of rank; employees of government-owned or government-controlled businesses; foreign political parties; party officials; candidates for political office; and employees of public international organizations (such as the United Nations or the World Bank). This list can include owner-employees as well. Even if the improper payment is not accepted, just offering it violates the FCPA. Likewise, other FCPA violations include instructing, authorizing, or allowing a third party to make a prohibited payment on a company's behalf; ratifying a payment after the fact; or making a payment to a third party knowing or having reason to know that it will likely be given to a government official. Prohibited payments include not only cash and cash equivalents but also gifts, entertainment, travel, and the like. The FCPA is discussed in greater detail in Chapter 25, "International Law and Global Commerce."

[11]A Trojan horse is a virus that appears to perform one function yet actually performs another, such as the unauthorized collection, exploitation, falsification, or destruction of data.

[12]USC. § 1030.

[13]USC. § 2712.

[14]*U.S. v. Correra*, Case No. H-15-679, (S.D. Texas)

[15]28 U.S.C. § 1602 et seq.

Self-Check White-Collar Crime

What white-collar crimes are at issue in the following circumstances?

1. WidgetCo applies for a permit to do business in Venezuela. The government official denies the permit, and a WidgetCo executive pays for a lavish meal at a four-star restaurant while discussing the permit application.
2. InvestCo advertises a return of 15 percent on any investments in its Super Duper Fund. Even when the market drops dramatically, Super Duper continues to perform at this level for 18 consecutive months. In its disclosures, InvestCo reports that its auditing firm is headed by an InvestCo officer's son-in-law.
3. WidgetCo and PlankCo agree to illegally fix prices so that the lack of competition drives the prices of their products artificially high. The companies begin the process to set prices but abandon the plan at the last moment.
4. Evidence exists that WidgetCo's CEO was funneling money from the corporation with the help of several other executive managers. The funds came from an investment fraud scheme in which each executive played a part to perpetrate the scheme and use WidgetCo as a front business to help bolster their scheme with investors.

Answers to this Self-Check are provided at the end of the chapter.

THE CRIMINAL JUSTICE SYSTEM

LO 22-7

Explain the steps in the criminal justice system.

The criminal justice system is best thought of as one process that operates in two phases: **investigation** and **adjudication.** This section describes the nuts and bolts of the criminal justice process. Procedural safeguards that are afforded to those suspected or accused of crimes constitute *criminal procedure* and are discussed in the next section of this chapter.

Investigation

During the investigation phase, the authorities become aware of an alleged criminal act and begin an investigation by gathering physical evidence and interviewing witnesses and potential suspects. Because most criminal acts are handled at the state level, most enforcement of criminal law is conducted by state or local police agencies. Violations of federal laws are investigated by various federal law enforcement agencies, including the Federal Bureau of Investigation (FBI). In a business context, investigators from federal regulatory agencies such as the Securities and Exchange Commission (SEC) or the Internal Revenue Service (IRS) may also undertake specialized criminal investigation. During this initial stage, investigators may also ask a court to authorize a search warrant in an effort to obtain more evidence. A warrant may be issued based only on **probable cause**. Once the authorities believe that sufficient evidence creates enough probable cause to indicate the

Legal Speak >))

Bail
The security, in the form of cash or a bond, given to the court to ensure the appearance of a defendant in court at a later date. If the defendant appears in court, the bail is returned. If he flees, the bail is forfeited.

culpability of a suspect, they will, depending on the circumstances, either obtain an *arrest warrant* or, more commonly, *arrest* the suspect by taking him into physical custody. If the criminal violation is a minor one, the authorities may simply issue a *citation,* whereby the violator may either resolve the charge by paying a fine or contest the charge in court. If an actual arrest has taken place, the authorities may continue their investigation by gathering more physical evidence, interviewing new witnesses, and attempting to further interview the suspect. The investigators then file formal criminal charges against the suspect and prepare a brief report for a local magistrate and prosecutors. The suspect, now charged, is referred to as the *defendant* and is formally read the charges by a magistrate. The magistrate then sets bail (if appropriate) and, if necessary, appoints an attorney to represent the defendant. Frequently, the prosecutor will review the investigator's report (and sometimes conduct additional investigation) and then decide whether she can prove the charges in a court of law based on available evidence. The prosecutor decides whether to (1) proceed with prosecuting the defendant on the original charge, (2) amend the charges as necessary, or (3) drop the charges altogether due to lack of evidence. The actual title of the prosecutor varies between jurisdictions, but local prosecutors are typically employed by the district attorney, state prosecutors are employed by the state's attorney general, and federal prosecutors work for the U.S. attorney general under the authority of the U.S. Department of Justice.

Adjudication

If the prosecutor elects to proceed with the charges, the defendant is entitled to a **preliminary adjudication**. Some jurisdictions use the *grand jury* system, while others use a *preliminary hearing* in front of a local magistrate. In each case, the prosecutor presents evidence of the defendant's guilt, and the decision maker (either the grand jurors or the magistrate) determines whether probable cause exists to hold the defendant over for trial. If the prosecutor cannot offer sufficient evidence of probable cause, the charges are dismissed. As a practical matter, very few cases are dismissed at this stage.

The defendant is notified that he is held over for trial through either an *indictment* (in the case of a grand jury) or formal filing of an *information* (in the case of a magistrate). The defendant is then entitled to an arraignment in a state trial court, at which he is informed of the final charges and is asked to enter a *plea* of guilty, not guilty, or no contest.[16] An overwhelming majority of defendants plead not guilty at this stage, even if they intend on negotiating an eventual guilty plea with the prosecutor. Following the arraignment, the prosecutor and defense counsel will typically enter into a plea-bargaining negotiation. This involves the parties agreeing to concessions from each side that will avoid trial and result in a voluntary plea of guilty or no contest by the defendant. All states also have some type of pretrial intervention for first-time offenders of nonviolent crimes, whereby the defendant typically agrees to fulfill certain conditions (community service, drug rehabilitation, etc.) in exchange for the charges being dismissed at a later date. If a plea agreement cannot be reached, the case proceeds to trial. In a trial, the finder of fact (usually a jury in a criminal trial)[17] weighs the evidence and determines whether the prosecutor has proved the charges against the defendant beyond a reasonable doubt. If the jury finds the defendant guilty, this results in a *conviction.* If the jury finds the defendant not guilty, this results in an *acquittal* and the defendant cannot be prosecuted for the same charges again. If the jury is deadlocked (unable to reach a consensus decision), this results in a *mistrial* and the prosecutor decides whether or not to refile charges against the defendant a second time. If the defendant is convicted, he may file an *appeal* setting out the basis for having the conviction reversed.

[16]In a plea of no contest, sometimes called by its Latin form *nolo contendere,* the defendant does not admit or deny the charges but is willing to accept the sanctions as if guilty.

[17]Recall from Chapter 3, "The American Judicial System, Jurisdiction, and Venue," that the finder of fact may be either a jury *or* a judge.

CONCEPT SUMMARY *The Criminal Justice Process*

Investigative Phase	Adjudicative Phase
1. Investigate possible crime.	1. Preliminary adjudication (via grand jury or magistrate, depending on jurisdiction).
2. Interview witnesses.	2. File indictment (known as "information," depending on jurisdiction) *or* drop charges due to insufficient evidence.
3. Obtain search warrants if necessary.	3. Defendant enters plea and enters plea negotiations if necessary.
4. Obtain arrest warrant or take suspect into custody *or* issue a citation for minor infractions.	4. If no plea agreement is reached, defendant goes to trial.
5. Defendant is formally charged.	5. Conviction or acquittal of the defendant.
6. Local judicial authority sets bail and appoints defense counsel if necessary.	6. Sentencing (if convicted).

If the defendant is convicted, the judge sets a future date for *sentencing.* In the interim, the court considers requests and reports by authorities, victims of the defendant's crime, character witnesses for the defendant, and sentencing guidelines (or statutory mandatory minimum sentences) in determining the defendant's punishment.

CRIMINAL PROCEDURE

LO 22-8
Name and explain the various constitutional procedural protections afforded to those accused of a crime.

Recall from the beginning of this chapter the differences between criminal law and criminal procedure. While criminal law defines the boundaries of behavior and prescribes sanctions for violating those boundaries, *criminal procedure* refers to legal safeguards to protect the rights of individuals (and in some cases business entities) during investigation by the government, arrest, trial, and sentencing. The protections are primarily provided by the U.S. Constitution's Bill of Rights. For purposes of understanding criminal procedure in a business environment, our focus is on protections found in the Fourth, Fifth, and Sixth Amendments. While the Constitution regulates many aspects of criminal procedure, as a practical matter state and federal legislatures also enact statutes and rules setting forth certain procedures that authorities must follow during investigation, arrest, criminal trial, and sentencing. State constitutions may also provide *additional* criminal procedure protections for a state's citizens. For example, one state may be more apt to require a higher level of probable cause for arrest than is prescribed by the federal rules or courts. Of course, states may not repeal the federal constitutional rights of individuals.

Searches and Arrest

Legal Speak >))

Warrant
A court order authorizing an official to do something she would otherwise be prohibited from doing. The most common are warrants for arrest, search, or seizure.

Recall from Chapter 2, "Business and the Constitution," that the Fourth Amendment to the U.S. Constitution protects individuals (and sometimes businesses) from unreasonable search and seizure by government agents and permits warrants to be issued only if probable cause exists. The U.S. Supreme Court has developed a large body of law to guide courts in determining the appropriate boundaries of searches and arrests by authorities. First, the Court has held that the Fourth Amendment applies to both *searches* and *arrests.* However, a warrant is usually required before a search takes place (with certain exceptions).

Although the Fourth Amendment requires authorities to obtain a warrant before searching a citizen, the Supreme Court has allowed the police to conduct a limited pat-down search when an officer has reasonable suspicion that criminal activity is taking place. © Stockbyte/Getty Images RF

A warrant for arrest is generally not required in order to take a suspect into custody. Second, the Constitution requires that an impartial magistrate issue a search or arrest warrant only if probable cause has been established. Third, whether or not a search or arrest warrant exists, the action taken by authorities must always be *reasonable* and consistent with constitutional protections. Fourth, the authorities may conduct *limited,* warrantless searches in certain cases. For example, police may conduct short, pat-down searches even without probable cause when the officer has a reasonable suspicion[18] that criminal activity is taking place or when the officer's safety is an issue.

Expectation of Privacy

A fundamental part of the protections provided by the Fourth Amendment is that its protections are based on whether an individual's *reasonable expectation of privacy* has been violated by government authorities. The courts have held that individuals have the highest expectations of privacy in their own homes. However, once an individual goes into the public (such as driving a car on a public highway), the privacy expectations are diminished and Fourth Amendment protections become more limited in scope. Examples of evidence that is *not* protected under reasonable expectation of privacy include trash that has been set out on the public curb for pickup, any apparently abandoned property, and things a person says or does in public. In terms of the abandoned property example, note that if the evidence has been disposed of but is still located on the real estate (land) of the owner, then the owner may still have a reasonable expectation of privacy. For example, Scofield is being investigated for tax fraud. The authorities observe Scofield putting out large bags of paper for trash pickup. They wait until midnight and then take the bags from the curbside outside Scofield's residence. When Scofield is brought to trial, the prosecutor introduces the discarded papers as evidence of tax fraud. If Scofield claims his Fourth Amendment rights were violated, it is likely that he would lose that argument because courts have consistently held that public papers disposed of as garbage are abandoned property and not subject to reasonable expectations of privacy. Suppose, though, that the real estate at issue was a country home with a long driveway and that trash collectors actually traveled onto the property to collect the garbage. If the authorities entered the land without a warrant and confiscated the bags of discarded papers, a court may very well find the search to be illegal.

KEY POINT

Fourth Amendment protections apply only when an individual's reasonable expectation of privacy has been violated by government authorities (e.g., the warrantless search of a house).

Plain View Doctrine

Courts have held that authorities generally do not commit a Fourth Amendment violation when a government agent obtains evidence by virtue of seeing an object that is in his plain view and the agent has the right to be in the position to have that view. This is called the

[18]Reasonable suspicion has been described as a standard that is lower than probable cause but "more than just a hunch"; *Terry v. Ohio,* 392 U.S. 1 (1968).

plain view doctrine. For example, suppose that during a routine traffic violation stop, a police officer observes an illegal handgun lying on the seat next to the driver. The officer may then arrest the driver and confiscate the weapon without a warrant because the plain view search is not prohibited by the Fourth Amendment. The plain view doctrine also allows authorities to use simple mechanical devices that are available to the general public, such as a flashlight or a camera with telephoto lenses to enhance their view. However, courts have limited authorities' ability to obtain information by means of special high-tech devices that are not available to the general public. For example, in a 2001 case, the U.S. Supreme Court held that the use of a thermal imager (a device used to produce images of relative amounts of heat escaping from a structure) by authorities on a public sidewalk outside a residence was *not* covered by the plain view doctrine and constituted an illegal search. The case involved the use of a device by U.S. Drug Enforcement Agency officials to obtain information on a suspected marijuana-growing operation in a residence owned by Kyllo. The agents obtained a warrant based on the fact that the thermal imager revealed that the garage of the residence was emitting extraordinary levels of heat. Indeed, Kyllo had been using heat lamps to grow marijuana in the garage, and he was eventually convicted at trial. The Supreme Court reversed the conviction on the basis that the thermal search evidence was obtained in violation of the Fourth Amendment. Justice Scalia wrote famously that allowing the authorities to use advanced technology would "leave the homeowner at the mercy of advancing technology—including the technology that could discern all human activity in the home."[19] The Court reasoned that because the data could not be obtained through use of the naked eye or basic equipment available to the general public, the action constituted a search even though government authorities had not physically entered the house.

The courts have adopted a similar position regarding aerial observations made by authorities. That is, so long as the plane or helicopter is in public navigable airspace, anything the police can see with the naked eye or basic equipment such as binoculars will be considered in plain view. In *Dow Chemical Co. v. U.S.,*[20] the Supreme Court ruled that the use of an airplane by government agents to fly over one of Dow's chemical plant complexes for purposes of taking investigative photographs with a zoom lens fit into the plain view exception and did not require a warrant because a zoom lens was readily available for purchase by the public.

Search Incident to Arrest

The search incident to arrest exception allows a law enforcement officer who has lawfully arrested a defendant to search the defendant's person without obtaining a warrant. The primary reasons that justify this exception are: (1) protection of the officer/agent and others involved in the booking process, and (2) prevention of the destruction of evidence by the defendant. For example, suppose that a federal law enforcement agency arrests the kingpin of a Ponzi scheme. The kingpin is handcuffed and then brought to a booking facility where one of the agents discovers a small notebook with incriminating notes made by the kingpin. Despite the fact that the agent did not have a warrant, the notebook may be used as evidence against the kingpin discovered in a search incident to arrest.

Search of Electronic Devices

One increasingly important issue faced by law enforcement is the extent to which electronic devices, such as cell phones, fit into current law of unlawful search and seizure as defined by the Fourth Amendment. In Case 22.3, the U.S. Supreme Court considers whether the police need a search warrant to examine contents such as photos and videos from a suspect's cell phone.

[19]*Kyllo v. U.S.,* 553 U.S. 27 (2001).

[20]476 U.S. 227 (1986).

CASE 22.3 Riley v. California, 144 S. Ct. 2473 (2014)

FACT SUMMARY Riley was the driver of a car stopped by a San Diego, California, police officer for a traffic violation that eventually led to his arrest for concealed possession of two loaded handguns found under the seat of his car. Riley was arrested and transported to a booking facility where police retrieved Riley's cell phone from his pocket. At the police station about two hours after the arrest, a detective specializing in criminal gangs examined the contents of Riley's cell phone. The detective found videos and photographs that connected Riley with a gang-related shooting that had occurred a few weeks earlier. Based partially on the evidence from Riley's cell phone, the state charged him with attempted murder. The prosecutor also sought an enhanced sentence based upon Riley's membership in a criminal street gang. Riley moved to suppress all evidence that the police had obtained from his cell phone, claiming a violation of the Fourth Amendment's warrant requirement. Prosecutors argued that the search of the cell phone was proper because it was incident to a lawful arrest within the guidelines of previous case law. The government argued that the cell phone search was similar to any other method used by individuals to store information (e.g., a wallet) and that cell phones fell into that same category. The trial court denied Riley's motion to suppress the evidence based on the Fourth Amendment and Riley was convicted at trial. The state appellate court affirmed Riley's conviction and Riley appealed to the U.S. Supreme Court, arguing that the evidence obtained from his cell phone was a warrantless search that did not fall into any category of exception.

SYNOPSIS OF DECISION AND OPINION In a unanimous decision, the U.S. Supreme Court reversed the decisions of the lower courts and ruled in favor of Riley. The Court held that the digital era required a rule that individuals have a high level of expectation of privacy in their cell phones because they are capable of storing and accessing a quantity of information, some highly personal, that no person would ever have had on his person in hard-copy form. The Court also reasoned that the search incident to arrest exception to the warrant requirement had two primary purposes: officer safety and prevention of the destruction of evidence. In this case, the search of a cell phone incident to arrest could not be justified on those grounds. As a result, the Court would not extend the warrantless search exception to include cell phones confiscated from an arrested defendant.

WORDS OF THE COURT: No Danger of Harm "Digital data stored on a cell phone cannot itself be used as a weapon to harm an arresting officer or to effectuate the arrestee's escape. Law enforcement officers remain free to examine the physical aspects of a phone to ensure that it will not be used as a weapon—say, to determine whether there is a razor blade hidden between the phone and its case. Once an officer has secured a phone and eliminated any potential physical threats, however, data on the phone can endanger no one."

WORDS OF THE COURT: Importance of Warrant Requirement "Our holding, of course, is not that the information on a cell phone is immune from search; it is instead that a warrant is generally required before such a search, even when a cell phone is seized incident to arrest. Our cases have historically recognized that the warrant requirement is an important working part of our machinery of government, not merely an inconvenience to be somehow 'weighed' against the claims of police efficiency . . .

"Modern cell phones are not just another technological convenience. With all they contain and all they may reveal, they hold for many Americans the privacies of life. The fact that technology now allows an individual to carry such information in his hand does not make the information any less worthy of the protection for which the Founders fought. Our answer to the question of what police must do before searching a cell phone seized incident to an arrest is accordingly simple—get a warrant."

Case Questions

1. The Court has held previously that a search incident to arrest may include the defendant's wallet/purse. Is there really a difference between a wallet and a cell phone? What if Riley's wallet had contained incriminating photographs of him? Would the police be required to get a warrant?

(continued)

2. Why does the Court point out that the warrant requirement is "not merely an inconvenience to be somehow 'weighed' against the claims of police efficiency"? How is that related to Riley's circumstances?
3. *Focus on Critical Thinking:* In what way does this case illustrate the clash between technology and case precedent? What role does *stare decisis* ("let the decision stand") play in this case?

Searches of Business Premises

Courts have been very reluctant to extend reasonable-expectation-of-privacy rights to the workplace. This is particularly true when the business is highly regulated. Recall from Chapter 17, "Administrative Law," that certain businesses are classified as *pervasively regulated* and, therefore, are not entitled to full Fourth Amendment protections. Instead, the U.S. Supreme Court has fashioned an exception to the Fourth Amendment warrant requirements that applies when an agency is conducting regularly scheduled inspections pursuant to an administrative rule. Even in cases where courts have held that administrative agencies are required to obtain an *administrative warrant* to conduct an inspection of a business, the Court has held that agencies are held to a lower standard of probable cause to obtain the warrant than would be required if the government were obtaining a criminal warrant.

Table 22.1 summarizes the application of the Fourth Amendment's warrant requirement.

Self-Incrimination

The Fifth Amendment provides that no person "shall be compelled in any criminal case to be a witness against himself." This means that individuals have the right not to offer any information or statements that may be used against them in a criminal prosecution. If an individual believes that any statement or testimony may incriminate her in a criminal case, she may decline to testify on Fifth Amendment grounds. Note that the right against self-incrimination also protects those called as witnesses in other types of matters. For example, suppose that in the tax fraud hypothetical case discussed earlier, the government prosecutes Scofield for tax evasion. During the trial, the prosecutor issues a subpoena to Montgomery, Scofield's business partner. If Montgomery has a belief that any questions asked of him as a witness in Scofield's trial may uncover evidence of his own criminal culpability, Montgomery may refuse to testify at Scofield's trial even though he is not under investigation.

The Fifth Amendment right against self-incrimination also applies while authorities are *investigating* crimes. Generally, the context is that government authorities are interviewing an individual in the course of a criminal investigation. Although most case law

TABLE 22.1 Applying the Fourth Amendment Warrant Requirement

Issue	Example	Business Application
No expectation of privacy	Government searches through a trash-can placed out on the public curb of a private house for pick-up.	Environmental Protection Agency searches plant of a pervasively regulated business venture (government must still obtain *administrative* warrant).
Plain view	Police see a weapon laying on a car seat after a traffic stop.	Government agents use zoom lens photography to obtain information in a tax fraud investigation.
Incident to arrest	Contraband found in the pocket of an arrestee.	After the operator of a Ponzi scheme is arrested, agents find a notebook with incriminating entries in his suit coat pocket.

surrounding this right deals with police interrogations of a suspect, in a business context business owners and managers should realize that agents of regulatory agencies, such as the Internal Revenue Service, are bound by the same guidelines as agents of police agencies are when interviewing suspects during a criminal investigation. An important element of this protection is that it is limited to *custodial* interrogations, in which the interviewee has been taken into custody or deprived of his freedom in some significant way. In this event, the authorities are required to give affirmative preinterview warnings to the suspect that he has the right not to make any statements and that any statement that is given may eventually be used as evidence against him in a criminal trial.

For example, suppose that an FBI agent telephones Barrabas and requests a meeting in Barrabas's office. The agent explains that he is investigating a fraud scheme involving government contracts. Barrabas agrees to the meeting, and during the conversation he admits to certain incriminating facts. The admission will likely be admissible as evidence despite the failure of the agent to provide the self-incrimination warning. Because the statement was made voluntarily in a noncoercive setting (Barrabas's office) and because Barrabas could have stopped the interview at any time, the interview may not be considered custodial and Barrabas's Fifth Amendment protections are not triggered. Alternatively, if the agent had arrested Barrabas and transported him to a local FBI field office, the agent would be required to give the warnings about self-incrimination.

The warning requirements are set out in Landmark Case 22.4, *Miranda v. Arizona*, perhaps the most famous case in criminal procedure.

LANDMARK CASE 22.4 Miranda v. Arizona, 384 U.S. 436 (1966)

FACT SUMMARY Ernesto Miranda was a suspect in the knifepoint rape of an 18-year-old woman. Two police officers took Miranda into custody and detained him at a police station. They interviewed Miranda for two hours and obtained a full confession from him. The officers never told Miranda that he had the constitutional right to an attorney and the right to remain silent or that whatever he said could be used against him later at his trial. Only after Miranda confessed did the police have him sign a statement that said the confession was made voluntarily and with full knowledge of his legal rights. After being convicted on the strength of the confession, Miranda appealed, arguing that being interviewed in police custody is inherently coercive if the suspect is unaware of his rights. Thus, his confession was not, in fact, voluntary.

SYNOPSIS OF DECISION AND OPINION The U.S. Supreme Court ruled in favor of Miranda. In a decision that sent shock waves through the law enforcement community, the Court held that Miranda's confession was inherently involuntary and, thus, could not be used at his trial. The Court ordered a retrial. Even though the police did not physically force Miranda to confess, anything he said while trapped in a police interrogation room without knowing that he could have a lawyer or just stay quiet was inherently involuntary and violated the Fifth Amendment. The Court reasoned that because police always have inherent power in any custodial interrogation of a suspect, unless the suspect is informed of his rights beforehand, any confession may be presumed to be involuntary and coerced and therefore not admissible in court.

WORDS OF THE COURT: Coercive Environment "It is obvious that such an interrogation environment is created for no purpose other than to subjugate the individual to the will of his examiner. This atmosphere carries its own badge of intimidation. To be sure, this is not physical intimidation, but it is equally destructive of human dignity . . . Today, then, there can be no doubt that the Fifth Amendment privilege is available outside of criminal court proceedings and serves to protect persons in all settings in which their freedom of action is curtailed in any significant

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way from being compelled to incriminate themselves. We have concluded that without proper safeguards the process of in-custody interrogation of persons suspected or accused of crime contains inherently compelling pressures which work to undermine the individual's will to resist and to compel him to speak where he would not otherwise do so freely. In order to combat these pressures and to permit a full opportunity to exercise the privilege against self-incrimination, the accused must be adequately and effectively apprised of his rights and the exercise of those rights must be fully honored."[21]

Case Questions

1. What if the suspect is not in the police station? Is he still in "custody" in a police car? Pulled over for speeding? Sitting in his office with the police in front of him?
2. When do the police stop talking to the suspect and start "interrogating" such that they need to provide the Miranda warnings?
3. *Focus on Critical Thinking:* Do the Miranda warnings really matter? If you ask for a lawyer or will not talk, doesn't that mean you have something to hide? What would you do if you were a suspect?

Production of Business Records

Business records such as letters, memorandums, e-mail exchanges, inventory accounts, financial documents, and the like are often at the very crux of cases where government authorities are investigating potential criminal activity in the business environment. Although the U.S. Supreme Court has held that certain business records may be classified as private papers and are protected by the Fifth Amendment, this protection has been severely narrowed over the last several decades. In 1984, the Court ruled that certain business records of a sole proprietor could be considered private papers because a sole proprietor is a form of business entity that is essentially the alter ego of the individual.[22] The Court reasoned that because there is no legal separation between the business and the sole owner (unlike a corporation, which exists as a separate legal "person"), the owner's records are considered personal and are subject to Fifth Amendment protections. However, the Court has also made clear that records of a *corporation* are not subject to Fifth Amendment safeguards because that business entity is separate and distinct from its owners and thus does not qualify for self-incrimination protections.

In Landmark Case 22.5, the U.S. Supreme Court considers where to draw the line between personal and business records.

LANDMARK CASE 22.5 Braswell v. United States, 487 U.S. 99 (1988)

FACT SUMMARY Braswell was the sole shareholder and officer in two companies engaged in brokering (buying and selling) timber, land, oil interests, and machinery. The only other directors in the companies were his wife and his mother. Federal authorities that were investigating Braswell's business subpoenaed his business records. Braswell refused to hand over the documents, claiming that he was asserting his Fifth Amendment right against self-incrimination. Braswell argued that when a

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[21] What happened to Ernesto Miranda? On retrial he was found guilty based on other evidence. He spent over a decade behind bars. When he was paroled, he earned income selling police "Miranda cards" that he had autographed. In 1976, he was killed in a bar fight. *See* George C. Thomas, *Missing Miranda's Story*, 2 Ohio St. J. Crim. L. 677, 683–684 (2005).

[22] *U.S. v. Doe*, 465 U.S. 605 (1984).

business is so small that it is nothing more than a person's "alter ego," the Fifth Amendment safeguards should apply.

SYNOPSIS OF DECISION AND OPINION The U.S. Supreme Court ruled against Braswell and compelled him to hand over the books and records. The Court held that a corporation can act only through its officers and employees and when an officer or employee acts as a records custodian for that company, then he is not entitled to Fifth Amendment protection because he is no longer acting as a private individual but as part of a corporation. The Fifth Amendment protects only private individuals.

WORDS OF THE COURT: Corporate Records "Artificial entities such as corporations may act only through their agents, and a custodian's assumption of his representative capacity leads to certain obligations, including the duty to produce corporate records on proper demand by the Government. Under those circumstances, the custodian's act of production is not deemed a personal act, but rather an act of the corporation. Any claim of Fifth Amendment privilege asserted by the agent would be tantamount to a claim of privilege by the corporation—which of course possesses no such privilege."

Case Questions

1. What was Braswell's legal theory for his refusal to hand over the documents to the government?
2. What if Braswell's company was a sole proprietorship rather than a corporation? What if he ran it alone out of his apartment? When should the Fifth Amendment start or stop protecting him?
3. *Focus on Critical Thinking:* If a corporation has been recognized as a legal "person" for First Amendment purposes, shouldn't the Fifth Amendment protect it too?

Trial

The Sixth Amendment provides that in all criminal prosecutions the accused shall enjoy the right to a *speedy trial.* Although the U.S. Supreme Court has not set out specific time periods in which a trial must take place, it has given guideposts for state courts in applying the speedy trial guarantee. Courts apply a balancing test in which both the prosecutor's and the defendant's conduct is examined to determine reasons for delay. Ordinarily, a court weighs the length of the delay versus the severity of the crime. A general rule is that a delay of eight months or more is presumptively unconstitutional. The federal criminal justice system operates according to an infrastructure established by the **Speedy Trial Act**,[23] which sets out specific time periods in which an accused must be brought to trial. If the time limits are exceeded, the courts must dismiss the charges.

The Sixth Amendment also contains other important procedural rights such as a right to a jury trial for serious crimes (generally any offense that carries more than six months' incarceration as a penalty), the right to a public trial, and the right to confront witnesses through cross-examination.[24]

Double Jeopardy

Although the role of the Fifth Amendment is usually thought of in the context of self-incrimination, it also protects a defendant from being subject to prosecution twice for the same offense. This guarantee is known as a prohibition of **double jeopardy**. In essence, the doctrine prevents prosecutors from retrying a defendant on the same charges after a jury has acquitted her.

[23] 18 U.S.C. 3161.

[24] Cross-examination and other trial terminology are discussed in detail in Chapter 3, "The American Judicial System, Jurisdiction, and Venue."

Exclusionary Rule

LO 22-9 Understand the exclusionary rule and how it applies to business.

Trial courts are required to exclude presentation of any evidence that is obtained as a result of a constitutional violation. This is known as the *exclusionary rule.* For example, if a law enforcement officer wrongfully searches a suspect's house without first obtaining a search warrant, any evidence obtained in that search may not be used against the suspect if he is arrested and brought to trial. One important exception in the business environment is that the exclusionary rule applies only when violations of the Constitution occur and not when a government agency violates its own *internal procedures.* For example, suppose that a government agent secretly records a conversation with a suspected tax evader during a meeting in the agent's office. The suspect offers the agent a bribe. However, the agent has violated internal agency rules because he has failed to obtain a supervisor's permission to record any conversations with taxpayers. When the suspect is tried, she asserts that the recording cannot be introduced at trial because it is barred by the exclusionary rule. The U.S. Supreme Court has *rejected* such an argument and held that the exclusionary rule bars only evidence obtained in violation of a constitutional provision. In this case, an agency rule has been violated but no constitutional violations have taken place and, thus, the exclusionary rule does not apply.[25]

Even evidence that is only indirectly obtained in violation of a defendant's rights is subject to the exclusionary rule because it is considered the *fruit of the poisonous tree.* This means that once original evidence is shown to have been unlawfully obtained, all evidence that stems from the original evidence (called *derivative evidence*) is also excluded. For example, suppose an agent of the Securities and Exchange Commission is investigating Falstaff for criminal fraud. The agent illegally searches the handbag of Falstaff's secretary and discovers evidence that Falstaff is concealing incriminating documents in his garage at home. Using the illegally obtained evidence, the agent then obtains a search warrant for Falstaff's home and discovers the incriminating documents. Because the agent's original evidence (obtained from Falstaff's secretary) was obtained in violation of the secretary's constitutional rights, a court would likely hold that the fruit of the poisonous tree doctrine renders the warrant invalid and bars use of all evidence derived from the warrant (the incriminating documents) in a criminal trial against Falstaff.[26]

The exclusionary rule prohibits the use of evidence during a criminal trial that was obtained in violation of a defendant's constitutional rights. © Brand X Pictures

The exclusionary rule itself is controversial because it tends to benefit guilty parties by excluding key evidence that would help convict them. Many legal commentators have filled volumes of journals and treatises on the topic, but ultimately the exclusionary rule is justified by its proponents on the basis that it acts as a deterrent to violations of the Constitution by government authorities. Proponents argue that the integrity of the judiciary requires that courts not be made a party to lawless invasions of constitutional rights of citizens by permitting unhindered government use of unlawfully obtained evidence. Nonetheless, the Supreme Court has fashioned several exceptions to the exclusionary rule intended to differentiate between abuse by the authorities of an individual's constitutional rights and those cases where the government has made an innocent mistake in obtaining evidence. Perhaps the most important exception to the rule occurs when the government can show

[25] Based on *U.S. v. Caceres*, 440 U.S. 741 (1979).

[26] See *Silverthorne Lumber Company v. U.S.*, 251 U.S. 385 (1920).

that authorities were acting in *good faith* in obtaining evidence based on a search warrant issued by an authorized judge that was later found to be unsupported by an appropriate level of probable cause. In that case, even though the evidence is derived from a warrant that was granted but that was later found to have been a constitutional violation, the prosecutor may still introduce the evidence yielded from the search so long as the authorities were acting in good faith and with reasonable reliance on the search warrant.

In *Herring v. U.S.*, the U.S. Supreme Court considered the good faith exception in the context of a police clerical error. The case involved a defendant, Herring, who was arrested after officers were incorrectly informed that an active arrest warrant existed. In fact, no warrant existed and the incorrect information given to the arresting officer was a clerical error. After Herring was arrested, the police searched him incident to arrest and discovered illegal narcotics and a firearm. Herring sought to have the evidence excluded on the basis that it had been obtained without a warrant and only as a result of a wrongful arrest. The government cited the good faith exception because the officers were acting in objectively reasonable reliance on the subsequently invalidated warrant. The U.S. Supreme Court agreed with the government that the good faith exception applied and therefore the evidence should not be excluded. The Court wrote:

> [Herring's] claim that police negligence automatically triggers suppression cannot be squared with the principles underlying the exclusionary rule, as they have been explained in our cases. In light of our repeated holdings that the deterrent effect of suppression must be substantial and outweigh any harm to the justice system, we conclude that when police mistakes are the result of negligence such as that described here, rather than systemic error or reckless disregard of constitutional requirement, any marginal deterrence does not 'pay its way.' In such a case, the criminal should not 'go free because the constable has blundered.'[27]
>
> *555 U.S. 135 (2009).*

LEGAL IMPLICATIONS IN CYBERSPACE

Obscenity in Cyberspace: The Communications Decency Act

The Internet has an element of entrepreneurial spirit associated with it, and many new companies and new business models were created to take advantage of the rapid growth of consumers in cyberspace. At the same time, it is clear that a significant number of business models benefiting from the boom are those associated with the distribution of pornography. In the midst of some high-profile media stories involving the ease of access to online pornography by minors, Congress attempted to curb online content with the Communications Decency Act (CDA) in 1996. The CDA was intended to ban material that was "patently offensive" or "indecent" from being online if the content providers knew that children would have access to the material.

Challenges to the CDA

Shortly after the CDA was enacted, the American Civil Liberties Union (ACLU) filed a lawsuit challenging the act as an unconstitutional infringement on free speech. The case, *ACLU v. Reno* (called *Reno I*), was decided by the U.S. Supreme Court in 1997. It was the first time that the Court applied existing obscenity standards in cyberspace. One important element of the case was the Court's recognition of cyberspace as a unique medium that cannot be equated to broadcast media (such as radio or television) or any printed media (such as magazines or newspapers). This distinction was a key part of the

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[27] The Court used this famous passage from Judge Benjamin Cardozo's opinion criticizing the federal exclusionary rule, which was not then applicable to the states, from *People v. Defore*, 242 N.Y. 13 (1926). Cardozo would later become an associate justice of the U.S. Supreme Court.

Court's analysis that government was not entitled to as much deference in regulation of the Internet as the government is entitled to with other media. That said, the Court went on to strike down much of the act's substance, reasoning that the CDA's prohibition against "patently offensive" material being distributed on the web is too vague to pass constitutional muster.

Congressional Response to Reno I*: Child Online Protection Act of 1998*

Although the Court struck down much of the CDA, the opinion did set out, for the first time, the Court's view on the government's regulation of the Internet. The Court ruled that although the government had the right to regulate Internet traffic, the means employed by Congress was too broad a sweep. Using *Reno I* as a roadmap on constitutionality, Congress passed a similar piece of legislation the next year with the Child Online Protection Act of 1998 (COPA).

The ACLU again filed a lawsuit challenging the COPA as unconstitutional. The new case, *ACLU v. Reno (Reno II)*, was decided by the U.S. Court of Appeals for the Third Circuit in 2000. The court of appeals ruled in favor of the ACLU and struck the statute down as still too overly broad. In 2003, the U.S. Supreme Court upheld the court of appeals's decision and adopted much of the court of appeals's reasoning.

CONCEPT SUMMARY *Criminal Procedure*

- The Fourth Amendment requires authorities to obtain a warrant before searching areas where a citizen has a reasonable expectation of privacy.
- Important exceptions to the warrant requirement are plain view and search incident to arrest.
- The Fifth Amendment protects an individual from involuntary self-incrimination before, during, and after an investigation and trial, but it does not protect a person from disclosing business records made in the person's capacity as corporate agent. The Fifth Amendment does not protect corporations.
- Anything said during custodial interrogation is presumed to be involuntary unless and until the person has been read the Miranda warnings.
- The exclusionary rule bans evidence obtained in violation of the Constitution from being used at trial.

KEY TERMS

Criminal law p. 694 The body of law that, for the purpose of preventing harm to society, defines the boundaries of behavior and prescribes sanctions for violating those boundaries.

Model Penal Code (MPC) p. 695 A statutory text adopted by the American Law Institute in 1962 in an effort to bring greater uniformity to state criminal laws by proffering certain legal standards and reforms.

Criminal procedure p. 695 The body of constitutional protections afforded to individuals and business entities during criminal investigations, arrests, trials, and sentencing.

Burden of proof p. 696 The responsibility of producing sufficient evidence in support of a fact or issue and favorably convincing the fact finder of that fact or issue.

Preponderance of the evidence p. 696 The burden of proof used in civil cases, under which the fact finder need be convinced only that the defendant's liability was more likely than not.

Beyond a reasonable doubt p. 696 The heightened burden of proof used in criminal cases, under which a fact finder must be convinced that the defendant's criminal liability is not in doubt to a reasonable person.

Legality p. 696 A principle of criminal law that protects individuals from being charged with some unspecified general offense; requires that crimes be specifically proscribed by law in advance of the conduct sought to be punished.

Punishment p. 696 A principle of criminal law that imposes a hardship in response to misconduct; based on the concepts that criminal law acts as a deterrent, it removes dangerous criminals from the population, and rehabilitation is an important part of the criminal justice system.

Sentencing guidelines p. 696 Statutorily prescribed standards for determining the punishment that a convicted criminal should receive on the basis of the nature of the crime and the offender's criminal history.

Act requirement p. 697 For criminal liability, the requirement that the government prove that a defendant's actions objectively satisfied the elements of a particular offense. Also called *actus reus.*

Self-defense p. 697 A defense to avoid criminal liability whereby the defendant's actions are related to the necessity of using deadly force to repel an attack in which the defendant reasonably feared that death or substantial harm was about to occur either to the defendant or to a third party.

Mental incapacity p. 698 A defense to avoid criminal liability whereby the defendant's actions are related to some type of mental disease or defect.

Felonies p. 698 Crimes that generally carry one year or more of incarceration as the penalty.

Misdemeanors p. 698 Crimes that carry up to one year of incarceration as the penalty.

Mail Fraud Act p. 701 Federal legislation enacted in 1990 as a comprehensive approach to criminalizing any fraud in which the defrauding party uses the mail or any wire, radio, or television in perpetrating the fraud.

Insider trading laws p. 703 Federal securities statutes that prohibit corporate insiders who have access to certain information that is not available to the general investment public from trading their company's stock based on the insider knowledge.

Computer Fraud and Abuse Act p. 708 Federal legislation that prohibits unauthorized use of computers to commit espionage, the accessing of unauthorized information or of a nonpublic government computer, fraud by computer, damage to a computer, trafficking in passwords, and extortionate threats to damage a computer.

Foreign Corrupt Practices Act (FCPA) p. 708 A federal criminal statute enacted principally to prevent corporate bribery of foreign officials in business transactions.

Investigation p. 709 The initial phase of the criminal justice process in which authorities become aware of an alleged criminal act and begin gathering physical evidence and interviewing witnesses and potential suspects.

Adjudication p. 709 A phase of the criminal justice system in which the prosecutor, after investigation, elects to proceed with the charges.

Probable cause p. 709 A reasonable amount of suspicion supported by circumstances sufficiently strong to justify a belief that a person has committed a crime.

Preliminary adjudication p. 710 A hearing at which the prosecutor presents evidence of the defendant's guilt and the decision maker (either the grand jurors or a magistrate) determines whether sufficient probable cause exists to hold the defendant over for trial.

Plain view doctrine p. 713 A doctrine stating that authorities generally do not commit a Fourth Amendment violation when a government agent obtains evidence by virtue of seeing an object that is in plain view of the agent.

Speedy Trial Act p. 718 A federal statute that sets out specific time periods in which an accused must be brought to trial.

Double jeopardy p. 718 Situation in which a defendant could be subject to prosecution twice for the same offense; prohibited by the Fifth Amendment.

CHAPTER REVIEW QUESTIONS

1. What are the general requirements for criminal liability?

I. Preponderance
II. Act
III. Justice
IV. Mental

a. I and II
b. II and IV
c. II and III
d. III and IV

2. Which doctrine was created in a case involving the conviction of an individual executive under the Food, Drug, and Cosmetic Act?

a. Miranda
b. Park
c. Riley
d. Braswell

3. The U.S. Supreme Court held that the government's use of a zoom lens in a flyover of a chemical company fell into which warrant requirement exception?

a. Search incident to arrest
b. Good faith
c. Plain view
d. Privacy

4. Greco is arrested for insider trading based on evidence obtained by the government that violates Greco's Fourth Amendment rights. The evidence cannot be used against him at trial based on the ______ ______.

a. Rights doctrine
b. Violation rule
c. Exclusionary rule
d. Wrongful statute

5. Which amendment provides the right to a speedy trial?

a. First
b. Second
c. Fourth
d. Sixth

Answers and explanations are provided at the end of this chapter.

THEORY TO PRACTICE

Dania Beach Antique Supply (DBAS) Inc. is a wholesaler of antique merchandise. DBAS employs expert buyers who purchase antiques in Europe. The company then makes any cosmetic improvements necessary (such as cleaning) and resells the merchandise to retail antique shops in the United States. Grendel is a senior-level executive at the company in charge of its primary warehouse, located in Fort Lauderdale, Florida, and a smaller facility at the Port of Miami. One of Grendel's responsibilities is to oversee worker safety in the facilities, as the processing of the antiques sometimes involves use of industrial machinery and cleaning solvents.

It was well known among DBAS employees that the Fort Lauderdale warehouse had less than ideal working conditions. The air-conditioning was often broken, and during the summer months the indoor temperature was in excess of 100 degrees. The cleaning solvents were left unattended, and the noxious fumes made working conditions hazardous. When workers complained to Grendel, he purchased small fans to be placed in the facility but declined to overhaul the air-conditioning, claiming that the expense was too high and that the company was struggling financially. Grendel also ordered that the cleaning solvents be properly disposed of, but the on-site manager never carried out the order. In the meantime, several employees were hospitalized for heat exhaustion during their shift, and several others were made sick by the fumes from the cleaning solvents.

1. Assume that one worker notifies the Occupational Safety and Health Administration (OSHA) and that an OSHA agent informs Grendel that an investigation will be undertaken into the allegations of workplace hazards. Grendel immediately hires an air-conditioning repair company to fix the air-conditioning system. He also tells the on-site manager to destroy any maintenance records of the warehouse air-conditioning system history of inspections and repairs. What potential criminal culpability would DBAS, Grendel, and the on-site manager have at this point? Do Grendel's preinvestigation actions constitute a criminal act? Do Grendel's actions after OSHA's notification of an investigation constitute a crime in and of themselves? Is the on-site manager criminally liable for carrying out Grendel's orders?
2. Suppose that Grendel is charged with a crime related to the workplace hazards and he defends by showing evidence that he ordered subordinates to take care of the hazards but his directions were never carried out. Is that a valid defense? If Grendel had second thoughts about his orders to destroy maintenance records and he called the manager to reverse his previous directions, would he still have criminal liability for attempting the cover-up?
3. Assume that during the investigation, OSHA agents make a midnight visit to Grendel's residence and remove documents from Grendel's trash bin on the

public curb in front of his house. The documents contain incriminating evidence. Is the OSHA search illegal? Does the exclusionary rule apply in this case?

4. Assume that OSHA has information indicating that Grendel wrote about having a guilty conscience in regard to the working conditions in the warehouse. During the criminal investigation of Grendel, OSHA issues a subpoena for Grendel's personal diary. Is Grendel's diary protected from inspection via the Fifth Amendment?
5. Is OSHA required to obtain a search warrant if OSHA investigators use cameras with telephoto lenses (that are available to the general public) to take pictures of the broken air-conditioning unit adjacent to the warehouse? Assume the investigators take pictures while standing on the public sidewalk.

LEGAL STRATEGY 101

The Original Prisoner's Dilemma

The so-called "Prisoner's Dilemma" is perhaps the most well-known and famous example of legal strategy. It's called the *Prisoner's* Dilemma because of the original story told to illustrate this strategic situation:

> Two suspects are taken into custody and separated. The district attorney is certain that they are guilty of a specific crime, but does not have adequate evidence to convict them at trial. He points out to each prisoner that each has two alternatives: to confess to the crime the police are sure that they have done, or not to confess. If they both do not confess, then the district attorney states he will book them on some very minor trumped-up charge such as petty larceny and illegal possession of a weapon, and they will both receive minor punishment; if they both confess they will both be prosecuted, but he will recommend less than the most severe sentence; but if one confesses and the other does not, then the confessor will receive lenient treatment for turning state's evidence whereas the latter will get "the book" slapped at him.[28]

	You Confess	You Deny
They Confess	You both get 10 years	You get 20 years, they go free
They Deny	You go free, they get 20 years	You both get 5 years

Prisoner's Dilemma.

The two suspects in this hypothetical will thus have a very long night ahead of them, as they separately but simultaneously mull over their options. Pop quiz: What should they do? There are three possibilities:

a. If one suspect "snitches" while the other remains silent, the "snitch" will be treated leniently (and possibly even receive immunity), while the suspect who remains silent will receive the most severe sentence.
b. If both of them snitch (i.e., turn state's evidence), they will both end up with stiff prison sentences.
c. If both suspects remain loyal to each other (i.e., refuse to snitch), both will receive light sentences.

Sounds like an easy choice, right?

It's not! The reason why the Prisoner's Dilemma is called a "dilemma" is because—from the strategic point of view of each suspect—no matter what the other suspect does, snitching is always a best response.[29]

[28] See R. Duncan Luce and Howard Raiffa, *Games and Decisions: Introduction and Critical Survey*, Dover, reprint ed. (1989), p. 95.

[29] Stated formally, "snitching" in this situation is a *Nash Equilibrium*. Named after the mathematician John Nash, who inspired the original version of the Prisoner's Dilemma, a Nash Equilibrium is a combination of strategies that are mutual best responses. See, e.g., Sylvia Nasar, *A Beautiful Mind: A Biography of John Forbes Nash, Jr.*, Simon & Schuster, reprint ed. (2011), p. 118.

To see this, let's look at the prisoners' situation from a strategic perspective. From the first suspect's point of view, if the other suspect snitches, then the first suspect should snitch as well; otherwise, he or she will receive the most severe sentence.

But here's the rub: Even if the other suspect decides not to snitch, from a strategic perspective, the first suspect should still snitch anyway. Why? Because snitching results in a lighter sentence for the first suspect when the other suspect remains silent. Since the same logic holds for the other suspect, the suspects are trapped in a true dilemma, a dilemma exploited by savvy prosecutors in many criminal cases.

CRITICAL THINKING QUESTION

Do you see any possible solution to the Prisoner's Dilemma? What if the suspects are not held in separate jail cells; that is, what if they are allowed to communicate with each other?

MANAGER'S CHALLENGE

A common element in cases where corporate executives are found guilty of criminal charges related to corporate activity is the lack of a systematic compliance procedure in the company's infrastructure. Senior managers are responsible for having systematic, internal controls in place that will help ensure compliance with federal and state statutes. Assume that you are a DBAS employee in this chapter's Theory to Practice problem and that both Grendel and the on-site warehouse manager are fired. You receive the following e-mail from the new vice president of operations:

> Congratulations! You are being promoted to on-site manager at the Fort Lauderdale warehouse. The primary order of business is to develop a system of checks to be sure we are doing everything we can to avoid hazardous work conditions for our employees. Draft a two- to three-page memorandum that sets out a specific system for compliance. The system should address (1) how complaints from workers will be handled; (2) procedures for inspecting the facility, reporting problems, and ensuring follow-up; (3) a clear chain of command; and (4) a response plan to handle hazards that require immediate response.

See Connect for Manager's Challenge sample answers.

CASE SUMMARY 22.1 Bear Stearns & Co. v. Wyler, 182 F. Supp. 2d 679 (N.D. Ill. 2002)

PRODUCTION OF BUSINESS RECORDS

Bear Stearns had done business with Wyler, a Dutch businessman. A venture capitalist and resident of the Netherlands, Wyler kept offices in Toronto and Barbados. After the relationship soured, Bear Stearns sued Wyler for inducing one of its managing directors to make false statements and breach his fiduciary duties. In discovery, Bear Stearns requested that Wyler disclose any business records that related to that fraudulent inducement. Wyler invoked his Fifth Amendment right against self-incrimination.

CASE QUESTIONS

1. Will the court force Wyler to disclose the documents? Are they business records?
2. Does the Fifth Amendment apply in civil suits?

CASE SUMMARY 22.2 Dollar S.S. Co. v. United States, 101 F.2d 638 (9th Cir. 1939)

CRIMINAL LAW AND BUSINESS ENTITIES

A harbor patrolman was hit by a bucket of garbage "consisting of cabbage, orange peel, celery, tea leaves, and water" thrown from a steamer named the *President Coolidge* in Honolulu harbor. Unable to find the actual sailor who had dumped the trash, the government charged the ship owner under a federal law making off-loading garbage into navigable waters illegal. The ship's owner, however, had taken measures to prevent such dumping, such as issuing orders to the crew about its prohibition, hanging several warning signs in obvious places in both English and Chinese, and locking the "slop chutes" to prevent their use while in the harbor.

CASE QUESTIONS

1. Will the steamship company be criminally liable? Should it be even though it did everything to prevent the crime?
2. If the company should not be liable, what is the best way to prevent this crime?

CASE SUMMARY 22.3 United States v. Stewart, 323 F. Supp. 2d 606 (S.D.N.Y. 2004)

INSIDER TRADING

A wealthy businesswoman bought several thousand shares of a pharmaceutical company that was set to come out with a groundbreaking new cancer drug. She was a social friend of the company's CEO. On her way to vacation in Mexico, she received information from her broker that the CEO was selling all his shares. She eventually found out that the Food and Drug Administration was set to reject the cancer drug. She then sold all her shares and saved her own portfolio from devastation.

CASE QUESTIONS

1. Is the woman guilty of insider trading? Why?
2. Would you do what she did or just wait around to lose all your money?
3. Should the CEO get to sell his shares?

CASE SUMMARY 22.4 Lamb v. Philip Morris, Inc., 915 F.2d 1024 (6th Cir. 1990)

FOREIGN CORRUPT PRACTICES ACT

Philip Morris buys tobacco for its cigarettes from all around the world, including from South American growers in Venezuela. Philip Morris entered into a contract with La Fundacion del Niñó (the Children's Foundation) of Caracas, Venezuela, wherein the cigarette company would give the charity, which helped poor Venezuelan children, \$12.5 million. In exchange, the Venezuelan government would put price controls on the country's tobacco crop.

CASE QUESTIONS

1. What criminal law did Philip Morris possibly violate? Why?
2. Should the criminal law have a problem with providing money to poor Venezuelan children and offering work for poor Venezuelan farmers?

CASE SUMMARY 22.5 State v. Yenzer, 195 P.3d 271 (Kan. App. 2008)

EXCLUSIONARY RULE

The police received information that Yenzer, a fugitive, would be at a local dentist's office the next day. The police arrived at the dentist's office in hopes of capturing Yenzer, but she was not there. The receptionist informed them that Yenzer's appointment had been rescheduled for the next week. The police requested the exact date and time, and the dentist's receptionist complied. The police returned to the office at the rescheduled appointment time and arrested Yenzer when she arrived. Subsequent to her arrest, the police discovered evidence of additional crimes committed by Yenzer and charged her with various felonies. The Health Insurance Portability and Accountability Act (HIPAA) of 1996 prohibits dental offices from disclosing any information (including appointment times) about patients to third parties without the patient's permission. At trial, Yenzer argued that all evidence discovered after the dentist-office arrest should be excluded because the arrest was made as a result of a HIPAA violation.

CASE QUESTIONS

1. Is Yenzer's dental appointment time protected by the Fourth Amendment? Why or why not?
2. Did the police go too far in this case by requesting confidential information from the dentist's receptionist? Isn't the exclusionary rule intended to deter unlawful conduct by authorities?

Self-Check ANSWERS White-Collar Crime

1. FCPA. Buying a lavish meal for foreign government officials is prohibited.
2. Fraud (Ponzi scheme).
3. Conspiracy.
4. RICO.

CHAPTER REVIEW QUESTIONS: Answers and Explanations

1. **b.** Criminal liability requires both an act (or omission) and the mental element of a guilty mind. The remaining answers are incorrect because preponderance and justice are unrelated to criminal liability.

2. **b.** Created in *U.S. v. Park*, the doctrine is cited in the context of holding individual corporate officers liable for certain violations. The remaining answers are incorrect because they are names of cases unrelated to the Park doctrine.

3. **c.** In *Dow Chemical Co. v. U.S.*, the Court held that a zoom lens was readily available to the public and therefore could be used to enhance "plain view." Answer choice (a) is incorrect because no arrest was made. Answer choice (b) is incorrect since good faith refers to some mistake made by authorities. Answer choice (d) is not an exception to the warrant requirement.

4. **c.** The exclusionary rule requires that evidence obtained without a warrant and not falling into a warrant exception be excluded from trial. The remaining answers are fictional.

5. **d.** The Sixth Amendment provides for a speedy trial, a public trial, and the right to confront witnesses. The remaining answers are wrong because those amendments are unrelated to criminal trials.

CASE SUMMARY 9.6 Burton v. MDC PGA Plaza Corp., 78 So. 3d 732 (Fla. App. 4th Dist. 2012)

DANGEROUS CONDITION AND COMPARATIVE NEGLIGENCE

Burton worked for a marketing and merchandising company that helped new retail businesses prepare for openings. She was brought in to work at a new CVS Pharmacy getting ready for its grand opening. While unloading trucks, Burton noticed a pothole about 10 or 15 feet from the store's back door. The pothole was approximately 1 foot wide and 2 inches deep. Burton informed her co-workers and CVS's management of the pothole and urged everyone to exercise caution. One week later, Burton was seriously injured when, while loading a vehicle, she stepped into the pothole, tripped, and fell to the ground. Burton filed suit against both CVS and its landlord, MDC.

CASE QUESTIONS

1. Can a property owner be liable for injuries when a dangerous condition is open and obvious? Does the owner have a duty to warn when the dangerous condition is open and obvious?
2. Can a property owner be liable for injuries when a dangerous condition is open and obvious and the injured party was well aware of the dangerous condition?
3. Does Burton's knowledge of the dangerous condition merely raise an issue of fact as to her own comparative negligence?

Self-Check ANSWERS Intentional Torts

1. Defamation. Specifically, it is slander because the statements Jason made were oral.
2. No tort has been committed. This is not a tortious interference with a contract because Third Bank merely offered a better price for its services and MOT made the decision to switch.
3. Trespass to chattel. Wayne has interfered with his company's ability to use the car and will be responsible for the repairs and any damages suffered by the company because the car is unavailable.
4. Conversion. Nancy is stealing the stationery supplies and civilly is responsible for paying the company back for the full value of the supplies she has taken.
5. No tort has been committed. This is not a fraud because the deal had already been agreed to and the intentionally false statement was not material to the deal.

Proximate Cause

1. Yes. The injury (broken arm) was sufficiently proximate to the negligence (defective steering column). *McCown v. International Harvester Co.*, 342 A.2d 381.
2. No. Too many acts of intervening negligence on the part of the landlord. *Matthias v. United Pacific Ins. Co.*, 67 Cal. Rptr. 511, 514.
3. Yes. It was reasonably foreseeable that the employee would have been falsely arrested for the fire. The jury found that the employer had framed the employee. *Seidel v. Greenberg*, 260 A.2d 863, 871.
4. Yes. It was reasonably foreseeable that the intoxicated driver would have an accident and the liquor store also violated state dram shop laws. *Gonzales v. Krueger*, 799 P.2d 1318, 1321.

CHAPTER REVIEW QUESTIONS: Answers and Explanations

1. **d.** Malice is only required when the defamed party is a public figure or to disqualify a qualified privilege (e.g., media). Answer choices (a), (b), and (c) are incorrect because they are all elements of a defamation claim.
2. **d.** Each of the listed responses in (a), (b), and (c) are breaches of duty.
3. **d.** Ginger owes a general duty not to cause harm to the pedestrian. This duty was breached (*res ipsa*) and the explosion was the cause and proximate cause of the injuries. Answer choice (a) is incorrect because she owes him a general duty. Answer choice (b) is nonsensical. Answer choice (c) is incorrect because there is no special duty owed, only a general duty.
4. **c.** The fan knew of the risk, understood the risk, and went ahead with the activity. Answer choices (a) and (b) are incorrect because the fan did not contribute to his own injury. Answer choice (d) is unrelated to a negligence analysis.
5. **c.** Products can be made unreasonabley dangerous by either a design (improperly engineered) or a manufacturing (improperly made) defect. Answer choices (a), (b), and (c) are wrong because each contains a term unrelated to products liability.